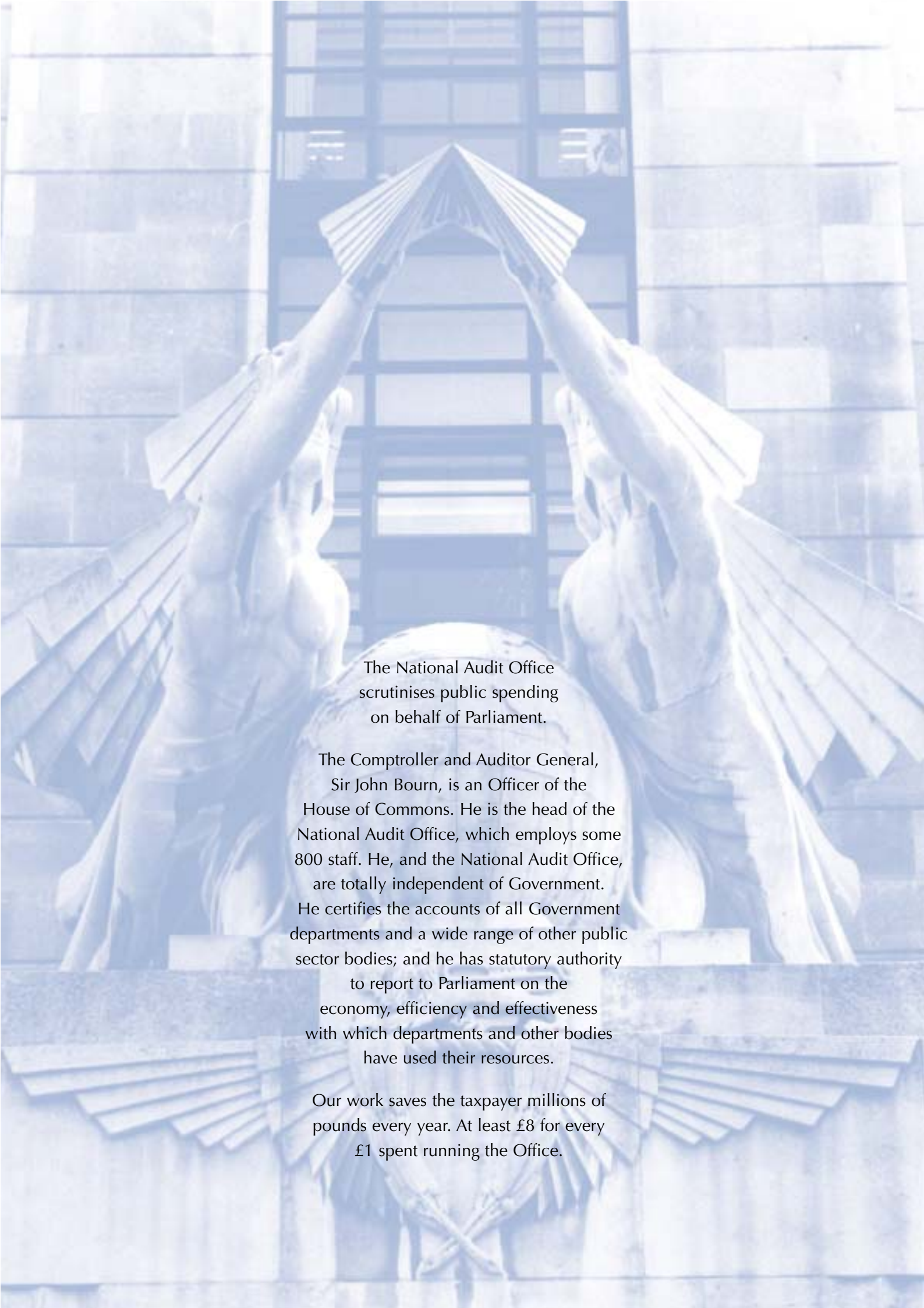


# Managing National Lottery Distribution Fund balances

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL  
HC 875 Session 2003-2004: 21 July 2004





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# Managing National Lottery Distribution Fund balances



REPORT BY THE COMPTROLLER AND AUDITOR GENERAL  
HC 875 Session 2003-2004: 21 July 2004

This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

*John Bourn* National Audit Office  
Comptroller and Auditor General 16 July 2004

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Front cover photograph and page 26: Ladywood Healthy Living Centre © Roy Peters, Page 12: Project Sunlight © Kois Miah; both courtesy of the Big Lottery Fund.

Figure 9: Hadrian's Wall © Countryside Agency - photographer McCoy-Wynne 03-5899, Page 18: Hadrian's Wall © Countryside Agency - photographer Graeme Peacock 02-5732, Figure 9: Chatham Historic Dockyard; all courtesy of the Heritage Lottery Fund.

Lottery ball photograph: Adrian Brooks/Imagewise.

# executive summary

- 1 Since its launch nearly ten years ago in November 1994, the National Lottery has raised over £15 billion for six good causes - the arts; sport; national heritage; charities and voluntary organisations; projects to mark the Year 2000 and the beginning of the Third Millennium; and health, education and the environment. Proceeds from lottery ticket sales are paid into the National Lottery Distribution Fund, which is maintained under the control and management of the Secretary of State for Culture, Media and Sport. The funds remain in the Distribution Fund until they are required by the 15 lottery distributors to make payments to the good causes or to meet their own costs. But while money is in the Distribution Fund it is not delivering the intended benefits in the community.



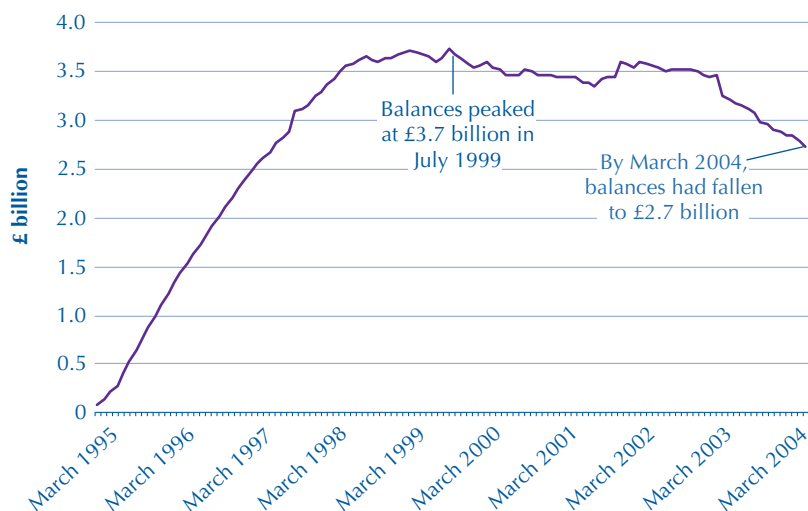
- 2 The Decision Document on National Lottery Funding, published by the Department for Culture, Media and Sport (the Department) in July 2003, highlighted "widespread concern" about how much lottery money was yet to be distributed and announced that, following discussions with the Department, the National Audit Office was to carry out an examination of balance management. This report therefore considers the management of National Lottery Distribution Fund balances and whether there are ways in which the balances could be reduced, within the existing framework of good causes set out in lottery legislation. Specifically we examined:
  - how the balances built up and what has been done to reduce them;
  - whether there is scope for the distributors to take action to reduce their balances further;
  - what uncertainties and risks the distributors face in managing their balances.

The methods we used are described in the Appendix.

## A brief overview

- 3 The balances in the National Lottery Distribution Fund peaked at £3.7 billion in July 1999 and by 31 March 2004 had fallen to £2.7 billion (**Figure 1**). Within this total, the balances held by individual distributors ranged from just over £2 million to nearly £943 million (**Figure 2**). The Heritage Lottery Fund and the New Opportunities Fund together held 61 per cent of the total balances: the nine distributors with the smallest balances held less than 10 per cent of the total.

## 1 Balances held in the National Lottery Distribution Fund since the start of the National Lottery



Source: Hansard, 26 March 2003 (for data to February 2003); Department for Culture, Media and Sport (for data after February 2003)

## 2 Distributors' National Lottery Distribution Fund balances at 31 March 2004

Distributor	National Lottery Distribution Fund balances at 31 March 2004 (£ million)	Percentage of the total National Lottery Distribution Fund balances at 31 March 2004
Heritage Lottery Fund	942.6	34.4
New Opportunities Fund	737.2	26.9
Arts Council England	224.1	8.2
Community Fund	213.3	7.8
Sport England	201.6	7.4
Millennium Commission	155.7	5.7
Sport Scotland	65.0	2.4
UK Film Council	44.3	1.6
Scottish Arts Council	42.0	1.5
Arts Council of Northern Ireland	35.6	1.3
Arts Council of Wales	24.0	0.9
Sports Council for Northern Ireland	23.5	0.9
Sports Council for Wales	21.5	0.8
UK Sport	3.8	0.1
Scottish Screen	2.2	0.1
<b>Total</b>	<b>2,736.3<sup>1</sup></b>	<b>100.0</b>

### NOTE

<sup>1</sup> This figure does not cast correctly due to rounding.

Source: data from the Department for Culture, Media and Sport

- 4 There is scope for the National Lottery Distribution Fund balances to be reduced further, in particular by distributors making more commitments to pay grants to deserving projects. But significant reductions in balances could take time. There can be considerable time lags between distributors making commitments to pay grants and the grants actually being paid. This is especially the case with high value grants as these are often for large projects which can take a long time to complete and involve the payment of grant over a number of years. There is though scope to speed up payments, which can also help to reduce balances.
- 5 However, distributors face uncertainties about future lottery distribution arrangements, income levels and expenditure (**Figure 3**). These uncertainties are important because each distributor must keep sufficient money in the National Lottery Distribution Fund to be able to meet its commitments and manage its business, and is not underwritten by other distributors or the Department.

### 3 Examples of the uncertainties that distributors face

- How much income will the National Lottery raise?
- What share of lottery proceeds will we receive after 2009?
- When will the projects we have funded draw down their grants?
- What if we don't have enough money to honour the grant commitments we have made?

*Source: National Audit Office*





## Our key findings

- 6 The balances in the National Lottery Distribution Fund peaked in 1999 and have fallen since then, but targets have not been met.**
- The balances in the National Lottery Distribution Fund increased steadily from the start of the National Lottery and peaked in 1999.
  - In 2002 the Secretary of State for Culture, Media and Sport announced a target for the balances in the National Lottery Distribution Fund to halve by 2004: since then balances have fallen by about a quarter. The progress made by individual distributors has varied: the balances of some have fallen significantly but others have increased.
- 7 There is scope to reduce the balances in the National Lottery Distribution Fund further.**
- There is scope for distributors to reduce balances by making more grant commitments.
    - Distributors' current levels of commitment vary considerably, with eight having commitments that exceed their National Lottery Distribution Fund balances. Distributors also have varying approaches to the maximum amount they are prepared to commit, and according to these policies at March 2004 distributors had scope to make additional commitments totalling nearly £450 million.
    - All distributors confirmed that they could attract sufficient, suitable applications to be able to make more commitments, without compromising value for money. And eight distributors, including those with the largest balances, consider that increasing commitments is a realistic way of reducing National Lottery Distribution Fund balances.
    - Increasing commitments could have a significant impact on National Lottery Distribution Fund balances, although it would take time for the impact to be felt.
  - There is some but more limited scope for distributors to reduce balances by increasing their speed of spending.
    - There is scope for distributors to influence the time projects take to complete and draw down their funding.
    - Speeding up projects could have some impact on National Lottery Distribution Fund balances, but the impact would be less than from increasing commitments. And eleven distributors do not consider that speeding up projects is a realistic way of reducing National Lottery Distribution Fund balances.
- 8 Distributors face a range of uncertainties and risks in managing their National Lottery Distribution Fund balances.**
- There is uncertainty about lottery distribution arrangements in the future and the lottery income that distributors will receive.
    - The current licence to operate the National Lottery runs until 31 January 2009 and the share of lottery proceeds that the good causes receive could change after that.
    - There is no guarantee about the amount of money that will be raised from lottery ticket sales and the impact of the proposed Olympic lottery games on the existing good causes is uncertain.
    - Investment income is uncertain and the Department proposes to change the way in which it is allocated to distributors to ensure there is no incentive to maintain high balances.
  - There is uncertainty about distributors' future expenditure and they lack confidence in the forecasts of expenditure that projects provide. Most distributors could estimate more accurately the amount of money they need to draw down from the National Lottery Distribution Fund, which would have financial benefits.
  - Distributors could find themselves in difficulty if income was significantly less and/or expenditure significantly more than expected. They could have insufficient funds to meet the grant commitments they have made or they might not be regarded as a 'going concern'.



## Our recommendations

The decisions about grant making that impact on the balances in the National Lottery Distribution Fund are the responsibility of individual distributors. Those distributors with the largest balances, particularly the Heritage Lottery Fund and the New Opportunities Fund, can make the biggest contribution to reducing the overall balances. However, the Department too has a role, especially in relation to the New Opportunities Fund where it decides the grant programmes to be run and the funding to be committed to them.

If distributors and the Department are to manage effectively the opportunities and risks in seeking to reduce balances, there are a number of areas that require attention.

