

The budget for the London 2012 Olympic and Paralympic Games

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SUMMARY

1 This is the second in a series of National Audit Office reports on the preparations for hosting the London 2012 Olympic and Paralympic Games. It examines the development of the budget – costs, provisions and funding – for the venues and infrastructure required to host the Games and related costs such as security. The development of the budget has been led by the Department for Culture, Media and Sport (the Department), with input from the Olympic Delivery Authority and the Treasury. A summary of the development of the budget over time is at Appendix 1.

Overview

- 2** On 15 March 2007 the Secretary of State for Culture, Media and Sport (the Secretary of State) announced to Parliament the budget for the Games and infrastructure associated with the Olympic Park and other venues totalling £9.325 billion (**Figure 1**).¹
- 3** References to the ‘budget’ for the Games tend to focus on those costs that are to be publicly funded and therefore exclude the staging costs to be incurred by the

¹ Hansard, 15 March 2007, Columns 450-452.

Summary text continued

London Organising Committee of the Olympic Games and Paralympic Games (LOCOG), which is intended to be self-financing.² As required by the International Olympic Committee, however, the Government is the ultimate guarantor of funding for the Games, including LOCOG's staging costs.

4 At the time of London's bid to host the Games the estimated gross cost of the Games was £4 billion comprising £2.992 billion core Olympic costs plus £1.044 billion for infrastructure on the Olympic Park. These costs were to be met by a public sector funding package of £2.375 billion for the core Olympic costs, £1.044 billion Exchequer funding for the infrastructure, plus an anticipated £738 million from the private sector.

5 The £9.325 billion budget announced in March 2007, which the Department for Culture, Media and Sport has told us represents the upper limit on the funding available for the Games from the public sector, is some £5.289 billion higher than the cost estimate at the time of the bid in gross terms (**Figure 2 overleaf**). Within this overall increase, the cost estimates (before deduction of anticipated private sector funding) for those elements which the Department defines as the 'core' costs of the Olympics are £1.1 billion higher than the estimates at the time of the bid (see Figure 6 on page 16). However, these 'core' costs exclude programme contingency, tax, and policing and wider security.

1 The budget as announced for the Games on 15 March 2007

Costs and provisions ¹	£ million	Public funding available	£ million
Olympic Delivery Authority (ODA) Olympic costs			
Olympic Delivery Authority Core Olympic costs	3,081		
Infrastructure and regeneration costs associated with the Olympic Park and other venues	1,673	Exchequer	5,975
Contingency (excluding tax) ³	500	National Lottery	2,175
Total (net of tax)	5,254	Greater London Authority	925
Other (Non ODA) Olympic costs²	388	London Development Agency	250
Other provisions			
Policing and wider security	600		
Tax (on ODA costs)	836		
General programme contingency (including tax) ³	2,247		
Grand total	9,325		9,325

Source: Department for Culture, Media and Sport

NOTES

- 1 The costs are net of £165 million of private sector funding (further details are provided in Figure 7 on page 17).
- 2 Other (Non ODA) Olympic costs such as support for elite and community sport to be met from public funding.
- 3 The Department's intention was that there would be a contingency of £2.747 billion (as reflected in the Secretary of State's statement of 15 March 2007). This contingency was intended to cover potential financial pressures on the construction of venues and infrastructure, potential increases in the £600 million costs of policing and security and cost increases arising from factors such as unforeseen ground conditions, inflation beyond existing provision, or changes in legislation. The Department intended that an initial amount of £500 million of the contingency would be given to the Olympic Delivery Authority to enable it to manage early pressures.

2 The staging of the Games is intended to be self-financing with the exception of a fifty per cent contribution in 2012 towards the costs of the Paralympics (a provision of £66 million was made in the March budget to cover this obligation).

