

HONG KONG ARTS FESTIVAL SOCIETY LIMITED

Executive Summary

1. The Hong Kong Arts Festival Society Limited (HKAFSL) is a non-profit-making organisation. It was established in 1972 under the then Companies Ordinance (Cap. 32) as a company limited by guarantee. The mission of HKAFSL is to present an annual arts festival (i.e. the Hong Kong Arts Festival — HKAF) of the highest artistic standard. In February 2019, HKAF entered into its 47th event. According to HKAFSL, HKAF has over the years become a major international arts festival. The festival includes arts programmes in different genres of performing arts, outreach and other arts education programmes conducted in community locations to promote arts appreciation and enhance engagement between artists and audience, and the Young Friends Scheme (YFS). Under YFS, full-time students of local secondary schools and tertiary institutions aged 25 or below are eligible to apply for membership (a YFS member is entitled to a total of two tickets for HKAF performances, rehearsals or arts programmes exclusively for YFS members).

2. HKAFSL is governed by an Executive Committee. Day-to-day operation of HKAFSL is under the management of an Executive Director. As at 31 December 2018, HKAFSL had a total of 58 staff (i.e. the Executive Director plus 57 other staff). In 2017-18, HKAFSL had a total income of \$127.7 million and a total expenditure of \$126.1 million. Of the total income, \$39 million was government subventions. The Leisure and Cultural Services Department (LCSD) oversees the government subventions provided to HKAFSL. The Audit Commission (Audit) has recently conducted a review of HKAFSL.

Programme management

3. *Procurement of goods and services.* HKAFSL procures goods and services (e.g. materials for setting up stages, and services of programme crews) for the production of arts programmes. According to HKAFSL's procurement guidelines, at least 2 quotations should be obtained for expenses between \$5,000 and \$25,000, and at least 3 quotations should be obtained for expenses above \$25,000. Audit examined

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15 cases of procurement of goods and services in 2017-18 and found that (paras. 2.6 and 2.7):

- (a) in 2 cases (with expenses of \$6,144 and \$21,000), the required number of quotations had not been obtained (para. 2.7(a));
 - (b) in the 15 cases, there were 13 types of goods and services procured. Of these 13 types, supplier lists had not been maintained for 3 types of goods and services (para. 2.7(b)); and
 - (c) to achieve best possible value for money, the Government obtains more quotations than HKAFSL does for purchases with an amount of more than \$50,000 (i.e. the Government obtains at least 5 quotations) (para. 2.7(c)).
4. ***Management of programme crews.*** Programme crews are freelancers who provide services in the production of arts programmes (para. 2.10):
- (a) ***Room for better control on the use of manpower resources.*** Audit examined the number of programme crews commissioned for the 42 arts programmes staged in 2018 (i.e. 2018 programmes). Audit found that the manpower resources deployed to the programmes were very different. According to HKAFSL, this was the best judgement of the responsible staff. However, HKAFSL records did not document that such a judgement had been subjected to supervisory scrutiny. There was a risk that the manpower resources had not been optimally used. There is room for HKAFSL to enhance its documentation on the use of manpower resources (e.g. keeping the use of manpower resources under supervisory scrutiny and documenting such scrutiny) (paras. 2.2 and 2.12); and
 - (b) ***Need to enhance documentation on payment of service fees.*** Programme crews are paid by the hour or session. For calculation of service fees, HKAFSL maintains a list of standard wage rates (per hour or per session) for different types of programme crews. Audit examined the service fee payments to 15 programme crews who were commissioned for the 2018 programmes and found that (paras. 2.13 and 2.14):

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- (i) a programme crew was paid for work under two different programmes simultaneously on one day in March 2018 (para. 2.14(a));
- (ii) the payments for 6 programme crews were in excess of the hours actually worked on a day in March 2018 (i.e. each worked 2.5 hours but was paid 4 hours) (para. 2.14(b)); and
- (iii) the service fee paid to a programme crew in March 2018 was calculated based on a wage rate higher than the standard rate (para. 2.14(c)).

Upon enquiry, in February and March 2019, HKAFSL provided Audit with further information which helped explain the above payments. However, such information had not been documented in records which supported the payments or, whilst documented, the records did not indicate that the information was the “justification” for the payment. Audit further noted that HKAFSL had not signed any service agreements stipulating the terms of engagement with the 15 programme crews (paras. 2.15 to 2.17).