### AREAS FOR ATTENTION

### RECOMMENDATIONS

#### Forecasting income

The uncertainty about lottery distribution arrangements beyond the end of the current licence in 2009 will start to affect distributors' grant making from 2005-06 as they reduce commitments to be sure of having sufficient funds available to meet them.

The sooner the Department can provide more clarity about future distribution arrangements, the more confident distributors will be in continuing to make further commitments.

In the more immediate future, distributors need reliable and regular information about the income that is expected to be raised from the sale of lottery tickets in the years to 2009.

- 1 The Department should set a clear timetable for making decisions about, for example, the proportion of lottery proceeds that will be allocated to the good causes, and the share of the proceeds that each good cause and distributor will receive.
- 2 The Department should seek to enhance distributors' confidence in the projections of future lottery income by:
  - producing the projections on time each quarter;
  - providing further information about the basis of the projections and the underlying assumptions;
  - reviewing periodically how accurate the projections have been and reporting the results to distributors.

## AREAS FOR ATTENTION

## RECOMMENDATIONS

## Managing expenditure

There are ways in which distributors can influence the time taken to complete projects and therefore their own speed of spending. In August 2003 the Department circulated good practice examples drawn from larger distributors on this area (see Figure 20 on page 25).

Distributors are dependent on projects' forecasts of expenditure to inform their own drawdown of money from the National Lottery Distribution Fund and to help calculate the amount of money that they have available to make new commitments. But at present they lack confidence in these forecasts.

Distributors draw down money from the National Lottery Distribution Fund to pay grants or meet their own expenses. Some distributors are better than others at predicting their cash requirements. If distributors draw down more money than they need, the money remains in their own bank accounts and is likely to earn a lower rate of interest than in the Distribution Fund.

- 3 Distributors should adhere to the good practice guidance on the earlier payment of grants and the Department should monitor the extent to which distributors are doing so.

- 4 Distributors should work with projects to achieve forecasts of expenditure that they have confidence in.

This could involve distributors:

- making clear to projects the criteria they will use to assess whether forecasts are reliable and realistic, the importance of such forecasts for projects themselves, and the impact of poor forecasting on distributors' capacity to fund other deserving projects;
- working with projects to ensure they have the capacity to provide such forecasts;
- considering ways of providing projects with positive financial incentives to draw down funding in line with their forecasts. An example of how such an incentive can work in certain circumstances is shown in Figure 25 on page 31.

- 5 A project's consistent failure to provide reliable and realistic forecasts or draw down funding in line with them may indicate wider problems with the project. In such cases, distributors should be prepared to reduce or withdraw funding.

Mindful of the community benefits that lottery funding can bring, distributors would have to weigh up the risks of continuing to fund a project that is struggling with the risks of a project being left unfinished. Distributors would also need to consider the materiality of a project's grant and the wider implications for their grant programmes.

- 6 Distributors should not draw down from the National Lottery Distribution Fund more money than they need. Drawdown should be based on the grants they expect to pay in the coming period and estimated administration costs.

## AREAS FOR ATTENTION

## RECOMMENDATIONS

## Focusing on funding capacity

A distributor's capacity to make new commitments (its 'funding capacity') is determined by:

- the balances it currently holds in the National Lottery Distribution Fund;
- **plus** its likely future income;
- **less** its likely future expenditure, stemming from existing commitments.

To manage their grant making, make informed decisions about making further commitments, and set targets for their National Lottery Distribution Fund balances, distributors need to know their funding capacity at any given time. They also need to be able to project the likely impact that their grant making decisions will have on their National Lottery Distribution Fund balances.

Distributors should be aiming to achieve a broadly stable position with annual income and expenditure more or less equal and minimum working balances in the National Lottery Distribution Fund.

Although addressing these areas for attention will enable distributors to manage more effectively the opportunities and risks in seeking to reduce balances, there will be residual uncertainties surrounding their future income and expenditure. This may lead distributors to maintain higher balances in the National Lottery Distribution Fund than would otherwise be necessary.

- 7 With a view to reducing their National Lottery Distribution Fund balances, distributors should identify whether they have the funding capacity to make more commitments without compromising value for money.

We have developed a model (see the Appendix) to help distributors assess their capacity to fund additional commitments. We have discussed the model with the Department and the Heritage Lottery Fund and have agreed that we will share it with other distributors. Accordingly, we are now preparing a user-friendly format for distribution.

- 8 In the short term, to provide a clear focus on tackling the accumulated balances currently held in the National Lottery Distribution Fund, distributors should set interim targets for bringing down their balances.

- 9 In the long term, distributors should hold no more money in the National Lottery Distribution Fund than is necessary to cover any short term differences between their income and expenditure.

- 10 Given the residual uncertainties, the Department should assess how a mechanism could be established within the National Lottery Distribution Fund to accommodate unexpected variations in individual distributors' income and expenditure.

# Part 1

## Introduction

### The National Lottery was set up to raise money for good causes

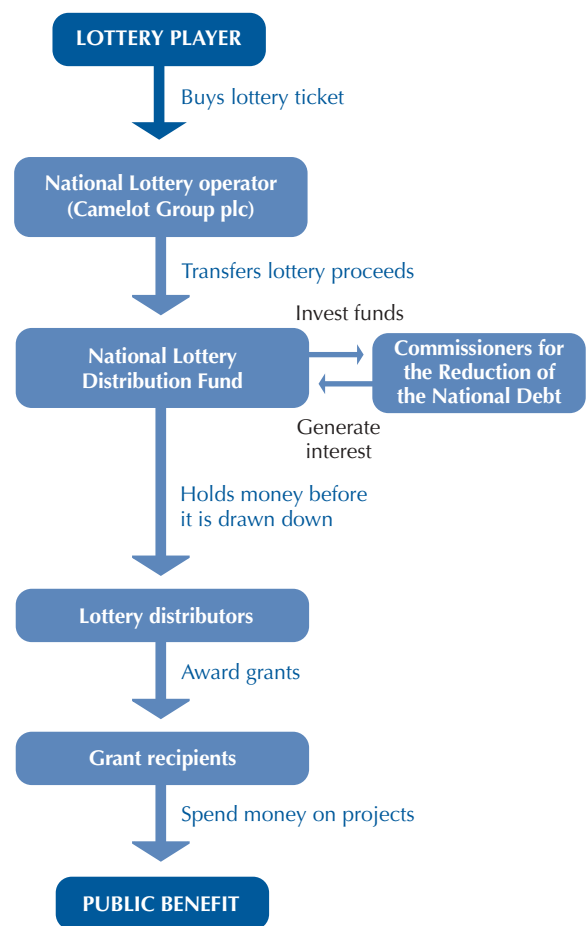
- 1.1 The United Kingdom National Lottery was launched on 14 November 1994 and since then has become one of the largest lotteries in the world in terms of ticket sales. The National Lottery was established to generate money for initially five 'good causes' - the arts; sport; national heritage; charities and voluntary organisations; and projects to mark the Year 2000 and the beginning of the Third Millennium<sup>1</sup>. A sixth good cause - health, education and the environment - was added in 1998.
- 1.2 Since 1994 around 28 pence of every £1 spent on National Lottery tickets has gone to the good causes, raising over £15 billion in total<sup>2</sup>. Some 166,000 grants have been made, ranging from multi-million pound awards to national flagship projects, such as the Eden Project in Cornwall and Tate Modern in London, to small grants for local community groups or individuals.

### Lottery proceeds are paid into the National Lottery Distribution Fund

- 1.3 The process by which lottery money flows from players to the good causes is outlined in **Figure 4**. The National Lottery is run under licence by a private sector operator, currently Camelot Group plc. Camelot pays the money generated for good causes from the sale of lottery tickets into the National Lottery Distribution Fund, which was set up under the National Lottery etc Act 1993 to:

- receive monies generated by the National Lottery for the good causes;
- allocate these monies to the distributors (see paragraph 1.6);
- invest the funds until such time as they are drawn down by the distributors for payment to approved grant applicants and to meet expenses (see paragraph 1.5).

#### 4 How lottery money gets from players to the good causes



Source: National Audit Office

<sup>1</sup> The Millennium good cause has received no income from the sale of lottery tickets since August 2001.  
<sup>2</sup> Including returns on the investment of lottery proceeds held in the National Lottery Distribution Fund - see paragraph 1.5.

- 1.4 The National Lottery Distribution Fund is maintained under the control and management of the Secretary of State for Culture, Media and Sport, and its Accounting Officer is the Permanent Secretary of the Department for Culture, Media and Sport (the Department). The Department's responsibilities over the Distribution Fund are to receive the lottery proceeds from Camelot Group plc, place the money with the Commissioners for the Reduction of the National Debt<sup>3</sup>, and make disbursements in response to requests from the distributors.
- 1.5 Under the National Lottery etc Act 1993 the lottery funds which the distributors do not require immediately for distribution are invested by the Commissioners for the Reduction of the National Debt, in accordance with directions issued by HM Treasury. Since 1994 investment income totalling over £1.5 billion has been earned on the balances in the National Lottery Distribution Fund. This income is currently attributed to the distributors in proportion to the share of the balances in the Distribution Fund held by each body.

## Lottery money is distributed to the good causes by 15 distributors

- 1.6 Responsibility for distributing lottery proceeds to the good causes rests with 15 distributors (Figure 5). The distributors are non-departmental public bodies, which operate at arm's length from government and make their funding decisions independently, within a framework set by the Secretary of State for Culture, Media and Sport. The Chief Executive of each distributor is designated as the Accounting Officer for the body and is responsible for ensuring that lottery funds are distributed with due regard to regularity, propriety and achieving value for money.
- 1.7 Lottery money is also handled by the National Endowment for Science, Technology and the Arts (NESTA), which was established in 1998. At inception, the Secretary of State for Culture, Media and Sport provided NESTA with an endowment of £200 million from the National Lottery Distribution Fund, which generates income to fund NESTA's programmes. In 2003 NESTA was granted additional lottery funding of £95 million - £50 million to add to the endowment and £45 million for programme spending over the following three years. NESTA's funds do not form part of the National Lottery Distribution Fund and it therefore falls outside the scope of this report. The Comptroller and Auditor General reported on NESTA in February 2004<sup>4</sup>.

## The Department for Culture, Media and Sport sets the framework for the National Lottery

- 1.8 The Secretary of State for Culture, Media and Sport is responsible for setting the general policy and legislative framework for the National Lottery and issues:
- **policy directions** setting out the factors that distributors should take into account when considering applications for grants. The policy directions for the New Opportunities Fund are more prescriptive than those for other distributors and set out the grant programmes it should run and how much funding it should commit to them;
  - **financial directions** setting out the broad framework of financial and management controls within which distributors must operate;
  - **accounts directions** setting out the accounts which distributors must prepare and the form and content of those accounts.
- 1.9 Under devolution, lottery matters are not devolved but are 'reserved' to Westminster. However, policy responsibility for the arts and sport rests with the devolved administrations and:
- in Scotland, all directions are given by Scottish Ministers with the consent of the Secretary of State for Culture, Media and Sport;
  - in Wales, policy directions are given by Welsh Ministers with the consent of the Secretary of State for Culture, Media and Sport; and financial and accounts directions are given by the Secretary of State for Culture, Media and Sport with the consent of the Welsh Assembly Government;
  - in Northern Ireland, all directions are given by the relevant government department within Northern Ireland with the consent of the Secretary of State for Culture, Media and Sport.

## This report examines the management of National Lottery Distribution Fund balances

- 1.10 Lottery money remains in the National Lottery Distribution Fund until it is required by distributors to meet expenditure by grant recipients or their own costs. At 31 March 2003 the balances held in the Distribution Fund totalled £3.3 billion and had stood at over £3 billion for some six years. The Decision Document on National Lottery Funding, published by the Department in July 2003, highlighted "widespread concern" about how much lottery money was yet to be distributed and announced that, following discussions with the Department, the National Audit Office was to carry out an examination of balance management, which would inform other steps aimed at reducing the balances.

<sup>3</sup> The Commissioners for the Reduction of the National Debt are responsible for the investment and management of government and other public funds.

<sup>4</sup> HC 267, Session 2003-04.

## 5 The lottery distributors

Good cause	Distributor	Share of income from lottery ticket sales in 2003-04 (%)
The arts	Arts Council England	11.85
	Scottish Arts Council	1.29
	Arts Council of Wales	0.83
	Arts Council of Northern Ireland	0.47
	UK Film Council	2.03
	Scottish Screen	0.19
		<b>16.67<sup>1</sup></b>
Sport	Sport England	12.60
	Sport Scotland	1.35
	Sports Council for Wales	0.75
	Sports Council for Northern Ireland	0.43
	UK Sport	1.53
	<b>16.67<sup>1</sup></b>	
National heritage	Heritage Lottery Fund	<b>16.67</b>
Charities and voluntary organisations	Community Fund <sup>2</sup>	<b>16.67</b>
Projects to mark the Year 2000 and the beginning of the Third Millennium	Millennium Commission <sup>3</sup>	<b>0<sup>4</sup></b>
Health, education and the environment	New Opportunities Fund <sup>2</sup>	<b>33.33</b>

### NOTES

- 1 These figures do not cast correctly due to rounding.
- 2 The Government announced in July 2003 that a new distributor (the Big Lottery Fund) would be created to take on the functions of the Community Fund and the New Opportunities Fund. Creating the new distributor will require legislation but the Community Fund and the New Opportunities Fund started to operate under the new name from June 2004. The new distributor will receive 50 per cent of the money generated for the good causes.
- 3 The Millennium Commission's grant giving functions should be completed by 31 March 2006, after which its residual functions (such as project monitoring) and any remaining assets will transfer to the new distributor, the Big Lottery Fund.
- 4 The Millennium Commission stopped receiving a share of income from lottery ticket sales in August 2001; prior to this it had received 20 per cent.

