

CHAPTER 2

**Innovation and Technology Commission
Hong Kong Design Centre**

Administration of the DesignSmart Initiative

**Audit Commission
Hong Kong
23 October 2008**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

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ADMINISTRATION OF THE DESIGNSMART INITIATIVE

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PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 It is the Government's policy to promote design and innovation to enhance the competitiveness of products and services of Hong Kong. The objective is to promote industry understanding of the importance of design and innovation as a means to enhance competitiveness, and to integrate them into business and industrial processes. The Government envisages that, through such efforts, Hong Kong industries will move up the value chain by switching the production mode from "original equipment manufacturing" to "original design manufacturing" and "original brand manufacturing".

The DesignSmart Initiative

1.3 In June 2004, in order to strengthen support for design and innovation, the Government launched the DesignSmart Initiative (DSI) with a funding commitment of \$250 million. The DSI comprised the following two programmes:

- (a) ***Design Support Programme (DSP)***. Under the DSP, \$180 million was set aside for financing projects in four categories:
 - (i) design research;
 - (ii) design-business collaboration;
 - (iii) design professional continuing education; and
 - (iv) general support activities.
- (b) ***InnoCentre Programme***. Under the Programme, \$70 million was set aside for setting up a one-stop-shop for creating and sustaining a design cluster. The funding was allocated as follows:
 - (i) ***Hong Kong Design Centre (HKDC)***. Under the InnoCentre Programme, \$45 million was allocated to the HKDC for supporting its operation on a time-limited basis; and

- (ii) *Design Incubation Programme (DIP)*. Under the InnoCentre Programme, \$25 million was allocated to the Hong Kong Science and Technology Parks Corporation (HKSTPC) for running an incubation programme for design.

1.4 The Tech Centre of the HKSTPC in Kowloon Tong was renamed the InnoCentre (Photograph 1) to serve as a one-stop-shop for the provision of the following services:

- (a) incubation services (Note 1) for design ventures;
- (b) professional education and training;
- (c) design-related exhibition, seminars and workshops;
- (d) design-related resources centre, such as design library; and
- (e) events and activities for networking among design professionals and user industries.

Note 1: *Incubation services refer to the provision of support services (e.g. management training, customised marketing services, business matching, business advisory services, networking services, and professional services such as legal and financial advice), as well as the provision of office accommodation at affordable rent rendered to start-up companies in their initial stage of development for operation and growth.*

Photograph 1

The InnoCentre



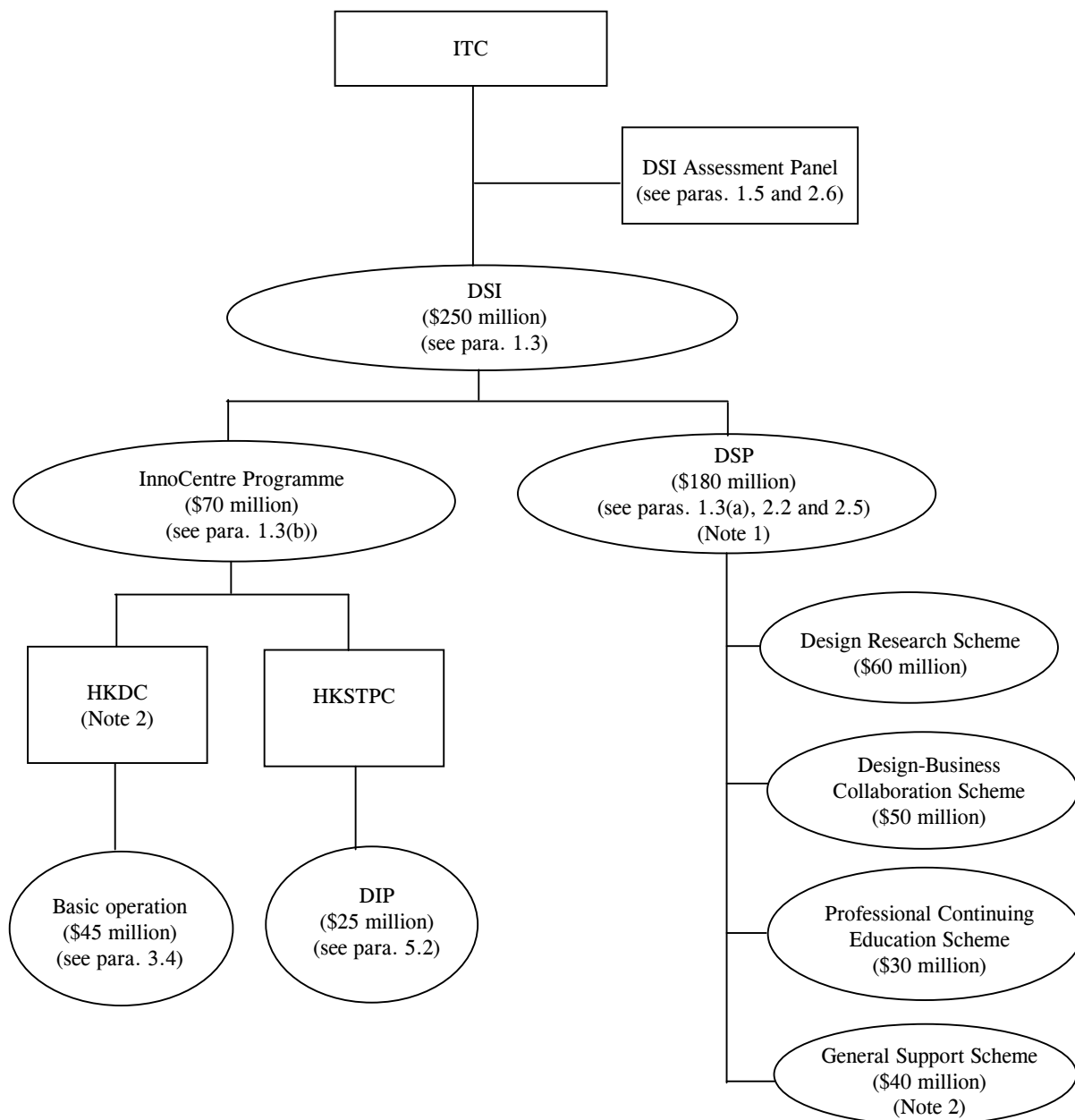
Source: HKDC records

1.5 The Innovation and Technology Commission (ITC) is responsible for managing the DSI. An assessment panel (see para. 2.6) was set up to assist the ITC in the monitoring and review of the DSI.

1.6 Up to 30 June 2008, 169 projects with a total funding support of \$104 million had been approved under the DSP, and 37 design start-ups had been admitted as incubatees under the DIP. Figure 1 shows the relationship between various programmes of the DSI and the parties concerned.

Figure 1

Relationship between various programmes of the DSI and the parties concerned



Source: Audit analysis of ITC records

Note 1: In March 2007, the ITC increased the funding to the DSP by \$14 million to \$194 million (see Table 2 in para. 2.5).

Note 2: Apart from DSI funding, the HKDC also received other government funding support. As at 30 June 2008, the total funding committed to the HKDC amounted to \$225 million (see Table 7 in para. 3.6).

Audit review

1.7 The Audit Commission (Audit) has recently conducted a review to examine the economy, efficiency and effectiveness of the administration of the DSI managed by the ITC. The review has focused on the following areas:

- (a) management of projects funded by the DSP (PART 2);
- (b) promotion of design by the HKDC (PART 3);
- (c) corporate governance and administration of the HKDC (PART 4);
- (d) administration of the DIP (PART 5); and
- (e) overseas practices in the promotion of design (PART 6).

General response from the Administration, the Hong Kong Design Centre and the Hong Kong Science and Technology Parks Corporation

1.8 The **Commissioner for Innovation and Technology** welcomes the value for money audit on the Administration of the DesignSmart Initiative. He has said that he generally agrees with the audit observations and recommendations and will work closely with the HKDC and the HKSTPC to ensure the implementation of improvement measures as appropriate.

1.9 The **Chief Executive Officer (CEO), HKDC** has said that the HKDC generally accepts the points made by Audit and will step up its internal financial control and audit functions to ensure that the irregularities identified will not recur in future. He has also said that:

- (a) the HKDC is seven years of age and, in comparison with similar institutions around the world, is a young organisation still probing its way to strive for facilitating the development of the design industries in Hong Kong. A review and audit at this point of its development is timely as it provides the necessary and useful feedback based on which the HKDC could improve its administration and management to achieve a higher degree of governance; and
- (b) the nature of the design industries is fast paced and forever evolving. To operate effectively in this unique environment, the HKDC, as an organisation funded mainly by the Government, must maintain proper checks and balance while ensuring that the bureaucracy does not inundate it to non-action. This precarious balancing act is a constant challenge for the HKDC.

1.10 The **CEO, HKSTPC** agrees with all the audit recommendations.

Acknowledgement

1.11 Audit would like to acknowledge with gratitude the full cooperation of the staff of the ITC, the HKDC and the HKSTPC during the course of the audit review.

PART 2: MANAGEMENT OF PROJECTS FUNDED BY THE DESIGN SUPPORT PROGRAMME

2.1 This PART examines the management of projects funded by the DSP, and notes that certain aspects of project management need to be strengthened.

Design Support Programme

2.2 When the DSI was launched in 2004, a sum of \$180 million was set aside for the DSP to finance design-related projects under the following four funding schemes:

- (a) ***Design Research Scheme (DRS)***. The DRS aims at supporting research-based activities in design or branding-related areas, with a view to providing a platform for attaining greater awareness and knowledge critical to the effective utilisation and deployment of design in mainstream industrial or business processes;
- (b) ***Design-Business Collaboration Scheme (DBCS)***. The DBCS aims at promoting the interest and investment of small-and-medium-sized enterprises (SMEs) in relation to utilising design and transforming design activities into tradable deliverables that manifest exploitation and deployment of intellectual property rights;
- (c) ***Professional Continuing Education Scheme (PCES)***. The PCES caters for the development of new professional continuing training courses that contribute to design capability building and nurturing of talents as well as appreciation and understanding of design by industry; and
- (d) ***General Support Scheme (GSS)***. The GSS caters for projects that contribute to fostering culture, greater appreciation and adoption of design, and honouring excellence in design in Hong Kong, including the organisation of conferences, seminars, exhibitions, roadshows, competitions and awards.

Number of projects approved

2.3 In June 2004, in seeking funding approval for the DSI, the Administration informed the Finance Committee of the Legislative Council that the four DSP funding schemes would benefit about 700 projects over five years. However, up to 30 June 2008 (i.e. four years after launching the DSI), only 169 projects (24% of 700 projects) were approved under the DSP (see Table 1).

Table 1

**Number of projects approved under the four DSP funding schemes
(up to 30 June 2008)**

	Number of projects		Progress (c) = (b)/(a) × 100%
	to be funded by June 2009 (a)	approved up to June 2008 (b)	
DRS	20	2	10%
DBCS	625	138	22%
PCES	35	9	26%
GSS	20	20	100%
Total	700	169	24%

Source: ITC records

Funding allocation of the four DSP funding schemes

2.4 As the Controlling Officer of the DSI, the Commissioner for Innovation and Technology is responsible for administering the DSP. The Commissioner has the authority to adjust the amounts allocated for the DSP (\$180 million) and the InnoCentre Programme (\$70 million), provided that the adjustment is within the \$250 million approved for the DSI, and that the scope of appropriation remains within the ambit approved for the DSI and is not varied by 25% or more.

2.5 In March 2007, about 96% of the \$40 million originally allocated to the GSS had been used up. The ITC increased the funding to the GSS by \$42 million to \$82 million, by transferring \$28 million from the other three DSP funding schemes and \$14 million from the \$45 million (see para. 1.3(b)(i)) funding originally earmarked for the HKDC under the InnoCentre Programme. Table 2 shows the funding allocation changes and utilisation of the DSP funding schemes as at 30 June 2008.

Table 2
Funding allocation changes and utilisation of the DSP funding schemes
(30 June 2008)

Scheme	Original allocation (\$ million)	Increase/ (Decrease) (\$ million)	Revised allocation (a) (\$ million)	Project funding approved (b) (\$ million)	Utilisation rate (Note 1) (c) = (b)/(a) × 100% (%)
DRS	60	(12)	48	6.5	13.5%
DBCS	50	(10)	40	12.6	31.5%
PCES	30	(6)	24	10.0	41.7%
GSS	40	42 (Note 2)	82	74.6	91.0%
Total	180	14	194	103.7	53.5%

Source: ITC records

Note 1: The utilisation rate is calculated based on the revised funding allocation.

Note 2: Of the \$42 million transferred to the GSS in March 2007, \$14 million came from the funding originally earmarked for the HKDC.

The DesignSmart Initiative Assessment Panel

2.6 The DSI Assessment Panel was established in September 2004 for assisting the ITC to assess applications and monitor progress of projects under the DSP. The Panel, chaired by the Commissioner for Innovation and Technology, comprises officials, professionals, industrialists, designers, businessmen and academics. Since its establishment, there have been three terms of office; 36 Panel members were appointed for the first term, 53 for the second term and 36 for the current term.

Audit observations and recommendations

Selection of members to attend DSI Assessment Panel meetings

2.7 Audit's examination of the records of 27 DSI Assessment Panel meetings held from October 2004 to June 2008 revealed that the number of Panel members attending these meetings varied (see Table 3), and that no quorum was set for the Panel meetings. In response to Audit's enquiry, the ITC explained in September 2008 that though not formally agreed upon and announced, there was in practice a quorum of four for DSI Assessment Panel meetings.

Table 3

**Analysis of number of members attending DSI Assessment Panel meetings
(October 2004 to June 2008)**

	Number of members attending the meeting				Total
	Five to Six	Seven to Eight	Nine to Ten	More than Ten (Note)	
Number of meetings	7	7	11	2	27

Source: ITC records

Note: Two special panel meetings were held on 27 March and 18 June 2008 to examine the results of the DBCS and DRS reviews carried out by the ITC (see para. 2.22). The meetings were attended by 26 and 21 Panel members respectively.

2.8 Audit could not find any documentation recording the justifications and the process adopted by the ITC in deciding the number of members to attend Panel meetings and in selecting the Panel members to be invited. Upon enquiry, the ITC explained to Audit that the selection of members to attend Panel meetings was made through discussion at internal pre-meetings with the Commissioner for Innovation and Technology. The general principle adopted was to draw up for each panel meeting a fair representation from the academia, industry, design sector and industry support organisations.

2.9 Audit considers that, to enhance transparency and accountability, proper documentation should be kept to record the basis and justification for selecting members to attend Panel meetings.

Management of conflicts of interest

2.10 The ITC issued a set of guidelines to Panel members on the declaration of conflicts of interest when they attended Panel meetings. These guidelines require a member to declare his interests, if he is:

- (a) a member of the project team of an application; or
- (b) an office bearer or a paid staff of the applicant organisation, a collaborating organisation, or a sponsoring organisation.

