(Unclassified version with commercially sensitive or confidential information and Members' names removed)

F.C. 11/2014 (Revised)

Revised Minutes of the 51st Meeting of the Finance Committee held at 2:30p.m. on Tuesday, 22 July 2014 in the Board Room, 2nd Floor, HKPC Building 78 Tat Chee Avenue, Yau Yat Chuen, Kowloon

Present :	Chairman -	Mr. Victor Ng, MH
	Members -	Mr. Adolph Leung, JP (representing Mrs. Helen Chan, JP) Mrs. Agnes Mak Tang Pik-yee, MH, JP Dr. David Ng Tai-chiu Dr. Dennis Ng Wang-pun, BBS, MH Mr. Frank Tsang
In attendance:		HKPC Chairman - Mr. Clement Chen, SBS, JP

In attendance from HKPC :

Mr. Tony Lam	Director, Corporate Services
Mr. Joseph Poon	Director, Technology Development
Mr. Gordon Lo	Director, Business Management
Mr. Edmond Che	General Manager, Finance and Procurement
Ms. Lilian Ho	General Manager, Human Resources and Administration (item V only)
Mr. Alfonso Tam	Chief Manager, Council Secretariat
Ms. Gillian Luk	Senior Manager, Council Secretariat

Welcome

The Chairman welcomed Mr. Gordon Lo, Director, Business Management, (DB) who joined the meeting for the first time.

Confirmation of Minutes (F.C. 3/2014 Revised)

The Revised Minutes of the 50th Meeting of the Finance Committee held on 18 March 2014 had been circulated to Members and there were no further requests for amendments. The Revised Minutes were taken as read, confirmed and signed by the Chairman.

I. Revised Programme and Estimates of HKPC for 2014/15 (F.C. 4/2014)

1. Invited by the Chairman, said that the proposal to revise the 2014/15 Programme and Estimates had taken account of the following considerations:

(a) at the last meeting of the Finance Committee held on 18 March 2014, the Management agreed to review the long standing accounting practice on capital expenditure with HKPC's external auditor, PricewaterhouseCoopers (PwC), to see if it should be changed and whether there would be any subsequent financial impact on HKPC's accounts;

(b) at the same meeting, Members noted that a professional consultant was engaged to conduct an extensive survey on the HKPC Building and had advised that the financial requirement for all the required building maintenance work to be implemented over a 10-year period would be around $110.55M. The Management was requested to consider how to prioritize the major building maintenance work items and proper allocation of resources in the coming Programme and Estimates of HKPC;

(c) the finalized 2013/14 financial results afforded the opportunity for the Management to examine whether the various 2014/15 financial estimates, which had been approved by the Council in November 2013, had indeed been set at realistic levels and whether any of them should be reviewed and revised; and

(d) the healthy financial surplus in 2013/14 had enabled the Management to advance the procurement of the high precision 5-axis vertical machine in 2013/14, thus obviating the need to utilize $5M from HKPC's reserve in 2014/15 as approved by the Council in November 2013.

2. On the existing long standing accounting practice on capital expenditure, said that PwC had conducted a review during May to June 2014 and confirmed that the practice was still acceptable under current Accounting Standards. But given that the annual subvention to HKPC was a block grant without differentiation into revenue subvention and capital subvention, there was therefore no requirement to match capital subvention with committed cost of fixed asset. In order to better reflect HKPC's current operation, PwC advised the Management to apply current market practice to record capital expenditure based on delivery of fixed asset and charge related depreciation in the Income and Expenditure Account. proposed to implement this change with effect from 2014/15. Arising from this

change, the capital expenditure for 2014/15 would be reduced from $20.2M (based on committed cost of fixed asset) to $3.3M (based on delivery of fixed asset) in accounting terms and therefore the 2014/15 Programme and Estimates should be revised to reflect this change. This would not, however, affect the actual amount to be disbursed for procuring the planned capital equipment which would remain the same at $20M.