Source: Department for Culture, Media and Sport

1.11 This report therefore considers the management of National Lottery Distribution Fund balances and whether there are ways in which the balances could be reduced, within the existing framework of good causes set out in lottery legislation. Rather than looking in detail at the grant making and monitoring arrangements of distributors on an individual basis, we focused on getting an overall sense of the opportunities for balances to be reduced. The methods we used are outlined in **Figure 6** and described in more detail in the Appendix.

## 6 Summary of the methods we used

- A survey of distributors to collect information and views on their approach to managing their National Lottery Distribution Fund balances.
- Interviews and data collection at four distributors: the Arts Council of Wales, the Heritage Lottery Fund, the New Opportunities Fund and Sport England.
- Development of a model to assess the impact changes in grantmaking behaviour might make on the National Lottery Distribution Fund balances held by a distributor.
- Interviews and data collection at the Department for Culture, Media and Sport.
- Interviews with four charitable grant making trusts: BBC Children in Need, Comic Relief, the Lloyds TSB Foundation for England and Wales, and the Wellcome Trust.

Source: National Audit Office





# Part 2

The balances in the National Lottery Distribution Fund peaked in 1999 and have fallen since then, but targets have not been met

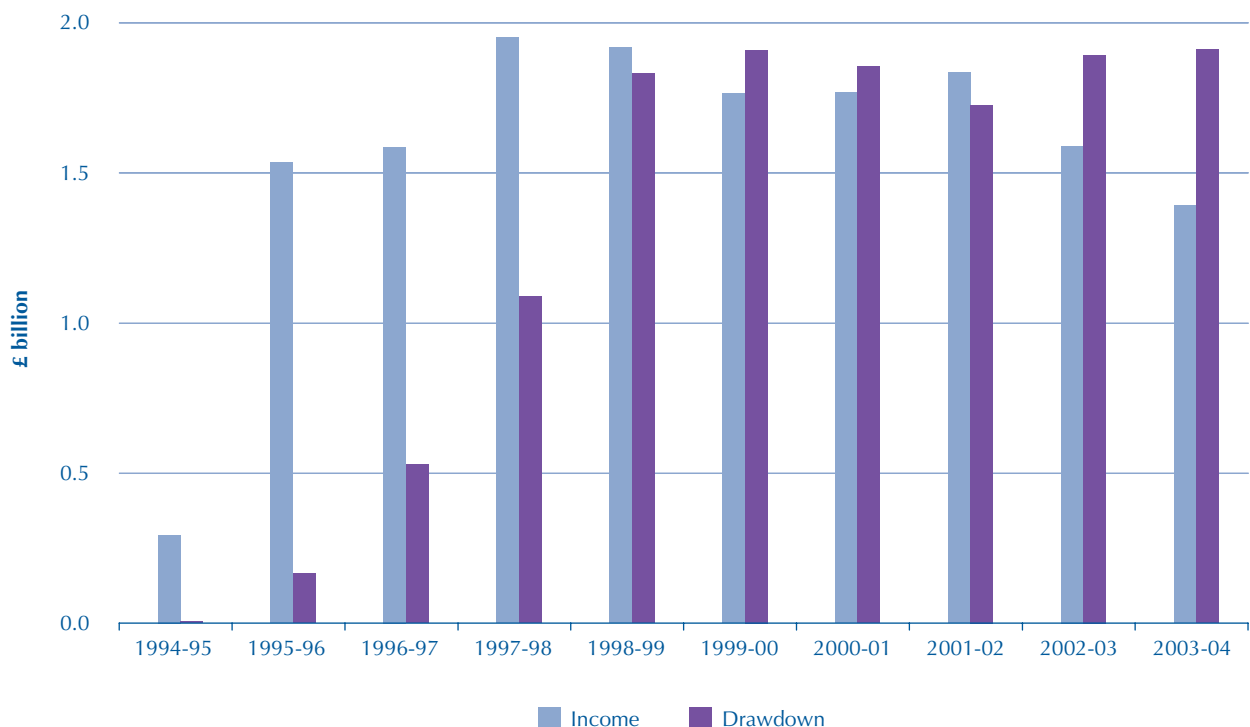
2.1 This part of the report examines how the balances in the National Lottery Distribution Fund built up, why the question of balances is important, what has been done to seek to reduce the balances, and with what success.

The balances in the National Lottery Distribution Fund increased steadily from the start of the National Lottery and peaked in 1999

2.2 In the first four years of the National Lottery, the balances in the National Lottery Distribution Fund built up steadily, peaking in July 1999 at £3.7 billion and remaining at over £3 billion until August 2003. By March 2004 the balances had fallen to £2.7 billion (see Figure 1 on page 2).

2.3 The build up of balances at the start of the National Lottery reflected the inevitable time lag between money being paid into the National Lottery Distribution Fund and it being awarded to and drawn down by grant recipients. Until 1997-98 income continued to be paid into the Distribution Fund much faster than it was drawn down, but from 1998-99 to 2001-02 the annual cash inflows to and outflows from the Distribution Fund were fairly close, and since then annual drawdown has considerably exceeded income (Figure 7). The current level of balances is therefore the result of the low rate of drawdown compared to income in the first four years of the Lottery.

## 7 Annual lottery income and drawdown from the National Lottery Distribution Fund since the start of the National Lottery



Source: National Audit Office analysis of data from the Department for Culture, Media and Sport

2.4 The lag between lottery income and expenditure arises because there are a number of steps in the process of distributing lottery funds (Figure 8). In particular there can be a significant gap between a grant being awarded and the project starting to incur expenditure and draw down funds. It is not possible to generalise about the time taken to complete the various stages, which will vary depending on the type of grant and the circumstances of the project, but the total time can range from a few months to several years.

### Money held in the National Lottery Distribution Fund is not delivering the intended public benefit

2.5 The balances in the National Lottery Distribution Fund are invested and earn interest (see paragraph 1.5). But money held in the Distribution Fund is not delivering the intended public benefit. While some benefits may start to be delivered once a project has been awarded funding and development work begins, the full benefits are realised only when projects are delivered.

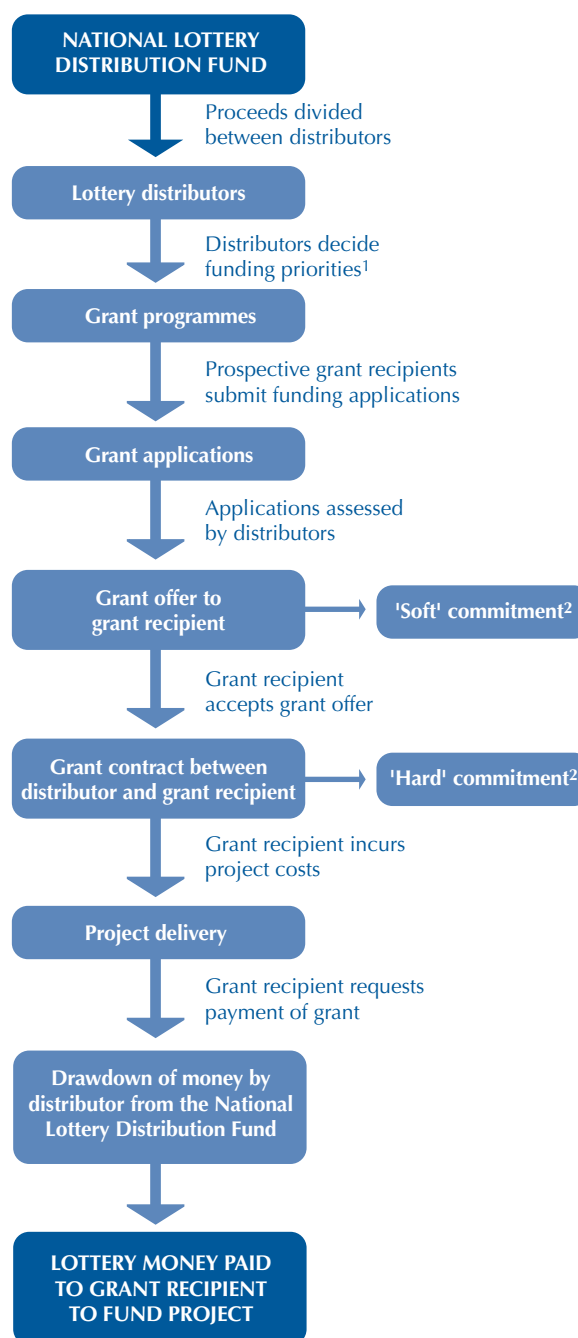
2.6 As well as benefiting the direct users of a project, lottery spending can also bring benefits to the surrounding community and to the economy in general. The economic impact of the National Lottery as a whole has not been quantified, although research has demonstrated the wider benefits that lottery funding can bring. Figure 9 gives examples of the benefits arising from two projects funded by the Heritage Lottery Fund.

### In 2002 the Secretary of State for Culture, Media and Sport announced a target for the balances in the National Lottery Distribution Fund to halve by 2004

2.7 Following exchanges with the then Secretary of State for Culture, Media and Sport about the level of balances in the National Lottery Distribution Fund, in September 2001 the Chief Executives of the distributors jointly submitted a note to the Department, drawing on information from 12 of the 15 distributors<sup>5</sup>. The note included a forecast that balances as a whole would fall from £3.4 billion in March 2001 to £1.5 billion by March 2004, a reduction of 55 per cent. Eight distributors forecast reductions of 60 per cent or more in their balances.

2.8 In March 2002, drawing on the information that distributors had provided in September 2001, the Secretary of State for Culture, Media and Sport announced a target for the total balances in the National Lottery Distribution Fund (which then stood at £3.6 billion) to halve by 2004.

### 8 How lottery money gets from the National Lottery Distribution Fund to projects



**NOTES**

- 1 In the case of the New Opportunities Fund, funding priorities are determined by the Secretary of State for Culture, Media and Sport and set out in the Fund's policy directions.
- 2 Both 'soft' and 'hard' commitments may be de-committed at any point in the event that the grant offer is withdrawn or the grant contract terminated because, for example, the project in question has not complied with the funding conditions or has not taken up the award as planned.

Source: National Audit Office

<sup>5</sup> The other three distributors (Sport Scotland, the Sports Council for Wales and UK Sport) did not provide information and the overall forecast included no amount for their likely balances in March 2004, although in March 2001 their balances had totalled nearly £111 million.

## 9 The wider benefits of lottery funding

A grant of £1.35 million from the Heritage Lottery Fund for the **Hadrian's Wall Path** has contributed to the economic regeneration of the surrounding rural area. The trail was opened in May 2003 and a business survey is underway to establish the positive economic effect that the trail is having on the region. Initial results show that 800 walkers are completing the trail each month, and that each walker takes between five and seven days and spends an average of £30 a day. In total therefore walkers are spending between £120,000 and £168,000 each month on accommodation, food and visitor services provided by local businesses.



The Heritage Lottery Fund provided nearly £13 million towards the development of the **Historic Dockyard in Chatham**, Kent. The funding enabled a museum to be opened on the site in April 2001, the creation of an 'historic warships attraction', and a major programme of building repair. The Dockyard has attracted some two million visitors, including almost 200,000 educational visitors, and is helping to support the wider retail and leisure economy of Chatham. The improvements have also helped attract 100 businesses, employing 1,000 people, and around 400 residents in a range of housing units. Research has concluded that the Historic Dockyard is worth £20 million a year to the local economy.



Source: Heritage Lottery Fund

Since 2002 the balances in the National Lottery Distribution Fund have fallen by about a quarter

2.9 At 31 March 2004 the balances in the National Lottery Distribution Fund stood at £2.7 billion (**Figure 10**), a fall of 24 per cent since March 2002 against the Secretary of State's target of 50 per cent.

The progress made by individual distributors has varied: while the balances of some have fallen significantly, others have increased

2.10 The balances held by distributors at 31 March 2004 ranged from just over £2 million for Scottish Screen to nearly £943 million for the Heritage Lottery Fund. Movements in the balances of distributors since they made their individual forecasts in 2001 have varied widely (**Figure 11**).

- The balances of ten distributors fell, including three by more than 50 per cent - the Community Fund, the Millennium Commission (which stopped receiving income from the sale of lottery tickets in 2001) and Sport England. Taken together, the balances of these three distributors fell by £829 million.
- With one exception (the Scottish Arts Council), no distributor's balances fell to the level that they forecast in 2001.
- The balances of five distributors increased, including the two with the largest balances - the Heritage Lottery Fund and the New Opportunities Fund.