The guidelines also require a member to refrain from participating in the discussion of the application in which he has declared an interest.

2.11 An audit examination of the records of 27 Panel meetings held from October 2004 to June 2008 showed that in 20 (74%) meetings, declarations of conflicts of interest were made. However, contrary to the above-mentioned guidelines, in 17 (63%) meetings the members concerned were allowed to participate in the discussion of applications in which they had declared an interest. In 12 (44%) meetings, these members were even allowed to vote in the approval of the applications concerned.

2.12 Audit considers it important that any perceived or actual conflicts of interest should be avoided. The ITC needs to ensure that the requirements stipulated in the guidelines on conflicts of interest are complied with.

Audit recommendations

2.13 **Audit has recommended that the Commissioner for Innovation and Technology should:**

- (a) **consider setting a quorum for Panel meetings;**
- (b) **keep proper documentation on the basis and justification for selecting members to attend Panel meetings; and**
- (c) **ensure that the Panel's guidelines on conflicts of interest are complied with.**

Response from the Administration

2.14 The **Commissioner for Innovation and Technology** accepts the audit recommendations. He has said that the ITC will:

- (a) formally set a quorum for Panel meetings;
- (b) keep proper documentation on the basis and justifications for selecting members; and
- (c) ensure that the Panel's guidelines on conflicts of interest are complied with. He has also said that:
 - (i) Panel members are prominent people selected from related fields. There is a high chance for them to be related in one way or another to an applicant organisation, e.g. being a HKDC director, a member of an applicant industry organisation, or a council member or teaching staff of an applicant university; and
 - (ii) of the 12 cases, where members with declared conflicts of interest were allowed to vote, the recommendations of the Panel were arrived at through consensus or by majority view. Voting as such had not occurred at the meetings. The notion that members were "allowed to vote" might be due to the fact that sometimes it was explicitly recorded in the notes of meeting that the Chairman did not allow members with conflicts of interest to vote and sometimes it was not so recorded.

Project evaluation

2.15 The DSP funding guidelines issued by the ITC require that fund recipients should submit a project completion report to the ITC within two months after the project is completed. Project information (e.g. achievements and performance of the project) is required to be included in the completion report, providing useful information to the ITC for project evaluation.

Audit observations and recommendations

Submission of project completion reports

2.16 Audit conducted a review of the ITC's records of project completion reports and found that, by the end of June 2008:

- (a) of the 148 project completion reports that were due for submission by the fund recipients, 129 (87%) reports were received by the ITC. The submission of the

remaining 19 (13%) reports had been overdue for a period ranging from less than a month to about eight months; and

- (b) of the 129 project completion reports received by the ITC, 83 (64%) were submitted on time. The remaining 46 (36%) reports were submitted late. On average, the delay was about 58 days, and the worst case was late for 342 days.

Post-project evaluation questionnaire

2.17 According to the DSP funding guidelines, the ITC may require a fund recipient to complete a post-project evaluation questionnaire to report on the efforts in publicising the project and to provide quantitative measurement on the industry's adoption of project achievements. Audit noted that:

- (a) up to July 2008, only fund recipients (18 in total) of the DBCS were asked to complete a post-project evaluation questionnaire. The ITC had not requested the fund recipients of other DSP funding schemes to complete the post-project evaluation questionnaires; and
- (b) of the 18 recipients of DBCS funding, 3 (17%) had not responded as requested.

2.18 As useful information would be provided by the questionnaires for the evaluation of DSP projects, the ITC should request fund recipients of all DSP funding schemes to complete and return a post-project evaluation questionnaire.

Audit recommendations

2.19 **Audit has recommended that the Commissioner for Innovation and Technology should:**

- (a) **ensure that project completion reports are submitted in a timely manner; and**
- (b) **consider requiring the fund recipients of all DSP funding schemes to complete and return a post-project evaluation questionnaire.**

Response from the Administration

2.20 The **Commissioner for Innovation and Technology** accepts the audit recommendations. He has said that:

- (a) at the Panel meeting held in July 2008, the Panel agreed that a warning letter should be sent to a DBCS fund recipient who had not submitted the report over three months after the due date;
- (b) currently, completing a post-project questionnaire is not a mandatory requirement but a fund recipient has an obligation to complete a questionnaire whenever so required by the ITC. The ITC will consider requiring fund recipients of all DSP funding schemes to complete and return post-project questionnaires;
- (c) DBCS fund recipients are reminded by e-mail alerts for the submission of project completion reports. The first e-mail alert is sent to the fund recipient one month in advance before the due date. The second e-mail alert will be sent to the recipient if the report has not been submitted after the seventh day from the due date. E-mail alert will be sent every seven days until the recipient has submitted the report; and
- (d) the ITC will revise the format of the DBCS completion report to ask the SMEs to provide more information on commercialisation and intellectual property rights generated pertaining to their projects. This would provide more information for assessing the effectiveness of the scheme.

Review of the Design Support Programme

2.21 In seeking funding approval for the DSI in June 2004, the Administration informed the Finance Committee of the Legislative Council that the Administration intended to review periodically the operation of the DSP.

2.22 Audit noted that since launching the DSI in 2004, the ITC had conducted the following two reviews on the DSP:

- (a) ***Review of the DBCS.*** In the third quarter of 2007, a detailed review of the DBCS was conducted. Following the review, the rules were revised to allow design companies and SMEs to become DBCS project co-applicants and SME applicants would be eligible for a maximum grant of \$100,000 for four projects at most; and

- (b) **Review of the DRS.** In June 2008, the ITC completed a review of the operation of the DRS. As a result of the review, the theme approach was abolished and a new approach was adopted for soliciting DRS project applications. Under the new approach, DRS applications with any themes would be accepted throughout the year. It was expected that the new approach would encourage more DRS applications.

Audit observations and recommendations

2.23 It is a good practice to review periodically the operation of the DSP funding schemes. Audit noted that the ITC had conducted reviews on the DRS and the DBCS as mentioned above. Similar reviews on the PCES and the GSS had yet to be conducted. Audit considers that both the PCES and the GSS need to be reviewed to see if the two schemes require any refinements, especially the GSS which received most of the funding approved under the DSP (i.e. about \$74.6 million or 72% of \$103.7 million, as at 30 June 2008). As the total number of projects which benefited from the DSP (169 as at June 2008) was very much lower than that expected (i.e. 700 by June 2009 — see para. 2.3), the ITC also needs to conduct an overarching review of the DSP to ascertain if any revisions are required.

Audit recommendations

2.24 **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.**

Response from the Administration

2.25 The **Commissioner for Innovation and Technology** accepts the audit recommendations. He has said that the ITC:

- (a) originally planned to conduct review on all the four schemes and the DSP as a whole. However, due to the heavy workload and limited staffing resources, the ITC can only work on it phase by phase. The reviews on the DBCS and the DRS have just been completed;

- (b) is working on the implementation of the new procedures and arrangements of the DBCS and the DRS. It will review the PCES and the GSS afterwards, tentatively from the first half of 2009; and
- (c) will conduct the overarching review of the DSP after the reviews on all the four schemes have been completed.

General Support Scheme projects undertaken by the Hong Kong Design Centre

2.26 Audit noted that up to June 2008, of the \$104 million DSP project funding approved, \$67 million (64%) were approved to support the GSS projects initiated by the HKDC. Audit selected for examination the operation of three GSS projects undertaken by the HKDC, namely Project 9707, the Business of Design Week (BODW) 2006, and the BODW 2007.

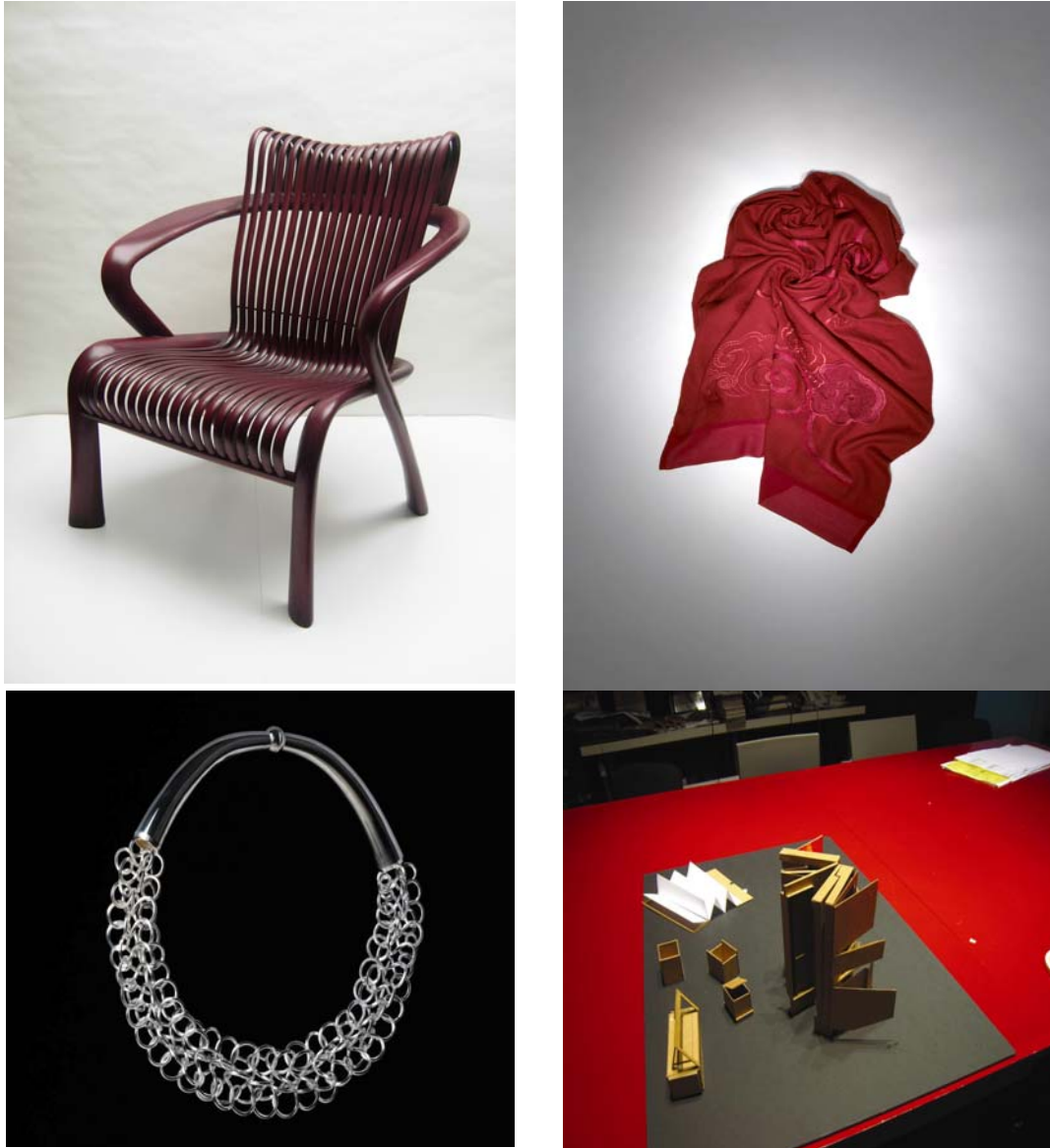
Project 9707

2.27 Project 9707 was a project initiated to commemorate the 10th anniversary of Hong Kong's return to China. It aimed to honour the achievements and excellence of the Hong Kong design industry in the period 1997 to 2007. The GSS provided funding of \$3.9 million to the project.

2.28 As part of Project 9707, ten international brands and ten Hong Kong designers were invited to produce ten collaborative creative products (Photograph 2). These products were exhibited in Hong Kong and the Mainland, and were sold in limited quantity.

Photograph 2

Examples of the ten creative products produced for Project 9707



Source: HKDC records

2.29 Audit's examination of the records of Project 9707 found that there was room for improvement in the following areas:

- (a) selection of participating brands and designers (paras. 2.30 and 2.31);
- (b) signing of Memorandum of Understanding (MOU) with brands and designers (paras. 2.32 to 2.34);

- (c) meeting the travel expenses of brands and designers (paras. 2.35 to 2.39);
- (d) project commencement before formal approval was given by the ITC (paras. 2.40 to 2.42); and
- (e) use of DSP funding to meet entertainment expenses (paras. 2.43 to 2.45).

Audit observations and recommendations

Selection of participating brands and designers

2.30 Audit could not find any documentation recording the basis adopted by the HKDC for shortlisting and selecting the brands and designers for the production of the ten creative products for Project 9707. In response to Audit's enquiry, the HKDC explained in September 2008 that:

- (a) the brands comprised both international brands as well as Hong Kong brands attaining international status. They were all world renowned with a strong emphasis on good design and craftsmanship. These brands established good rapport with the HKDC through their participation in previous HKDC's projects;
- (b) the ten creative products cut across a wide range of high-end and mass-appeal products from jewellery, hi-fi, furniture, fashion accessories to household appliances, targeting at different age groups and price ranges of the consumer market;
- (c) the designers were selected by the brands from a shortlist of 25 designers suggested by the HKDC based on their strong records of international achievements and proven ability to convey the strengths of Hong Kong design to global audience; and
- (d) in selecting their designers, the brands would take into account the compatibility of the designers' style with the brands' culture and essence, as well as previous collaboration experience (if any). Furthermore, some brands had always been interested in commissioning certain designers.

2.31 Audit noted that the creative products produced by the brands and designers in Project 9707 were displayed in various exhibitions and shows. This provided an exposure opportunity to help the brands and designers promote their business/service, resulting in real or intangible benefits to the brands/designers. Given that the project was funded by public money, it is important to ensure that the selection of brands and designers was conducted, and seen to be conducted, in a fair and open manner. Therefore, the HKDC needs to keep proper documentation on the shortlisting, selection and approval processes.

Signing of MOU with brands and designers

2.32 In the project proposal submitted for Project 9707, the HKDC stated that it would sign an MOU with the participating brands and designers. Among other things, the MOU specified the rights and obligations of the parties concerned. For example, the brands would be responsible for all costs and expenses in respect of the production and sales of the products, and the designers would have to warrant that the designs were their original work and they possessed complete copyrights. Any consequence of copyright infringement would be the personal responsibility of the designers, who should indemnify the HKDC and the brand for any loss or damage arising from the infringement.

2.33 However, up to 30 June 2008 (i.e. three months after Project 9707 was completed), only three brands and three designers had signed such an MOU. To ensure that the HKDC is protected from loss or damage as a consequence of copyright infringement, the HKDC needs to ensure that all parties concerned would sign the MOU as early as possible.

2.34 In response to Audit's enquiry, the HKDC informed Audit in September 2008 that the participating brands and designers of Project 9707 were very supportive of the HKDC's efforts and, short of signing the MOU, general agreement was secured in all cases. The signing of the MOU was held up in some cases because of the delay in the agreement between the brand and the designer on the number of units of the product to be made for public sale.

