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Panel on Commerce and Industry

Meeting on 19 May 2009

**Background brief on
Hong Kong Design Centre**

Purpose

This paper gives the background to the Government's support for the operation of Hong Kong Design Centre (HKDC) and also a summary of views and concerns expressed by the Panel on Commerce and Industry (the Panel).

Background

2. HKDC is a non-profit making infrastructure organization established in 2001 to further the development of design. It is a company limited by guarantee, with the Hong Kong Designers Association, Chartered Society of Designers, Hong Kong, Interior Design Association Hong Kong, Hong Kong Fashion Designers Association, and the Hong Kong Federation of Design Associations as members. The objectives of HKDC are to, among other things, promote design as a value-added activity and integration of design into mainstream business processes, which are in line with Government's policy on the promotion of design and innovation. HKDC has since its inception been Government's main partner in promoting design. To support HKDC's initial operation, the Government provided a one-off funding of \$10 million to HKDC as seed money in 2001.

3. On 11 October 2006, the Chief Executive announced in his 2006-2007 Policy Address that the Government would earmark \$100 million over five years for HKDC to further assist the trades and industries in Hong Kong to make full use of their designs and build their brand names. Following consultation with the Panel, the Administration submitted a funding proposal of \$100 million to support the operation of HKDC over five years to promote the importance of design and

innovation. The proposal was approved by the Finance Committee (FC) on 25 May 2007.

4. HKDC is governed by a Board of Directors with a balanced composition comprising representatives from the relevant design-related industrial and business sectors and professions, as well as two government officials viz. the Commissioner for Innovation and Technology (CIT) and Deputy Secretary for Home Affairs. The Innovation and Technology Commission (ITC) disburses funds to HKDC subject to necessary safeguards and funding requirements as set out in a Funding Agreement between HKDC and ITC (**Appendix I**).

5. HKDC has instituted a system to measure and evaluate the effectiveness of its programme, such as conducting regular tracking surveys on design awareness and standard in Hong Kong, and exploring with other organizations to conduct benchmarking study on the economic/social benefits brought about by design and innovation. Other quantitative key performance indicators include the revenue stream of HKDC, number of participants in HKDC events, number of visitors to the HKDC website, size of HKDC's database on designers and number of international design awards won by Hong Kong. HKDC is required to report to CIT its operation, cashflow position and performance as measured against a set of performance indicators in the annual report. The Government also provides input to this performance evaluation system.

6. Apart from conducting annual reviews on its performance, HKDC is required to conduct a major review in the fourth year of the five-year funding period to evaluate its overall performance, strategy and financial position. The results of the review would enable the Government to assess whether HKDC could be operationally and financially self-sustainable at the end of the five-year funding period. HKDC is expected to operate on a self-financing basis as early as possible and the Government does not plan to provide recurrent subvention to HKDC upon depletion of the \$100 million commitment. HKDC may be required to draw up a timely exit plan if it is unlikely to be financially self-sustainable within a reasonable period of time.

Discussion by the Panel on Commerce and Industry

7. The Panel discussed the work of HKDC on 17 April 2007 and 15 April 2008. In general, the Panel welcomed the Government's support for HKDC as they considered that it would be conducive to the development of local enterprises as well as the long-term economic development of Hong Kong.

8. In order to solicit more co-operation and hence business opportunities, some Panel members took the view that HKDC should conduct more promotional activities overseas to showcase Hong Kong's design talents. The Administration assured the Panel that it would arrange Hong Kong designers to partner with

world-renowned international manufacturers to produce and showcase limited-edition signature products in overseas mega events, which would help raising the profile and reputation of Hong Kong's design talents in the international arena.

9. In addition to promoting design, Panel members were also keen to ensure that safeguards would be put in place by HKDC to protect the intellectual property (IP) of designers and their products. In this regard, the Panel noted that HKDC had compiled a business manual for local designers which covered IP protection on how to apply for registration for their IP and related legal issues. The Administration assured the Panel that HKDC would continue to provide assistance to the design industries on this front.

10. In view of the development in the Mainland in recent years, Panel members considered that efforts should be stepped up in nurturing design talents to meet with market demand so that Hong Kong would maintain its competitive edge in the long run. The Administration should strive to obtain international recognition of the local design qualification with a view to encouraging more inspired talents to join the design industry, thereby raising the quality of the local design industry.