## 10 Summary of forecast, target and actual National Lottery Distribution Fund balances at 31 March 2004

Date		Level of balances at the time	Level of balances at 31 March 2004
September 2001	Total of individual <b>forecasts</b> by the Chief Executives of the distributors	£3.4 billion	£1.5 billion (forecast)
March 2002	Overall <b>target</b> announced by the Secretary of State for Culture, Media and Sport	£3.6 billion	£1.8 billion (target)
March 2004	<b>Actual</b> balances		£2.7 billion (actual)

Source: Department for Culture, Media and Sport

## 11 Balances in the National Lottery Distribution Fund at 31 March 2001 and 31 March 2004, compared with forecast, by distributor

Distributor	Actual balances at 31 March 2001 (£ million)	Forecast balances for 31 March 2004 (£ million)	Forecast change in balances		Actual balances at 31 March 2004 (£ million)	Actual change in balances	
			£ million	%		£ million	%
Arts Council England	255.1	75.0	(180.1)	(71)	224.1	(31.0)	(12)
Arts Council of Northern Ireland	30.2	12.0	(18.3)	(60)	35.6	5.5	18
Arts Council of Wales	27.9	4.7	(23.2)	(83)	24.0	(4.0)	(14)
Community Fund	486.7	163.0	(323.7)	(67)	213.3	(273.4)	(56)
Heritage Lottery Fund	929.9	791.0	(139.0)	(15)	942.6	12.7	1
Millennium Commission	463.8	18.0	(445.8)	(96)	155.7	(308.1) <sup>2</sup>	(66)
New Opportunities Fund	568.3	361.2	(207.1)	(36)	737.2	168.9 <sup>3</sup>	30
Scottish Arts Council	46.2	46.1	(0.1)	0	42.0	(4.2)	(9)
Scottish Screen	4.3	0.5	(3.7)	(87)	2.2	(2.1)	(49)
Sport England	449.2	50.0	(399.2)	(89)	201.6	(247.6)	(55)
Sport Scotland <sup>1</sup>	69.9	-	-	-	65.0	(4.9)	(7)
Sports Council for Northern Ireland	16.6	15.5	(1.1)	(7)	23.5	6.8	41
Sports Council for Wales <sup>1</sup>	35.7	-	-	-	21.5	(14.2)	(40)
UK Film Council	41.5	3.0	(38.5)	(93)	44.3	2.8	7
UK Sport <sup>1</sup>	5.4	-	-	-	3.8	(1.6)	(30)
<b>Total</b>	<b>3,430.6</b>	<b>1,540.0<sup>1</sup></b>	<b>(1,779.7)<sup>1</sup></b>	<b>(52)<sup>1</sup></b>	<b>2,736.3</b>	<b>(694.4)</b>	<b>(20)</b>

### NOTES

- 1 Three distributors did not provide forecasts and the forecast totals include no provision for them.
- 2 The Millennium Commission made an award of £100 million in 2002 to endow the Millennium Awards Trust, which will provide lottery grants to people throughout the United Kingdom.
- 3 In 2003 the National Endowment for Science, Technology and the Arts received £95 million taken from the New Opportunities Fund's share of lottery proceeds (see paragraph 1.7). Also in 2003, the New Opportunities Fund gave £50 million to the Community Foundation Network to manage as an expendable endowment, which will be committed across the United Kingdom over 10 years to 2013.
- 4 Distributors are shown in alphabetical order.
- 5 Not all figures cast correctly due to rounding.

Source: National Lottery Distribution Fund Accounts 2000-2001 and Department for Culture, Media and Sport

2.11 If the percentage movements in individual distributors' balances between 2001 and 2004 were replicated in the coming three years, the total balances in the National Lottery Distribution Fund would fall by a further £133 million (five per cent) between March 2004 and March 2007. Further significant progress in reducing total balances will largely depend on movement in the balances of the larger distributors, in particular the Heritage Lottery Fund and the New Opportunities Fund which together held 61 per cent of the total balances at 31 March 2004; the nine distributors with the smallest balances held less than 10 per cent of the total balances between them.

### Five distributors have now set individual targets for their National Lottery Distribution Fund balances

2.12 The target for the total balances held in the National Lottery Distribution Fund announced by the Secretary of State in March 2002 was not disaggregated into targets for individual distributors. However, the Decision Document on National Lottery Funding, which the Department published in July 2003, proposed making

each distributor responsible for setting a target for their level of balances. This was confirmed in guidance issued by the Department in August 2003 which recommended that distributors should set a target and report progress against the target in their annual report and accounts.

2.13 At March 2004 five distributors had set a target for their balances (**Figure 12**). If the targets were to be achieved, the total balances held by these distributors would fall by at least £887.5 million (66 per cent) by April 2006.

2.14 Four other distributors (the Arts Council of Northern Ireland, the Scottish Arts Council, Sport England and the Sports Council for Northern Ireland) are intending to set a target for their balances by the end of 2004. The remaining distributors were not intending to set a target either because they did not feel that the level of their balances was a problem at present, or because they considered that it would not be appropriate to set a target since balances were largely a product of factors (such as lottery income) over which they did not have control.

## 12 Distributors' targets for their National Lottery Distribution Fund balances

Distributor	National Lottery Distribution Fund balances at 31 March 2004	Target for National Lottery Distribution Fund balances
Arts Council England	£224 million	Balances to fall to £50 million by 31 March 2006.
Community Fund	£213 million	Balances to fall to: <ul style="list-style-type: none"> <li>■ £115 million by 31 March 2005;</li> <li>■ between £50 million and £100 million by 31 March 2006 (equivalent to between three and six months' worth of lottery income).</li> </ul>
Millennium Commission	£156 million	Balances to fall to zero by 31 March 2006 when the Commission will be wound up.
New Opportunities Fund	£737 million	Balances to fall to: <ul style="list-style-type: none"> <li>■ £572 million by 31 March 2005;</li> <li>■ £307 million by 31 March 2006;</li> <li>■ £240 million as soon as possible.</li> </ul>
Sports Council for Wales	£21 million	Balances to fall to: <ul style="list-style-type: none"> <li>■ £12.5 million by 1 April 2005;</li> <li>■ £6.5 million by 1 April 2006;</li> <li>■ £1.5 million by 1 April 2007.</li> </ul>

Source: National Audit Office survey of lottery distributors (February/March 2004)



# Part 3

## There is scope to reduce the balances in the National Lottery Distribution Fund further

- 3.1 The level of balances held by distributors in the National Lottery Distribution Fund is determined by two factors - how much money is raised by the National Lottery and how much money is paid out by distributors. Since distributors have no control over lottery income, any action to reduce balances needs to focus on lottery expenditure. Distributors can increase the amount of money that they pay out in grants by **making more commitments to pay grants or increasing the speed with which they pay grants**. This part of the report explores the scope that distributors have to reduce their balances in these two ways.
- 3.2 This report does not consider the use made of endowments by the Department or distributors. Large, one-off payments to create endowments can reduce the balances held in the National Lottery Distribution Fund but they involve the creation of separate funds from which the capital or income generated is distributed over time to projects in the community.

### There is scope for distributors to reduce balances by making more grant commitments

Distributors' current levels of commitment vary considerably, with eight having commitments that exceed their National Lottery Distribution Fund balances

- 3.3 At 31 March 2004 distributors' commitments to pay grants<sup>6</sup> **exceeded** the funds immediately available in the National Lottery Distribution Fund by £873 million (31.9 per cent). The excess commitments are equivalent at current levels to between seven and eight months of lottery income, but based on previous experience discharging the commitments (ie paying the grants to projects) will take considerably longer than this.
- 3.4 The position of individual distributors at 31 March 2004 varied considerably, with eight having made commitments that exceeded the balances they held in the National Lottery Distribution Fund (**Figure 13**).

### Distributors have varying approaches to the maximum amount they are prepared to commit

- 3.5 There is considerable variation in the maximum level of commitments that distributors are prepared to make and in how these levels are expressed.
- Five distributors are not prepared to make grant commitments that exceed the level of funds that they hold in the National Lottery Distribution Fund (the Arts Council of Northern Ireland, the Scottish Arts Council, Sport Scotland, the Sports Council for Northern Ireland and the UK Film Council). And the Millennium Commission is unable to do so since it no longer receives a share of the income generated from lottery ticket sales.
  - Six distributors are prepared to make grant commitments that exceed the level of funds that they hold in the National Lottery Distribution Fund and have specified the maximum extent of this 'over-commitment' that they are prepared to accept (the Arts Council of Wales, the Community Fund, the Heritage Lottery Fund, the New Opportunities Fund, Scottish Screen and the Sports Council for Wales). For example, the Heritage Lottery Fund is prepared to make commitments equivalent to the total of its balances plus its projected lottery income for the next two years, and the New Opportunities Fund is prepared to make commitments equivalent to the total of its balances plus 130 per cent of its projected annual income.
  - Three distributors have not specified a maximum acceptable level of commitments: Arts Council England will make commitments as necessary to meet its policy of moving towards and then maintaining balances of £50 million in the National Lottery Distribution Fund; Sport England aims to balance existing and future commitments against its total balances plus projected income to the end of the current lottery licence in 2009; and while UK Sport agreed with the Department to commit up to £100 million over the four years to March 2005, between 2005 and 2009 it will balance expenditure against income.

<sup>6</sup> Throughout the report, the figures shown for commitments comprise both 'hard' commitments (where there is a signed contract between the distributor and the grant recipient) and 'soft' commitments (where the distributor has made an offer of a grant to an applicant).



**13 Distributors' levels of commitments compared with their National Lottery Distribution Fund balances at 31 March 2004**

Distributor	National Lottery Distribution Fund balances at 31 March 2004 (£ million)	Commitments at 31 March 2004 (£ million)	Commitments as a percentage of balances (%)
UK Sport	3.8	18.1	477
Community Fund	213.3	438.1	205
Scottish Screen	2.2	4.2	189
Sport England	201.6	335.9	167
New Opportunities Fund	737.2	1,144.5	155
Sports Council for Wales	21.5	28.9	134
Heritage Lottery Fund	942.6	1,123.1	119
Arts Council of Wales	24.0	24.6	102
Arts Council England	224.1	205.3	92
Millennium Commission	155.7	130.6	84
Scottish Arts Council	42.0	33.7	80
Arts Council for Northern Ireland	35.6	27.1	76
Sport Scotland	65.0	47.9	74
Sports Council for Northern Ireland	23.5	16.7	71
UK Film Council	44.3	30.6	69
<b>Total</b>	<b>2,736.3</b>	<b>3,609.0</b>	<b>132</b>

**NOTE**

Not all figures cast correctly due to rounding.

Source: National Audit Office analysis of data from the Department for Culture, Media and Sport and data provided for the Department by distributors as at 31 March 2004 (which may be subject to adjustment)

3.6 We looked at the approach to making commitments at four charitable grant making trusts. In all four cases, the trusts do not award grants unless they are certain of having the funds available to meet them in full, irrespective of when the actual payment of grant might occur (**Figure 14**). In contrast, nine lottery distributors are prepared to make commitments in excess of the balances they have immediately available in the National Lottery Distribution Fund.

According to their own policies, at March 2004 distributors had scope to make additional commitments totalling nearly £450 million

3.7 **Figure 15** compares distributors' actual levels of grant commitments at 31 March 2004 (as shown in Figure 13) with the maximum levels of commitments that they are prepared to accept. For the 12 distributors that had specified a maximum level:

- eight distributors had made fewer commitments than they were prepared to according to the policies that they had set for themselves and the New Opportunities Fund also had scope to make more commitments<sup>7</sup>. The two distributors furthest away from their maximum acceptable level of commitments were the Heritage Lottery Fund (by £243 million) and the New Opportunities Fund (by £142 million);
- three distributors had commitments above their maximum acceptable level - the Community Fund, which had excess commitments of £21 million; Scottish Screen, which had excess commitments of £1.3 million, and the Arts Council of Wales, which had excess commitments of almost £600,000;
- the total maximum level of commitments was £3,494 million compared with actual commitments of £3,050 million - that is, according to their own policies, distributors could have made further commitments totalling £444 million.

<sup>7</sup> The New Opportunities Fund's level of commitments is determined by the policy directions it receives from the Secretary of State for Culture, Media and Sport (see paragraph 1.8).