Meeting the travel expenses of brands and designers

2.35 A major event of the Project 9707 was to show the ten creative products at an exhibition held in Beijing to demonstrate the design talents of Hong Kong. Audit noted that the HKDC originally included in the project proposal for Project 9707 a budget for the travel expenses of brands and designers participating in the project.

2.36 In assessing the project proposal of Project 9707, the DSI Assessment Panel commented that as the brands and designers involved would get good exposure to promote their business/service, they should pay their own travel and accommodation costs as part of their business promotional activities. Therefore, funding from the GSS should not be used to cover such travel expenses.

2.37 Notwithstanding the comment from the DSI Assessment Panel, the travel expenses of the participating brands and designers of about \$600,000 were met by the HKDC, from funds obtained by auctioning nine of the ten creative products at a fund-raising auction held in December 2007. The fund-raising auction was another major event of Project 9707.

2.38 Audit notes that applying the funds raised to meet the travel expenses of the participating brands and designers is at variance with the DSI Assessment Panel's advice that such expenses should be paid by the brands and designers themselves.

2.39 In response to Audit's enquiry, the HKDC commented in September 2008 that:

- (a) the funds raised were not meant to offset the approved project cost;
- (b) the HKDC noted the views of the DSI Assessment Panel (see para. 2.36), but considered that the participation of the brands and designers had actually created multi-win for all concerned;
- (c) the participation of brands and designers in the exhibitions/symposiums in Beijing and Hong Kong in December 2007 was critical in promoting Hong Kong's design industry and to develop international frontiers for the design profession;
- (d) it was fair to use part of the auction proceeds to offset the travel and hotel expenses incurred by staff of the brands and designers, particularly as the designers had contributed their time and service free of charge, and the brands had made substantial investments in the research, prototyping and manufacturing of the products;
- (e) indeed, some designers and brands had indicated in response to informal enquiries that they would not participate in the Beijing and Hong Kong events if they had to pay their own travel and hotel expenses; and
- (f) as no government funding was involved, the ITC confirmed that it saw no objection to the arrangement. The donors concerned had also re-affirmed their understanding of the specific usage of the funds.

Project commencement before formal approval was given by the ITC

2.40 According to the DSP funding agreement:

- (a) the recipient shall apply the funds exclusively for the purpose of the project at such time and in such manner as specified in the budget set out in the project proposal;
- (b) unless otherwise agreed by the ITC, the recipient shall not incur any expenditure prior to the commencement date or after the completion date; and
- (c) the recipient shall account for and make good any payments or expenditure made in contravention of the above provisions.

2.41 Project 9707 was approved for commencement in June 2007. However, Audit found that expenses had already been incurred for the Project before June 2007. The total pre-project commencement expenses charged to the Project 9707 account were about \$173,000. In accordance with the DSP funding agreement, such pre-project commencement expenses should not be charged to the DSP project account, as no ITC approval had been obtained.

2.42 In response to Audit's enquiry, the HKDC explained in September 2008 that a great deal of research and preparatory work was required before the project proposals could be finalised and submitted to the DSI Assessment Panel for approval. Owing to an oversight, the expenses incurred for such purposes, involving mainly airfare and hotel accommodation costs for the HKDC's staff to travel to meet and discuss with the brands and designers, had erroneously been charged to the project vote. The mistake was subsequently rectified.

Use of DSP funding to meet entertainment expenses

2.43 Audit also noted that a sum of \$75,000 was charged to the Project 9707 account for "publications and promotional kits". However, further audit examination of the HKDC's records revealed that the amount was actually incurred for buying 60 tickets to participate in the HKDC Annual Award Gala Dinner.

2.44 Audit notes that it is explicitly stated in the DSP funding guidelines that DSP project funding should not be used to meet entertainment expenses. It is therefore questionable that expenses on buying tickets of the Gala Dinner could be charged to the DSP project account.

2.45 In response to Audit's enquiry, the HKDC informed Audit in September 2008 that the expenditure in question was incurred mainly to pay for the tickets for the brand representatives and designers attending the HKDC Annual Award Gala Dinner. As these people participated as supporters and speakers in the Project 9707 symposium, it was considered justified to invite them as guests for the dinner. Owing to an oversight, the expenses incurred were erroneously charged to the project vote. The mistake was subsequently rectified.

Audit recommendations

2.46 **Audit has recommended that the HKDC should:**

- (a) **keep proper documentation on the shortlisting and selection of participants for projects funded by the DSP in future;**
- (b) **ensure that all the participating brands and designers of Project 9707 sign an MOU with the HKDC as early as possible;**
- (c) **follow the advice given by the DSI Assessment Panel as far as possible. In cases where there are difficulties in following the advice strictly, approval from the ITC should be sought;**
- (d) **ensure that the ITC's approval is obtained if expenditure needs to be incurred before commencement of a DSP project; and**
- (e) **ensure that DSP project funding is not used to meet entertainment expenses in future.**

Response from the Hong Kong Design Centre

2.47 The CEO, HKDC accepts the audit recommendations. He has said that the HKDC will:

- (a) keep proper documentation on the shortlisting and selection of participants for projects funded by the DSP in future. The shortlisting and selection of the brands and designers involved in Project 9707 were steered by the Chairman and the Vice-chairman of the Board of Directors (Board), in consultation with the design community. The DSI Assessment Panel was also briefed. It is unfortunate that no proper documentation was kept of these processes to show that they were conducted in a fair and open manner;
- (b) finalise signing the MOUs before end of September 2008;

- (c) seek the ITC's approval in future where there are difficulties in following the advice of the DSI Assessment Panel;
- (d) obtain the ITC's approval if expenditure needs to be incurred before commencement of a DSP project; and
- (e) tighten up control procedures to ensure that DSP project funding is not used to meet entertainment expenses.

Business of Design Week 2006 and 2007

2.48 The BODW is the annual flagship event of the HKDC. The first BODW was organised in 2002. The BODW is a combination of concurrent conferences, exhibitions, awards and outreach programmes. It focuses on the relationship between business and design, and provides an international platform for designers, experts and entrepreneurs to network and share ideas. The total project expenditure of BODW 2006 and BODW 2007 was \$14.5 million and \$16.9 million respectively. Audit examined the records of these two events and found that there was room for improvement in a number of areas.

Audit observations and recommendations

Long-term financial sustainability

2.49 Records of the DSI Assessment Panel meetings showed that the Panel had been urging the HKDC to develop a long-term financial sustainability plan for the BODW and to reduce its reliance on the GSS funding support. Audit noted that while project income (including sponsorship income) of the BODW was increasing over the last few years, it still constituted less than half of the project expenditure, and funding support sought from the GSS remained at about the same level, as shown in Table 4. As at August 2008, the HKDC had yet to develop a long-term financial sustainability plan with a timetable for achieving self-sufficiency.

Table 4
Project income/expenditure and GSS funding for the BODW
(2004 to 2008)

BODW	Project income (a) (\$ million)	GSS funding support (b) (\$ million)	Project expenditure (c) (\$ million)	Percentage (d) = (a)/(c) × 100%
2004	4.6	10.0	14.6	32%
2005 (Note)	5.6	9.1	16.9	33%
2006	6.1	8.4	14.5	42%
2007	8.0	8.9	16.9	47%
2008 (Projected)	8.4	9.7	18.1	46%
Total	32.7	46.1	81.0	40%

Source: HKDC records

Note: There was a deficit of \$2.2 million in the BODW 2005, which was absorbed by the HKDC.

Repeated renewal of contracts for three BODW staff

2.50 According to the HKDC's Corporate Governance Manual, the CEO may employ contract staff for not more than six months. An examination of the payroll records of the BODW 2006 and BODW 2007 revealed that the contracts of three BODW project staff had been renewed repeatedly (see Table 5).

Table 5

Repeated renewal of contracts for three BODW project staff

Case	Position	First contract commencement date (a)	Last contract expiry date (b)	Duration of employment with the HKDC (c) = (b) - (a) (months)
1	Project Executive	9 July 2007	31 May 2008	11
2	Project Executive	1 June 2007	31 December 2008	19
3	Senior Project Executive	21 June 2006	31 May 2008	23

Source: HKDC records

2.51 As shown in Table 5, the repeated renewal of contracts for these three BODW project staff had the effect of continuously employing them for a period considerably exceeding the six-month threshold. Audit considers it advisable that the CEO should seek the advice of the Board in future cases, before renewing the contracts of the project staff.

2.52 In response to Audit's enquiry, the HKDC commented in September 2008 that staff recruited for the BODW project were normally offered fixed-term contracts for less than 12 months up to November/December when the event (i.e. BODW) took place. However, as a matter of practice, a few of the best performers were offered renewal of contracts to take care of the post-event administrative work. To ensure work continuity and knowledge retention/transfer, some of them were also offered a contract to work for the same project for the following year. The cases quoted by Audit fell within these categories. The HKDC accepted that the Board's advice should have been sought.

ITC's approval for making salary adjustment for BODW staff

2.53 According to the DSP funding guidelines, the ITC's approval is needed if the DSP project funding is used to cover annual salary increments, except for cost-of-living adjustments at a rate comparable with and applicable to the civil service. Audit's examination of the payroll of the BODW 2007 project revealed that in one case, the salary of DSP project staff was adjusted without obtaining the ITC's prior approval, as shown below.

The monthly salary of Staff A was \$18,000 in July 2007 when her employment contract commenced. In December 2007, her contract was extended for three months to March 2008. Her salary was adjusted to \$22,000 in January 2008, two months before the expiry of the contract. There was no evidence showing that prior approval from the ITC had been obtained for the salary adjustment.

Source: HKDC records

2.54 In response to Audit's enquiry, the HKDC informed Audit in September 2008 that the case in question involved the transfer of a staff for a period of five months to fill a vacant approved post with higher responsibilities. The enhanced salary was commensurate with the approved pay level for the senior post. The arrangement was approved retrospectively by the ITC.

Entertainment expenses

2.55 It is explicitly stated in the DSP funding guidelines that DSP project funds should not be used to cover entertainment expenses. However, Audit's sample checking of the expenses of the BODW 2006 and BODW 2007 projects revealed that there were nine cases where entertainment expenses were charged to project accounts (see Table 6).

Table 6
Entertainment expenses charged to DSP project accounts

Case	Date	Project	Description	Total expenses (\$)	Number of HKDC staff/Board members	Number of guests
1	22.9.2006	BODW 2006	Dinner meeting with a business partner in Shanghai	867	1	1
2	6.11.2006	BODW 2006	Lunch meeting with partnering sponsors and guests	3,500	2	5
3	1.12.2006	BODW 2006	Drinks with BODW speakers	950	1	2
4	8.2.2007	BODW 2006	Lunch meeting	580	2	1
5	9.2.2007	BODW 2006	Lunch meeting	1,000	1	2
6	2.7.2007	BODW 2007	Dinner meeting with a consultant in Japan	1,535	1	1
7	7.9.2007	BODW 2007	Lunch meeting with media representatives	1,593	1	3
8	14.9.2007	BODW 2007	Lunch meeting with contractors	589	1	2
9	18.9.2007	BODW 2007	Lunch meeting with media representatives	861	1	2
Total				11,475	11	19

Source: HKDC records

2.56 In response to Audit's enquiry, the HKDC informed Audit in September 2008 that all the cases reported involved meal expenses incurred by the BODW Project Director during working meetings with contractors, business partners and media representatives. They were charged improperly to the project account and the mistake was subsequently rectified with the ITC's endorsement.

ITC's approval for budget variation

2.57 According to the DSP funding guidelines, for project budget control purpose, the ITC's prior written approval is needed if the budget of a project item is expected to be exceeded by 15% or more. This requirement also applies to the budgets of payroll items.

2.58 Audit noted a case where the total payroll expenses of \$793,000 incurred for employing the project leader to oversee the BODW 2006 exceeded the budget of \$600,000 by about 32%. However, no approval from the ITC had been sought as per the requirement of the DSP funding guidelines. In response to Audit's enquiry, the HKDC explained in September 2008 that it had mistaken that the threshold of 15% applied to the total manpower cost for the project instead of payroll expenses for individual staff. It informed Audit that retrospective approval from the ITC for the variation had been obtained.

Appointment of an incumbent to a permanent post without open recruitment

2.59 According to the Corporate Governance Manual of the HKDC, all staff should be appointed through an open recruitment process (see para. 4.17). Audit's examination of the employment records of the project leader of the BODW 2006, who was then a contract consultant, revealed that he was offered a new permanent project director post of the HKDC in March 2007 without going through an open recruitment process.

2.60 As the appointment involved a creation of post that constituted a manpower variation of the HKDC, approval from the ITC was therefore required (see para. 4.18). In granting its covering approval for the manpower variation, the ITC commented that retention of an incumbent to fill a permanent post without going through an open recruitment process was at variance with the general corporate governance principles.

2.61 In response to Audit's enquiry, the HKDC explained in September 2008 that because of the urgency of the situation, the need to ensure work continuity and knowledge retention/transfer, and the robust job market at the time, the HKDC considered that open recruitment would unlikely yield a better candidate. This was an extremely exceptional arrangement for which ITC approval was given.

Audit recommendations

2.62 **Audit has recommended that the HKDC should:**

- (a) **consider developing a long-term financial sustainability plan for the BODW, as requested by the DSI Assessment Panel;**
- (b) **ensure that the requirements regarding the hiring of staff stipulated in the Corporate Governance Manual/DSP funding guidelines are complied with. In particular, the HKDC should:**
 - (i) **seek the Board’s advice on whether its approval is needed for the repeated renewal of contracts of project staff, which would result in their continuous employment for a period exceeding six months;**
 - (ii) **seek approval from the ITC prior to making salary adjustment to DSP project staff; and**
 - (iii) **ensure that an open recruitment process is carried out for appointments to permanent posts. Proper approval should be obtained if open recruitment is not carried out;**
- (c) **ensure that the DSP funding support would not be used to meet entertainment expenses; and**
- (d) **seek approval from the ITC if the budget of a DSP project item is exceeded by 15% or more.**

Response from the Hong Kong Design Centre

2.63 The **CEO, HKDC** accepts the audit recommendations. He has said that the **HKDC:**

- (a) **undertakes to review the existing financial arrangements for the BODW and develop a long-term financial plan, in consultation with the ITC;**
- (b) **does not envisage that the BODW could be self-sufficient at this stage. Experiences elsewhere indicate that substantial government funding is required for similar projects. The BODW has contributed to the Hong Kong brand and the HKDC’s goal to become the design hub of Asia;**
- (c) **has delegated to the CEO the authority to renew an employment contract upon its expiry for not more than six months and delegated to the Finance and Administration Committee (FAC — see para. 4.3) the authority for further renewals. These rules will be strictly complied with in future;**

- (d) will strictly follow the rule to seek prior approval from the ITC for making salary adjustment to DSP project staff in future;
- (e) has tightened up its internal control procedures to ensure that the DSP funds are not used to meet entertainment expenses;
- (f) will seek specific approval from the ITC in future, if the budget of a DSP project item is exceeded by 15%; and
- (g) will ensure that the requirement for open recruitment will be strictly adhered to for appointment to its permanent posts in future.