2 The difference between the estimates at the time of the bid and the March 2007 budget

	Estimate at the time of the bid (£ million)	March 2007 budget (£ million)	Difference (£ million)
Net cost of the Games to be met from public sector funding	3,298 ¹	9,325 ²	6,027
Expected private sector contribution ⁴	738 ¹	165 ²	(573)
Gross cost of the Games ⁴	4,036 ¹	9,325 ²	5,289
Public funding available	3,419 ³	9,325 ³	5,906

Source: National Audit Office drawing on information from the Department for Culture, Media and Sport

NOTES

1 See paragraph 34 on page 15.

2 The Department told us that, should the anticipated £165 million private sector funding not materialise, this would be met from within the contingency provision (which is included within the £9.325 billion) or from a reduction in costs. Therefore, the gross and net cost of the Games as stated here are the same, with the £9.325 billion representing the Department's upper limit on public funding for the Games.

3 See paragraph 37 on page 18.

4 The figure for gross cost of the Games includes the expected public sector contribution to the cost of the Olympic Village, but does not include the gross cost of the Village itself, which is expected to be largely funded by the private sector. Similarly, the figure for expected private sector contribution does not include the expected contribution to the cost of the Village.

6 This increase in cost estimates, along with a reduction in anticipated private sector funding, means that public sector funding for the Games has increased by £5.906 billion (Figure 2). The costs to be covered by this increase in funding include £1.173 billion of tax³ which will ultimately flow back to the Exchequer. On the basis that the Department has confirmed to us that the tax liabilities associated with the Games will be met entirely from Exchequer funding, this means that the net increase in public sector funding should be £4.733 billion. The funding increase of £5.906 billion includes contingency of £2.747 billion which the Department has made clear to us may not be used in full.

7 The main reasons for the difference between the cost estimates at the time of the bid and the budget announced in March 2007 are:

- A new provision of £2.747 billion for programme contingency (including £337 million of tax).
- A new provision of £836 million for tax, following the Treasury's confirmation that the Olympic Delivery Authority would be liable to VAT in the normal manner and unable to reclaim it (which, although a real cost to the Games, will flow back to the Exchequer).
- A new estimate of £600 million for policing and wider security (which remains subject to further oversight and scrutiny).
- An increase in the Olympic Delivery Authority's programme delivery budget from £16 million to £570 million (the original estimate of £16 million

at the time of the bid was based on the costs of a small Urban Development Corporation and did not include the costs of complex site logistics, or a delivery partner to undertake programme and project management which the Department and the Delivery Authority deem necessary for successful delivery of the venues and infrastructure).

- A decrease in anticipated private sector funding from £738 million to £165 million. This excludes, however, the significant increase in the estimated private sector contribution to the Olympic Village which is outside of the budget. It also excludes any receipts from future sales of land and property after the Games, out of which the Government has since estimated, in June 2007, that £675 million would be available for repayment to the National Lottery.

8 From the outset of any programme or project it is vital to use sound processes to establish a clear and accurate budget. The budget should not only set out the costs involved and the funding to meet these, but also the main benefits to be delivered, with a clear statement of any underlying judgements and assumptions. It enables stakeholders to plan and progress with confidence and certainty, and establishes a baseline against which to assess progress and performance. A programme of the scale, complexity and profile of the 2012 Games gives rise to a high level of inherent risk and uncertainty, and the need for significant judgements and assumptions about future costs and benefits. This increases the importance of adopting a rigorous and sound approach in establishing a budget for the Games.

3 £1.173 billion is the sum of £836 million and £337 million as set out in notes 5 and 6 to Figure 6 on page 16.

9 Against this background, our overall conclusion is that the budget announced by the Secretary of State in March 2007 represents a significant step forward in putting the Games on a sound financial footing and should help those involved in delivering the Olympic programme to move forward with greater confidence. The budget process followed since London was chosen to host the Games has been thorough, and the judgements and assumptions made by the Department and the Olympic Delivery Authority have been informed by detailed analysis and expert advice. Significant areas of uncertainty remain such as the finalisation of detailed design specifications, the legacy benefits to be delivered, how potential suppliers will respond to invitations to bid for work, and the impact of inflation in construction prices, as reflected in the high level of contingency that has been provided for. The Department and the Delivery Authority have continued to develop detailed project plans, budgets and cash flow analysis as a basis for cost control and financial management.