## 14 Examples of charitable grant making trusts' approach to managing commitments

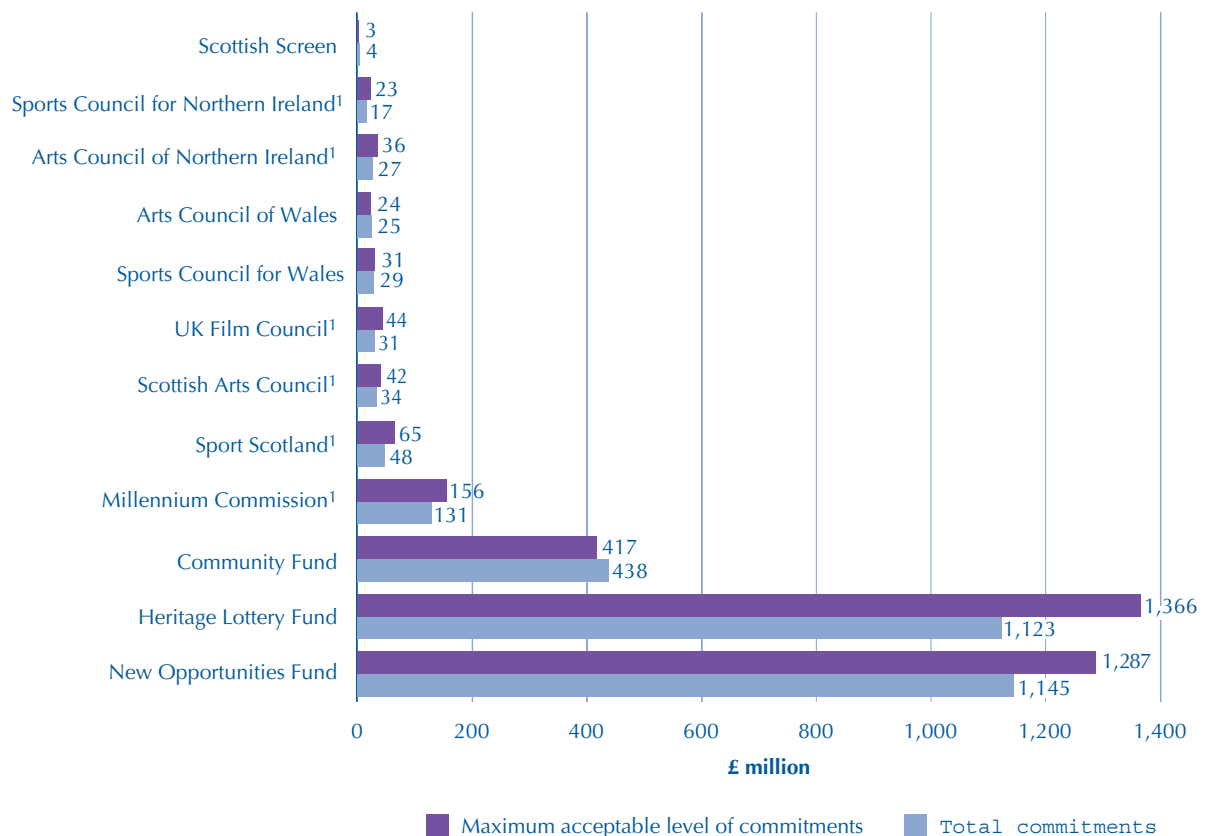
**BBC Children in Need** and **Comic Relief** are dependent on annual fundraising appeals. Both organisations know soon after these events how much they have raised and make commitments based on this information. All commitments made during any one year are covered in full by the funds raised in that year, irrespective of whether the grant will be paid over one or more years. And all the money raised in one appeal is allocated to projects before the next campaign begins. BBC Children in Need raised over £30 million from its most recent appeal in November 2003 and expects to have committed that amount by August 2004. Comic Relief raised an average of £48 million a year and, after the cost of fundraising and transfers to reserves, made grants averaging some £32 million a year in the two years to September 2003.

The **Lloyds TSB Foundation for England and Wales** receives each year a percentage of the profits of Lloyds TSB Group plc (a separate organisation) based on an average over the previous three years. The timing and sensitivity of the announcement of the latest annual profits means that the Foundation is not wholly certain of its income each year until after the start of its financial year. But it does not make commitments in excess of its annual income and has time over the rest of the year to adjust its grant making if income is lower than expected.

The **Wellcome Trust** is funded through money generated by its asset base of over £9 billion. The trustees have set a target for earnings of 4.5 per cent a year, which they consider to be a prudent and achievable level. Each year the Trust aims to make grants equivalent to four per cent of a three year weighted average value of its underlying asset base, which allows for target growth of 0.5 per cent a year in the asset base and a consequent growth in grant making.

Source: National Audit Office interviews with charitable grant making trusts (March/April 2004)

## 15 Distributors' levels of commitments at 31 March 2004 compared with their maximum acceptable levels of commitments



### NOTES

- Where distributors do not make 'excess' commitments (see paragraph 3.5), their maximum acceptable level of commitments is equal to their National Lottery Distribution Fund balances.
- Arts Council England, Sport England and UK Sport are not shown since these distributors have not specified a maximum acceptable level of commitments (see paragraph 3.5).

Source: National Audit Office survey of lottery distributors (February/March 2004) and analysis of data provided for the Department for Culture, Media and Sport by distributors as at 31 March 2004 (which may be subject to adjustment)

All distributors confirmed that they could attract sufficient, suitable applications to be able to make more commitments, without compromising value for money

- 3.8 If they are to increase their commitments, distributors need to attract more grant applications or fund more of the applications that they receive already. The applications must be worthy of funding so that value for money is not compromised. All distributors confirmed that they could attract sufficient, suitable applications to be able to make more commitments. And all considered that there was capacity within the sectors they funded to deliver more projects, although the New Opportunities Fund had experienced capacity difficulties on some of its programmes (specifically those relating to childcare and palliative care).
- 3.9 All but two distributors<sup>8</sup> confirmed that they had the internal capacity to handle more grant applications and to manage the grants that would result from making more commitments.

Eight distributors, including those with the largest balances, consider that increasing commitments is a realistic way of reducing National Lottery Distribution Fund balances

- 3.10 Eight distributors regard increasing the value of commitments as a realistic way of reducing their National Lottery Distribution Fund balances (Figure 16). Between them, these eight distributors currently receive 83 per cent of the income from the sale of lottery tickets and they accounted for 82 per cent of the balances held in the National Lottery Distribution Fund at 31 March 2004.

Increasing commitments could have a significant impact on National Lottery Distribution Fund balances, although it would take time for the impact to be felt

- 3.11 Further progress in reducing total National Lottery Distribution Fund balances will be largely dependent on movement in the balances of the larger distributors (see paragraph 2.11). So to test whether increasing commitments is a realistic way of reducing balances, we modelled the impact of a large distributor making more grant commitments, using historical data from the Heritage Lottery Fund as a starting point. **The modelling was an illustrative exercise, designed to project the impact that changes to grant making could have on the level of balances.** More details of our approach are set out in the Appendix.

- **Figure 17** shows a baseline scenario which assumes that the National Lottery continues beyond 2009 and distribution arrangements remain unchanged, lottery income remains steady, and the distributor makes grant commitments totalling £2.5 billion over the next 10 years, gradually declining year on year until annual commitments and annual income are more or less equal.
- **Figure 18** shows the impact of the distributor significantly increasing its level of grant making from 2005-06 to 2007-08 compared with the baseline scenario, but still making grant commitments totalling £2.5 billion over the next 10 years. No changes were made to income or other assumptions.

Increasing commitments in this way would halve the distributor's National Lottery Distribution Fund balances almost a year earlier than under the baseline scenario, and the balances would reach a stable state - with annual commitments and annual income more or less equal - at least three years earlier.

**16 Distributors' views on the statement: "Increasing the value of commitments is a realistic way of reducing our National Lottery Distribution Fund balances"**

Strongly agree	Tend to agree	Tend to disagree	Strongly disagree
Heritage Lottery Fund	Arts Council England	Arts Council of Northern Ireland	Millennium Commission
Sport Scotland	Community Fund	Arts Council of Wales	Scottish Arts Council
Sports Council for Northern Ireland	New Opportunities Fund		Scottish Screen
Sports Council for Wales	UK Sport		Sport England
			UK Film Council

Source: National Audit Office survey of lottery distributors (February/March 2004)

<sup>8</sup> The two distributors were the Millennium Commission, which is winding down, and the Sports Council for Northern Ireland, one of the smallest distributors.

There is some but more limited scope for distributors to reduce balances by increasing their speed of spending

Eleven distributors do not consider that speeding up projects is a realistic way of reducing National Lottery Distribution Fund balances

3.12 Eleven distributors do not see speeding up projects as a realistic way of reducing their National Lottery Distribution Fund balances, although four do (Figure 19). Between them, these four distributors currently receive 52 per cent of the income from the sale of lottery tickets and they accounted for 37 per cent of the balances held in the National Lottery Distribution Fund at 31 March 2004.

However, there is scope for distributors to influence the time projects take to complete and draw down their funding

3.13 Figure 8 on page 14 sets out the steps between a distributor awarding funding to a project and the grant recipient drawing down the money. The time taken to complete projects and for all the funding to be drawn down can vary considerably depending on the type of grant and the particular circumstances of the project in question. Grants to pay for the provision of services are given usually for periods of either one or three years. Projects in receipt of grants to fund construction work can be scheduled to take many years to be completed and in general the larger the grant, the longer the project takes to be completed. And projects can also run into problems which cause them to be delayed beyond their scheduled completion date.

**17 An illustration of movement in a distributor's National Lottery Distribution Fund balances assuming a gradual reduction in grant making from 2005-06 onwards**



**NOTE**

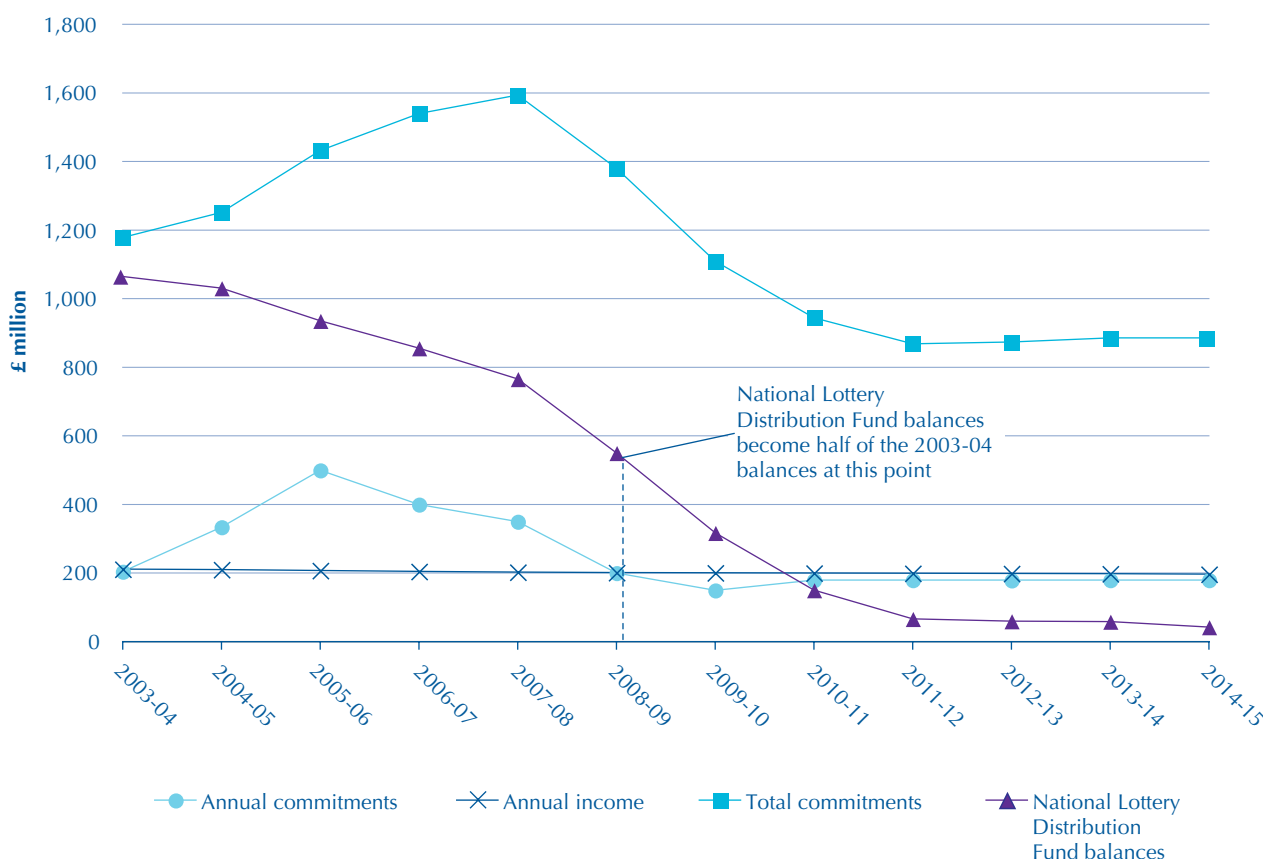
Figure 17 shows the position if grants totalling £2.5 billion are made between 2005-06 and 2014-15, with a gradual reduction over time until annual commitments and annual lottery income are more or less equal.

Under this illustrative scenario, the distributor's balances in the National Lottery Distribution Fund would become half of their 2003-04 level in around late 2009 or early 2010, and a stable position would not be reached until at least 2014-2015.

The scenario assumes that the National Lottery and current distribution arrangements continue beyond 2009 and that lottery income remains steady. Uncertainty surrounding these factors is considered in Part 4.

Source: National Audit Office

**18** An illustration of movement in a distributor's National Lottery Distribution Fund balances assuming higher levels of grant making from 2005-06 to 2007-08



**NOTE**

Figure 18 takes the baseline shown in Figure 17 but changes the pattern of grant making so that commitments are significantly higher in the three years from 2005-06 to 2007-08, although the total value of grants made remains at £2.5 billion between 2005-06 and 2014-15.

Under this illustrative scenario, the distributor's balances in the National Lottery Distribution Fund would become half of their 2003-04 level about a year earlier, in early 2009, and a stable position would be reached several years earlier, in 2011-12.

The scenario assumes that the National Lottery and current distribution arrangements continue beyond 2009 and that lottery income remains steady. Uncertainty surrounding these factors is considered in Part 4.