PART 3: PROMOTION OF DESIGN BY THE HONG KONG DESIGN CENTRE

3.1 This PART reviews the initiatives implemented by the HKDC for the promotion of design, and notes that there are areas with room for improvement.

The Hong Kong Design Centre

3.2 The HKDC is a non-profit-making infrastructure organisation established in 2001. It is a company limited by guarantee, comprising the following five members (similar to shareholders in the case of a company limited by shares):

- (a) the Hong Kong Designers Association;
- (b) the Chartered Society of Designers, Hong Kong;
- (c) the Interior Design Association Hong Kong;
- (d) the Hong Kong Fashion Designers Association; and
- (e) the Hong Kong Federation of Design Associations.

3.3 In line with the Government's policy on the promotion of design and innovation, the objective of the HKDC is to promote design as a value-added activity and to integrate design into mainstream business processes.

3.4 Since its inception, the HKDC has been the Government's main partner in promoting design. To support its initial operation, in September 2001, the Government provided a one-off funding of \$10 million as seed money to the HKDC. In 2004, an additional amount of \$45 million was provided to the HKDC under the InnoCentre Programme (see para. 1.3(b)). In March 2007, the ITC transferred \$14 million to the DSP, thereby reducing the funding support for the HKDC from \$45 million to \$31 million. In May 2007, the Government earmarked another \$100 million over a five-year period for the HKDC to support its basic operation, which included manpower, overhead and general administration, and some basic activities (Note 2). Funding agreements were signed

Note 2: *The basic activities included programme planning and development, networking activities in the Mainland and overseas, website and database development, educational seminars, workshops and classes, and designer-business networking events.*

between the Government and the HKDC, which set out the ambit of use and the conditions for allocation of funds.

3.5 For major projects that go beyond the basic operational activities set out above, the HKDC applies funding separately under the DSP (see para. 1.3(a)). As at 30 June 2008, the HKDC had a total of 31 permanent staff. An organisation chart of the HKDC is shown at Appendix A.

Government funding for the HKDC

3.6 Up to 30 June 2008, the Government provided a total of \$129 million to support the operation of the HKDC. As at the same date, the remaining funding committed to support the HKDC until 2012 was about \$87 million. Table 7 shows details of the Government funding committed to and utilised by the HKDC.

Table 7

**Government funding provided to the HKDC
(30 June 2008)**

Government funding	Period	Amount (\$ million)			
		Committed (a)	Utilised (b)	Funding lapsed (c)	Remaining available funding (d) = (a) - (b) - (c)
Start-up capital	September 2001 to March 2005	10	10	0	0
Funding under the InnoCentre Programme	September 2004 to June 2007	31 (Note 1)	22	9 (Note 2)	0
Additional funding approved in May 2007	July 2007 to June 2012	100	24	0	76
Project funding under the DSP	November 2004 to April 2009	70	59	0	11
Other project funding from the Government (Note 3)	September 2002 to August 2005	14	14	0	0
Total		225	129	9	87

Source: ITC records

Note 1: \$45 million was originally committed under the InnoCentre Programme. The amount was reduced to \$31 million in March 2007 (see para. 3.4).

Note 2: The \$9 million unutilised funding lapsed upon the approval of the additional funding of \$100 million in May 2007.

Note 3: Apart from the four funding schemes under the DSP, the HKDC had also received other government funding support (e.g. the Innovation and Technology Fund) over the years.

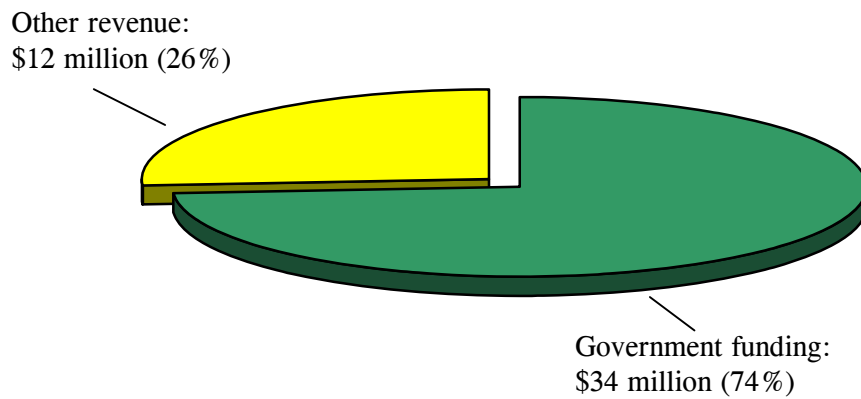
Income and expenditure of the HKDC

3.7 Figure 2 below summarises the HKDC's income and expenditure for 2007-08.

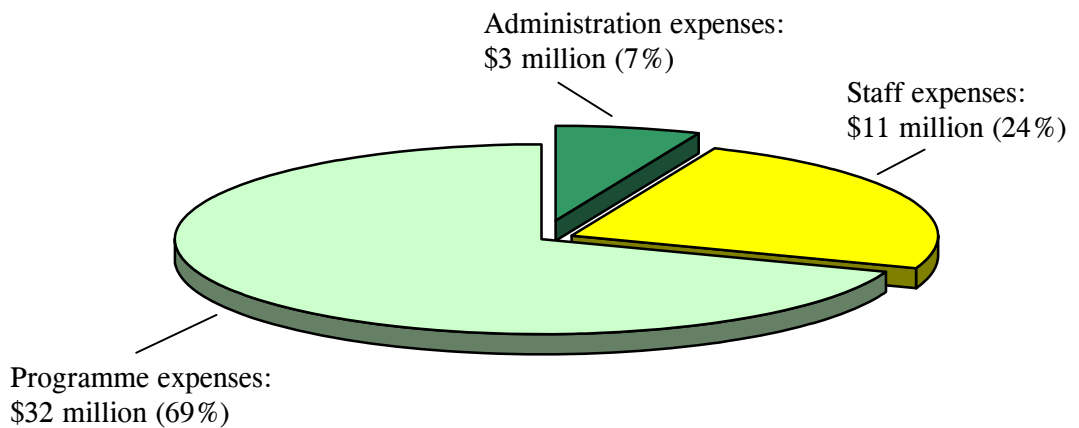
Figure 2

**Income and expenditure of the HKDC
(2007-08)**

(A) Income: \$46 million



(B) Expenditure: \$46 million



Source: HKDC records

Business planning for the promotion of design

3.8 In June 2006, the DSI Assessment Panel requested that the HKDC should submit a three-year business plan for its consideration. In the business plan submitted in December 2006 for the three-year period starting on 1 April 2007, the HKDC stated that it should:

- (a) focus on cultivating a wider and more strategic use of design in Hong Kong; and
- (b) adopt a thematic and sectoral approach to design education and promotion for its target audience.

Audit observations and recommendation

3.9 While the ITC considered that the HKDC's future development as stated in its business plan submitted in December 2006 was in the right direction, the DSI Assessment Panel commented that the success of the plan would depend very much on the implementation details. The DSI Assessment Panel therefore recommended that the HKDC should work out the implementation plan and set out the priorities.

3.10 Audit noted that in the annual plan for 2008-09 and the three-year business plan for 2009-2012, the HKDC outlined the implementation of various programmes it intended to carry out. However, only very brief information about the programmes was provided therein. For example, the justifications and basis adopted for setting out the priorities of various programmes were not provided. Outcome targets for measuring the achievements of the programmes outlined in the business plan were also not shown.

Audit recommendation

3.11 **Audit has recommended that the HKDC should provide more detailed information regarding the implementation of various programmes in its business plan (e.g. the justification and basis adopted for setting out the priorities of various programmes, and the outcome targets for measuring the achievements of the programmes).**

Response from the Hong Kong Design Centre

3.12 The CEO, HKDC accepts the audit recommendation. He has said that the justifications for priority setting of programmes and the determination of performance targets will be spelt out in detail when the HKDC compiles its 2009-10 Annual Plan and the 2010-12 Business Plan. More detailed information regarding the implementation of various programmes in these plans will also be provided.

Implementation of design infrastructure projects

3.13 Audit noted that various initiatives were stated by the HKDC in its business plan and annual budget for enhancing the design infrastructure, which included:

- (a) establishing a design resource centre;
- (b) setting up a design directory (Note 3); and
- (c) revamping the HKDC's website as a gateway to design information.

Audit observations and recommendations

3.14 Audit's examination of the HKDC records revealed that implementing these initiatives had met with considerable delays, as follows:

- (a) ***Establishing a design resource centre.*** In June 2004, the Finance Committee of the Legislative Council was informed that the HKDC would set up a design-related resource centre. Audit noted that the HKDC had included in its 2004-05 budget a sum of \$1.8 million for the setting up of the resource centre. The target completion date was February 2005. However, there had been a number of delays. The work for the setting up of the resource centre was only commenced in February 2008. The work was completed four months later and the design resource centre was officially opened in June 2008, i.e. almost 3.5 years after the target completion date;
- (b) ***Setting up a design directory.*** In its 2004-05 budget, the HKDC stated that it planned to complete the development of a design database by January 2005. However, Audit noted that no action was taken by the HKDC in 2004-05 and 2005-06. In March 2007, the HKDC submitted an application for funding of \$1 million under the DSP for developing a design directory. The DSI Assessment Panel rejected the HKDC's application, stating that funding for the development of a design database had already been provided in the HKDC's budget. The design directory eventually became available to the public in September 2008, i.e. almost four years after the planned completion date; and

Note 3: *The design directory is a comprehensive online database of professional designers and design companies in Hong Kong. It is expected that potential users of design around the world could reach professional design service providers in Hong Kong via this online platform. The directory is expected to showcase the expertise of Hong Kong designers.*

- (c) **Revamping the HKDC's website.** In its three-year business plan for 2007-08 to 2009-10, the HKDC stated that its website should be overhauled as a gateway to design information, know-how, contacts and activities both locally and internationally. The HKDC pledged in its 2007-08 budget that its website would be so revamped by the third quarter of 2007-08. Audit's examination of the HKDC records revealed that the target completion date for revamping the HKDC website had subsequently been deferred to the second quarter of 2008-09.

3.15 In response to Audit's enquiry, the HKDC informed Audit in September 2008 that:

- (a) the design resource centre project originally envisaged the setting up of a library of materials for designers and engineers to get inspired in the innovative use of material for designing functional and aesthetically appealing products. It was a multi-million dollar investment and had therefore taken the HKDC considerable time in assessing its feasibility and cost benefits. In the end, it was concluded that the project was not financially sustainable and hence its scale was curtailed to that of a library of books;
- (b) as regards the design directory, the delay in completing the project was due to the long time taken to discuss with the design community and business users to formulate the project proposals, the change in personnel responsible for managing the project and the abortive work done to seek funding support from the DSP; and
- (c) the delay in revamping the HKDC's website was mainly due to the deployment of a key staff from her usual duties to managing the Project 9707. The revamp exercise was considered less critical than the unique opportunity in 2007 to capitalise on the tenth anniversary of the Hong Kong's re-unification with China to promote Hong Kong design globally.

Audit recommendations

3.16 **Audit has recommended that the Commissioner for Innovation and Technology should take measures to ensure that delays in implementing the HKDC's design infrastructure projects are identified and dealt with in a timely manner.**

3.17 **Audit has recommended that the HKDC should take action to improve on its project management capability so as to ensure that its design infrastructure projects will not be further delayed.**

Response from the Administration and the Hong Kong Design Centre

3.18 The **Commissioner for Innovation and Technology** has said that the ITC understands the reasons causing delays in implementing the HKDC's design infrastructure projects and has been/will be closely monitoring their progress.

3.19 The **CEO, HKDC** accepts the audit recommendation. He has said that:

- (a) the HKDC regrets that there had been significant delay in implementing the three design infrastructure projects in question; and
- (b) the HKDC's project management capability has been strengthened by holding frequent internal project review meetings among staff and the involvement of the Board in reviewing project progress on a quarterly basis. This should ensure that its design infrastructure projects will not be unduly delayed.

Management of funding for promotion of design

3.20 At present, the promotion of design by the HKDC is mainly funded by the Government (see paras. 3.6 and 3.7). In order to encourage the HKDC to build up its revenue generating capacity and to seek more income from industries and other sources for its long-term development, the HKDC was required to achieve an income target, fixed by the ITC, under the Funding Agreement. The respective income targets for 2007-08 and 2008-09 were 10% and 20% of the HKDC's basic operation expenditure (see para. 3.4).

3.21 Audit examined the HKDC's management of funding for the promotion of design and found that there was room for improvement in the following areas:

- (a) meeting income target; and
- (b) reporting of unspent funds.

Audit observations and recommendations

Meeting income target

3.22 Audit noted that in its original budget for 2008-09 submitted to the ITC in February 2008, the HKDC estimated that income from non-government sources would amount to 28% of its basic operation expenditure. However, one of its major income-generating events, which was expected to generate revenue of \$2.4 million, was cancelled in early 2008 due to poor response to the HKDC's initial marketing work.

In July 2008, the HKDC also found that the target sponsorship of \$625,000 for holding exhibitions at the InnoCentre was unlikely to be met. The HKDC therefore revised downward the estimated non-government income to 12.4% of its basic operation expenditure, which was considerably below the income target of 20% set for 2008-09.

3.23 It is a condition stated in the Funding Agreement that the HKDC should meet the income target set by the ITC. It is important that more non-government income should be raised to ensure the long-term sustainability of the HKDC. Audit considers that the HKDC needs to analyse the reasons for the low income generated and take improvement actions, with a view to meeting the income target.

Reporting of unspent funds

3.24 Audit noted that funding for the HKDC under the InnoCentre Programme was disbursed by instalments. The instalment amounts were determined according to the estimated net cash flow requirements submitted by the HKDC. If the actual cash flow for the relevant period was less than that estimated, the unspent amount would be deducted from the funding for the following period. When the new funding of \$100 million was approved in May 2007 (see para. 3.4), the ITC decided that the unspent amount of the funding already disbursed under the InnoCentre Programme would be used to offset the HKDC's cash flow requirements under the current funding arrangements.

3.25 In July 2007, the HKDC reported to the ITC that the unspent balance of the funding allocated to the HKDC under the InnoCentre Programme was about \$2.5 million. In December 2007, the HKDC advised the ITC that the unspent balance should be adjusted to \$2 million.

3.26 Audit reviewed the HKDC's audited accounts and found that the adjusted unspent balance of \$2 million as reported by the HKDC was only for the three-month period 1 April to 30 June 2007. The accumulated unspent balance of the funding provided under the InnoCentre Programme as stated in the audited accounts was about \$6.5 million.