11. Noting that many business and industry players were not yet convinced of or conversant with design and branding, Panel members were concerned whether the Administration would take appropriate measures to assist the trades and industries to make fuller use of design and innovation to build their brand names. The Administration assured the Panel that in addition to the DesignSmart Initiative (DSI) which aimed to promote the interest and investment of Hong Kong entrepreneurs in relation to utilizing design and transforming design activity into tradable deliverables, HKDC had spared no efforts in promoting the private sector to move from Original Equipment Manufacture to Original Brand Manufacture by various promotional activities including conferences, workshops, discussion fora and experience sharing sessions.

Recent development

12. The Audit Commission conducted a review from March 2007 to June 2008 to examine the economy, efficiency and effectiveness of the administration of the DSI managed by ITC. The review focused on the corporate governance and administration of HKDC, management of projects funded by the Design Support Programme, promotion of design by HKDC, administration of the Design Incubation Programme, and overseas practices in the promotion of design. The summary of the observations and recommendations made by the Audit Commission is in **Appendix II**. The summary of conclusions and recommendations made by the Public Accounts Committee on the subject is in **Appendix III**.

Latest position

13. The Administration and the representative of HKDC will report to the Panel the progress of work of HKDC and the relevant initiatives taken to promote design and innovation at the Panel meeting on 19 May 2009.

Relevant papers

14. A list of relevant papers is at **Appendix IV**.

Council Business Division 1
Legislative Council Secretariat
13 May 2009

**Funding Agreement between Hong Kong Design Centre and
the Innovation and Technology Commission**

- (a) Unless with Government approval, there should be no change in the appointment arrangements for the Board of Directors during the Government funding period to ensure a balanced representation of stakeholders;
- (b) HKDC is required to submit to the Commissioner for Innovation and Technology (CIT) annually, before the submission of the annual plan, a three-year business plan, and roll it over every year. The plan should set out the strategic targets of Hong Kong Design Centre (HKDC), the use of Government funding with defined time frame, missions, deliverables, performance indicators, staffing structures and a system to interface with stakeholders;
- (c) HKDC is subject to various controls on its operation such as submission of annual plan, budgets and audited accounts for Government approval, performance indicators and assessment, acceptance of the quarterly/annual operational reports and financial statements by CIT before disbursement of funds on a quarterly basis, prior Government approval for non-budgeted items and over 30% variation between categories of expenditure, compliance with corporate governance manual, and value-for-money checks by the Audit Commission if required by Government;
- (d) HKDC is required to build up and enhance its revenue stream with a view to achieving self-financing as soon as possible. CIT may set and revise an income target from time to time which HKDC has to meet;
- (e) disbursement of the five-year Government funding will be subject to a review and exit mechanism. For example, if CIT considers that HKDC is unlikely to be operationally or financially self-sustainable within a reasonable period of time, HKDC may be required to draw up a timely exit plan to take care of its operation without further public funding support;
- (f) HKDC is not allowed to keep and retain any unspent Government funding as reserve. Any unspent balance of the Government funding, including any surplus income generated from such funding, has to be returned to Government after expiry of the five-year funding period or if HKDC ceases business before that; and

- (g) the operation and programmes of HKDC funded by Government must be kept in a specific account distinct and separate from that for operation not funded by Government (covering, for example, any HKDC liabilities out of non-Government-funded operation and expenditure in a Government funded project over and above the approved Government funding and not otherwise covered by other project income). The Government will not assume any responsibility for the liabilities and expenditures in the non-Government funded account; HKDC has to seek separate donations and other incomes to cover such liabilities and expenditures.

Report No. 51 of the Director of Audit — Chapter 2

ADMINISTRATION OF THE DESIGNSMART INITIATIVE

Summary

1. In June 2004, the Government launched the DesignSmart Initiative (DSI) with a funding commitment of \$250 million. The DSI comprised two programmes, the Design Support Programme (DSP) and the InnoCentre Programme. Under the DSP, \$180 million was set aside for financing projects under four funding schemes, namely: (a) Design Research Scheme (DRS); (b) Design-Business Collaboration Scheme (DBCS); (c) Professional Continuing Education Scheme (PCES); and (d) General Support Scheme (GSS). Under the InnoCentre Programme, \$45 million was allocated to the Hong Kong Design Centre (HKDC) for supporting its operation and \$25 million was allocated to the Hong Kong Science and Technology Parks Corporation (HKSTPC) for running an incubation programme for design ventures. The Innovation and Technology Commission (ITC) is responsible for managing the DSI. The Audit Commission (Audit) has recently conducted a review on the administration of the DSI.