Source: National Audit Office

**19** Distributors' views on the statement: "Speeding up projects is a realistic way of reducing our National Lottery Distribution Fund balances"

Strongly agree	Tend to agree	Tend to disagree	Strongly disagree
Scottish Arts Council	Community Fund	Arts Council of Northern Ireland	Arts Council England
	New Opportunities Fund	Millennium Commission	Arts Council of Wales
	Sports Council for Northern Ireland	Sport Scotland	Heritage Lottery Fund
		UK Film Council	Scottish Screen
			Sport England
			Sports Council for Wales
			UK Sport

Source: National Audit Office survey of lottery distributors (February/March 2004)

- 3.14 Responsibility for the management of each funded project rests with the grant recipient and the time taken to complete projects lies essentially in their hands and beyond the direct control of distributors. Nevertheless there are ways in which distributors can influence the time taken to complete projects and in August 2003 the Department circulated good practice examples of steps some larger distributors were already taking to pay grants more quickly (Figure 20).
- 3.15 As part of their applications for funding, grant recipients provide distributors with a timetable for their project and details of when they expect to draw down their funding. Getting projects started once funding has been awarded can take some time. The need to raise partnership funding from other sources can be particularly difficult and time-consuming, especially for small organisations working in sectors where it can be difficult to raise funds independently. In deciding whether to relax partnership funding requirements, distributors have to weigh up the benefits of getting a project going and lottery money spent more quickly with the fact that providing a higher grant to one project will mean less money available for others.
- 3.16 Most grants are paid in stages after grant recipients have submitted claims for reimbursement of expenditure already incurred, supported by appropriate receipts or other evidence. However, under Treasury guidance, distributors have the flexibility to make payments ahead of expenditure being incurred where a need for advance payment has been identified, for example in the case of voluntary and community groups which may not have the resources to undertake an activity first and receive payment later. The Department highlighted this flexibility in the timing of payments in the guidance it issued to distributors in August 2003.
- 3.17 Most distributors make advance payments in certain circumstances, most commonly to low value and/or low risk projects. For example, the Arts Council of Wales will pay in advance some small capital grants to fund the purchase of musical instruments or other equipment. From the distributors' perspective, making advance payments means that the funds stay in the National Lottery Distribution Fund for less time, although it reduces the control that they have over the money and means they lose the benefit of any interest that might be generated.
- Speeding up projects could have some impact on National Lottery Distribution Fund balances, but the impact would be less than from increasing commitments
- 3.18 For illustrative purposes, we modelled the impact that speeding up projects might have on the National Lottery Distribution Fund balances held by a large distributor.
- Using the lottery income and grant assumptions in Figure 17 on page 23 as a baseline, we looked at the effect of projects awarded funding after 2004-05 claiming five per cent of their total grant a year earlier. Under this scenario, the distributor's balances would halve sometime in mid-2009, compared with late 2009 or early 2010 if previous patterns of spending were to continue.
  - To achieve the same effect as that achieved by increasing commitments in the three years from 2005-06 to 2007-08 in the way shown in Figure 18, the amount paid each year would have to be 50 per cent higher.

## 20 How distributors can reduce the time taken to complete projects and pay grants

- Simplifying application processes for their main grant programmes, and adopting performance indicators that encourage greater simplicity and speed in their processing of applications.
- Focusing their smaller grant programmes on outputs that can be delivered quickly.
- Making commitments only where the prospective grant recipient is fully committed to the project and has a clear timetable for moving it to the next stage.
- Relaxing partnership funding requirements to help small organisations, those lacking liquidity or others which might have difficulty in raising funds independently, to get their projects underway in good time once an award has been made (see paragraph 3.15).
- Agreeing action plans with successful grant applicants, including deadlines for the drawdown of funding to encourage the fastest practicable drawdown.
- Advancing a proportion of grant to low risk and/or low value projects to help with their cash flow (see paragraph 3.16 and 3.17).

Source: Department for Culture, Media and Sport guidance note (August 2003)



# Part 4

## Distributors face a range of uncertainties and risks in managing their National Lottery Distribution Fund balances

4.1 To manage their National Lottery Distribution Fund balances effectively and identify the scope to reduce balances by increasing their commitments, distributors need to know how much money they have available to commit to new projects. A distributor's capacity to make new commitments is determined by:

- the balances it holds in the National Lottery Distribution Fund;
- **plus** its assessment of likely future lottery income;
- **less** its assessment of likely future expenditure on grants (stemming from existing commitments) and administration.

Although distributors know the level of balances that they hold in the Distribution Fund, the other components of their funding capacity are uncertain. This part of the report examines the uncertainties and risks that distributors face in managing their balances.

### There is uncertainty about lottery distribution arrangements in the future

#### The current licence to operate the National Lottery runs until 2009

4.2 The current licence to operate the National Lottery runs until January 2009 and the Department is currently working on the arrangements for licensing the Lottery after that. All distributors<sup>9</sup> rate the risk that the Lottery will not continue beyond the current licence as low, although they are somewhat less sure about the proportion of lottery proceeds that might be allocated to the good causes in the future. Some distributors also highlighted that their own future as distributors is not guaranteed.

4.3 Although low risk, the uncertainty about future distribution arrangements beyond the end of the current licence affects distributors' ability to plan their grant programmes up to, as well as after, 2009. Distributors

told us that, given the time lag between awarding and paying grants, without assurances they would need to stop making new grants well before 2009, and possibly as early as 2005-06, to ensure that all of the grant commitments they have made can be met from lottery proceeds up to 2009.

4.4 We used our lottery distribution model (see the Appendix) to assess the potential impact of this uncertainty on a distributor. We took the scenario shown in Figure 18 on page 24 (which modelled a distributor making increased commitments in the three years from 2005-06 to 2007-08 and assumed income continuing beyond 2009) and looked at the effect of the distributor ceasing to receive any income from the sale of lottery tickets after the end of the current licence period in January 2009. In this new scenario, the distributor would run out of money by 2010 and have outstanding commitments to projects of around £700 million which it would be unable to meet.

### The share of lottery proceeds that the good causes receive could change

4.5 Since the National Lottery was established, the Government has made a number of changes to distribution arrangements, with adjustments to the funds available for the existing distributors. For example, in 1998 the Government introduced a new good cause (health, education and the environment) to be administered by a new distributor, the New Opportunities Fund. The Fund initially received 13.33 per cent of lottery proceeds and the shares received by the arts, sport, national heritage, and charities and voluntary organisations were each reduced from 20 per cent to 16.67 per cent to allow for this.

4.6 The Government has given a commitment that the percentage share of lottery proceeds allocated to each of the arts, sport, national heritage, and charities and voluntary organisations will remain at least at their current levels until 2009 (see Figure 5 on page 11). No

<sup>9</sup> The analysis in this part of the report relating to future lottery distribution arrangements and lottery income excludes the Millennium Commission, which stopped receiving income from the sale of lottery ticket in 2001 and will no longer exist after 2006.



such guarantee has been given about the share of proceeds received by the New Opportunities Fund. Beyond 2009 the Government has made no commitments about how lottery proceeds will be split between the existing good causes or whether any new good causes will be added. However, all but one distributor rate the likelihood of any reduction in their share of lottery proceeds as medium or low.

## There is uncertainty about the lottery income that distributors will receive

There is no guarantee about the amount of money that will be raised from lottery ticket sales

- 4.7 The operator of the National Lottery, presently Camelot Group plc, contributes a proportion of the proceeds from the sale of lottery tickets (after the deduction of prize money and lottery duty) to the good causes. The proportion varies depending on the level of sales and the value of prizes paid. The amount of income that distributors will receive is therefore uncertain.
- 4.8 The uncertainty about future lottery income is more significant for distributors given the gradual decline in ticket sales in recent years. Total proceeds from the sale of lottery tickets fell from a peak of £5.5 billion in 1997-98 to £4.6 billion in 2002-03.
- 4.9 To help distributors plan their grant programmes, the Department provides them with projections of annual income for the National Lottery Distribution Fund as a whole for the remainder of the current licence period, which runs until January 2009. The projections are based on historical sales data, which the Department receives from the National Lottery Commission<sup>10</sup>. Most distributors rely heavily on the projections for managing their business and consider that the

projections provide them with confidence for planning purposes in the short term. Distributors are less confident in the projections when it comes to using them for planning in the medium and long term.

- 4.10 The Department provides a commentary with the projections to explain the assumptions that underlie them. However, some distributors are unclear about the basis on which the income projections are compiled and consider that the Department tend to be over-optimistic in projecting lottery revenue. The Scottish Arts Council and the UK Film Council abate the projections before using them, and the Arts Council of Wales has set aside a contingency of £500,000 from its projected income for 2004-05 as a cushion against possible reductions in the projections over the course of the year. It proposes to release the contingency during the year if lottery proceeds are in line with the projections.
- 4.11 We reviewed the accuracy of the projections by comparing projected income against actual income for 2002-03. This indicated that the Department's June 2001 projection, the last one before the start of the financial year 2002-03, was within 2.4 per cent of the actual income received. Subsequent projections were revised downwards during the course of the year and were lower than the income received (**Figure 21**).
- 4.12 The Department's aim is to issue projections every quarter and most distributors consider that the projections are issued sufficiently frequently to be of use to them. However, a gap of seven months between projections in 2003 (while the impact of the proposed Olympic lottery games was being assessed) had caused difficulties.
- 4.13 Distributors made a range of suggestions to us as to how the Department might improve the income projections to make them more useful (**Figure 22**).

## 21 Comparison of projected and actual lottery income for 2002-03

Projection issued in	Projected lottery income for 2002-03 (£ million)	Difference between projected and actual lottery income for 2002-03	
		(£ million)	(%)
June 2001	1,630	38	2.4
June 2002	1,543	(49)	(3.1)
September 2002	1,568	(24)	(1.5)
February 2003	1,569	(23)	(1.4)
<b>Actual</b>	<b>1,592</b>	-	-

Source: Department for Culture, Media and Sport and National Lottery Distribution Fund Account 2002-03

## 22 How the Department could improve the income projections

- Provide the projections in accordance with a clear timetable.
- Tailor the projections to individual distributors to make them more user-friendly, in particular for the projections of investment income.
- Provide further information about the basis of the projections and the underlying assumptions.
- Review periodically the accuracy of the projections against actual income and report the results of the reviews to distributors.

*Source: National Audit Office survey of lottery distributors (February/March 2004)*

### The impact of the proposed Olympic lottery games on the existing good causes is uncertain

4.14 From our survey of distributors, it is clear that the factor causing them most concern at present is the uncertainty arising from the proposed introduction of Olympic lottery games. The Horserace Betting and Olympic Lottery Bill, which is currently before Parliament, provides for the introduction of lottery games which will raise money specifically for the Olympic and Paralympic Games in 2012. Camelot plans to raise £750 million through these Olympic lottery games to help meet the costs of staging the Games, should London's bid be successful. A decision on which city will host the Games will be made by the International Olympic Committee in July 2005.

4.15 All but two distributors consider that there is a high likelihood that the introduction of Olympic lottery games will reduce the money available to the existing good causes by diverting sales from other games, and all but two think the impact would be high. Assessments of the impact of the Olympic lottery games, provided by Camelot to the National Lottery Commission, suggest that 59 per cent of the £750 million to be raised from the new games over their seven year life might come from players switching from existing lottery games. This could mean an average reduction in income to the existing good causes of some £64 million (five per cent) a year. Camelot expects that the reduction in income to the existing good causes would be lower in the early years and more in the years leading up to the Games in 2012.

4.16 The Department has taken account of the estimated impact of Olympic lottery games in its recent projections of future lottery income, although most distributors tend to lack confidence in this aspect of the projections.

4.17 As well as the impact of the proposed Olympic lottery games, the proposals for funding the 2012 Olympics and Paralympics are also causing other uncertainties for distributors. In total the National Lottery is expected to provide up to £1.5 billion to help meet the costs of staging the Games, should London's bid be successful. In addition to the £750 million to be raised from the new games, the Government proposes that:

- £340 million will come via expenditure by the five sports distributors, who will decide how the money is spent in their part of the United Kingdom. How this money might be apportioned between these distributors has not yet been decided but the Department envisages that the bulk will come from Sport England;
- the remaining £410 million, should it be needed to meet the costs of the Games, could be derived from changing the shares of lottery proceeds allocated to the existing good causes after 2009. No decisions have yet been made about the shares beyond 2009.

### Investment income is uncertain and the Department proposes to change the way in which it is allocated to distributors to ensure there is no incentive to maintain high balances

4.18 As well as the proceeds from lottery ticket sales, distributors also receive investment income on their balances in the National Lottery Distribution Fund. The balances are invested by the Commissioners for the Reduction of the National Debt (see paragraph 1.4) in gilt-edged and other government guaranteed securities<sup>11</sup>.

4.19 Investment income is uncertain since it comprises interest on the balances, which depends on the interest rate paid on the gilts, plus or minus any gains or losses on the sale or revaluation of the investments, which depends on changes in the financial markets. The uncertainty of investment income is illustrated in **Figure 23**.