3.27 In May 2008, Audit informed the ITC of the above audit findings. In response to the ITC's enquiry, the HKDC confirmed that the unspent balance up to 30 June 2007 was in fact \$6.5 million. Hence, the unspent balance was understated by about \$4.5 million. In the event, in June 2008, the ITC deducted \$4.5 million from the disbursement to the HKDC for 2008-09.

- 3.28 In response to Audit's enquiry, the ITC informed Audit in September 2008 that:
- (a) in late December 2007, the ITC received an audited account from the HKDC on the final expenditure position of the InnoCentre Programme funding and noted that the total unspent balance was \$6.5 million;
 - (b) due to very heavy commitment around March 2008 and in trying to meet the payment deadline at close of financial year, the third quarterly disbursement was made without further updating the unspent balance according to the audited account. Meanwhile, Audit raised this issue and after confirmation with the HKDC, the updating and offsetting was made when considering the fourth disbursement in June 2008. The updating and offsetting was thus delayed by a quarter; and
 - (c) the ITC agreed that it was more proper to confirm the unspent balance with the HKDC and carry out updating and offsetting in the first practical opportunity.

Audit recommendations

3.29 **Audit has recommended that the Commissioner for Innovation and Technology should take measures to ensure that the unspent balance is properly reported by recipients of DSI funding.**

3.30 **Audit has recommended that the HKDC should analyse the reasons for the low income generated and take improvement actions, with a view to meeting the income target set by the ITC.**

Response from the Administration and the Hong Kong Design Centre

3.31 The **Commissioner for Innovation and Technology** accepts the audit recommendation. He has said that the ITC will verify reported unspent balance against other independent sources such as bank balance statement and audited accounts at each quarterly disbursement.

3.32 The **CEO, HKDC** accepts the audit recommendation. He has said that the HKDC will continue to look for means to boost income for 2008-09 and identify new programmes which will serve the same purpose. He has also said that:

- (a) the updated estimate of income for 2008-09 is less than the original estimate in the approved 2008-09 Annual Plan. The deviations are mainly due to the following:

- (i) the summer overseas design and cultural tour for students was cancelled due to an unexpectedly low response to the HKDC's initial marketing;
 - (ii) some projects in the original plan have been organised as part of the "Reinventing with Design" conference held in June 2008 under the DSP funding instead; and
 - (iii) the target sponsorship of \$625,000 for holding exhibitions at the InnoCentre is unlikely to be met under the prevailing economic conditions when businesses are expected to be less generous in sponsorships; and
- (b) the ITC has accepted in principle that sponsorship-in-kind could also be taken into account in assessing the expenditure/revenue ratio. This should improve the ratio in favour of the HKDC significantly.

PART 4: CORPORATE GOVERNANCE AND ADMINISTRATION OF THE HONG KONG DESIGN CENTRE

4.1 This PART examines corporate governance and administration of the HKDC. Audit notes that the HKDC needs to improve on its corporate governance.

Governance structure of the Hong Kong Design Centre

4.2 When the HKDC was established in 2001, it was governed by a board of governors and a board of directors. In March 2007, the two boards were merged and became the Board. According to the HKDC's Articles of Association, the Board should comprise:

- (a) two government directors (i.e. the Commissioner for Innovation and Technology and the Deputy Secretary for Home Affairs);
- (b) five "Class A" directors representing the five members (see para. 3.2) of the HKDC; and
- (c) at least five "Class B" directors who should be nominated by the Class A directors jointly and approved by the Government (Note 4).

As at 30 June 2008, the Board had 21 directors, comprising one government director, four Class A directors (Note 5), and 16 Class B directors.

4.3 The Board is responsible for directing the development and operations of the HKDC. The CEO of the HKDC is responsible to the Board for the overall management of the HKDC. Two functional standing committees, i.e. the FAC and the Business Development Committee (BDC), were set up in June 2007 to assist the Board to conduct its business. As at 30 June 2008, the FAC and the BDC had seven and twelve members respectively. According to the HKDC's Corporate Governance Manual, the Board should convene no less than four meetings annually, and the FAC and BDC should meet quarterly.

Note 4: *The HKDC's Articles of Association specify that Class A directors have the right exercisable jointly to appoint any person from the design, cultural, creative, business, industry, professional and academic sectors as Class B directors and to remove any such directors, subject to approval of the Secretary for Commerce and Economic Development.*

Note 5: *The Class A director representing the Chartered Society of Designers, Hong Kong resigned in January 2008. The Deputy Secretary for Home Affairs also ceased to be a director of the HKDC in March 2008. Up to 30 June 2008, the two vacancies were not filled.*

Audit observations and recommendations

4.4 Audit conducted an examination of the HKDC's corporate governance issues and found that there was room for improvement in the following areas:

- (a) attendance of directors at Board/Committee meetings (paras. 4.5 and 4.6);
- (b) submission of Board/Committee papers (paras. 4.7 and 4.8); and
- (c) management of potential conflicts of interest (paras. 4.9 to 4.11).

Attendance of directors at Board/Committee meetings

4.5 From March 2007 to June 2008, the Board met eight times, and the FAC and BDC met five and four times respectively. Audit's analysis of the attendance of the HKDC's directors at these 17 Board/Committee meetings revealed that:

- (a) ***Low attendance rates.*** The attendance rates of directors at these Board/Committee meetings ranged from 14% to 83%. In particular:
 - (i) at four (50%) of the eight Board meetings, the attendance rates were below 60%;
 - (ii) at three (60%) of the five FAC meetings, the attendance rates were below 40%; and
 - (iii) at one (25%) of the four BDC meetings, the attendance rate was below 50%;
- (b) ***Directors with low attendance records.*** Audit noted that some directors had low attendance records at Board/Committee meetings. For example:
 - (i) during his tenure as one of the government directors, the Deputy Secretary for Home Affairs attended three (43%) of the seven Board meetings. No alternate director was appointed at the four meetings from which he was absent. The attendance of the Home Affairs Bureau (HAB) representative at the 4th meeting was not counted towards the attendance of the Deputy Secretary for Home Affairs because of the technical consideration that the representative had not been duly appointed as alternate director; and
 - (ii) six non-government directors had a low attendance rate (below 40%) at Board/Committee meetings. In particular, three of them had an attendance rate of 25% or below; and

- (c) ***Quorum of the FAC.*** According to the Corporate Governance Manual of the HKDC, the quorum necessary for the transaction of business at FAC meetings shall be a minimum of four directors. Audit noted that at three (60%) of the five FAC meetings held during the period March 2007 to June 2008, this quorum requirement was not met. This might render the decisions made at these meetings invalid (see also paras. 4.31 and 4.32).

4.6 Audit considers that the low attendance of some directors at Board/Committee meetings is a matter of concern. This is because the overall effectiveness of the Board/Committee might be compromised if a large number of directors representing different sectors of the community did not attend meetings to participate in the decision-making process. **The HKDC needs to take appropriate measures to improve the attendance of directors at Board/Committee meetings. The HKDC also needs to ensure that the quorum requirement is always met in all meetings in future.**

Submission of Board/Committee papers

4.7 According to the corporate governance guidelines for public bodies issued by the Hong Kong Institute of Certified Public Accountants, members of the governing board should ensure that they are provided with all the information that they need to properly consider issues to be discussed at a governing board meeting, in good time before the meeting. At a Board meeting of the HKDC held in April 2007, it was also agreed that papers for Board meetings should be provided to directors **one week in advance**, in order to allow sufficient time for the directors to review the papers.

4.8 However, Audit found that, of the eight Board meetings held in the period March 2007 to June 2008, the one-week requirement for the submission of Board papers was not met at six (75%) meetings. Similarly, in seven (78%) of the nine Committee meetings held in the same period, the Committee papers were provided to directors less than one week in advance of the meetings.

Management of potential conflicts of interest

4.9 As many HKDC directors come from the design trade, potential conflicts of interest may arise when issues about the promotion of design and innovation are discussed at the Board/Committee meetings. At present, the HKDC adopts a “one-tier reporting system”, which requires a director to declare and report a conflict of interest only when he becomes aware of it.

4.10 Audit notes that many public organisations (e.g. the Airport Authority, the Hong Kong Tourism Board, the Hong Kong Applied Science and Technology Research Institute Company Limited, and the University Grant Committee) have a more stringent requirement for members appointed to their boards/committees to declare their interests. These public organisations have adopted a “two-tier reporting system” for managing conflicts of interest of their governing body members. Under such a system, members are required to disclose their general interests, direct or indirect, pecuniary or otherwise, on appointment to the board or committee. The declaration shall be made on a registration form, which would be made available for inspection by members of the public upon request. The registration of interests is in addition to the report on conflicts of interest at board or committee meetings as and when they arise.

4.11 In 2005, the HAB issued a guideline on the need to introduce a system for declaration of interests for advisory and statutory bodies. The guideline states that a board or committee should adopt the two-tier reporting system if it:

- (a) has a high degree of management and financial autonomy;
- (b) has extensive executive powers in matters of public interest; or
- (c) is responsible for the control and disbursement of substantial public funds.

To a large extent, the HKDC meets the above criteria. Audit considers that the HKDC needs to consider whether there are merits in adopting the two-tier reporting system for managing potential conflicts of interest of its directors.

Audit recommendations

4.12 **Audit has recommended that the Secretary for Commerce and Economic Development should take into account the attendance of directors at Board/Committee meetings when considering the approval of Class B directors nominated by Class A directors of the HKDC.**

4.13 **Audit has recommended that the HKDC should:**

Attendance of directors at Board/Committee meetings

- (a) **take measures to improve the attendance of directors at Board/Committee meetings;**
- (b) **issue reminders to those directors with low attendance records, urging them to make efforts to attend Board/Committee meetings as far as possible in future;**

- (c) ensure that the quorum requirement is always met at all meetings in future;
- (d) review the decisions made at the three FAC meetings where the quorum requirement was not met to see whether remedial actions are needed;

Submission of Board/Committee papers

- (e) ensure that Board/Committee papers are submitted in good time before the meeting and, in particular, the one-week requirement for submitting Board papers is followed as far as possible; and

Management of potential conflicts of interest

- (f) consider adopting the two-tier reporting system for managing potential conflicts of interest of its directors.

Response from the Administration and the Hong Kong Design Centre

4.14 The **Secretary for Commerce and Economic Development** accepts the audit recommendation. She has said that she will take into account the attendance of Class B directors when considering approval of the nominated list of Class B directors in future. She has also said that the current HKDC Board is the first Board after the revamp in March 2007 (see para. 4.2), and as such, there was no past attendance for reference when appointing the current Class B directors.

4.15 The **Secretary for Home Affairs** has said that:

- (a) the role of the Deputy Secretary for Home Affairs has been to provide support to the HKDC from the policy area of the HAB. This role should have also been discharged at other meetings attended by the Bureau; and
- (b) the ITC and the HAB have been in discussion on the more appropriate capacity for any representative of the HAB to hold on the Board. Consideration is being made on whether it should be an appointment as director on an ad personam basis or an appointment in an official capacity as observer or any other status.

4.16 The CEO, HKDC accepts the audit recommendations. He has said that the HKDC:

- (a) acknowledges that low attendance of some directors at Board/Committee meetings is a matter of concern. Measures taken to improve attendance include:
 - (i) the Board Chairman has issued a letter appealing to all directors, urging them to make efforts to attend future Board/Committee meetings;
 - (ii) the Board secretary will in future monitor the situation and remind directors concerned of their low attendance, with a view to improvement; and
 - (iii) the date and time of Board/Committee meetings are now normally fixed three months before the meetings so that members can plan their schedules in advance;
- (b) will ensure that the quorum requirement will be met at all meetings in future;
- (c) has carried out a review of the decisions made at these meetings and concluded that, except for the issue raised in paragraphs 4.31 and 4.32, no rectification is required for other decisions as they have either been re-affirmed by the Board or superseded by subsequent events;
- (d) agrees with Audit that Board/Committee papers should be submitted in good time before the meeting so that the directors can properly consider issues to be discussed. The one-week requirement for submitting Board papers will be strictly followed in future; and
- (e) will seriously consider the recommendation of adopting the two-tier reporting system for managing potential conflicts of interest of its Board directors.

Hiring of staff

4.17 According to the HKDC's Corporate Governance Manual and the Funding Agreement, the recruitment process for all HKDC posts should be open, fair and competitive (e.g. placing advertisement of vacancies and convening of recruitment panels to interview candidates) without discrimination in respect of race, age and sex.

4.18 Appointment of staff at director level is subject to the FAC's approval (Note 6). All other appointments, including the employment of contract staff for not more than six months, can be approved by the CEO. If the appointment involved a creation of new post, approval from the Board is needed. The ITC's approval is also required if the appointment constitutes a manpower variation of the HKDC.

Audit observations and recommendations

Approval for the creation of new post

4.19 Audit noted that in the case mentioned in paragraph 2.59, prior approval from the Board and the ITC should have been sought as it involved a creation of new post and constituted a manpower variation of the HKDC. Audit's examination of the recruitment records of the case revealed that the approvals of the Board and the ITC were only sought after the appointee had started working in the HKDC.

Information provided for seeking approval from the Board for new appointment

4.20 An audit examination of the recruitment records of ten HKDC staff revealed that in three cases, inadequate information was provided to the Board for seeking its approval for the appointment. In all these three cases, prior approval from the Board was needed. As far as Audit could ascertain, the Board was informed that the recruitment process was completed and suitable candidates were identified. Details of the candidates (such as their names, background and qualifications) were not provided. In this connection, it is worth noting that the Commissioner for Innovation and Technology, in his capacity as one of the government directors of the HKDC, had expressed serious concern and remarked that the covering approval for the case mentioned in paragraph 4.19 was only given on an exceptional basis.

Audit recommendations

4.21 **Audit has recommended that the HKDC should ensure that:**

- (a) **the requirements regarding the creation of posts as stipulated in the Corporate Governance Manual are complied with. Where necessary (e.g. the creation constitutes a manpower variation), prior approval from the ITC should also be sought; and**
- (b) **adequate information is provided in seeking approval for appointment of staff.**

Note 6: *Prior to October 2007, the authority to approve appointment of staff at manager or higher level rested with the Board.*

Response from the Hong Kong Design Centre

4.22 The CEO, HKDC accepts the audit recommendations. He has said that:

- (a) the HKDC will ensure that the requirements regarding the creation of posts as stipulated in the Corporate Governance Manual are complied with. Where necessary, prior approval from the ITC will be sought. The HKDC will also ensure that adequate information is provided in seeking approval for staff appointments at all approval levels;
- (b) the HKDC's offer of appointment for the post of BODW project director (see para. 4.19) was made as a very exceptional arrangement, justified by the exigencies of service and the need to maintain work continuity while ensuring knowledge retention/transfer for repeating the BODW project annually. Prior approval from the Board and the ITC was not obtained in time because of the urgent need to recruit the staff to commence work for the BODW 2007; and
- (c) regarding the other three cases mentioned in paragraph 4.20, the HKDC admits that in the process of seeking the Board's approval to make these appointments, full details of the appointments were not provided. With the delegation of authority to make appointment to staff at manager level and below from the Board to the CEO since September 2007, this issue will not recur.