Management of projects funded by the Design Support Programme

2. *Review of the DSP.* The ITC had conducted reviews only on the DRS and the DBCS. Audit considers that the PCES and the GSS also need to be reviewed. As the total number of projects which benefited from the DSP (169 as at June 2008) was much lower than that expected (i.e. 700 by June 2009), the ITC needs to conduct an overarching review of the DSP. *Audit has recommended that the Commissioner for Innovation and Technology should conduct: (a) reviews on the operation of the PCES and the GSS; and (b) an overarching review of the DSP to ascertain the reasons for low utilisation of some of its funding schemes, and to identify areas for improvement.*

3. *Project 9707.* Project 9707 was a project initiated to commemorate the 10th anniversary of Hong Kong's return to China. International brands and Hong Kong designers were invited to produce ten collaborative creative products which were exhibited in Hong Kong and the Mainland. Audit's examination of the records of Project 9707 found that there was no documentation to record the basis for selecting these brands and designers, and that up to 30 June 2008, only three brands and three designers had signed a Memorandum of Understanding (MOU) which specified the rights and obligations of the parties concerned. Furthermore, pre-project commencement expenses of about \$173,000 were charged to the project account without the ITC's approval. *Audit has recommended that the HKDC should: (a) keep proper documentation on the shortlisting and selection of participants for projects funded by the DSP; (b) ensure that all the participating brands and*

designers sign an MOU with the HKDC as early as possible; and (c) ensure that the ITC's approval is obtained if expenditure needs to be incurred before commencement of a DSP project.

4. ***Business of Design Week.*** Business of Design Week (BODW) is the HKDC's annual flagship event. It is a combination of conferences, exhibitions, awards and outreach programmes. Audit's examination of the records of the BODW 2006 and 2007 revealed that the salary of a DSP project staff was adjusted without obtaining the ITC's prior approval, and that entertainment expenses were charged to project accounts, contrary to the DSP funding guidelines. Furthermore, payroll expenses incurred for employing the project leader exceeded the budget by about 32% (i.e. over the 15% limit set by the ITC) with no prior approval from the ITC. *Audit has recommended that the HKDC should: (a) seek the ITC's approval prior to making salary adjustment to DSP project staff; (b) ensure that the DSP funding support is not used to meet entertainment expenses; and (c) seek the ITC's approval if the budget of a DSP project item is exceeded by 15% or more.*

Promotion of design by the Hong Kong Design Centre

5. Since its inception in 2001, the HKDC has been the Government's main partner in promoting design. As at 30 June 2008, the total Government funding (including that allocated under the DSI) committed to support the operation of the HKDC amounted to \$225 million.

6. ***Implementation of design infrastructure projects.*** The HKDC stated in its business plan and annual budget various initiatives for enhancing the design infrastructure, including: (a) establishing a design resource centre; (b) setting up a design directory; and (c) revamping the HKDC's website as a gateway to design information. Audit noted that the implementation of these initiatives had met with considerable delays. *Audit has recommended that the Commissioner for Innovation and Technology should ensure that delays in implementing the HKDC's design infrastructure projects are dealt with in a timely manner. Audit has also recommended that the HKDC should improve its project management capability to ensure that its design infrastructure projects are not further delayed.*

7. ***Management of funding for design promotion.*** In order to encourage the HKDC to build up its revenue generating capacity for its long-term development, it is required to meet an income target fixed by the ITC. The target for 2008-09 was 20% of the HKDC's basic operation expenditure. The HKDC estimated in July 2008 that the income in 2008-09 would be about 12.4% of its basic operation expenditure, which was considerably below the target of 20%. *Audit has recommended that the HKDC should take improvement actions to meet the income target.*

Corporate governance and administration of the Hong Kong Design Centre

8. The HKDC was established in 2001. It is governed by a Board of Directors (Board). The Finance and Administration Committee (FAC) and the Business Development Committee of the HKDC were set up in June 2007 to assist the Board to conduct its business.

