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10 January 2014

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The Hon C Y Leung GBM GBS JP
Chief Executive
Office of the Chief Executive
Hong Kong

Dear Chief Executive

HKIoD's Submission on the 2014 Policy Address

The Hong Kong Institute of Directors ("HKIoD") is pleased to forward our views for your consideration in preparing the 2014 Policy Address.

HKIoD is Hong Kong's premier body representing professional directors working together to promote good corporate governance. We are committed to promoting director professionalism and good corporate governance, as well as contributing towards the formulation of public policies that are conducive to the advancement of Hong Kong's international status.

In relation to the 2014 Policy Address, we have conducted focused review by our Economics & Public Affairs Committee under the chairmanship of Prof Christopher To.

Thank you very much for your kind attention. Should you have any enquiries about our submission, we will be pleased to discuss with you.

With best regards

Yours sincerely
THE HONG KONG INSTITUTE OF DIRECTORS

Dr Carlye Tsui

Enc

cc: Dr Kelvin Wong, Chairman, HKIoD
Prof Christopher To, Deputy Chairman, HKIoD &
Chairman, Economics and Public Affairs Committee

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**HKIoD's recommendations
for
the Chief Executive's Policy Address
scheduled to be delivered on 15 January 2014**

As we turn into a New Year, we at the HKIoD do not see much change in the state of the SAR. With an ageing population, fewer people will be working to support a growing number of elder retirees. We therefore need more diverse an economy that yields ever higher value from a shrinking workforce. But if we are to develop our economy, to be and to remain competitive, we need to nurture homegrown talents as well as to attract expertise from abroad. If our talents are to stay, we need to keep up a pleasant livable place.

Unfinished business lingers on. Challenges continue to mount ahead. Society can debate the best policy measures to tackle the many livelihood issues still confronting us, but economic strength is the surest guarantee of sustained firepower. We need to grow the economy, and to do so we need to be and to remain competitive in light of the fierce competition from places around us. The difficult task remains: put ourselves back on course for growth, for development and for prosperity.

As the old saying goes, the younger generation today will indeed be the pillars of society tomorrow. The way Hong Kong is at the moment, the young generation easily find themselves being squeezed in the middle of many livelihood issues facing Hong Kong. The younger generation deserves help where due, but in our mind, the best surrogate to arrive at a good "youth policy" outcome is an effective economic development strategy. A more diversified economy will create more opportunities for them to construct their future.

We do have a manpower situation to worry about. We need to fill the many unfilled jobs, so labour shortage does not become an immediate choke on the economy. Over time, we need to shape up the workforce to go along with a Creative Economy that we ought to develop. Companies old and new can make good use of design to come up with innovative products and services that win customers. But it may be the case that design realises its true value when put into addressing societal challenges and instigating positive changes. Many of us will want to see our Government display more courage and determination to innovate and to create positive changes to redress the many livelihood issues facing us.

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Managing the economy

The macro-environment

Around the world, a retreat from several years of quantum easing is now imminent. The Government will have to assure Hong Kong people that it is prepared and ready to meet the challenge.

Refresh our tax system to keep us competitive

The availability of tax incentives and concessions has the effect of lowering the effective tax rates for businesses. This is an important factor for investment decisions. Our neighbouring jurisdictions are all competing with Hong Kong for investments, and they offer tax incentives and concessions in many forms and shapes to do so. This has dulled so much the Hong Kong

tax system's competitive edge. We repeat our call on the Government to review the tax regime and to add or augment tax incentives to better match business needs, to spur development.

The case for a tax policy unit

Demands of global economy and new realities stemming from evolving accounting standards should warrant not expedient and patchwork fixes, but strategic and holistic look at the tax rules to be sure they keep pace with developments and are attuned to how business is conducted in practice. There is a strong argument for and a practical need to have a high-level tax policy unit outside of the Inland Revenue Department to formulate tax policy that make us competitive. Separate the role of tax collector and tax policy-maker.

A more rounded financial centre

One would be hard pressed to disagree with the broad conclusions drawn in the various reports of the Financial Services Development Council. HKIoD has been on the side calling for the financial sector to be more rounded. It will be so if investors have the choice of a wider variety of investment tools and platforms, such as commodities, bonds and other debt instruments, venture capital, private equity and hedge funds. These developments in the financial sector can in turn support other industries which need greater wider sources of funds for growth and expansion.

To play its proper part as a major international financial centre, Hong Kong must keep up with the other major financial markets at efforts to improve banking and financial regulations. Nonetheless, the strive for market stability should not stifle quick response and action to hasten the pace at which new products are brought to the market.