5. ***Ticketing matters.*** In May 2018, HKAFSL reported to LCSD that, for the 46th HKAF in 2018, the total number of paid audience was 105,034, and that the attendance rate was 92% (para. 2.21):

- (a) ***Need to improve the reporting of attendance.*** According to HKAFSL, attendance rate is calculated by applying the formula: “number of paid audience” ÷ “number of tickets available for sale” × 100%. Audit noted that (para. 2.22):
 - (i) ***Complimentary tickets should have been excluded.*** According to the funding and service agreements (FSAs) signed between HKAFSL and LCSD, the number of paid audience should exclude all complimentary tickets. However, HKAFSL reported the number of paid audience in the 46th HKAF in 2018 as 105,034, which included 708 complimentary tickets provided to press media and guests. The number of paid audience should be 104,326 (i.e. 105,034 less 708) and, accordingly, the attendance rate for the

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arts programmes should be 91% instead of the 92% reported (para. 2.22(a)); and

- (ii) ***Audience attending other programmes were included.*** Included in the number of paid audience (i.e. 104,326 — see (i) above) were 2,960 paid audience who were not audience of HKAF arts programmes. These 2,960 people were paid audience of an HKAF outreach programme. Inclusion of these 2,960 people might not be proper (para. 2.22(b)); and

- (b) ***Need to better account for blocked seats.*** According to HKAFSL, blocked seats refer to seats reserved for specific purposes (e.g. for setting up control panels and for use by HKAFSL staff on duty at performance). Audit found that, for the 2018 programmes, 4,506 of the 21,746 blocked seats had subsequently been released. However, the FSAs did not specify any requirements about the use of blocked seats by HKAFSL. HKAFSL also has no written guidelines on blocked seats (e.g. the number of seats to be blocked, their designated purposes and when they should be released). It was therefore uncertain whether all blocked seats that could be released by HKAFSL had been released, or whether some seats had been blocked unnecessarily (paras. 2.24 and 2.27).

Funding of the Hong Kong Arts Festival Society Limited

6. ***Income of HKAFSL.*** The three key sources of income of HKAFSL are sponsorship/donations, government subventions and income from ticket sales (para. 3.2):

- (a) ***Need to monitor the use of subventions by HKAFSL.*** According to HKAFSL, heavy reliance on sponsorship/donations may put sustainability of HKAFSL at risk as this income stream is dependent on many factors outside HKAFSL's control. According to the Home Affairs Bureau (HAB — the policy bureau of LCSD), it is the policy of HAB to encourage all arts groups/organisations to solicit more private sponsorship/donations and build up their audience base. Nevertheless, in March 2019, HAB informed Audit that from 2019-20, subject to the passage of the Appropriation Bill 2019 by the Legislative Council, LCSD will increase the recurrent subvention to HKAFSL. For the five years from 2018-19, LCSD will also provide an additional one-off funding each year to HKAFSL with specific

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policy intent (e.g. to groom local artists). LCSD will also review the effectiveness of the five-year funding. The LCSD needs to ensure that the review of the effectiveness of the five-year funding is carried out in a timely manner. It also needs to continue to monitor the use of government subventions by HKAFSL to ensure that HKAFs are delivered in accordance with FSAs (paras. 3.4 to 3.6); and

- (b) ***Some relevant factors not taken into account when setting ticket prices.*** According to HKAFSL practice, in setting ticket prices for HKAFs, it takes into account various factors (e.g. buying power/habits of different types of audience, audience satisfaction and venue locations, and popularity of programmes and venues). However, HKAFSL has not set any target proportion of costs to be recovered through ticket sales. HKAFSL's expenditure recovered through ticketing income dropped from 39% in 2013-14 to 30% in 2017-18. Moreover, while HKAFSL provides discounted tickets (50% discount on original ticket prices) to full-time students and people with disabilities, no similar concessions are available to senior citizens (paras. 3.7 and 3.8).

