INNOVATION AND TECHNOLOGY FUND: MANAGEMENT OF PROJECTS

Executive Summary

1.   Innovation and technology are drivers of economic development and competitiveness.   The Government attaches great importance to the significant contribution of innovation and technology to the development of Hong Kong's economy and industries. It launched the Innovation and Technology Fund (ITF) in November 1999 to provide funding support for research and development (R&D) projects that contribute to innovation and technology upgrading in manufacturing and service industries. Up to 30 June 2013, approved ITF project funds amounted to $7.5 billion.   The ITF has four programmes, namely the Innovation and Technology Support Programme (ITSP), the Small Entrepreneur Research Assistance Programme (SERAP), the University-Industry Collaborative Programme and the General Support Programme. ITSP and SERAP projects had accounted for 90% of the ITF funds.   The former provides funding for comparatively larger applied R&D projects while the latter provides dollar-for-dollar matching grants to small, technology-based and entrepreneur-driven companies.   In April 2006, the Government established five R&D centres to coordinate R&D efforts in selected technology focus areas.   The Innovation and Technology Commission (ITC) is responsible for administering the ITF.   This includes processing applications of R&D projects under the ITF, disbursing funds to successful applicants, and monitoring the progress and achievements of the approved projects.

2.   The Audit Commission (Audit) has recently conducted a review of the ITF.   The audit findings are contained in two separate Audit Reports: (a) ITF: Overall management (Chapter 9 of the Director of Audit's Report No. 61); and (b) ITF: Management of projects (the subject matter of this Audit Report).

Processing of ITSP applications

3.   *Assessment mechanism and framework.* Applications falling within the technology focus areas of R&D centres are vetted by the centres while other applications are vetted by the ITC. All applications will be further checked by the ITC for completeness of information and compliance with the relevant ITC guidelines. Applications are assessed under seven components, including innovation and technology component, technical capability and realisation/commercialisation. Audit noted that: (a) the ITC did not set a passing mark for applications vetted by the ITC, and the R&D centres adopted different practices in setting passing marks; and (b) both the ITC and the R&D centres did not identify and set a passing mark for key assessment components failing which would lead to rejection of a project proposal (paras. 2.6, 2.11, 2.14 to 2.18).

4.   *Processing time*. Audit analysed the processing time for applications of ITSP projects approved in the period from January 2011 to June 2013, and found that: (a) for applications of Tier 1 projects (monitored by the R&D centres), the average combined processing time taken by the R&D centres and the ITC ranged from 158 to 222 days. The overall average processing time was 192 days; and (b) for applications of Tier 2 projects and Tier 3 projects (overseen directly by the ITC), the average processing times were 257 and 162 days respectively. Given the rapid development of innovation and technology and keen competition in the industry, long processing time might dampen the interest of researchers, discourage support of the industry, delay the commercialisation of deliverables, and choke the advancement of innovation and technology. The long processing time needs to be shortened so that the R&D project work can commence earlier (paras. 2.3, 2.23 to 2.26).

5.   *In-kind sponsorship.* For the period from 2006-07 to 2012-13, the R&D centres received $75.4 million in-kind sponsorship for their projects. Industry sponsorship constituted a large percentage of project costs for collaborative projects. However, the ITC has not promulgated detailed guidelines on valuation of in-kind sponsorship (paras. 2.30 and 2.32).

Monitoring of ITSP projects

6. ***Submission of reports and audited accounts.*** Applicants of ITSP projects have to submit to the ITC for approval: (a) half-yearly Progress Report within one month from the end of the period covered by the Report; (b) Final Report within two months after project completion; (c) annual audited accounts within three months after the end of the financial year; and (d) final audited accounts within three months after the project completion date. Audit analysed the submission of the Reports and accounts for the period from April 2006 to June 2013 and found that a large percentage of the Reports and accounts were submitted late (paras. 3.2, 3.4 to 3.8).

Processing of SERAP applications

7. ***Checking of applications.*** A company is eligible to apply for funding support from SERAP if it is incorporated in Hong Kong under the Companies Ordinance (Cap. 32), has less than 100 employees in Hong Kong, is not a large company, and is not a subsidiary of or significantly owned/controlled by a large company. The ITC only verifies the first eligibility criterion. For the other three criteria, the ITC relies on the information provided by the applicant without requiring the submission of any supporting documents. Audit examined 26 projects approved in 2011-12 and 2012-13. Audit noted that on average, 62% of the total project expenditure was on manpower. However, there were cases with large variations in the monthly salaries of similar proposed project posts, and cases where the applicants did not state the minimum qualifications/experience required of the posts in the budgets (paras. 4.8, 4.10 and 4.11).