9. **Attendance of directors at Board/Committee meetings.** Audit found that, from March 2007 to June 2008, some directors had low attendance records at Board/Committee meetings. Furthermore, at three (60%) of the five FAC meetings held during the period, the quorum requirement was not met. This might render the decisions made at these meetings invalid. *Audit has recommended that the HKDC should: (a) issue reminders to those directors with low attendance records, urging them to make efforts to attend Board/Committee meetings; and (b) ensure that the quorum requirement is always met at all meetings.*

10. **Management of potential conflicts of interest.** According to the Home Affairs Bureau's guideline issued in 2005 on declaration of interests for advisory and statutory bodies, a board or committee should adopt a "two-tier reporting system", which requires members to disclose their general interests on appointment to the board/committee, if it has a high degree of management and financial autonomy, extensive executive powers in matters of public interest, or is responsible for the control and disbursement of substantial public funds. To a large extent, the HKDC meets such criteria. *Audit has recommended that the HKDC should consider adopting the two-tier reporting system for managing potential conflicts of interest of its directors.*

11. **Hiring of staff.** According to the HKDC's Corporate Governance Manual, the Board's prior approval is needed for the creation of new posts. The ITC's approval is also needed if the creation of new post constitutes a manpower variation. Audit noted that there was a case involving a creation of new post, which constituted a manpower variation. However, approvals of the Board and the ITC were only sought after the appointee had started working in the HKDC. Audit also noted that in three other cases, inadequate information was provided to the Board in seeking its approval for the appointment. *Audit has recommended that the HKDC should ensure that: (a) the requirements regarding the creation of posts are complied with and, where necessary, the ITC's prior approval should also be sought; and (b) adequate information is provided in seeking approval for appointment of staff.*

12. **Procurement of goods and services.** The HKDC's guidelines for procurement of goods and services are set out in its Corporate Governance Manual. Among other things, the guidelines specify that: (a) for procurement amounts of over \$5,000 but less than \$10,000, at least two quotations should be obtained; and (b) for procurement of goods and services from a single supplier, if the lowest bid is not accepted, full justifications must be documented and approvals from the Chief Executive Officer (CEO) and the ITC are

required. Audit found that in 2007-08, the HKDC's procurement guidelines were not always followed. *Audit has recommended that the HKDC should ensure that sufficient number of quotations is obtained in accordance with the procurement guidelines set out in the Corporate Governance Manual.*

13. ***Overseas travel expenses.*** Audit's examination of overseas travel expenses in 2006-07 and 2007-08 revealed that in 3 of a total of 18 cases, air tickets were purchased before application for approval was made or written approval was obtained. In another case, the CEO travelled to the United States by business class. However the decision that the CEO could travel by business class might be invalid because it was made at an FAC meeting that did not meet the quorum requirement. Furthermore, in three cases, overseas travel expenses incurred by a Board member were reimbursed with the Chairman's approval. This was not in accordance with the requirement of the HKDC's Corporate Governance Manual that the Board's approval be obtained for such expenses. *Audit has recommended that the HKDC should: (a) remind all staff that prior written approval should be obtained for overseas travel, and proper documentation should be kept if approval is given verbally; (b) seek the Board's covering approval regarding the authorisation for the CEO to travel by business class; and (c) remind all Board members to obtain proper approval from the Board before seeking reimbursement of travel expenses.*

Administration of the Design Incubation Programme

14. Under the DSI, \$25 million was earmarked for the HKSTPC to operate the Design Incubation Programme (DIP). The objective is to support design start-up companies for a period up to two years. Design start-up companies admitted under the DIP (known as incubatees) are eligible for a financial assistance package, up to \$500,000, to help cover business development costs during their start-up period. The financial package consists of five categories of assistance, namely: (a) rental, (b) promotion and development, (c) operation, (d) technical and management matters, and (e) training. The Design Advisory Panel and the Design Admission Panel help the HKSTPC process DIP applications. Up to March 2008, 33 incubatees were admitted.

15. ***Utilisation of rental assistance.*** The estimate that incubatees would receive financial support of up to \$500,000 was based on the assumption that incubatees would occupy up to 1,200 square feet (sq. ft.) office space. Audit noted that as at 31 March 2008, only one of the 33 incubatees occupied an office of 1,200 sq. ft.. The average office size of the other 32 incubatees was about 556 sq. ft., which is far less than the original estimation. *Audit has recommended that the HKSTPC should monitor the office space requirements of incubatees, and consider adjusting the ceilings of the financial support of the five categories under the DIP to better meet the needs of incubatees.*

16. ***Conditional approval cases.*** The HKSTPC's DIP admission guidelines specify that for conditional approval cases, further information from DIP applicants should be sought and reported to the Design Admission Panel. Up to June 2008, there were

six conditional approval cases. There was no documentation showing that supplementary information was submitted to the Design Admission Panel to clarify its concerns. *Audit has recommended that the HKSTPC should ensure that the Design Admission Panel is provided with the necessary supplementary information for conditional approval cases.*