Procurement of goods and services

4.23 For the procurement of goods and services, the following guidelines were set out in the HKDC's Corporate Governance Manual:

- (a) at least two quotations should be obtained for procurement amounts of over \$5,000 but less than \$10,000;
- (b) at least three quotations should be obtained for procurement amounts of \$10,000 or more but less than \$500,000;
- (c) at least five quotations should be obtained for procurement amounts of \$500,000 or more; and
- (d) if the HKDC decided to procure goods or services from a single supplier, or not to accept the lowest bid, full justifications must be given and documented, and approvals from the ITC and the CEO were required.

4.24 In the past, for procurement amounts of \$100,000 or below, approval could be given by the CEO. For procurement amounts of over \$100,000 and up to \$1 million, joint approval of the CEO and a director was needed. For procurement amounts

of over \$1 million, approval from the Finance and Manpower Committee of the Board was required. Effective from April 2008, the approval limit of the CEO was \$200,000. For procurement amounts of over \$200,000 and up to \$1 million, joint approval of the Chairman, the Vice-Chairman of the Board and the CEO was needed.

Audit observations and recommendations

4.25 Audit's examination of the procurements made by the HKDC in 2007-08 revealed the following cases where the procurement guidelines mentioned above were not followed:

- (a) **Single quotation.** In May 2007, a single quotation of \$100,000 was obtained for a consultancy study for conducting research and drafting the report "Hong Kong's blue ocean: from creative industries to creative economy". There was no documentation of the justifications and the approval for not seeking three quotations, contrary to the HKDC's procurement guidelines (see para. 4.23(b));
- (b) **Procurement of goods and services for the DSP projects.** An audit examination of 100 randomly selected procurements for the DSP projects, with value of more than \$5,000 each, revealed that:
 - (i) in 37 cases, only a single quotation was obtained; and
 - (ii) in 5 other cases, the lowest bids were not selected.

In all these 42 cases, there was no evidence of approval by the ITC (see para. 4.23(d)); and

- (c) **Approval limit.** The HKDC engaged two consultants in May 2007 for the publication of the book "Very Hong Kong: design 1997 to 2007". One of the contracts amounted to \$120,000. The contract was approved and signed by the Vice-Chairman, who was also the Acting CEO at that time. However, as the contract amount exceeded the threshold of \$100,000, it should have been jointly approved by the CEO and a director in accordance with the HKDC's procurement guidelines at the time (see para. 4.24).

Audit recommendations

4.26 **Audit has recommended that the HKDC should ensure that:**

- (a) **sufficient number of quotations is obtained in accordance with the procurement guidelines set out in the Corporate Governance Manual; and**

- (b) **the approval limits stipulated in the Corporate Governance Manual are strictly followed.**

Response from the Hong Kong Design Centre

4.27 The **CEO, HKDC** accepts the audit recommendations. He has said that the HKDC regrets the irregularities identified by Audit. It has tightened up the procurement procedures to ensure that full justifications for non-compliance with procurement procedures are properly recorded, prior approval from the HKDC's internal authority or the ITC for non-compliance cases is obtained where necessary, and that approval limits stipulated in the Corporate Governance Manual are strictly followed. He has also said that:

- (a) the consultancy company involved in paragraph 4.25(a) was the only university-research based centre devoted to writing business cases in Hong Kong and was in charge of a creativity and business innovation undergraduate programme. The price represented value for money in view of the research hours required to complete the project. The HKDC accepts that no documentation was kept to record these justifications;
- (b) retrospective approval from the ITC was obtained for the cases mentioned in paragraph 4.25(b). The departure from normal procurement rules was justified mainly on grounds of urgency of the requests and that the lowest bid did not satisfactorily meet the user requirement; and
- (c) the HKDC accepts that the contract mentioned in paragraph 4.25(c) should have been approved by the CEO and another Board director. The mistake was due to an oversight and has been rectified by the Chairman's retrospective approval.

Overseas travel expenses

4.28 In 2006-07 and 2007-08, overseas travel expenses amounted to about \$236,000 and \$395,000 respectively. The regulations on the control of overseas travel expenses are set out in the HKDC's Corporate Governance Manual and other relevant guidelines issued. These guidelines include the following key provisions:

- (a) prior approval from the CEO is needed. In cases involving the CEO, prior approval from the Board Chairman is required;
- (b) economy class travel should be used in all cases, whereas individuals may top up the difference at their own expense if they wish to travel at a higher class; and
- (c) Board members should bear their own travel expenses unless decided otherwise by the Board.

Audit observations and recommendations

4.29 Audit's examination of overseas travel expenses in 2006-07 and 2007-08 revealed that there was room for improvement in a number of areas.

Documentation of approval

4.30 Audit found that in three cases (out of a total of 18 cases), air tickets were purchased before application for approval was made or written approval was obtained (see Table 8). In response to Audit's enquiry, the HKDC explained that in all these cases, prior verbal approval was given. The HKDC agreed that it would ensure that prior written approval would be obtained as far as possible and proper documentation should be kept for verbal approval obtained.

Table 8

The three cases where prior written approval was not obtained

Case	Visit period	Date		
		Application	Approval	Airfare invoice
1	22 to 24 August 2006	18 August 2006	Not dated	17 August 2006
2	18 and 19 July 2007	17 July 2007	25 July 2007	16 July 2007
3	28 to 30 November 2007	23 November 2007	26 November 2007	23 November 2007

Source: HKDC records

Travel by business class

4.31 In October 2007, the CEO travelled to the United States by business class. Originally, he planned to travel by economy class and booked a return ticket for about \$9,700. The subject of air travel for HKDC staff travelling overseas on duty was first raised at the FAC meeting on 7 September 2007. However, no decision was made at the meeting. On 8 October 2007, the FAC held another meeting and agreed that subject to approval from the Board Chairman, the CEO might travel by business class. Two days after the FAC meeting, the CEO submitted his application for upgrading his ticket to business class. The Board Chairman approved the application on the same day.

4.32 Audit noted that the number of directors attending the FAC meeting on 8 October 2007 did not meet the quorum requirement and, therefore, the decision made at the meeting might be invalid (see para. 4.5(c)). Audit considers that the HKDC needs to

seek the covering endorsement of the FAC on the decision made at its meeting of 8 October 2007.

Overseas travel expenses incurred by a Board member

4.33 Audit noted that in three cases, approved in 2006-07, overseas travel expenses (about \$55,000 in total) incurred by a Board member were reimbursed. In these three cases, the Board member concerned had only obtained approval from the Chairman of the Board of Governors (see para. 4.2), but not the Board as required by the HKDC's Corporate Governance Manual (see para. 4.28(c)).

Audit recommendations

4.34 **Audit has recommended that the HKDC should:**

- (a) **remind all staff that prior written approval should be obtained as far as possible for overseas travel. Proper documentation should be kept if approval is given verbally;**
- (b) **seek the covering approval from the Board for the revision made to the Corporate Governance Manual and to endorse the decision made by the FAC at its meeting of 8 October 2007 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.**

Response from the Hong Kong Design Centre

4.35 The CEO, HKDC accepts the audit recommendations. He has said that:

- (a) the HKDC has reminded all staff that prior approval should be obtained for overseas travel. Proper documentation will be kept for both written and verbal prior approvals, all Board members have also been reminded to observe the rules stipulated in the Corporate Governance Manual;
- (b) the Board has given approval for the revision made to the Corporate Governance Manual and endorsed the decision made by the FAC at its meeting of 8 October 2007 regarding the Chairman's authorisation for the CEO to travel by business class; and
- (c) regarding the case mentioned in paragraph 4.33, the Board has given retrospective approval for the Board member concerned to incur the overseas travel expenses.

PART 5: ADMINISTRATION OF THE DESIGN INCUBATION PROGRAMME

5.1 This PART examines the administration of the DIP operated by the HKSTPC, and notes that there are certain areas where the administration of the programme can be improved.

Background

5.2 Under the DSI, a sum of \$25 million was earmarked for the HKSTPC to operate the DIP at the InnoCentre. The objective of the DIP is to support design start-up companies for a period up to two years. During the incubation period, 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 their business development costs during their start-up period.

5.3 When the DIP was approved in June 2004, it was expected that the \$25 million funding would provide a financial support of up to \$500,000 to at least 50 incubatees over a five-year period (from January 2006 to December 2010). The HKSTPC's records showed that, up to 31 March 2008, there were 33 incubatees admitted. The total financial assistance granted was about \$5 million (about 20% of the total DIP funding of \$25 million), as shown in Table 9.

Table 9

Number of incubatees and amount of financial assistance granted

	Number of incubatees			
	Admitted	Graduated	Dropped out	Total amount of financial assistance granted (\$'000)
2005-06	5	—	—	36
2006-07	13	—	—	1,522
2007-08	15	4	1 (Note)	3,449
Total	33	4	1	5,007

Source: HKSTPC records

Note: The incubatee dropped out of the DIP in October 2007 because its shareholders decided to dissolve the company.

5.4 According to the Memorandum of Administrative Arrangements signed between the HKSTPC and the ITC for the DIP (hereinafter refers to as the DIP-MAA), the HKSTPC is responsible for administering the DIP, as well as the pertinent costs incurred for promotion, admission and housekeeping. The DIP-MAA provides, among other things, that:

- (a) the funding of \$25 million is the maximum sum set aside for the DIP;
- (b) the HKSTPC should submit annually for the ITC's approval an annual programme and estimates which shall contain maximum number of incubatees and estimated amount of the financial support to incubatees for the forthcoming financial year;
- (c) on or before 30 September of each year, the HKSTPC should submit to the ITC audited accounts of the funds granted under the DIP in the preceding financial year, and also a report on the operation of the DIP;
- (d) a Design Advisory Panel comprising designers, industrialists and academics of various design disciplines will be set up. The Design Advisory Panel will give expert advice on proposal and vet the business plan submitted by DIP applicants. They will be required to give written reports for consideration by the Design Admission Panel (Note 7). They will also comment on the competency of the core members of the applicants; and
- (e) the Design Admission Panel will review the criteria for admission to the DIP, make recommendations to the HKSTPC to ensure the effectiveness of the DIP, and approve applications for admission to the DIP, taking into account advice from the Design Advisory Panel.

Financial assistance for incubatees

5.5 Under the DIP, the following five categories of financial assistance are available to the incubatees:

- (a) **Rental.** A ready-to-use office is provided to each incubatee at a special rental package up to 1,200 square feet (sq. ft. — Note 8);

Note 7: *The Design Admission Panel comprised staff from the HKSTPC and the HKDC, representatives from related design institutions, and the business and industrial sectors.*

Note 8: *During the first year of the incubation period, the monthly rent for the first 800 of the 1,200 sq. ft. occupied by the incubatee is free. The rent for the remaining 400 sq. ft. is \$8.65 per sq. ft.. Rental for the second year is \$8.65 per sq. ft..*

- (b) **Promotion and development.** Incubatees may claim reimbursement for up to 75% of the expenses incurred on promotion and related matters;
- (c) **Operation.** Up to 50% of the general operating costs incurred by incubatees may be reimbursed;
- (d) **Technical and management matters.** Incubatees may claim reimbursement of up to 75% of the expenses incurred for consultancy services on technical and management matters. A mentorship programme (see para. 5.10) for incubatees is also provided under this category; and
- (e) **Training.** Up to 50% of the actual expenses incurred by incubatees on training can be reimbursed.

Within the first six months after admission to the DIP or before the first milestone assessment (see para. 5.27) is completed, incubatees are only entitled to rental assistance. Assistance under other categories will become available after the incubatees concerned have been assessed as progressing satisfactorily in their first milestone assessment by the HKSTPC (Note 9).

5.6 Each of the five assistance categories is also capped by a quantitative limit. For categories (b) to (e) in paragraph 5.5, certain flexibility is available to shift the financial assistance between the categories. Details of the financial assistance of the five categories are shown at Appendix B.

Audit observations and recommendations

Utilisation of rental assistance

5.7 Audit noted that the estimate that incubatees would receive financial support of up to \$500,000 was based on the assumption that they would occupy up to 1,200 sq. ft. office space once they were admitted. Audit's examination of the HKSTPC's records revealed that incubatees did not require such a large office. 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. (or about 46% of 1,200 sq. ft.).

Note 9: *In April 2008, it was agreed that milestone assessments for incubatees admitted after July 2008 should be carried out every four months.*

5.8 In this connection, Audit noted that at a meeting held in September 2006, members of the DSI Assessment Panel commented that incubatees might not be able to make full use of the rental assistance and recommended that the HKSTPC should look into the matter to see if any adjustment was needed. In response to Audit's enquiry, the HKSTPC advised that it was aware that incubatees' need for office space was less than that originally anticipated. The HKSTPC had therefore revised downwards the office space to 950 sq. ft. for 2006-07 and to 800 sq. ft. and 600 sq. ft. for 2007-08 and 2008-09 respectively.

5.9 In Audit's view, as incubatees' need for office space is far less than that originally anticipated, the HKSTPC should consider making necessary adjustments to the five categories of financial assistance, so as to ensure that the financial support would better meet the needs of incubatees. For example, the ceilings for categories of financial assistance other than rental assistance may be raised.

Mentorship programme

5.10 According to the DIP-MAA, the HKSTPC should offer a one-year mentorship programme, as part of the technical and management assistance to be provided to incubatees. Participation in the programme is on a voluntary basis. An incubatee who joins the programme will enter into a tripartite mentorship agreement with its mentor and the HKSTPC. He is expected to meet his mentor at least three times during the mentorship period and to inform the HKSTPC about the progress of the mentorship regularly.

5.11 Prior to August 2007, incubatees were responsible for the honorarium of \$3,000 payable to mentors. The payment could be treated as technical and management expenses. As such, up to 75% of the amount paid could be reimbursed. In August 2007, the HKSTPC decided that the full amount of the honorarium would be borne by the HKSTPC. The mentorship programme has since become a free service to incubatees.

5.12 Despite the fact that the mentorship programme was heavily subsidised (or free since August 2007), it was not very popular among incubatees. Audit's examination of the HKSTPC's records revealed that up to August 2008, only 9 (27%) of the 33 incubatees joined the mentorship programme.

5.13 Given that the mentorship programme is beneficial to incubatees, the HKSTPC should ascertain the reasons for the low utilisation of the mentorship programme, and take necessary action to encourage incubatees to participate in the programme.