3. With regard to building maintenance, said that proposed to provide $25.4M in 2014/15 for overall building maintenance which also included the priority work items which we had identified from the consultant's findings and which had not been provided for in the original estimates for 2014/15. At the same time, following on a review of the 2014/15 estimates, the Management considered that the aim to achieve a ratio of project expenses to external income at 37% was not credible at all given that such expenses were still required by quite a lot of the technology-oriented projects. Meanwhile, the original target for value-added was overly stretched and might risk being too aggressive as it was 13% over that achieved in 2013/14 which already represented an accumulated increase of about 15% in the previous two years. The opportunity had also been taken to fine tune some recurrent expenditure items, for example, to reduce the estimate for staff emoluments (by around 1%).

4. said that under the revised 2014/15 estimates (summarized in paragraph 5 of the paper), the original estimate of external income at $384M would be maintained but total operating expenditure would be reduced by 1.4% from $419.59M to $413.92M. While value-added would come down to $232.21M from the original estimate, it was still higher than the actual value-added for 2013/14 by close to 8%. The revised budget was forecast to produce a budget surplus of $6.68M after expenditure for the ERP system maintenance, compared to $3M in the original estimates.

5. supported PwC's advice on applying the current market practice to record capital expenditure based on delivery of fixed asset and charge related depreciation in the Income and Expenditure Account. This had the effect of modernizing HKPC's accounting arrangements. said that this accounting practice would better reflect actual operation and it would also enable the Management to closely monitor the income and expenditure position of the different divisions.

6. In reply to , said that, purely for reference purpose, the Management could consider to prepare proforma accounts putting through these changes as prior year adjustments to HKPC's accounts for the past two to three years to provide a consistent

basis for comparison. commented that this should not be reflected as “real” prior period adjustments in the statutory accounts of HKPC as firstly it was not a change in accounting policies and secondly it was not a fundamental error. said that PwC had confirmed that there would be no prior year adjustment to speak of because the accounting arrangements used in previous years were valid.

7. In reply to , said that a schedule of the planned capital expenditure items would be provided when the proposed revised Programme and Estimates for 2014/15 was submitted for the Council’s approval.

8. Members also agreed that given the procurement of the 5-axis vertical machine ($5M) in 2013/14, it was no longer necessary to make such provision in the 2014/15 estimates.

9. Members endorsed for the Council’s approval the revised Programme and Estimates for 2014/15 at paragraph 5 of the paper. Upon the Council’s approval, the revised Programme and Estimates for 2014/15 would be submitted to the Innovation and Technology Commission (ITC) for approval by the Government.

II. Three-year Strategic Plan of HKPC for 2015/16 - 2017/18 (F.C. 5/2014)

10. introduced the paper and said that the existing strategic plan of HKPC was anchored on a four-pronged strategy focusing on scaling up platforms, creating value for SMEs, sharpening core competencies and developing strategic partnership. The Management had revisited the existing strategic plan and considered that the four-pronged strategy was still valid. then went on to brief Members on the major initiatives under the 2015/16 - 2017/18 strategic plan (paragraph 6 of the paper) which would be taken forward subject to the availability of resources. The various initiatives under the strategic plan had been considered and supported by the Business Development Committee (BDC) at its 54th meeting held on 15 July 2014. The Management would consider the necessity of revisiting the strategic plan during the year if there were any fundamental changes in the relevant macro environment to ensure that the plan was in line with Government policy.

11. As regards the exit plan, said that at this point, no services were planned for exit in the next three years. However, the Management would aim to withdraw from providing secretariat service to industry/trade associations in 2014/15. The planned withdrawal was necessary taking account of the impact of the amended Companies

Ordinance earlier this year which imposed more stringent requirements, and hence liabilities, on entities performing company secretariat functions. Withdrawal was also advisable given the availability of professional company secretary service providers in the market. Instead, we would provide technical and industry support focusing on HKPC's core competence, and licensee service which would meet the operation and business networking needs of the associations. But HKPC would steer clear of secretarial services and logistic and administrative support to non-business related functions (e.g. social/recreational events) of the associations.

