

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

## ADMINISTRATION OF THE DESIGNSMART INITIATIVE

### Summary

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

#### Management of projects funded by the Design Support Programme

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

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

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

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

#### **Promotion of design by the Hong Kong Design Centre**

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

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

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

## Corporate governance and administration of the Hong Kong Design Centre

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

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

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

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

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

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

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

#### **Administration of the Design Incubation Programme**

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

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

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

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

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

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

#### **Overseas practices in the promotion of design**

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

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

#### **Response from the Administration, the HKDC and the HKSTPC**

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

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