Audit recommendations

5.14 **Audit has recommended that the HKSTPC should:**

- (a) **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; and**
- (b) **investigate the reasons for the low participation rate of the mentorship programme, and take necessary action to encourage incubatees to participate in the programme.**

Response from the Hong Kong Science and Technology Parks Corporation

5.15 The CEO, HKSTPC accepts the audit recommendations. He has said that the HKSTPC:

- (a) will revise the maximum office space allocation from 1,200 sq. ft. down to 800 sq. ft.. The reduction of maximum rental subsidy will be shifted to other subsidies effective from October 2008. While the total maximum subsidy remains the same (i.e. \$500,000), incubatees will have more flexibility in claiming subsidies under the DIP. Details will be sent to the ITC for approval; and
- (b) recently conducted a survey in August 2008 to investigate the reasons for low participation of the mentorship programme. It will, with agreement from participating incubatees and mentors, publicise success cases of mentorship to non-participating incubatees to encourage their participation.

Applications for admission

5.16 According to the DIP-MAA and the HKSTPC's guidelines, DIP applications should be assessed based on the following qualitative admission criteria:

- (a) quality, competence and motivation of the designers;
- (b) quality and competence of the management team;
- (c) business viability of the start-up venture;
- (d) innovative design potential;
- (e) contribution to the development of design industry in Hong Kong; and

- (f) drive and commitment of the start-up venture.

5.17 DIP application will be vetted by a member of Design Advisory Panel. The member's assessments and recommendations will be forwarded to the Design Admission Panel for consideration and approval. Once admitted, a licence agreement, which lists out the obligations of the incubatee, will be signed between the HKSTPC and the incubatee.

Audit observations and recommendations

Due diligence visits

5.18 It is stated in the HKSTPC's DIP guidelines that, as part of the application vetting process, the responsible HKSTPC staff should conduct a due diligence visit to the office of the DIP applicant to verify the information provided in the application (e.g. company size, scale of operations, product/service nature, and the company's development plan). After the visit, an evaluation report should be prepared and filed.

5.19 Audit's examination of the application records of the 33 incubatees revealed that no records/evaluation reports were kept to show that due diligence visits had been carried out. In response to Audit's enquiry, the HKSTPC explained that since November 2007, the HKSTPC staff responsible would interview DIP applicants at the InnoCentre. Due diligence visits would only be carried out in case of doubt.

Documentation of the evaluation of applications

5.20 At a meeting held in January 2007, the Design Admission Panel agreed that a marking sheet (with passing score set at 60 out of 100) should be used for facilitating panel members to assess the qualitative aspects of DIP applicants. For the period January 2007 to June 2008, 24 cases were approved. However, Audit found that the marking sheet had not been used in any of these 24 cases.

Conditional approval cases

5.21 According to HKSTPC's DIP guidelines, for conditional approval cases, the HKSTPC should notify the applicants, seeking further information to satisfy the concerns raised by the Design Admission Panel. Information obtained would be submitted to the Design Admission Panel at the next meeting. Once the Design Admission Panel is satisfied that all stated conditions are met, the HKSTPC would issue a confirmation letter of full approval to the applicant.

5.22 Up to June 2008, there were six conditional approval cases. Audit could not find any documentation showing that supplementary information was submitted to the Design Admission Panel to clarify the concerns raised by the Panel. However, confirmation letters of full approval were issued by the HKSTPC in two of these cases.

Application processing time

5.23 In May 2006, the HKSTPC committed that the DIP application process would be completed within 11 weeks. Guidelines issued by the HKSTPC also require that if an application cannot be completed within 11 weeks, documentation of the reasons must be kept.

5.24 From May 2006 to June 2008, the HKSTPC processed 50 DIP applications. Audit examined the records of all these 50 applications and noted that, in 11 (22%) cases, the processing time took more than 11 weeks. However, the reasons for taking longer time to process the applications were not documented. In response to Audit's enquiry, the HKSTPC informed Audit in September 2008 that fixing a date when all members of the Design Admission Panel, whose discipline was the same as the applicants, were available was difficult. The long time taken in all these cases was due to the non-availability of panel members.

Audit recommendations

5.25 **Audit has recommended that the HKSTPC should:**

- (a) **keep a proper record of the interviews and due diligence visits carried out;**
- (b) **ascertain the reason for not implementing the decision of using a marking sheet in assessing DIP applications, and take necessary follow-up action;**
- (c) **for DIP applications approved on a conditional basis, ensure that the Design Admission Panel is provided with the necessary supplementary information; and**
- (d) **ensure that the DIP application process is completed within 11 weeks in accordance with the HKSTPC's guidelines, and the reasons for taking longer time to process an application are properly documented.**

Response from the Hong Kong Science and Technology Parks Corporation

5.26 The CEO, HKSTPC accepts the audit recommendations. He has said that the HKSTPC:

- (a) will keep a proper record by revising the due diligence evaluation report format to capture the name of interviewers/interviewees and the date/time/venue of interview;
- (b) will seek the Design Admission Panel's formal decision as to the applicability of the original proposed quantitative marking sheet for assessing DIP applications;
- (c) has submitted all the collected supplementary information on previous conditional approval cases to the Design Admission Panel meeting held in September 2008. The HKSTPC will also provide the necessary supplementary information to the Panel for every conditional approval case in future; and
- (d) will in future record the reasons for taking longer time to process an application and will report to the Design Admission Panel for appropriate actions. He has also said that the long time taken to process the applications mentioned in paragraph 5.24 was mainly due to non-availability of panel members.

Monitoring the performance of incubatees

Milestone assessment

5.27 According to the DIP guidelines, incubatees admitted before July 2008 were assessed at six-month intervals. The assessment was to determine if incubatees were making satisfactory progress in meeting the milestones set out in their business plan. In case the HKSTPC considers that an incubatee is not making satisfactory progress at the first and second milestone assessments, the incubatee would be re-assessed within the next three months or be asked to withdraw from the DIP.

5.28 Milestone assessment is carried out mainly through interviews. Incubatees are required to submit a milestone assessment report before the interview, listing out the progress they made within the period (e.g. product development progress, usage of the DIP support services, headcount and sales revenue). Since October 2007, a standard milestone assessment form is used to record the assessment results.

5.29 Apart from carrying out half-yearly milestone assessment, the HKSTPC also requests incubatees to submit the following financial and management reports to facilitate its monitoring of incubatees' progress:

- (a) annual audited accounts/financial statements within three months after the end of each financial year; and
- (b) a monthly report within one week after the end of each calendar month.

Audit observations and recommendations

Milestone targets

5.30 Audit randomly selected five DIP applications submitted, and examined the milestones set out in the business plans submitted therein. Audit noted that the milestone targets set out by incubatees were often non-quantitative, which did not facilitate progress assessment or benchmarking (see Examples 1 and 2).

Example 1

1. Companies A, B and C were fashion design companies which were admitted as incubatees under the DIP.

2. **Company A.** In its business plan, the target set for product development (for its first, second and third six-month milestones) was as follows:

“evening and bridal wear, hi-end casual wear, styling jobs, design product/service for companies – menswear/ladieswear”.

3. **Company B.** The targets set for product development in its business plan were as follows:

- (a) for the first six-month milestone: development;
- (b) for the second six-month milestone: developing and market testing; and
- (c) for the third six-month milestone: launch in market.

4. **Company C.** The targets set for product development were as follows:

- (a) for the first six-month milestone: develop three collections (around ten items), and develop sales distribution in London and Hong Kong;
- (b) for the second six-month milestone: develop three to four more collections (around 12 more items), and explore more distribution in Paris and Japan; and
- (c) for the third six-month milestone: develop three to four more collections (around 12 more items), and start brand building projects.

Audit comments:

5. The targets set for product development by Companies A and B were non-quantitative and did not show the progress to be made during the incubation period. In contrast, the targets set by Company C were quantitative and showed clearly the progress to be made. **Audit considers that the HKSTPC should urge DIP applicants to set quantitative milestone targets in their business plans.**

Source: HKSTPC records

Example 2

1. **Company D.** It was an overseas product design company. No target for product development was stated in the business plan submitted in its DIP application. Its business plan was considered by the Design Advisory Panel as “too broad and too general” and was difficult to assess.

2. Notwithstanding the Design Advisory Panel’s comments, the Design Admission Panel approved the application of Company D without requesting the company to set out more specific and clear milestone targets in its business plan.

Audit comments:

3. **Audit considers that the HKSTPC should ensure that milestone targets set out in the business plans submitted by DIP applicants are specific and clear.**

Source: HKSTPC records

Documentation of milestone assessment

5.31 According to the DIP guidelines issued by the HKSTPC, staff responsible for carrying out milestone assessment should record the assessment results in a standardised assessment form.

5.32 Audit examined 30 milestone assessment forms completed between October 2007 and June 2008. Audit noted that in 16 (53%) cases, although relevant figures shown in the assessment forms clearly showed that some of the milestone targets were not met, the HKSTPC staff still assessed that satisfactory progress was being made by the incubatees concerned (see Example 3).

Example 3

1. Company B set out in its business plan that cumulative sales revenue by the end of the 18th month of its incubation period should amount to \$1 million. The HKSTPC's records showed that the actual cumulative sales revenue was only about \$300,000 (i.e. 30% of the target). Despite the shortfall, the HKSTPC still considered the progress of the incubatee in sales revenue was satisfactory. There was no record documenting the justifications for the judgment.

2. Company D stated in its business plan that it would hire about three staff at the beginning of its incubation period. The number of staff hired would be five to seven by the end of the 18th month. The HKSTPC's records showed that the number of staff hired by Company D remained at four throughout its incubation period. Notwithstanding this, the HKSTPC still considered that Company D's progress in hiring staff was satisfactory.

3. Company E stated in its business plan that it expected its sales revenue would have a 10% growth in the second six-month period, and a further 15% rise in the third six-month period. Actual figures from the HKSTPC's records showed that sales of Company E for the first three six-month periods were about \$340,000, \$210,000 and \$233,000 respectively. In fact the sales revenue showed a decline over the period. However, the HKSTPC still considered that Company E was making satisfactory progress.

Audit comments:

4. **Audit considers that the HKSTPC should remind its staff to document the justifications for the judgements made in their milestone assessments, particularly in cases where incubatees fail to meet quantitative targets.**

Source: HKSTPC records

Supporting documents for milestone achievements reported by incubatees

5.33 To facilitate milestone assessment, incubatees are required to submit to the HKSTPC, before the assessment interview, a completed milestone assessment report including information about its activities in the past six months. The HKSTPC would discuss the milestone assessment report with incubatees to assess their progress.

5.34 Audit's examination of the 30 milestone assessment forms completed up to June 2008 revealed that, in 25 (83%) cases, there was no record showing that the HKSTPC staff had reviewed supporting evidence for the information provided in the milestone assessment forms. In response to Audit's enquiry, the HKSTPC explained that incubatees were requested to provide supporting documents for review during assessment interview.

However, the HKSTPC would not keep the documents to avoid leaking incubatees' confidential information. The HKSTPC would modify the milestone assessment form to include a checklist on supporting documents reviewed.

Submission of audited financial statements

5.35 An audit examination revealed that 18 (55%) of the 33 incubatees were admitted before April 2007 (i.e. they had been admitted for 15 months or more as at 30 June 2008). However, the HKSTPC's records showed that only six (33%) of these 18 incubatees had submitted their audited financial statements by 30 June 2008. Of these six incubatees, five took more than three months to submit their statements. The delays in submitting the statements ranged from five to nine months. Regarding the remaining 12 (67%) incubatees, the submission of their financial statements had already been overdue.

Submission of monthly progress reports

5.36 Apart from annual audited financial statements, an incubatee is also required to complete a monthly progress report within the first week of each month, which provides information about its success (e.g. awards received, patents filed, funding obtained, manpower growth and sales). Audit found that, up to June 2008, five (15%) of the 33 incubatees had not filed any monthly report to the HKSTPC. Details of the audit findings are shown in Table 10.

Table 10

Analysis of the percentage of omission in submission of monthly reports

Percentage of omission (%)	Number of incubatees
0	5 (15%)
1 — 19	3 (9%)
20 — 59	10 (31%)
60 — 79	8 (24%)
80 — 99	2 (6%)
100	5 (15%)
Total	33 (100%)

Source: Audit analysis of HKSTPC records

5.37 Table 10 shows that only five (15%) of the 33 incubatees managed to submit their monthly progress reports on time. The HKSTPC needs to remind incubatees to submit monthly progress reports in a timely manner.

Audit recommendations

5.38 **Audit has recommended that the HKSTPC should:**

- (a) **consider issuing guidelines to DIP applicants to help them set quantitative milestone targets in their business plans;**
- (b) **document the justifications for the judgements made in milestone assessments, particularly in cases where incubatees fail to meet quantitative targets;**
- (c) **ensure that adequate records are kept to document the review of supporting documents submitted by incubatees for the information provided in milestone assessment reports; and**
- (d) **remind incubatees to submit annual audited financial statements and monthly progress reports in a timely manner.**

Response from the Hong Kong Science and Technology Parks Corporation

5.39 The **CEO, HKSTPC** accepts the audit recommendations. He said that the HKSTPC will:

- (a) request the Design Advisory Panel to give guidelines to DIP applicants to help them set realistic quantitative milestone targets;
- (b) modify the milestone assessment form so that the assessor can fill in justifications for the judgments made;
- (c) modify the milestone assessment form to include a checklist on supporting documents to be reviewed; and
- (d) change the requirement for incubatees to submit the audited reports/financial statements 18 months after admission to the incubation programme. The HKSTPC will ensure that all incubatees submit monthly reports on time.

Disbursement of financial assistance

5.40 Audit selected a sample of 100 claims for reimbursement submitted by incubatees up to June 2008 for examination. The sample comprised 25 claims for each of the following four types of expenses:

- (a) training;
- (b) operation;
- (c) technical and management matters; and
- (d) promotion and development.

Audit observations and recommendations

5.41 Audit's examination of the 100 samples of claims for reimbursement revealed that there was room for improvement in the following areas:

- (a) ***Percentage of training expenses claimed.*** According to the DIP-MAA, each incubatee is allowed to seek reimbursement up to 50% of the actual training expenses under the DIP. The audit sample check revealed that 15 incubatees had mistakenly claimed 75% (instead of 50% in accordance with the DIP-MAA) of the training expenses they incurred during the incubation period. The total amount over-claimed was about \$41,000. In April 2008, these cases came to the notice of the ITC. In response to the ITC's enquiry, the HKSTPC agreed that the amount over-claimed would be borne by the HKSTPC;
- (b) ***Attendance records for training.*** Audit examined 25 reimbursement claims for training expenses and noted that no attendance records were submitted in 22 (88%) claims. In response to Audit's enquiry, the HKSTPC agreed that, as a good practice, incubatees should have been asked to produce attendance records to support their claims for reimbursement of training expenses; and
- (c) ***Supporting documents for operational expenses.*** According to the terms set out in the reimbursement form, original invoices, receipts or payment proofs should be submitted as supporting documents for reimbursement of operational expenses. Moreover, all supporting documents must bear the name and address of the incubatee concerned. If the incubatee cannot submit adequate supporting documents, the incubatee should be asked to make a declaration. Audit's examination of the 25 reimbursement claims for operational expenses revealed that in one case (4%), no receipt was submitted for a reimbursement of

\$140 expenditure. In seven (28%) other cases, some of the supporting documents (i.e. invoices) did not bear the names and addresses of the incubatees concerned. In two of these seven cases, no declaration was made by the incubatees stating that the expenses were incurred for their operational expenses.