12. Members endorsed for the Council's approval HKPC's Three-year Strategic Plan for 2015/16 - 2017/18 at Annex A of the paper.

III. Annual Accounts for the Year 2013/14 (F.C. 6/2014)

13. Invited by the Chairman to report, said that external income for the year was $374.5M which was higher than the budget by $6.2M or 1.7%. The income surplus came mainly from government funded projects ($26M) which was offset by the shortfall in consultancy projects ($10.9M), in-class training ($6.6M) and study missions ($2.6M). The value added was short by $15.4M against the budget. On the expenditure side, total expenditure came to $389.4M which was $19.5M or 4.8% less than the budget of $408.9M. Separately, the APAS R&D Centre Ltd. had merged with HKPC as the APAS Division since 1 November 2012. The operation of the APAS Division was separately funded by the Government. The financial result of the APAS Division in 2013/14 had been incorporated into HKPC's Annual Accounts for the same year.

14. In reply to , said that software was classified as intangible assets. Together with fixed assets, it was entered into the annual accounts under capital expenditure. advised that it should be ensured that intangible assets were uniformly entered into the annual accounts under capital expenditure.

16. referred to page 59 of the paper said that ideally the entries under the capital subvention fund should be itemized to give a clear picture. requested the Management to consider this presentation format in future.

17. In reply to , said that HKPC's cash in bank at any time included monies as working capital for HKPC's daily operation as well as cash advance for implementation of government projects. Hence, not all the cash in bank was funds with no immediate

use and could therefore be invested for financial returns.

18. In reply to , said that direct project expenses had come down quite substantially in the past two years. While staff were under instruction to continue to closely monitor and control direct project expenses, a certain level of such expenses was unavoidable or indeed be necessary especially for the larger and more complex technology development projects, including those under government funding schemes. In response, said that the ERP system together with the value-added approach to gauge performance should be gainfully employed as a standing mechanism to control direct project expenses and attain a healthy ratio of such expenses to project income.

19. Members endorsed for the Council's approval the Annual Accounts of HKPC for the year ended 31 March 2014 which had also been considered by the Audit Committee at its 30th meeting on 27 June 2014 with no major adverse comments.

IV. HKPC Standard Staff Rates for 2014/15 (F.C. 7/2014)

20. Members noted a high level review of the full costing structure conducted in 2013 which showed a substantial increase (about 40%) in the costing level on the assumption of nil subvention from the government. Members supported the Management's plan to conduct a detailed review of the overall costing structure in the first quarter of 2015 by which time more data over a sufficiently long period of time would basically be available from the new ERP system.

21. Members approved the proposed revised staff rates for 2014/15 under the current review mechanism as listed out at Appendix 1 of the paper.

V. Consultancy Study on HKPC Building Maintenance (F.C. 8/2014)

22. Invited by the Chairman, said that the HKPC Building had been in operation for more than twenty years. In September 2013, (the Consultant) was appointed through open tender to conduct an extensive study on the HKPC Building. The study report submitted by the Consultant suggested a series of works (paragraph 7 of the paper) in the coming ten years (2014 - 2023) with total costs estimated at $110.55M. The work items set out by the

Consultant had been examined and prioritized into top, medium and low priorities with regard to legal compliance, conformity to business requirements, preventive maintenance and safety enhancement for staged implementation. It was estimated that the total building maintenance financial outlay for the first three years would be about $25.41M, $24.4M and $21.6M for 2014/15, 2015/16 and 2016/17 respectively which also included the regular maintenance cost.

23. suggested to the Management that periodic house keeping and tidying exercises should be conducted so that space usage could be optimized for HKPC's operation needs and any unoccupied space could be exploited for their income potential at the earliest instance.