4.20 At present the investment income earned on the total National Lottery Distribution Fund balances is apportioned between distributors according to the percentage of the balances that they hold (see paragraph 1.5). In July 2003 the Decision Document on National Lottery Funding announced that, to ensure there is no financial incentive for distributors to retain funds in balances, the Department would introduce legislation to provide that in future the investment income would be shared in the same proportion as the proceeds from lottery ticket sales and not directed to those with the largest balances.

<sup>11</sup> Gilt-edged securities are United Kingdom Government bonds which mature at a specified date and which give an agreed dividend until then. The other government guaranteed securities are cash deposits for periods of up to six months.

**23 National Lottery Distribution Fund investment income between 2001-02 and 2003-04**

Year	Interest from investments (£ million)	Gains/losses from: sale of investments (£ million)	revaluation of investments (£ million)	Net income (£ million)
2001-02	204	1	(22)	183
2002-03	192	15	5	212
2003-04	156	(48)	(16)	91 <sup>1</sup>

**NOTE**

1 This figure does not cast correctly due to rounding.

Source: National Lottery Distribution Fund Account for 2001-2002 (HC 573, Session 2002-03) and 2002-2003 (HC 313, Session 2003-04); National Lottery Distribution Fund draft account for 2003-2004

4.21 Based on the investment income received and balances held in the National Lottery Distribution Fund in 2003-04, we calculated that six distributors would have received more investment income using the proposed new method of apportionment and eight would have received less<sup>12</sup>. In absolute terms, the largest impact would have been on the Heritage Lottery Fund, whose investment income in 2003-04 would have been £15.7 million (53 per cent) less under the new proposals. The largest percentage impact would have been on UK Sport, whose investment income in 2003-04 would have been 1,847 per cent (£1.2 million) more.

## There is uncertainty about distributors' future expenditure

### Distributors lack confidence in the forecasts of expenditure that projects provide

4.22 As part of the funding application process, projects provide distributors with forecasts of when they expect to incur expenditure and claim grant. Distributors use these forecasts to inform their own requests to draw down funds from the National Lottery Distribution Fund so that they have cash available when projects submit their claims for payment (see paragraph 4.25) and to help calculate the amount of money they will have available in the future to make other commitments.

4.23 Our survey revealed mixed views about the forecasts of expenditure that projects provide in terms of the accuracy of the forecasts and the extent to which projects draw down money in line with them. And distributors also had a range of views about whether the forecasts allowed them to predict accurately their own drawdown from the National Lottery Distribution Fund, with distributors less confident in the forecasts in the medium and long term (Figure 24).

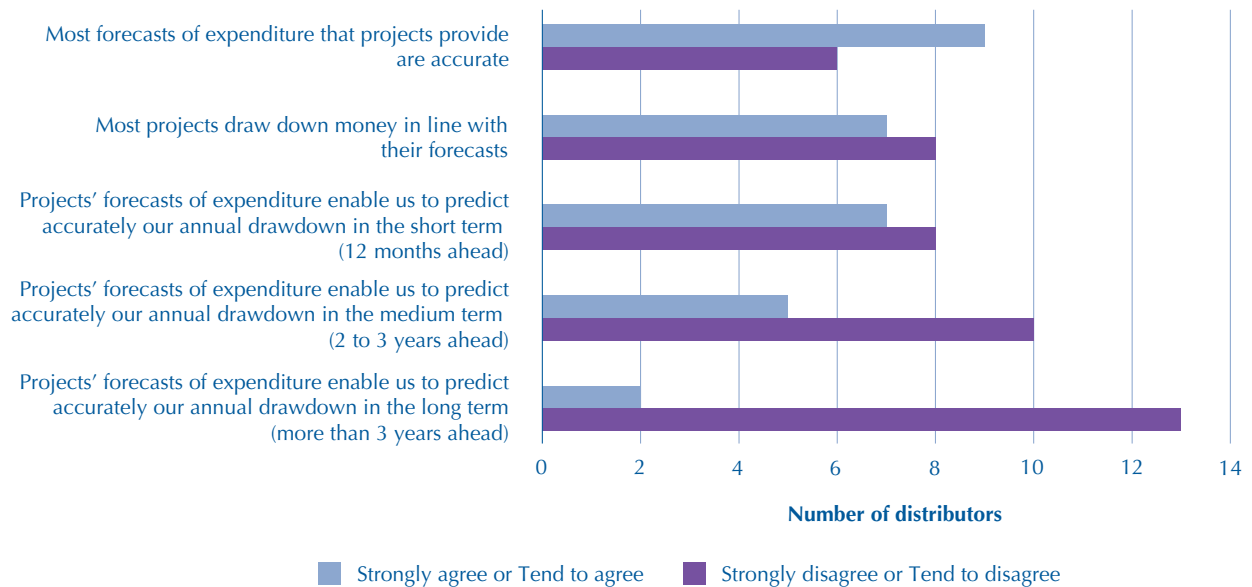
4.24 One of the charitable trusts we visited had introduced arrangements for making some payments in advance which provided projects with an incentive to draw down funding in line with their forecasts (Figure 25).

Most distributors could estimate more accurately the amount of money they need to draw down from the National Lottery Distribution Fund and this would have financial benefits

4.25 Distributors submit 'drawdown requests' to the Department each time they wish to obtain cash from their National Lottery Distribution Fund balances to pay grants or meet their own expenses. Distributors may hold funds in their own bank accounts for a short time to facilitate the smooth and timely payment of grants but should not draw down more funds than they think they will need during the period as this has a financial cost in terms of lost interest (see paragraph 4.28). Most distributors make monthly drawdown requests but four make weekly requests. All distributors have the facility to make emergency drawdown requests in between their regular requests, if the need arises, and seven distributors made use of this facility in 2003-04.

4.26 We reviewed drawdown requests made by distributors in 2002-03 and 2003-04 and compared their estimates of payments to be made in the next period with the payments actually made. This analysis showed that some distributors were much better at predicting their cash requirements than others. Most distributors over-estimated the payments that they expected to make in the next period, and therefore drew down more money than they needed. Some distributors estimated the same standard amount for expected grant payments each month.

## 24 Distributors' views on the forecasts of expenditure provided by projects



Source: National Audit Office survey of lottery distributors (February/March 2004)

## 25 Example of an incentive for projects to draw down money in line with their forecasts

The **Wellcome Trust** usually pays grant instalments quarterly in arrears to the research projects it supports, on the basis of certified claims. However, provided projects are drawing down grant in line with their original forecasts, the Trust will pay 60 per cent of the grant monthly in advance by standing order. This has cash flow advantages for the projects and allows the Trust to keep control of the grant through the final adjusting payment, which is claimed in the usual way.

Source: National Audit Office interview with the Wellcome Trust (April 2004)

4.27 To assess the accuracy of distributors' estimates of the cash they require, we analysed distributors' drawdown requests to the Department for drawdown periods (either monthly or weekly) for April 2003 to March 2004 to see what cash balances distributors were carrying forward (**Figure 26**).

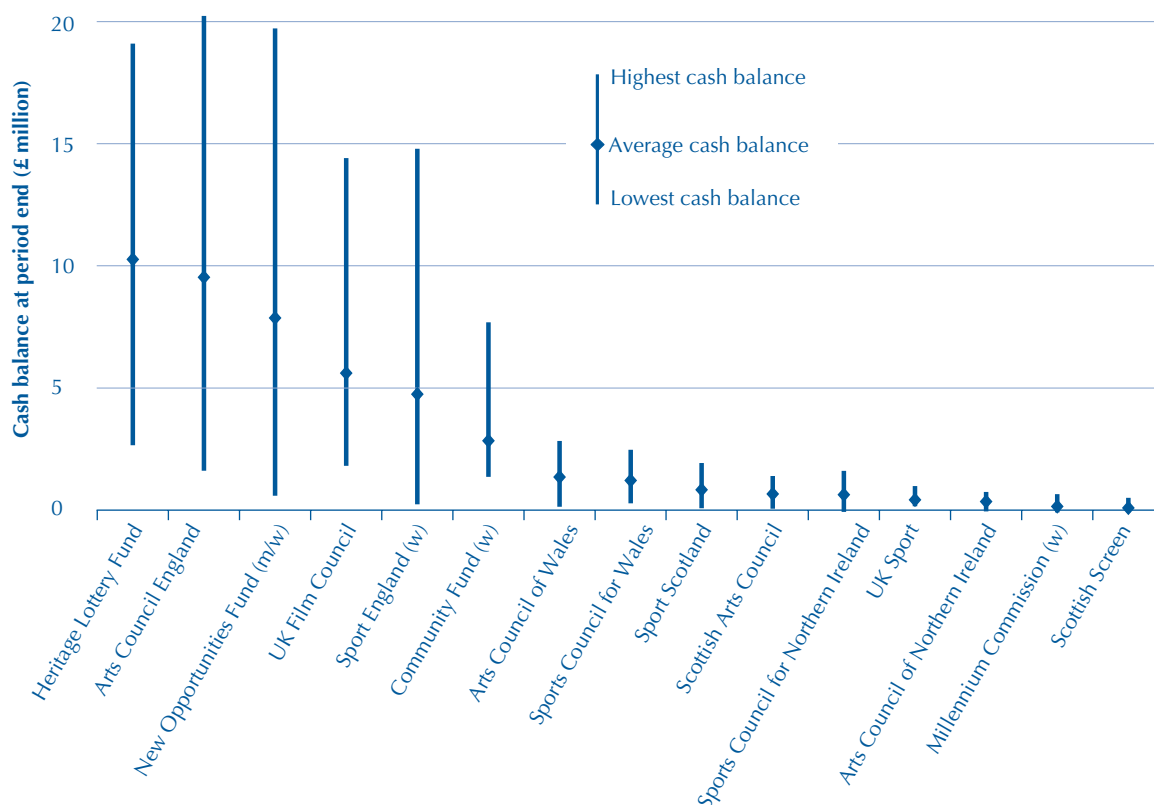
- Eight distributors had an average cash balance of over £1 million, of which four had an average balance of over £5 million.
- Five distributors had maximum cash balances of between £14 million and £21 million.

4.28 Although distributors can place the money they draw down from the National Lottery Distribution Fund in interest-bearing instant access accounts, the rate of interest achieved is likely to be less than the return received on the balances in the Distribution Fund and the interest may be taxable, further reducing the rate of return achieved. The financial benefits of distributors making more accurate drawdown requests, leading to money remaining in the National Lottery Distribution Fund rather than in distributors' own bank accounts, could be sizeable. For example, in 2002-03 concerns about the level of cash balances being held by the New Opportunities Fund led to the Fund making more frequent and accurate drawdown requests, with a potential financial benefit of between £1 million and £3 million a year through increased interest received and less tax paid. An example of good practice in making more accurate drawdown requests is shown in **Figure 27**.

**Distributors could find themselves in difficulty if income was significantly less and/or expenditure significantly more than expected**

4.29 The uncertainties surrounding future lottery income and expenditure expose distributors to a number of risks that could materialise if income ended up significantly less and/or expenditure significantly more than expected.

**26 Distributors' highest, lowest and average cash balance at the end of each drawdown period in 2003-04**



**NOTE**

Eleven distributors drew down from the National Lottery Distribution Fund on a monthly basis in 2003-04. Three distributors drew down on a weekly basis (w) throughout 2003-04 (the Community Fund, the Millennium Commission and Sport England) and the New Opportunities Fund switched from monthly to weekly drawdowns in October 2003 (m/w).

Source: National Audit Office analysis of data from the Department for Culture, Media and Sport

**Distributors could have insufficient funds to meet the grant commitments they have made**

4.30 If their estimates of lottery income and/or expenditure turned out to be very inaccurate, distributors could have insufficient funds to meet the grant commitments they have made or they might have to refrain from making any further commitments. Such a situation could harm distributors' own reputation and have damaging effects on the sectors they support and on the individual projects in question. Incomplete projects would need to seek funding from elsewhere or remain unfinished, with the money already spent wasted.

4.31 Based on their current approach to making commitments (see paragraph 3.5), all distributors considered that the likelihood of their being unable to meet the grant commitments that they had already made was low and all but three distributors rated the likelihood of being unable to make further commitments also as low. **Figure 28** outlines what happened at Sport England when it identified that there was a risk that it might have insufficient funds to cover the commitments it had made.

**27 An example of good practice in making more accurate drawdown requests**

The Millennium Commission makes weekly drawdown requests from the National Lottery Distribution Fund. Each week it calculates the amount it needs to draw down by adding up the grants it has approved for payment and an estimate of its administration costs for the week ahead, and subtracting its current bank balance. It also maintains a working balance of £30,000 in its bank account.

In 2003-04 the Millennium Commission's weekly estimates of grant payments were within two per cent of the payments actually made, other than for three weeks. The average balance in the Millennium Commission's bank account was £134,047.

Source: National Audit Office analysis of data from the Department for Culture, Media and Sport

## 28 What happened at Sport England

In 2002 Sport England identified that there was a risk that it might have insufficient funds to cover all the commitments it had made. Sport England's income had turned out to be lower than it had once expected because of the decline in lottery ticket sales, and its share of lottery proceeds had fallen with the setting up of the New Opportunities Fund and UK Sport. The position was aggravated by the fact that some capital projects had taken longer than expected to draw down funds.