17. ***Milestone targets.*** DIP applicants are required to set milestone targets in their business plans submitted when applying for admission. Audit noted that some milestone targets set were often non-quantitative, which did not facilitate progress assessment or benchmarking. *Audit has recommended that the HKSTPC should issue guidelines to DIP applicants to help them set quantitative milestone targets in their business plans.*

18. ***Documentation of milestone assessment.*** According to the HKSTPC's DIP guidelines, results of milestone assessment should be recorded in a standardised assessment form. An audit examination of 30 milestone assessment forms revealed that in 16 cases, although relevant figures shown in the assessment forms showed that some of the milestone targets were not met, incubatees concerned were still assessed to be making satisfactory progress. *Audit has recommended that the HKSTPC should document the justifications for the judgements made in milestone assessments, particularly in cases where incubatees fail to meet quantitative targets.*

Overseas practices in the promotion of design

19. ***Setting quantitative targets on design promotion.*** The performance targets/indicators adopted by the ITC and the HKDC are mainly output targets. There is a lack of outcome targets/indicators which can help all stakeholders evaluate the effectiveness of the Government's initiatives to promote design in Hong Kong. Audit noted that in some of the countries renowned for their design capability, quantitative outcome targets were set for implementing their national design policies. *Audit has recommended that the Commissioner for Innovation and Technology should consider setting more quantitative outcome targets for measuring the performance and evaluating the effectiveness of the DSI.*

20. ***Good practices adopted to promote design.*** Audit considers that drawing on the experiences of those countries renowned for their design capability could further improve the effectiveness of the Government's efforts for promoting design in Hong Kong. *Audit has recommended that the Commissioner for Innovation and Technology should keep in view overseas developments in the promotion of design, in order to identify good practices for adoption in Hong Kong.*

Response from the Administration, the HKDC and the HKSTPC

21. The Commissioner for Innovation and Technology, the CEO, HKDC, and the CEO, HKSTPC agree with the audit recommendations.

November 2008

Administration of the DesignSmart Initiative

~~work closely with the trades to boost the development of creative industries. It would also consider providing more effective support for Hong Kong's creative industries through integration of resources; and~~

- ~~to implement the above policy initiative, the CEDB should work together with and listen to the views of the relevant trades and industries. The CEDB had commenced work in this respect and was consulting the relevant representatives from the industries on how to take forward the policy initiative. The CEDB aimed to set up the Creative Industry Office on 1 April 2009 and would, at the same time, formulate strategic measures for implementing the government policy on promoting the development of creative industries.~~

65. ~~The Committee further asked about the progress made in developing suitable targets and methods/indicators for measuring the performance and effectiveness of the DSI. The Secretary for Commerce and Economic Development said that the Administration would study the experience of overseas countries in evaluating and reporting the performance of their initiatives to promote design, with a view to developing more suitable outcome targets and indicators on design promotion in Hong Kong.~~

G. Conclusions and recommendations

66. The Committee:

Corporate governance and administration of the Hong Kong Design Centre ("HKDC")

- regrets that the HKDC is yet another government-funded organisation found to have problems and inadequacies in corporate governance that has become the subject of a report by the Director of Audit and has required examination by the Committee in recent years, the others being the English Schools Foundation, Hong Kong Applied Science and Technology Research Institute Company Limited, Hong Kong Tourism Board and Society for the Aid and Rehabilitation of Drug Abusers;
- expresses serious concern and finds it unacceptable that the Board of Directors ("Board"), which is responsible for directing the development and operations of the HKDC and monitoring the performance of the HKDC's management, has not properly discharged its responsibilities, as reflected by the following:

- (a) the attendance rates of some directors, including the Deputy Secretary for Home Affairs as one of the two government directors, at the Board/Committee meetings were low;
 - (b) at three (60%) of the five Finance and Administration Committee ("FAC") meetings held between March 2007 and June 2008, the quorum requirement was not met;
 - (c) the HKDC has adopted a "one-tier reporting system" for its directors to declare and report conflicts of interest, despite the fact that it meets, to a large extent, the criteria for adopting a "two-tier reporting system" set out in the guideline issued by the Home Affairs Bureau;
 - (d) there were weaknesses in the HKDC's internal control and accounting systems, details of which are given in the part on "Management of projects funded by the Design Support Programme ("DSP")" below; and
 - (e) the HKDC has failed to comply with the requirements and guidelines on governance and administration matters set out in its Corporate Governance Manual, for example:
 - (i) for the procurement of goods and services, the guidelines on the number of quotations required and the approval limits stipulated in the Corporate Governance Manual were not followed in some cases;
 - (ii) air tickets were purchased before application for approval was made or written approval was obtained in a number of cases; and
 - (iii) approval for reimbursing the travel expenses incurred by a Board member was given by the Chairman instead of the Board as required by the Corporate Governance Manual in a number of cases;
- expresses serious concern and finds it unacceptable that whilst the two government directors (i.e. the Commissioner for Innovation and Technology and the Deputy Secretary for Home Affairs) on the Board may not carry a heavier weight than the other directors, they have together not been able to discharge the added dimension of their responsibilities as the guardian of the public interest to ensure proper utilisation of the public funds allocated to the HKDC, in so much that problems and inadequacies have been found in the HKDC's corporate governance;