Seizing opportunities

The Mainland Government is to embark on another round of reform to the economy and its financial industry. We see the establishment of free trade zones as one chance for Hong Kong to showcase its luster.

As the Mainland Government experiments with financial reform and RMB business in the Shanghai FTZ, the Chief Executive must bring Hong Kong influence to the table, such that the desirable development of the Shanghai market does not come at the expense of Hong Kong. The concept of a Guangdong-Hong Kong-Macao FTZ is another chance for us to shine once more. If that seems far away still, there is yet more room for the service sector to develop under the CEPA and Guangdong-Hong Kong cooperation framework.

We expect the Government to make good the effort spent on G2G external relationships and internal diplomacy to remove obstacles to market access. We know the Chief Executive is committed to helping Hong Kong people and Hong Kong business explore and enter the Mainland market. But he can also carry on the progress in another front, and make Hong Kong part of the ASEAN-initiated Regional Comprehensive Economic Partnership a reality.

Selling the Hong Kong brand, offering the excitement of a Hong Kong experience

We see merits in reviving high-value farming and fishery, to satisfy a growing appetite for safe and wholesome food and to add attractions for leisure travel. We see value in bringing back high-skilled manufacturing as part of a more diverse Creative Economy. But we know well Hong Kong has arrived at a post-industrial era where the service sector will be the biggest job creator. The service sector already accounts for over 90% of GDP, more than the

70% average among developed economies. In many areas the Hong Kong service sector is world-class.

A vibrant hospitality industry, can't-miss conventions and events, far-ranging offerings for a true culinary experience and a full menu for leisure options beyond shopping will help attract visitors and keep them here longer. When they are here, they can experience the personable service that Hong Kong can offer, something which will make sure they leave with a good impression.

Hong Kong also has service expertise to export. Our rail company changed to meet changing needs to give local riders an ever better experience, and is now bringing that experience to subway riders in far and away places.

When there is a desire, even obsession, to buy things in Hong Kong for their safety and reliability, we also have testing and certification expertise on offer so product safety in other places can be assured.

Shaping up the workforce

But for one reason or another, some of the service sectors that can make our economy stronger remain under-developed. Worse, some are in acute shortage of labour. Job vacancy is at its highest rate for two decades.

Wide spread importation may raise some eyebrows, but importing labour to fill jobs in specific sectors or for defined projects under strict criteria would seem a reasonable measure.

There is also the possibility of unleashing the untapped work force. To bring the latent work force into being active participants in the economy will require some better incentives. To entice the homemakers, we will need flexible work hours and better availability of high quality child care facilities near the workplace as an attractive alternative to hiring domestic helpers.

Some tweaking of social policy to delay the retirement age and some tweaking of business practices to result in more widespread adoption of flexible work arrangements may wrestle more workers out of retirement and attract some more to join or rejoin the workforce.

For the many workers now having to work longer hours, handle more tasks, and risk more mistakes and injury as a result of fatigue, we can give better incentives to businesses, especially the SMEs, to upgrade and improve work environment and equipment so we get better efficiency and improve safety.

While there are many job vacancies left unfilled, a good number of those available for hire cannot or simply just do not want to take up employment that may be on offer. The paradoxical manpower situation that we have is a worry. Shaping up the quality and supply of our workforce is critical if we are to aim for success.

Education and vocational training to serve the economy

When our education system churns out graduates that are not suited for the job market, it will put a big dent in our hope to be competitive. Our schools must produce the workforce for current needs as well as future development.

The FSDC reports, for instance, highlighted the need to have a sustained talent pool to retain the competitiveness of the financial sector. Closer connection between industry and schools in course curricular design and for practical training is seen as important elements to enable new graduates and practitioners alike to have and to keep up with new developments. The concept of course applies to other sectors.

Many have been asking why our young graduates are not willing to take up jobs available to them, or lack the skills to take the employment that they desire. It is fairly easy to lament that the young just need to be more realistic. The Hong Kong economy right now, however, is relying too much on the financial industry and property investment as means to generate wealth. The way the economy is, the young generation and their parents may have been led to have a narrowed vision as to career prospect.

If we are to have the young generation and their parents see and appreciate the real prospect of a satisfying career and meaningful life in vocations other than finance, we must have the real prospect a more diverse economy. If we have a more diverse economy and work qualification and accreditation schemes to match, more number of youngsters might be enticed to seek vocational training and certification that will lead them to jobs in demand now, real career development over time and recognition and respect later on.