To address the potential shortfall between commitments and the funds it had available, Sport England stopped making further commitments to new projects for nine months. It also:

- reviewed projects that had made no recent progress to confirm whether they were still 'live' and de-committed funds from those that were no longer active, and
- de-committed grants from projects that it considered were no longer in line with its strategic priorities,

which enabled it to de-commit some £31 million.

*Source: National Audit Office*

4.32 All distributors are managed by trustees or board members who are responsible for approving individual grant awards and who, in some cases, could potentially be personally liable for honouring the grant commitments that their organisation has made, if the organisation turns out to have insufficient funds. However, all distributors rated as low the likelihood that trustees or board members would have to meet grant commitments that could not be met from lottery income.

## Distributors might not be regarded as a 'going concern'

4.33 Accounts prepared by the distributors should comply with United Kingdom Financial Reporting Standards (or explain any material departure from those standards). Under the Standards, distributors are required to prepare their accounts on a 'going concern' basis unless there are significant doubts as to their ability to continue as a going concern<sup>13</sup>.

4.34 The accounts directions within which distributors work (see paragraph 1.8) require distributors to recognise 'hard' commitments<sup>14</sup> as liabilities in full in the year they are made, even if the grants are not due to be paid for a number of years. Lottery income is recognised as an asset in the accounts only when it is receivable, so income for future years cannot be anticipated. This means that distributors may find that their liabilities exceed their assets, which in some situations could be interpreted as an indication that they are not a going concern. Distributors must be able to satisfy themselves and their auditors that they are reasonably certain that they will be able to meet their liabilities in the future.

4.35 The need to ensure that they are a going concern may inhibit some distributors from making large amounts of commitments against future income. However, at the levels of commitment described in paragraph 3.5, all but two distributors considered that the likelihood of their organisation not being a going concern because of the value of its assets and liabilities was low.

<sup>13</sup> Financial Reporting Standard 18, Accounting Policies. The assumption that an entity is a going concern is "the hypothesis that the entity is to continue in operational existence for the foreseeable future". The term 'foreseeable future' is not defined but is generally taken to mean one year after the approval of the accounts by management.

<sup>14</sup> A commitment is 'hard' when there is a signed contract between the distributor and the grant recipient.

# Appendix

## Study scope and methods

### Objectives and scope

- 1 The Decision Document on National Lottery Funding, published by the Department for Culture, Media and Sport in July 2003, highlighted "widespread concern" about how much lottery money was yet to be distributed and announced that, following discussions with the Department, the National Audit Office was to carry out an examination of balance management, which would inform other steps aimed at reducing the balances.
- 2 The objective of our examination was to consider whether there were ways in which the balances held in the National Lottery Distribution Fund could be reduced, within the existing framework of good causes set out in lottery legislation. Rather than looking in detail at the grant making and monitoring arrangements of lottery distributors on an individual basis, we focused on getting an overall sense of the opportunities for balances to be reduced.
- 3 We used an issue analysis approach to design the study and determine the nature of the evidence we required. We identified five high-level questions on which to base our assessment of whether there were ways in which balances could be reduced.
  - Do distributors have all the necessary information to manage their National Lottery Distribution Fund balances effectively?
  - Can distributors reduce balances by increasing their commitments to pay grants?
  - Can distributors reduce balances by turning commitments into payments more quickly?
  - Are there other factors that may affect distributors' ability to reduce balances?
  - Can the Department do more to help distributors manage their balances better?

### Methods

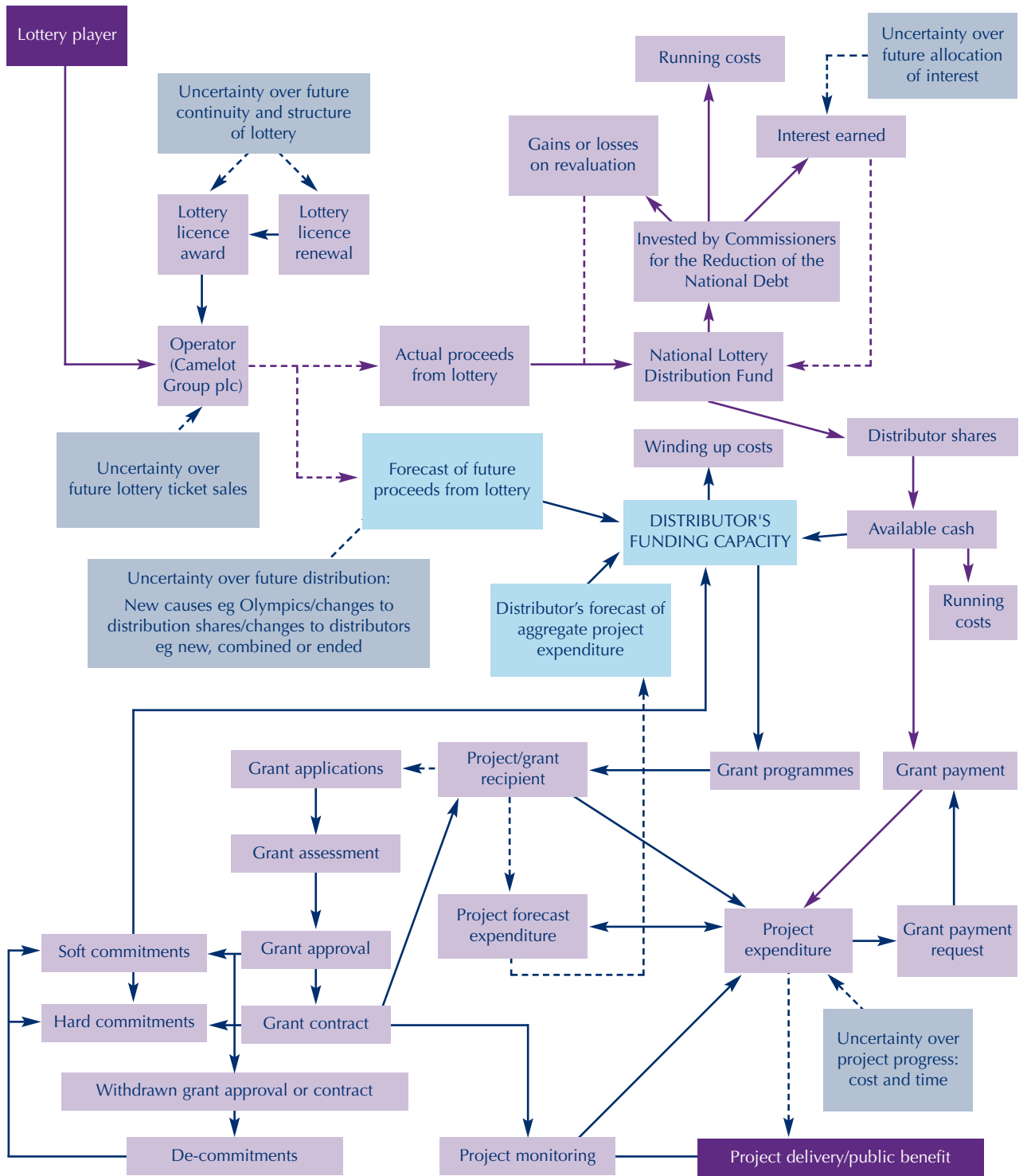
#### Mapping National Lottery funding and distribution

- 4 To develop our understanding of the factors that affect lottery funding and distribution, we mapped the flow of National Lottery funds and the uncertainties that impact on the various stages of the process (**Figure 29**). From this work, we identified the importance of what we termed a distributor's 'funding capacity' - that is its capacity at any time to make new commitments to pay grants. The funding capacity is the net total of the balances held by the distributor in the National Lottery Distribution Fund plus its likely future income less its likely future expenditure stemming from the commitments it has already made.

#### Modelling National Lottery distribution

- 5 We developed a model of National Lottery distribution to assess the impact changes in grant making behaviour (for example, in a distributor's level of commitments to pay grants or in the speed with which commitments are turned into payments) might make on the National Lottery Distribution Fund balances held by a distributor. The modelled scenarios we have shown in the report are illustrative exercises designed to project the impact that changes to grant making could have on the level of balances. The scenarios are not designed to predict what any distributor might do in future years or what its level of balances might be. We are grateful to the Heritage Lottery Fund and the Arts Council of Wales, who provided us with historical data so that we could develop the model.
- 6 The model is based on the premise that, over the life of a distributor, its lottery income and expenditure should balance (that is, all its lottery income should be spent and all its commitments to pay grants should be met) and, by the end of its life, it should have no funds outstanding.

29 Map of National Lottery funding and distribution



- Events in the flow of money, information or grant application, award and monitoring processes. Not all stages are necessarily shown.
- Areas of significant uncertainty, which generate risk and require judgement.
- Areas of strategic or fundamental judgement.
- These lines show the flow of lottery money and have two 'dimensions' (not shown): 'width' ie the volume of the flow (eg of money or value of grants) and 'length' ie the time taken between stages or events.
- Solid lines show process or information flows where there is certainty.
- Dotted lines show process or information flows where there is uncertainty (i.e. processes, flows, or decisions that are outside of distributors' control).



7 The model uses the following groups of data to calculate, on an annual basis, the cumulative level of commitments a distributor has made and the balances it holds in the National Lottery Distribution Fund.

Income	<ul style="list-style-type: none"> <li>■ Total lottery income from the sale of National Lottery tickets each year.</li> <li>■ Distributors' shares of the income from the sale of National Lottery tickets.</li> <li>■ Rate of return on the balances held in the National Lottery Distribution Fund.</li> </ul>
Commitments	<ul style="list-style-type: none"> <li>■ Net level of commitments made by a distributor each year (new grant commitments made less grants de-committed or withdrawn).</li> <li>■ The percentage of commitments made each year within specified value bands or split between capital grants and grants for the provision of services.</li> </ul>
Expenditure	<ul style="list-style-type: none"> <li>■ The percentage paid each year of grants of different values or types.</li> <li>■ A distributor's running costs.</li> </ul>

8 The model could provide a tool to help distributors assess their funding capacity and manage their National Lottery Distribution Fund balances effectively. We have agreed with the Department that we will share the model with distributors. Accordingly, we are now preparing a user-friendly format for distribution.

### Survey of lottery distributors

9 We carried out a survey of the 15 National Lottery distributors to collect information and views on their approach to managing their National Lottery Distribution Fund balances. All distributors responded. The survey covered the following main areas.

Area	We looked at this to see:
Policies and targets	<ul style="list-style-type: none"> <li>■ Whether distributors have written policies for managing their National Lottery Distribution Fund balances and targets for the level of balances.</li> </ul>
Lottery income	<ul style="list-style-type: none"> <li>■ What distributors' views are on the projections of lottery income provided by the Department for Culture, Media and Sport and how they use the projections.</li> <li>■ What distributors' views are on possible risks to future lottery income and how these risks might be managed.</li> </ul>
Grant commitments	<ul style="list-style-type: none"> <li>■ What levels of grant commitments distributors are prepared to make.</li> <li>■ What distributors' views are on the possible risks surrounding grant commitments and how these risks might be managed.</li> <li>■ Whether making more commitments would be a realistic way of reducing balances.</li> </ul>
Payments	<ul style="list-style-type: none"> <li>■ How distributors calculate the amounts they need to draw down from the National Lottery Distribution Fund.</li> <li>■ What distributors' views are on the forecasts of expenditure provided by projects and how they use the forecasts.</li> <li>■ Whether speeding up projects would be a realistic way of reducing balances.</li> </ul>
Good practice	<ul style="list-style-type: none"> <li>■ Whether distributors have identified examples of good practice in balance management.</li> <li>■ What changes distributors consider would help them manage their balances better.</li> </ul>

## Structured interviews with selected lottery distributors

- 10 We carried out structured interviews and collected data at four distributors - the Arts Council of Wales, the Heritage Lottery Fund, the New Opportunities Fund and Sport England. These distributors were selected to provide us with good coverage in terms of their different scale of distribution, level of National Lottery Distribution Fund balances, sectors supported and geographical focus.
- 11 We used the structured interviews to supplement the information the distributors had provided in response to our survey and to ensure that we fully understood the answers they had given, in particular on: the impact and likelihood of possible risks to future lottery income and in relation to commitments; their approach to making grant commitments; and managing the delivery of projects and the drawdown of funds from the National Lottery Distribution Fund.

## Other interviews

- 12 We carried out interviews and collected data at the Department for Culture, Media and Sport. This work covered the Department's role in managing the National Lottery Distribution Fund, the target for reducing balances, the projections of future lottery income, the data it receives from distributors, and the provision of guidance to distributors.
- 13 We also carried out interviews with officials from the National Lottery Commission to help our understanding of projections of lottery income and with the Arts, Lottery and Sport Division of the Welsh Assembly Government to assess whether there are any particular implications for devolved distributors from changes in lottery distribution.

## Interviews with charitable grant making trusts

- 14 We carried out interviews with four charitable grant-making trusts to compare their approach to grant making and managing the associated risks with that of lottery distributors. The four trusts were: BBC Children in Need, Charity Projects (better known by its working names of Comic Relief and Sport Relief), the Lloyds TSB Foundation for England and Wales, and the Wellcome Trust.
- 15 We are grateful to the trusts for discussing with us their approach to risk, the uncertainties surrounding their future income and expenditure and how they seek to manage these, their approach to making grant commitments, and managing project delivery and grant payment.