Main findings

10 Our main findings are as follows.

- The Department started work to develop cost and funding estimates for the Games in 2002, commissioning discrete pieces of work from Arup in 2002, from PricewaterhouseCoopers LLP in 2003 and 2004, and from Partnerships UK in 2004, prior to the submission in November 2004 of London's bid to host the Games. All made clear in their advice to the Department that significant uncertainties existed and that further work was required to develop robust budget figures, and this work was based on plans that have subsequently changed significantly. Although the Department anticipated that the public sector funding package that it had put in place would be sufficient, the Secretary of State for Culture, Media and Sport had also highlighted that there would be a need to take stock of the cost estimates should London's bid be successful.
- The budget announced in March 2007 was the result of a good deal of work during the course of an iterative process over some 17 months. Development of the budget was informed by advice from KPMG LLP and a number of other consultants with expertise in costing major projects. The cost estimates for the venues and infrastructure were built up using industry benchmarks and information from potential contractors and suppliers, and include allowances for uncertainty over design specifications which have not yet been finalised. The budget includes a number of new categories for costs and provisions which account for the bulk of the increase in costs from the time of the bid.
- The main areas of uncertainty that remain include the impact of construction price inflation, the response of contractors to the Olympic Delivery Authority's invitations to bid for work and the terms of contracts subsequently agreed, and the level of funding that can be secured from the private sector for building the Olympic Park.⁴ In view of the uncertainties and the tendency for the costs of major projects to be under-estimated, the budget for the Games now includes a programme contingency of £2.747 billion. The estimate of contingency was aggregated from broad assessments on each part of the programme, with reference to Treasury guidance and the experience of other Games. The Olympic Delivery Authority is to refine the estimate of contingency as individual projects go forward, by carrying out a more detailed assessment informed by quantitative risk analysis.
- The revised funding package announced by the Secretary of State in March 2007 is sufficient to cover the estimated costs of the Games and the contingency provision in full, so long as the assumptions on which it is based hold good. This is a most important proviso. Exchequer funding now accounts for £5.975 billion (nearly two thirds of the total), of which £5.570 billion is to be secured through forthcoming Spending Reviews. The National Lottery is expected to contribute £2.175 billion, the Greater London Authority £925 million and the London Development Agency £250 million.
- The expected funding from the National Lottery has increased by £675 million. This means that the total National Lottery contribution of £2.175 billion now includes over £1 billion which will be taken directly from the proceeds raised for the other non-Olympic good causes. The designated Olympic lottery games, expected to contribute some £750 million towards the total £2.175 billion lottery contribution, will also divert sales from mainstream lottery games. This is to be offset, as stated in the Secretary of State's budget announcement, by providing the other good causes with a share in the expected profits from the sale of land in the Olympic Park after 2012. As the ownership of the land rests with the London Development Agency, profits arising from land sales are not included in the Olympic Delivery Authority's budget. The profits will be shared with the Government, which in June 2007 expected to recoup for the lottery an estimated £675 million.

4 This does not include LOCOG's sponsorship income from the private sector to help meet the costs of staging the Games.

■ At the time of the announcement of the Games budget in March 2007 work to complete a cash flow forecast to show the timing and amount of expected future calls on funds had not been completed. While the Olympic Delivery Authority has an assessment of when spending will occur against the programme, following the Games budget announcement on 15 March the Department is developing a cash flow forecast to show the timing and amount of expected future calls on funds. Going forward it is likely that cash-flow requirements will vary year on year requiring effective and rapid decision making, and flexibility, on the part of funders. In turn funders will need regular, timely and accurate updated cash-flow forecasts from the Department and the Delivery Authority.

Recommendations

11 As we set out in our first report on the preparations for London 2012, the requirement for the budget to be clearly determined and effectively managed is one of the key areas of risk that need to be managed for successful delivery of the Games. The Department and the Olympic Delivery Authority are taking action in many areas and, now the top level budget has been finalised, their focus is on finalising the detailed plans needed to support the delivery of the Olympic programme, including a full detailed project plan over the whole life of the programme.

12 The box opposite sets out what we see at present as the key actions required to manage risk in relation to the budget for the Games. It is, however, important to recognise that the Games budget is just that – a budget not a target. Whilst effective risk management is essential, it is also important to seek opportunities where possible to manage within the available resources including the contingency if used, for example, by providing, where appropriate, suitable incentives for suppliers to come within the target cost for individual projects.