- notes that the Home Affairs Bureau intends to send a representative to sit on the Board in the capacity of an observer instead of a director, and expresses concern as to how the single government director left on the Board can effectively safeguard the public interest in dealing with any problems and inadequacies in the HKDC's corporate governance;
- acknowledges that:
 - (a) the HKDC has put in place an internal audit mechanism to ensure compliance with the requirements and guidelines in the Corporate Governance Manual, and the Government has appointed a professional accountant to the Board who serves as the Chairman of the FAC and will oversee the mechanism;
 - (b) the Board has decided to adopt the two-tier reporting system for declaration of interests by its directors;
 - (c) the Secretary for Commerce and Economic Development has accepted the audit recommendation in paragraph 4.12 of the Director of Audit's Report ("Audit Report"); and
 - (d) the Chief Executive Officer, HKDC has accepted the audit recommendations in paragraphs 4.13, 4.21, 4.26 and 4.34 of the Audit Report;
- urges the HKDC to consider publishing the attendance records of Board/Committee meetings in its annual reports;
- in view of the repeated occurrence of corporate governance problems in government-funded organisations, urges the Administration to attach the utmost importance to ensuring sound corporate governance in such organisations, educate their staff about the importance of achieving sound corporate governance and accountability in using public funds, and consider taking measures, including but not limited to the following, to strengthen their corporate governance by system design:
 - (a) formulating a code of best practice on corporate governance for government-funded organisations for reference by the organisations, and requiring the organisations to produce a report on compliance with the code and publish the same in their annual reports to enhance accountability;

- (b) in selecting individuals for appointment to the governing bodies of government-funded organisations, appointing persons with knowledge and experience in corporate governance who could afford the time to contribute their service;
- (c) providing briefings on corporate governance requirements to members of the governing bodies of government-funded organisations; and
- (d) for small-sized government-funded organisations like the HKDC, which may not have sufficient resources to hire an internal auditor to oversee compliance issues, arranging for the secondment of a government treasury accountant to such organisations to help train up their staff in corporate governance matters, or extending the scope of service provided by the external accountants hired by the organisations to cover compliance matters;

Management of projects funded by the DSP

- expresses great dissatisfaction and disappointment that:
 - (a) the total number of projects which benefited from the DSP (i.e. 200 as at December 2008) was very much lower than that expected (i.e. 700 by June 2009); and
 - (b) the Commissioner for Innovation and Technology, being the Controlling Officer of the DesignSmart Initiative ("DSI") and responsible for administering the DSP, has failed to:
 - (i) strictly enforce the DSP funding guidelines and the DSP funding agreement, as follows:
 - in some cases, the requirements stipulated in the guidelines on conflicts of interest issued by the Innovation and Technology Commission ("ITC") to members of the DSI Assessment Panel were not complied with; and
 - despite the requirement in the DSP funding guidelines issued by the ITC, there were delays in the submission of project completion reports by fund recipients of the DSP; and
 - (ii) review the operation of the DSP periodically as undertaken by the Administration in seeking funding approval for the DSI in June 2004. Of the four DSP funding schemes, the ITC had only completed reviewing the Design Research Scheme and the Design-Business Collaboration Scheme by June 2008 while no

review had been conducted on the Professional Continuing Education Scheme ("PCES") and the General Support Scheme ("GSS"). The failure to review the funding schemes in a timely manner might have led to delays in identifying any areas for improvement that could help optimise the utilisation of some of the funding schemes;