Audit recommendations

5.42 **Audit has recommended that the HKSTPC should:**

- (a) **ensure the disbursements of financial assistances are made in accordance with the DIP-MAA, licence agreements and the HKSTPC's guidelines; and**
- (b) **ensure that sufficient and relevant supporting documents are submitted by incubatees in making claims for reimbursement.**

Response from the Hong Kong Science and Technology Parks Corporation

5.43 The CEO, HKSTPC accepts the audit recommendations. He has said that the HKSTPC will modify its guidelines and ensure that they are complied with.

PART 6: OVERSEAS PRACTICES IN THE PROMOTION OF DESIGN

6.1 This PART reports some of the good practices adopted by other countries in the promotion of design.

Government initiatives to promote design in Hong Kong

6.2 It has been the Government's policy to promote design in Hong Kong. The \$250 million DSI launched in June 2004 was the first Government design promotion initiative. Another initiative providing \$100 million to the HKDC to enhance its roles in promoting design was launched in the 2006-07 Policy Address. Over the past few years, some achievements have been made. These include:

- (a) *Organising the largest annual design event in Asia.* Since 2002, the HKDC has been holding the BODW event. In 2005 and 2006, some 50,000 attendees and visitors were attracted to the BODW conferences and shows, providing business matching opportunities between design professionals and SMEs of the region; and
- (b) *Organising various award schemes to commend achievements in design.* Some of the schemes have become prestigious recognitions in the design sector, such as the Design Leadership Award and the Design for Asia Award.

Use of design by other countries to enhance competitiveness

6.3 Audit noted that in recent years, many countries which are renowned for their design capability (such as Denmark, Finland, Korea, Singapore and the UK) have formulated national design policies and programmes to promote design. For example, the UK Department for Innovation, Universities and Skills published a White Paper entitled "Innovation Nation" in March 2008, listing out details of actions that the UK Government would carry out to promote design. In Korea, its Government has, since 1993, prepared a five-year plan for industrial design promotion.

Audit observations and recommendations

6.4 Audit notes that it is the policy of the Government to strengthen the support for design and innovation and to better harness the economic potentials of design. In the above-mentioned countries which are renowned for their design capability, some good practices have been adopted to promote design, as follows:

- (a) setting quantitative outcome targets on design promotion (see paras. 6.5 and 6.6);

- (b) leveraging on public-sector expenditure in promoting design (see para. 6.7); and
- (c) enhancing design education (see para. 6.8).

Audit considers that drawing on the experiences of these countries could further improve the effectiveness of the efforts put in by the Government for promoting design in Hong Kong.

Setting quantitative outcome targets on design promotion

6.5 The ITC has established a number of quantitative targets for the DSI. However, these targets are mainly output targets, such as the number of projects to be funded by the DSP funding schemes. While these targets are useful for measuring the progress of the DSI, they do not provide sufficient information for measuring the performance and evaluating the effectiveness of the DSI. Similarly, the performance targets and indicators adopted by the HKDC are also mainly output targets (e.g. the number of event participants and the target completion dates of the design directory and the resource centre). 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.

6.6 Audit noted that in some of the countries mentioned in paragraph 6.3, quantitative outcome targets were set for implementing their national design policies (see Examples 4 to 6).

Examples of quantitative outcome targets adopted by other countries

Example 4

Denmark

The following quantitative targets were set by the Danish Government in its five-year (1997 to 2002) plan to promote design in Denmark:

- (a) to increase the number of companies who agreed that design would affect the competitiveness of their new products from 62% to 80% by 2002; and
- (b) to increase the number of companies using design consultants in developing and designing new products from 30% to 50% by 2002.

Source: University of Art and Design, Finland

Example 5**Finland**

The following quantitative targets were adopted by the Finnish Government in its five-year (2005 to 2010) national plan:

- (a) 200 new enterprises would adopt design annually as part of their operations during 2005 to 2010;
- (b) 80% of companies would take design into account in their strategic planning by 2010;
- (c) 50% of the companies would take design into account in their business operations by 2010; and
- (d) 20 Finnish design companies would operate internationally by 2010.

Source: University of Art and Design, Finland

Example 6**Singapore**

Quantitative targets set by the Singaporean Government for promoting design in Singapore are as follows:

- (a) double the Gross Domestic Product contribution of the creative cluster from an estimated 3% in 2000 to 6% in 2012; and
- (b) to rank among the top 10 countries in global competitiveness rankings for design-related categories by 2012.

Source: Ministry of Trade and Industry, Singapore

Leveraging on public-sector expenditure in promoting design

6.7 According to a study commissioned by the Chancellor of the Exchequer of the UK Government in 2005, public-sector expenditure could have an influence on the business environment in encouraging or even demanding creativity. Audit notes that some countries have formulated programmes and policies to leverage on public-sector expenditure (e.g. Government procurement) in promoting design (see Examples 7 to 9).

**Examples of government initiatives
to leverage on public-sector expenditure in promoting design**

Example 7

UK

Building on the government procurement policy, the White Paper entitled “Innovation Nation” published by the UK Department for Innovation, Universities and Skills in March 2008 stated that all UK government departments and agencies would have to:

- (a) set out how they would embed innovation in their procurement practices; and
- (b) provide details of how they would seek to increase procurement of innovative products and services.

Source: Department for Innovation, Universities and Skills, UK

Example 8

Singapore

In order to promote the use of effective design by the public sector (e.g. in the design of public buildings, amenities and services), the Singaporean Government announced the Percent-for-the-Arts Scheme in 2002. Under the Scheme, 1% of the development budget was set aside for commissioning or procuring artworks. The Scheme was initially implemented in Singapore’s science park development. The Singaporean Government planned to extend the Scheme eventually to all public agencies.

Source: Ministry of Trade and Industry, Singapore

Example 9

Korea

In Korea, there is a scheme to award good design products. Products so awarded will carry a Good Design mark. Since 2002, the Korean Government’s procurement policy has been revised to offer preferential treatment to such products.

Source: Korea Institute of Design Promotion

Enhancing design education

6.8 A research on manpower conducted by the Hong Kong Polytechnic University in 2007 found that local industries were frustrated that they were not getting designers with the skill levels that they needed. Audit notes that many countries are facing the same problem. The following are examples of policies implemented by some countries in recent years to address this issue.

Examples of government initiatives to enhance design education**Example 10****Korea**

The Korean Government has been embedding design in all levels of education in Korea, including:

- (a) lowering the starting age of design education to identify and educate design prodigies;
- (b) identifying and educating “star” designers to be globally acknowledged;
- (c) establishing each industry’s design education institutes;
- (d) offering industrial design education to art teachers in elementary, junior high and high schools;
- (e) educating professionals for design management; and
- (f) an e-Design Academy was created to meet the on-line education demand by business for design education and training.

Source: Korea Institute of Design Promotion

Example 11

Finland

The Finnish Government's policy to enhance design education in Finland was outlined in its design policy paper entitled "Design 2005! Programme", which stated that the Finnish Government would:

- (a) raise the standard of design education and business competitiveness for design professionals by increasing the number of tertiary-level designers; and
- (b) multi-disciplinary degree and research programmes linking design to other university programmes and research.

Source: Ministry of Education, Finland

6.9 Government's policy initiative on design can be implemented more effectively by focusing on the outcome of the various measures taken. In addition, because of changing circumstances, it is always desirable to see how other countries, which are renowned for their design capacity, respond to these changes by keeping in view developments in such countries.

6.10 In response to Audit's enquiry, the ITC informed Audit in September 2008 that it had been making efforts to keep in view overseas developments in the promotion of design. Some examples are as follows:

- (a) senior officials of the ITC undertook overseas duty visits to keep posted of overseas development and experiences in design promotion. In 2007, the Deputy Commissioner for Innovation and Technology visited Italy and in 2008, the Commissioner for Innovation and Technology visited the Netherlands. Both were partnering countries in the BODW for the respective years;
- (b) the three-year business plan prepared by the HKDC's senior consultant in 2006 had drawn reference to overseas developments and suitably adapted some prevailing concepts and themes (e.g. service design) into the plan;
- (c) the HKDC commissioned a research study on creative economy and the role of education which provided case study of three foreign countries, namely Finland, Spain and Korea. The HKDC also held a follow-up forum in July 2008 on "*From Creative Industry to Creative Economy: The Role of Education*" with stakeholders including representatives from related policy bureaux; and

- (d) the ITC co-organised with the Efficiency Unit and the HKDC, and provided input to the March 2008 Public Sector Reform Conference in which there was a half-day session on design and branding. Overseas speakers were invited to share why the public sector should be concerned about design, and trends and essentials in public service branding. Overseas cases and developments were shared at that session.

Audit recommendations

6.11 **Audit has recommended that the Commissioner for Innovation and Technology should:**

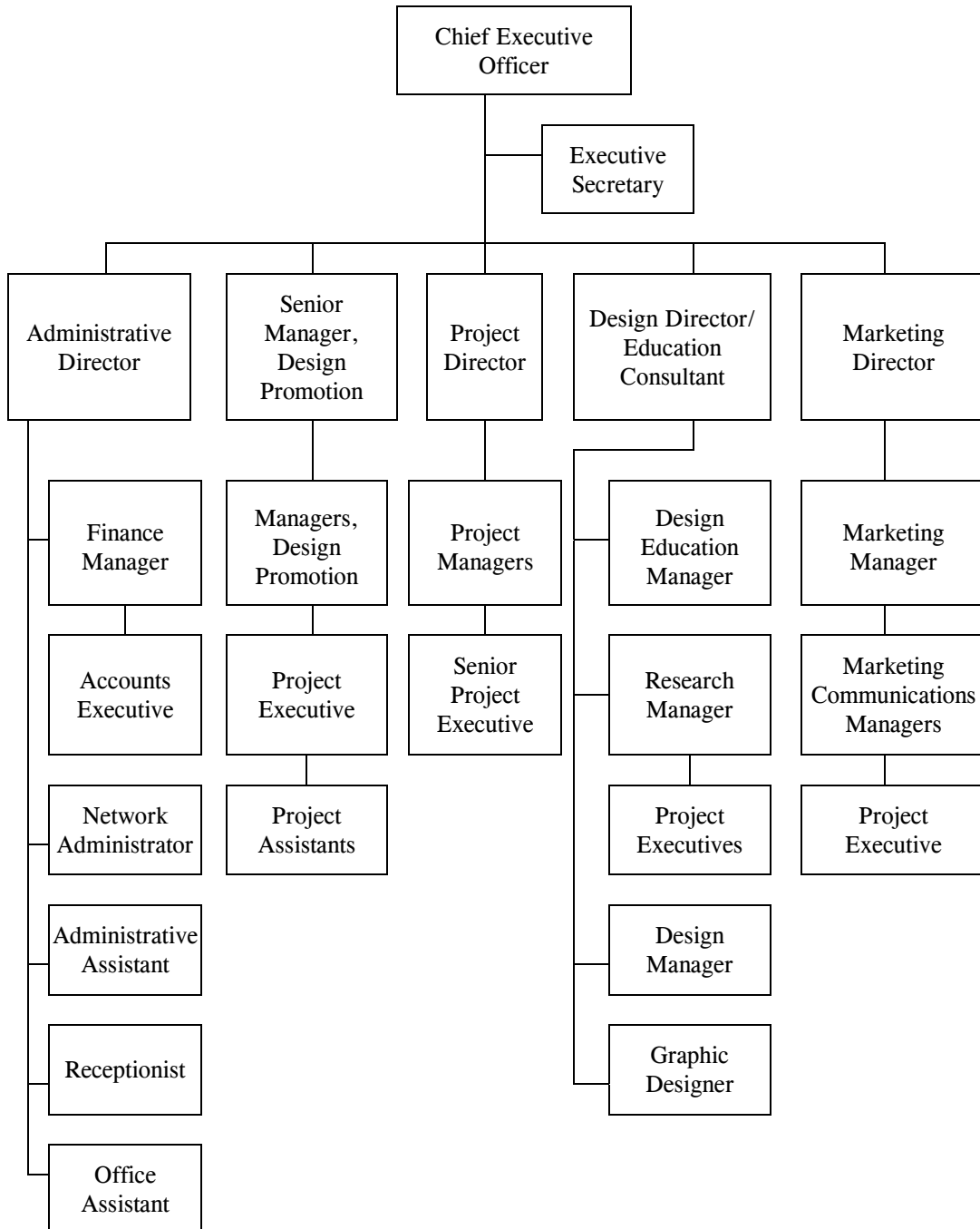
- (a) **consider setting more quantitative outcome targets for measuring the performance and evaluating the effectiveness of the DSI; and**
- (b) **keep in view overseas developments in the promotion of design, in order to identify good practices for adoption in the further development of design promotion in Hong Kong.**

Response from the Administration

6.12 The **Commissioner for Innovation and Technology** accepts the audit recommendations. He has said that the ITC will:

- (a) consider setting more quantitative outcome targets for measuring and evaluating the effectiveness of the DSI, and will explore the possibility of engaging a consultant to work out suitable targets and methods/indicators for measuring performance and evaluation of effectiveness of the DSI; and
- (b) make reference to overseas experience in the further development of design promotion in Hong Kong.

**Hong Kong Design Centre
Organisation chart
(30 June 2008)**



Source: HKDC records

**Limits of the financial assistance of the five categories
under the Design Incubation Programme**

Category of assistance	Maximum limit		
(a) Rental	\$307,200		
(b) Promotion and development	\$160,000	Combined limit: \$175,000	Joint limit: \$212,000
(c) Operation	\$60,000		
(d) Technical and management matters	\$31,000	Combined limit: \$37,000	
(e) Training	\$24,000		
Maximum ceiling			

Source: ITC records

Acronyms and abbreviations

Audit	Audit Commission
BDC	Business Development Committee
Board	Board of Directors
BODW	Business of Design Week
CEO	Chief Executive Officer
DBCS	Design-Business Collaboration Scheme
DIP	Design Incubation Programme
DIP-MAA	Memorandum of Administrative Arrangements for the Design Incubation Programme
DRS	Design Research Scheme
DSI	DesignSmart Initiative
DSP	Design Support Programme
FAC	Finance and Administration Committee
GSS	General Support Scheme
HAB	Home Affairs Bureau
HKDC	Hong Kong Design Centre
HKSTPC	Hong Kong Science and Technology Parks Corporation
ITC	Innovation and Technology Commission
MOU	Memorandum of Understanding
PCES	Professional Continuing Education Scheme
SME	Small-and-medium-sized enterprises