7. ***Conditions of subvention.*** LCSD enters into FSAs with HKAFSL on the government subventions (para. 1.11). Audit found that HKAFSL and LCSD need to better observe conditions of subvention:

- (a) ***Need for HKAFSL to better observe conditions of subvention.*** HKAFSL is required to observe the conditions of subvention stipulated in FSAs (para. 3.13):
- (i) ***Need to maintain records of consultation with the Government on selecting the Chairman of the Executive Committee.*** According to FSAs, HKAFSL needs to consult the Government in advance in each and every selection of the Executive Committee's Chairman. Audit noted that, while there were changes of Chairman of the Executive Committee in 2012 and 2015, there were no records of advance consultation with the Government. Upon enquiry in February 2019, HKAFSL informed Audit that it had verbally consulted the Government representatives in advance on both occasions (para. 3.13(a)); and

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- (ii) ***Need to submit reports in a timely manner.*** According to FSAs, HKAFSL was required to submit reports/accounts (referred to as reports) to LCSD by specified dates each year. Audit found that the number of reports submitted after the deadlines increased from 1 in 2013-14 to 3 in 2017-18 (para. 3.13(b)); and

- (b) ***Need for LCSD to better oversee government subventions to HKAFSL.*** LCSD is responsible for overseeing the government subventions provided to HKAFSL (para. 3.14):
 - (i) ***Need to better ensure timely submission of reports.*** In 2013-14 to 2017-18, of the 26 reports required to be submitted to LCSD, 13 (50%) reports were submitted after the deadlines. Of these 13 reports, for 4 reports, 7 to 112 days had elapsed before LCSD's follow-up actions. For the remaining 9 reports, LCSD records did not indicate that LCSD had taken any follow-up actions (para. 3.14(a));

 - (ii) ***Need to maintain proper records of report submission.*** In 2013-14 to 2017-18, for 4 reports, LCSD could not locate the reports for Audit's examination. Moreover, for three years 2013-14 to 2015-16, LCSD did not record the dates of HKAFSL's submission of audited accounts. LCSD took the dates of signing the accounts by HKAFSL's auditor as the submission dates (para. 3.14(b)); and

 - (iii) ***Need to set more appropriate expected levels of performance.*** For each performance indicator in FSAs, an expected level of performance was set by LCSD in consultation with HKAFSL. In 2013-14 to 2017-18, the expected levels of performance were not met on 6 occasions (involving 6 indicators). LCSD records indicated that when HKAFSL did not attain an expected level in a year, the expected level was lowered in the ensuing year. The lowered expected level would not be raised again, or sometimes would even be further lowered, even though HKAFSL outperformed the expected levels in subsequent years (para. 3.14(c)).

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Governance and administrative issues

8. **Governance issues.** The Executive Committee is the overall governing body of HKAFSL. As at 31 December 2018, HKAFSL had 10 Executive Committee members (paras. 4.2 and 4.3):

- (a) **Need to improve practices on declaration of conflicts of interest.** HKAFSL required every member of the Executive Committee and its supporting committees to sign an undertaking that, when he/she has a potential conflict of interest in a matter placed before the committees, he/she should make full disclosure of his/her interests, and that the undertaking should be signed upon joining the committees and, subsequently, after each annual general meeting. However, HKAFSL records indicated that in each year from 2014-15 to 2018-19, some members (35% to 54%) of the Executive Committee and its supporting committees did not sign the undertakings on declaration of conflicts of interest. Audit further noted that HKAFSL had not adopted a two-tier reporting system for the declaration of conflicts of interest (paras. 4.4 to 4.6); and
- (b) **Need to obtain prior endorsement for salary adjustment.** HKAFSL staff receive a monthly salary and may receive a year-end bonus. Each year, the Executive Director makes a proposal on a cost of living adjustment for monthly salary, and on the year-end bonus where appropriate. The proposal is submitted to the Finance Committee for discussion, and then to the Executive Committee for further discussion and endorsement. Audit noted that in 2015, details of the new salary scale had not been discussed and endorsed at Executive Committee meetings before the new salary scale was implemented (paras. 4.7, 4.8 and 4.10).

9. **Administrative issues.** As at 31 December 2018, HKAFSL had 58 staff, which comprised 18 (31%) permanent staff and 40 (69%) contract staff (para. 4.13):

- (a) **Need to take measures to address high staff turnover rate.** Audit analysed changes in the number of HKAFSL staff from 2016 to 2018 and noted that, in each year, 22% to 34% of staff left HKAFSL, and 29% to 51% of staff had newly joined HKAFSL for less than one year. High staff turnover rate is not conducive to operational efficiency and fulfilling the mission of HKAFSL (paras. 4.14 and 4.16); and

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- (b) ***Need to promptly report details about non-resident entertainers to the Inland Revenue Department.*** Every year, HKAFSL engages local and overseas artists to perform in HKAF. According to the Inland Revenue Ordinance (Cap. 112) and the Inland Revenue Department (IRD)'s information pamphlet, for a non-resident entertainer (i.e. overseas artist) (para. 4.17):
- (i) the sums received from performances in Hong Kong are chargeable to Hong Kong Profits Tax (para. 4.17(a)); and
 - (ii) the person who paid the sums (i.e. the Hong Kong payer) is responsible for completing the IRD's form "IR623 — Notification of Arrival in Hong Kong of Non-resident Entertainer(s)/Sportsmen" (the IR623 form) to provide details about the non-resident entertainer and report the gross amount payable to him/her. The Hong Kong payer should complete the IR623 form immediately when the non-resident entertainer arrives in Hong Kong (para. 4.17(b) and (c)).