At the more basic level, we need to re-instill confidence among parents in our primary and secondary schools. For while we need international schools for the children of talents we attract from abroad, we will never have enough if local kids are flocking to international schools to soak up the new seats. Alongside the need to retune our school curriculum, 15 year free education is an investment Hong Kong ought to make.

Corporate governance training

HKIoD believes lifelong training for directors in corporate governance knowledge and skills is an important yet often neglected segment when it comes to nurturing talents for the economic development of Hong Kong. The HKIoD has long supported the promotion of corporate governance training, which is crucial to the long-term survival of their businesses and also the health and growth of the economy.

There is evidence of an ever stronger appreciation that company directors must have and must continue to improve on their skills, knowledge and qualities required to meet the corporate governance demands of today. All company directors, when they first assume their posts, should have a firm measure of competence to perform. Over time, they should strive to remain up-to-date with best corporate governance practices.

The passage and implementation of the New Companies Ordinance is the perfect opportunity to further raise company directors' awareness of the rising expectation on how they perform their duties. But if we want more from directors, then give them tools to perform and shields to protect. Hong Kong company directors will have widely-recognised references and practice notes to guide their conduct and behaviour, but there should still be complementary measures. Directors ought to be protected in legal proceedings for good faith business

judgment and decisions they made. They also need adequate indemnification, insurance or other risk coverage to shield their exposure.

Corporate governance is not just for listed companies

The benefit of proper initial training and continuous professional development for directors will flow not only for big corporations but also small companies. SME owners will benefit from corporate governance training. Many SMEs still find it difficult to take full advantage of loan schemes of one kind or another. There are a number of reasons for this, but one common impediment is that many SMEs could not demonstrate proper internal control and are ill-prepared to submit sound loan proposals. A better corporate governance scorecard will make it more likely for a business to obtain credit and financing. The Government will serve the economy well to roll out measures to help owners and directors of SMEs to obtain training to enhance their corporate governance practices.

The benefit of proper initial training and continuous professional development for directors will flow not only for business corporations but also social enterprises and charitable organisations. While the Government considers the recommendations in the Law Reform Commission's report on Charities, it would not go wrong to require charitable organisation directors to raise their game and be even better at corporate governance.

An attractive home for its denizens

The foremost livelihood issue on people's mind is the situation of housing. That was the main focus of last year's Policy Address. For us, the overall long term goal has not changed. We need to re-establish a flight of steps for younger persons and families to improve on their housing condition and quality of living in realistically reachable climbs. Another longer term goal that should not be forgotten is to increase the living area per person, a statistical measure where Hong Kong ranks rather low at the moment.

As we build more homes, we should not do so at the expense of quality urban life. To build more housing in already crowded communities without worsening the living environment for everyone is not easy.

The frantic search for housing sites cannot be at the expense of land needs for education, healthcare, recreation and other public amenities. We will also need sites for industry and commerce. How to reconcile land needs and how to come up with the land to fill those needs is question number one. For the right choice to be made and the community to understand why that choice is in the best interest of all, the Chief Executive must present a realistic picture of land supply over the medium term.

With many old districts undergoing redevelopment, neighbourhood shops disappear, in come chain stores. Many are feeling that our street economy is fading away. The street economy is a cityscape to be cherished. The possibility of living on the town along street fronts doted with shops of all kinds is a character of living in Hong Kong and a source of the Hong Kong community spirit. As we build more housing and as we redevelop old districts, we have to keep that cityscape and community spirit.

Ageing population and medical need

An ageing population will demand more health services and the Government needs to prepare for it. The projected need for more hospital beds over time needs to be met. Hospitals specialising in Chinese medicine deserve their place in their own right. Geriatric hospitals

combining Chinese and Western medicine will be welcome alternatives for many of our ageing population.

Garbage ... what to do with our garbage?

If we are to institute a levy on garbage disposal that is fair, we must first have in place the infrastructure to segregate waste at the source and to make better use of the recyclables. We need better incentives for residential and commercial buildings to reduce waste and keep recyclable materials off our landfills. We also have to stop discarded electronic products from causing more damage to our land. We should also have plans to introduce advanced incineration and other waste disposal technologies, including those that will turn waste into energy.

Of cars and air quality

When we read and hear about bad air quality in Mainland cities, we should never be complacent and too lenient about that of our own. Air quality in the Pearl River Delta is not going to be a problem solvable by the effort of any one locale acting on its own. Internal diplomacy can be put to work and the progress can be made more transparent to the public. Too many cars may be the local source of poor roadside air quality, not to say road congestion. Introduce road pricing in congested zones.