Monitoring of SERAP projects

8. ***Helping applicants.*** Audit noted that the percentage of SERAP applications withdrawn was high and increasing, partly due to the applicants' misunderstanding of the assessment process and criteria. Furthermore, the approval rate of SERAP applications was low and declining. Unsuccessful applicants were only briefly informed of the reasons why their applications were not successful. They were not informed of their specific shortcomings or the comments made by the SERAP Project Assessment Panel (paras. 4.18 and 4.19).

9.   ***Submission of Progress Reports and Final Reports.*** The ITC required the recipient companies to submit half-yearly Progress Reports and a Final Report after the completion of the project. For the period from 2008-09 to 2012-13, 287 Progress Reports and Final Reports were due for submission. Of these 287 Reports, 183 (64%) were submitted late. The average delay was 95 days (paras. 5.15 and 5.16).

10.   ***Site visits.*** The ITC's Operation Manual requires that site visits to all the recipient companies should be conducted once every six months to assess their progress and check compliance with the terms in the Fund Agreement. The ITC had not issued detailed guidelines setting out the items to be checked or discussed during site visits, and the reporting requirements for documenting the visits (para. 5.19).

11.   ***Projects not proceeded to Phase II.*** Prior to April 2008, each SERAP project had to be carried out in two phases. The two-phase system was changed to a single-phase one because the ITC considered that the system had drawbacks. For two-phase projects, the Fund Agreement stated that if the recipient company and the Government were unable to reach an agreement for Phase II by a prescribed date after the completion of Phase I, the company should refund to the Government all payments made to it unless it was the Government's discretion not to proceed with Phase II (i.e. the ITC rejected the application for Phase II). There were 72 such cases (which involved total SERAP fund of $23 million) and the ITC had not received such refund. Audit examined five cases and noted that the ITC had not taken adequate and timely follow-up action to recover SERAP fund made to the projects. These funds may have become irrecoverable due to the long lapse of time (paras. 5.25 to 5.28).

Audit recommendations

12.   **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Commissioner for Innovation and Technology should:**

Processing of ITSP applications

(a)   **consider setting an overall passing mark on ITSP applications (para. 2.21(a));**

(b)   **consider identifying the key assessment components, failure to achieve the passing marks of which would render an ITSP application not be supported (para. 2.21(b));**

(c)   **review the procedures of processing ITSP applications with a view to finding out the reasons for the long processing time and identifying room for improvement (para. 2.27(a));**

(d)   **promulgate guidelines on the valuation of in-kind sponsorship to ensure that the assessed value is well supported by evidence from independent parties (para. 2.33(a));**

Monitoring of ITSP projects

(e)   **regularly remind the lead applicants of the need to comply with the submission requirements relating to Reports and audited accounts (para. 3.10(a));**

(f)   **follow-up closely with the lead applicants of overdue cases with a view to expediting the submission of Reports/audited accounts (para. 3.10(b));**

Processing of SERAP applications

(g)   **take necessary action to verify the eligibility of the applicants and information relating to the project teams (para. 4.15(a));**

(h)   **ensure that the applicants state in the project budgets the minimum qualifications/experience of project staff to be hired (para. 4.15(b));**

(i)   **issue guidelines to ITC staff and assessors of the SERAP Project Assessment Panel to facilitate their assessment on the reasonableness of the salary levels of the project staff stated in the project budgets (para. 4.15(c));**

(j)   **consider publishing commonly made mistakes and shortcomings in the SERAP applications on the ITF website to help the prospective applicants (para. 4.20(c));**

Monitoring of SERAP projects

(k)   **closely monitor the progress of the SERAP projects and take measures to ensure that recipient companies submit Progress Reports and Final Reports in a timely manner according to the reporting schedule set out in the Fund Agreement (para. 5.17(a)); and**

(l)   **conduct a review of the 72 projects which did not proceed to Phase II to ascertain whether the SERAP fund disbursed to them should be recovered (para. 5.30(b)).**

Response from the Administration

13.   The Commissioner for Innovation and Technology welcomes the value for money audit of the ITF and agrees with the audit recommendations.