Audit noted that as at 31 January 2019, of the 42 performance contracts of overseas artists engaged by HKAFSL for the 46th HKAF in 2018, for 29 (69%) performance contracts, the IR623 forms had not been submitted to IRD. In March 2019, HKAFSL informed Audit that it had submitted the outstanding IR623 forms for the 29 performance contracts in February and March 2019 (paras. 4.18 and 4.21).

Audit recommendations

10. **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 Executive Director, Hong Kong Arts Festival Society Limited should:**

- (a) **take measures to ensure that the quotation requirements as laid down in the HKAFSL's procurement guidelines are complied with (para. 2.8(a));**

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- (b) consider maintaining a supplier list for each individual type of goods and services (para. 2.8(c));
- (c) consider obtaining more quotations in procuring goods and services involving larger amounts and keep under review the need for setting a financial limit on procurement, exceeding which tender procedures have to be followed (para. 2.8(d));
- (d) take measures to enhance documentation on the use of manpower resources in the production of arts programmes (para. 2.18(a));
- (e) enhance documentation on the payment of service fees to programme crews (para. 2.18(b));
- (f) consider the need for signing service agreements with programme crews, having regard to the need for enhancing accountability and control on payment of service fees (para. 2.18(c));
- (g) clarify with LCSD the definition of paid audience and attendance rate and report accordingly to LCSD (para. 2.31(a));
- (h) draw up written guidelines on the use of blocked seats to ensure that the number of blocked seats is kept to a minimum and blocked seats are released as soon as possible and as far as possible (para. 2.31(b));
- (i) report to LCSD periodically information on blocked seats, including the number of seats blocked and the number of blocked seats subsequently released (para. 2.31(c));
- (j) taking into account all relevant factors, review the practices on setting ticket prices for HKAF programmes (para. 3.10);
- (k) maintain records of the consultation with the Government regarding the selection of the Chairman of the Executive Committee (para. 3.17(a));
- (l) step up efforts to ensure that reports are submitted to LCSD in a timely manner in accordance with FSAs (para. 3.17(b));

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- (m) remind members of the Executive Committee and the supporting committees to sign and submit undertakings on declaration of conflicts of interest (para. 4.11(a));
 - (n) consider adopting a two-tier reporting system for declaration of conflicts of interest (para. 4.11(b));
 - (o) seek the Executive Committee’s endorsement of the details of salary revisions in future (para. 4.11(c));
 - (p) take effective measures to address the high staff turnover rate, taking into account staff’s reasons for leaving HKAFSL (para. 4.22(a)); and
 - (q) ensure that IR623 forms are promptly submitted when non-resident entertainers arrive in Hong Kong (para. 4.22(b)).
11. Audit has *recommended* that the Director of Leisure and Cultural Services should:
- (a) specify in FSAs whether paid audience of programmes other than HKAF arts programmes should be included in the “number of paid audience” (para. 2.32);
 - (b) ensure that the review of the effectiveness of the time-limited subvention to HKAFSL is carried out in a timely manner (para. 3.9(a));
 - (c) continue to monitor the use of government subventions by HKAFSL to ensure that HKAFs are delivered in accordance with FSAs (para. 3.9(b));
 - (d) take follow-up actions on late submission of reports (e.g. ascertain why the reports are not submitted on time and urge for their timely submission) by HKAFSL (para. 3.18(a));
 - (e) maintain proper records of reports submitted by HKAFSL, including the date of submission (para. 3.18(b)); and

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- (f) **in consultation with HKAFSL, consider revising the expected levels of performance for indicators in FSAs, taking into account the actual performance results (para. 3.18(c)).**

Response from Hong Kong Arts Festival Society Limited and the Government

12. The Executive Director, Hong Kong Arts Festival Society Limited and the Director of Leisure and Cultural Services agree with the audit recommendations.