24. said that top priority should be given to E&M related repairs and upgrading to ensure safety. The Management should also ensure that the mandated regular examination of such systems by professional consultants was conducted to ensure full statutory compliance.

25. said that the Management should ensure that the necessary and adequate insurance coverage was in place during the works. It would also be advisable to build in some green features and advance technologies in the improvement works as HKPC was a leader in these fields and there was a role for HKPC to lead by example.

26. said that the Management was essentially dealing with a legacy issue and that the necessary works would need to be implemented progressively in a staged approach so that the normal operation of HKPC would not be unduly affected. A staged approach would also ensure close supervision of the works under implementation.

27. In reply to , said that breakdown of the building maintenance budget and work items for 2014/15 and the following two years would be provided in the paper on the Revised Programme and Estimates for 2014/15 when it was submitted to the Council.

28. Members noted and supported that resources be enhanced to augment the necessary building maintenance work.

VI. Financial Performance of HKPC for the First Quarter of 2014/15 (April-June 2014) (F.C. 9/2014)

29. Members noted that for the first quarter of 2014/15, HKPC's total fee income was $75.8M, which was less than the budget by $20.2M (or

21%) mainly due to less than budgeted income from consultancy projects, public training courses and study missions. Value added for the period was $14.4M less than the budget. Total expenditure was $92.1M, or 12.2% less than the budget, mainly on account of under expenditure in staff emolument, other fixed expenses and capital expenditure. Surplus for the period came to $0.9M (before expenditure for the ERP system maintenance and high precision 5-axis vertical machine) which was less than the budgeted surplus by $1.6M. Members also noted that during the period, the provision for staff annual leave was reduced by 6.6% to $17.5M in June 2014 compared to a year ago, and the number of staff annual leave days with financial implication was also reduced from 10,494 to 9,310, or by 11.3%.

30. said that staff should be reminded that project clients should be billed along the way of project implementation to facilitate early income realization. also said that, given the large number of projects in the pipeline, there should not be big variations in the level of income in an aggregate sense at the corporate level from quarter to quarter or from estimated amount to actual amount. In response, said that a policy on deposit and staged payment had already been adopted to ensure no negative cash flow during project implementation. also pointed out that as capabilities and skill sets across divisions were heterogeneous and not homogeneous, there was a limit to which capabilities and skill sets could be flexibly deployed from one business division to another. agreed with that the new ERP system would facilitate higher efficiency in billing and income realization for projects.

31. Members noted the financial performance of HKPC during the first quarter of 2014. Members also noted the financial performance of the APAS Division during the same period which was summarized under paragraph 8 of the paper.

VII. Quarterly Report on HKPC's Funds (F.C. 10/2014)

32. Members noted that as at 30 June 2014, HKPC's cash balance was $179M. Bank interest income in 2013/14 was $0.9M, representing an average return rate of 0.75%. Bank interest income in the first quarter of 2014/15 was $0.2M, representing an average return rate of 0.77%. Both return rates were higher than the average interest rate (around 0.01%) for savings account currently offered by the major banks in Hong Kong.

33. Members noted that the Management had already reviewed the Government's latest guidelines for investment of public funds. The guidelines put down comprehensive requirements to ensure safe and

proper investment options, including the need to establish a governing board and an investment committee to guide and monitor such investment regardless of the size of the investment. Given the relatively small amount of funds that HKPC could invest at any given time, the requirement might be too complicated to be worthwhile. The Management would consider further this issue and might have to relinquish establishing an investment framework.

VIII. <u>Any Other Business</u>

(A) Attendance Record of FC Members

34. <u>Members</u> noted their attendance record in 2014 tabled at the meeting.

IX. <u>Date of Next Meeting</u>

35. It was agreed that the date of the next meeting be scheduled on 18 November 2014 at 2:30pm.

36. There being no other business, <u>the Chairman</u> thanked Members for their attendance and the meeting was adjourned at 4:30pm.