13 Within the actions required to manage risk, and acknowledging that the Department and the Delivery Authority have been doing further work in these areas, we have identified three aspects which require particular attention now.

■ **Producing a clear statement of the key deliverables that are expected in return for the public funding of £9 billion, making clear the time, cost and quality assumptions.** A statement of this kind would provide a basis for accountability to Parliament and the public by spelling out what is to be delivered, in terms of both the Olympic venues and infrastructure and the wider benefits. The outputs and outcomes should be specific and where possible quantified so it will be clear whether they have been achieved (for example, venue specifications and legacy benefits). And making clear the underlying assumptions means that any changes in cost or quality to achieve delivery should be transparent.

■ **Producing more robust estimates of contingency.** In line with Treasury guidance, provision has now been made for programme contingency which has increased the budget for the Games by £2.747 billion. The Olympic Delivery Authority now needs to take forward the work it has begun to refine the estimate of contingency so it better reflects the specific risks associated with particular elements of the programme. By more realistically reflecting the risk of additional costs, a risk based contingency should provide a better basis for effective cost control.

■ **Developing a cash flow analysis.** As well as the total amount of funding, the timing of funding is also vital so the Olympic Delivery Authority has money available and is not delayed in taking forward its delivery programme. Work is underway to develop a detailed project plan which will profile the Olympic Delivery Authority's expenditure (i.e. funding need) over the coming years. In the same way, the timing of the various sources of funding needs to be worked through and action taken in good time where the Olympic Delivery Authority's demand for funds is projected to exceed the supply. The Department is currently preparing a cash flow forecast, based on the Delivery Authority's draft detailed budget, to show the timing and amount of expected calls on funds.

The requirement for the budget to be clearly determined and effectively managed – action required to manage risk

Making clear what is to be delivered in return for the budget

- a Producing a clear statement of the key deliverables that are expected in return for the agreed funding package to provide a basis for assessing in due course whether they have been delivered (paragraph 82).
- b As part of this, finalising and making clear the legacy plans for the venues and facilities that will remain after the Games to address one of the remaining areas of cost uncertainty (paragraphs 51 and 83).

Establishing a detailed baseline for managing and controlling the budget

- c Finalising a detailed delivery plan showing when costs are expected to be incurred and the interdependencies between different elements of the Olympic programme.
- d Setting out the key assumptions that underpin the cost estimates and monitoring against these to provide early warning of potential budget implications if the assumptions prove not to be correct.
- e Being clear about the scope of the budget for the Games and where the boundaries lie between the Olympic Delivery Authority and LOCOG (in particular the boundary between venue construction and fit-out), and with other bodies, such as the Home Office, who will be spending money in support of the Games (paragraphs 55 and 56).
- f Capturing data on the costs of the Games consistently and in line with the definitions used in establishing the budget.
- g Communicating the detailed budget clearly to stakeholders and delivery partners so they share a common and clear understanding of the available budget and how it has been determined.

Managing the contingency effectively

- h Making the entire estimate of programme contingency more robust by underpinning the estimate with a systematic analysis of risk (paragraph 66).
- i Putting in place arrangements for managing the 'general programme contingency' of £2.247 billion (paragraph 67) and establishing clear criteria for its use.

Delivering the funding

- j Making clear how and when the £6 billion of Exchequer funding will be made available to the Olympic Delivery Authority (paragraphs 69 and 75).
- k Confirming how and when the £1.1 billion of funding to be provided from 2009 from general National Lottery proceeds will be made available to the Olympic Delivery Authority (paragraph 70).
- l Finalising a cash flow analysis for the Olympic Delivery Authority, being clear how the Authority's cash flow needs will be met and providing regular, timely and accurate updated forecasts to enable effective decision making on the part of funders (paragraphs 75 and 76).
- m Clarifying how requirements for funding and release of the contingency will be apportioned across the various funders. This will require clear and quick decision making and financial control (paragraph 77).

Exercising effective oversight of LOCOG

- n Exercising effective government oversight of LOCOG, including review of the assumptions underlying its separate budget for the staging of the Games, and monitoring against these, as LOCOG's financial position will determine directly the extent of any call on the Government's underwriting guarantee (paragraphs 57 and 58).