- expresses serious dismay and finds it unacceptable that the HKDC, in managing Project 9707 and the Business of Design Week ("BODW") project, has failed to comply with the DSI Assessment Panel's advice, the DSP funding guidelines and the DSP funding agreement, and to see to the good and proper management of the projects, as follows:
 - (a) there was no documentation to record the basis adopted by the HKDC for shortlisting and selecting the brands and designers to participate in Project 9707;
 - (b) three months after Project 9707 was completed, as at 30 June 2008, only three brands and three designers participating in the project had signed a Memorandum of Understanding ("MOU") with the HKDC, contrary to the HKDC's undertaking in its project proposal that it would sign an MOU with all parties concerned;
 - (c) despite the advice given by the DSI Assessment Panel that brands and designers participating in Project 9707 should pay their own travel and hotel expenses, such expenses were met by the HKDC;
 - (d) notwithstanding the advice given by the DSI Assessment Panel that the HKDC should reduce its reliance on the GSS for funding the BODW project, the HKDC did not develop a long-term financial sustainability plan for the project; and
 - (e) the following errors have occurred in connection with the projects:
 - (i) contrary to the DSP funding agreement, pre-project commencement expenses of about \$173,000 were charged to the Project 9707 account without the ITC's approval;
 - (ii) a sum of \$75,000 incurred for buying tickets to participate in the HKDC Annual Award Gala Dinner was wrongly charged to the Project 9707 account, contrary to the DSP funding guidelines that DSP funding should not be used to meet entertainment expenses; and

- (iii) contrary to the DSP funding guidelines, entertainment expenses were wrongly charged to the BODW project accounts;
- acknowledges that:
- (a) the ITC has introduced the two-tier reporting system for declaration of interests by all DSI Assessment Panel members with effect from 1 January 2009;
 - (b) the DSI Assessment Panel has agreed that the ITC would send a warning letter to a fund recipient of the Design-Business Collaboration Scheme who has not submitted the project completion report over three months after the due date;
 - (c) the ITC will review the PCES and the GSS from the first half of 2009 and, after completing these reviews, conduct an overarching review of the DSP;
 - (d) all the participating brands and designers of Project 9707 have signed the MOUs with the HKDC;
 - (e) the HKDC has appointed a consultant to review the positioning and strategy of the BODW, including making recommendations on the development of a long-term financial plan. The consultant's report would be considered by the Board in early February 2009;
 - (f) the Commissioner for Innovation and Technology has accepted the audit recommendations in paragraphs 2.13, 2.19 and 2.24 of the Audit Report; and
 - (g) the Chief Executive Officer, HKDC has accepted the audit recommendations in paragraphs 2.46 and 2.62 of the Audit Report;
- urges that:
- (a) the Commissioner for Innovation and Technology should:
 - (i) unless for good and justifiable reasons to be fully documented, strictly enforce the requirements in the DSP funding guidelines and the DSP funding agreement; and
 - (ii) review the PCES and the GSS and then the DSP as a whole without delay, with a view to identifying areas for improvement to help optimise the utilisation of the funding schemes; and

- (b) the Chief Executive Officer, HKDC should:
 - (i) unless for good and justifiable reasons to be fully documented, comply with the DSI Assessment Panel's advice, the DSP funding guidelines and the DSP funding agreement, and ensure the good and proper management of the projects funded by the DSP; and
 - (ii) take measures to improve the HKDC's internal control and accounting systems;

Promotion of design by the HKDC

- expresses great dissatisfaction and disappointment that:
 - (a) the implementation of a number of initiatives stated in the HKDC's business plan and annual budget for enhancing the design infrastructure had met with considerable delays;
 - (b) it is unlikely the HKDC will meet the income target of 20% for 2008-2009 set by the ITC; and
 - (c) the amount of unspent balance of the funding approved under the InnoCentre Programme reported by the HKDC had been understated by about \$4.5 million;
- acknowledges that:
 - (a) the ITC has accepted in principle that sponsorship-in-kind could also be taken into account in assessing the expenditure/revenue ratio of the HKDC;
 - (b) in June 2008, the ITC deducted \$4.5 million from the disbursement to the HKDC for 2008-2009 and, in future, the ITC will verify reported unspent balance against other independent sources such as bank balance statements and audited accounts at each quarterly disbursement;
 - (c) the Commissioner for Innovation and Technology has accepted the audit recommendations in paragraphs 3.16 and 3.29 of the Audit Report; and
 - (d) the Chief Executive Officer, HKDC has accepted the audit recommendations in paragraphs 3.11, 3.17, and 3.30 of the Audit Report;
- urges the Commissioner for Innovation and Technology and the Chief Executive Officer, HKDC to expeditiously implement the above audit recommendations;