Public transport and pricing incentives

A good public transportation system can make it more likely to get people out of their own cars. We believe strategic placement of transfer points, a better transfer fare mechanism and the wider adoption of monthly and weekly travel pass across different public transport service platforms will be an integral part of a larger public transport solution.

Traffic among the three cross-harbour tunnels are not even. We view this less an issue of insufficient capacity but more an issue of wrong pricing incentives. To put in the right pricing incentives to re-distribute the traffic load would require unified control over the three facilities. Act.

Creative Economy, Creative Society

As our neighbouring economies are undergoing design-led transformations, we in Hong Kong must be more able to acquire a creative mindset, to be innovative. Hong Kong must continue to build its innovative ecosystem and foster creativity and cross-disciplinary collaborations.

Firmer steps led by the Government towards the development of a Hong Kong intellectual property hub, one with well-grounded rules to protect IP and with professional intermediaries to facilitate financing or trading transactions to realize the IP's commercial value, will give designer-founders, local or from abroad, better reason and encouragement to see Hong Kong as fertile ground for innovation and to set up shop here. With the right incentives, existing enterprises will also find new impetus to put efforts into design-led transformations that could take them to new heights.

Hong Kong the hub of creativity and innovation

Hong Kong can leverage the research capabilities of the Mainland and Hong Kong universities and R&D centres, and link up those capabilities with the manufacturing capacities on the Mainland or elsewhere. But there remains a wide gap between academic research and commercialisation of the research output into products and services. So while

there are government assistance programs, we ought to consider, one, to increase the amounts funded, and two, to adjust the conditions for grant assistance to encourage more applied research leading to commercialisation of research output.

The Chief Executive can set us on the right track by increasing spending on R&D relative to the size of our economy. Putting more money to support existing or new incubator programmes will give more entrepreneurs an opportunity to succeed. Committing to buy more local innovations in procurement will give them a reason to persevere. The inaugural StartMeUpHK Venture Programme that took place in December was a resounding success, and the event should continue in coordination with The Business of Design Week.

Hong Kong's expertise in asset management can be put to good use if we are to develop a fuller venture capital market. The Government can in fact chip in as passive investor, making available more funds for R&D and for incubator support of early-to-growth companies.

Made in Hong Kong with pride

Though mass production capacities are available on the Mainland or elsewhere, prized skills and craftsmanship that once made Hong Kong proud remain found among some Hong Kong workers. They are raring for renewed opportunities to put their skills to use. They have the ability to fabricate those specialty parts or to accomplish those intricate work steps that go into prototypes of innovative designs. Great things can still be Made in Hong Kong with pride. Manufacturing of a different, higher-end kind can still happen here. If only Hong Kong can truly support entrepreneurship for a Creative Economy.

An enduring culture of innovation

Corporate governance demands of today will require the ability to understand and identify the risks and rewards that may come from creativity and innovation in creating business value. Directors ultimately have the responsibility in setting organisational strategy that leads to creation of long term value. As corporate leaders, directors have many good reasons to factor the potential of creativity and of innovation into their corporate strategy. As part of the corporate strategy they devise, directors have as good reasons to instill a culture of innovation into their organisations, and to leverage design and innovation to advance competitive advantages and business performance.

Not just directors, not just corporate leaders or professionals, the citizenry should all develop a heightened sense of wider use of design to create economic value, to enhance competitiveness and to achieve societal progress. As we shape up our workforce, we must not overlook the important element of fostering creativity and a culture of innovation.

Wider use of design in the delivery of public service

The power of better design does not just spark innovations fetching more profits. The power of better design, the power to conceive a newer different way of doing things, can be deployed to improve work productivity at the office or at the factory. Not only do business enterprises earning profits want innovation, social enterprises and public agencies should also tap the power of better design in finding new and better ways to deliver services. It is perhaps the case that design realizes its true value when put into addressing societal challenges and instigating positive changes.

We have our international airport and the octopus card as examples of good system design to boast. The redesign of the Mongkok post office and the Cornwall Street Park are also good

examples of innovative public service design. We can go further, by testing out on a wider basis the adoption of new information and telecommunication technology to make Hong Kong a show case Smart City.

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Much of the content of what we have recommended in recent years remains timely and appropriate. In this communication, we seek to highlight what we see as over-riding issues that deserve particular mention in the second Policy Address of this Administration. From a governing standpoint, the state of the SAR hasn't changed. Unfinished business lingers on. Challenges continue to mount ahead. It calls for ever more courage and determination to innovate and to create changes that will bring us onto the path towards fulfilling our ambitions and aspirations.

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