Administration of the Design Incubation Programme ("DIP")

- expresses serious dismay and finds it unacceptable that:
 - (a) in some cases, disbursement of financial assistance was not made in accordance with the Memorandum of Administrative Arrangements for the DIP and the guidelines issued by the Hong Kong Science and Technology Parks Corporation ("HKSTPC"); and
 - (b) supporting documents submitted by incubatees in making claims for reimbursement of expenses under the DIP were often inadequate;
- expresses dissatisfaction that:
 - (a) no records were kept to show that due diligence visits had been carried out by the HKSTPC to verify information provided by DIP applicants;
 - (b) there was no documentation showing that the HKSTPC had submitted supplementary information to the Design Admission Panel to clarify its concerns in conditional approval cases;
 - (c) the milestone targets set by incubatees in their applications were often non-quantitative, which did not facilitate progress assessment or benchmarking; and
 - (d) documentation of milestone assessments was not always kept;
- acknowledges that:
 - (a) the HKSTPC will:
 - (i) revise the due diligence evaluation report format to capture the name of interviewers/interviewees and the date/time/venue of interview; and
 - (ii) modify the milestone assessment form to enable the assessor to fill in justifications for the judgments made, and to include a checklist on supporting documents to be reviewed; and
 - (b) the Chief Executive Officer, HKSTPC has accepted the audit recommendations in paragraphs 5.14, 5.25, 5.38 and 5.42 of the Audit Report;

- urges the Chief Executive Officer, HKSTPC to ensure compliance with the Memorandum of Administrative Arrangements for the DIP and the HKSTPC's guidelines, and expeditiously implement the above audit recommendations;

Overseas practices in the promotion of design

- notes that the Government has devoted a large amount of money to promoting design in Hong Kong over the past five years, i.e. 250 million for launching the DSI in June 2004 and another \$100 million to the HKDC in May 2007 to enhance its roles in promoting design;
- expresses serious concern that there is a lack of outcome targets/indicators to evaluate the effectiveness of the Government's initiatives to promote design in Hong Kong;
- acknowledges that:
 - (a) the Commerce and Economic Development Bureau aims to set up a dedicated Creative Industry Office with integrated and realigned resources from related departments on 1 April 2009. The Office will co-ordinate the work of different departments and work closely with the trades to boost the development of creative industries; and
 - (b) the Commissioner for Innovation and Technology has accepted the audit recommendations in paragraph 6.11 of the Audit Report;
- strongly urges the Secretary for Commerce and Economic Development to expeditiously issue a policy paper to set out the Government's vision and policy for promoting the development of creative industries, including design, and engage various stakeholders and the public in its policy direction; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the HKDC's decision regarding publishing the attendance records of Board/Committee meetings in its annual reports;
 - (b) the Administration's decision regarding the measures proposed by the Committee to strengthen corporate governance in government-funded organisations by system design;
 - (c) the progress of the ITC's reviews of the PCES, the GSS and the DSP;

- (d) the measures taken by the Chief Executive Officer, HKDC to improve the HKDC's internal control and accounting systems;
- (e) the progress made by the Administration in issuing a policy paper on the development of creative industries, including design; and
- (f) the progress made in implementing the various audit recommendations.

Appendix IV

Committee	Paper	LC Paper No.
Panel on Commerce and Industry on 17 April 2007	Administration's paper : "Funding Support for Hong Kong Design Centre" Minutes of meeting	CB(1)1319/06-07(03) CB(1)1644/06-07
Finance Committee on 25 May 2007	Administration's paper : HEAD 155 – GOVERNMENT SECRETARIAT : INNOVATION AND TECHNOLOGY COMMISSION Subhead 700 General non-recurrent New Item "Hong Kong Design Centre" Minutes of meeting	FCR(2007-08)14 FC124/06-07
Panel on Commerce and Industry on 15 April 2008	Administration's paper : "Report on Hong Kong Design Centre's activities from July 2007 to March 2008" Minutes of meeting	CB(1)1211/07-08(05) CB(1)1534/07-08
Public Accounts Committee	Chapter 1 of Part 8 of the Public Accounts Committee's Report No. 51 on the Administration of the DesignSmart Initiative Summary on the Administration of the DesignSmart Initiative from the Director of Audit's Report on the results of value for money audits (Report No. 51)	http://www.legco.gov.hk/yr08-09/english/pac/reports/51/m_8a.pdf http://www.aud.gov.hk/pdf_e/e51ch02sum.pdf