



National Audit Office

Report

by the Comptroller
and Auditor General

Department for Digital, Culture, Media & Sport

Investigation: National Lottery funding for good causes

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Department for Digital, Culture, Media & Sport

Investigation: National Lottery funding for good causes

Report by the Comptroller and Auditor General

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Commons in accordance with Section 9 of the Act

Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

8 December 2017

This report investigates the fall in National Lottery income for good causes in 2016-17. It reviews the trends in total National Lottery sales and income for good causes, focusing on the six distributors with the largest share of National Lottery income and the way they have managed the balances within the National Lottery Distribution Fund.

Investigations

We conduct investigations to establish the underlying facts in circumstances where concerns have been raised with us, or in response to intelligence that we have gathered through our wider work.

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Contents

What this investigation is about 4

Summary 7

Part One

About the National Lottery 10

Part Two

Income for good causes 18

Part Three

Management of balances in the
National Lottery Distribution Fund 27

Appendix One

Our investigative approach 36

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This report can be found on the
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What this investigation is about

1 The Department for Digital, Culture, Media & Sport (the Department) launched the National Lottery (the Lottery) in November 1994. The Lottery, currently run by Camelot UK Lotteries Limited (Camelot), aims to raise money for good causes in the arts, sports, heritage, health, education, environment and charitable sectors. A proportion of proceeds from the Lottery is paid into the National Lottery Distribution Fund (the Fund). This money is drawn on by 12 non-departmental public bodies (the distributors) that make payments to good causes.

2 This investigation looks into concerns discussed at board level by Lottery distributors since April 2016. These concerns include:

- the recent fall in Lottery income for good causes;
- the impact of reduced funding on distributors' ability to meet future spending commitments and the work being done to model the potential further impact; and
- the amount of information given to distributors to help them plan their future awards.

3 This investigation sets out the facts relating to Lottery income for good causes and the way balances in the Fund are managed. It covers:

- trends in Lottery funding over time and how Lottery income for good causes varies across Lottery games;
- research into the impact on Lottery income of competition and changes in player behaviour, among other factors;
- information provided by the Department, the Gambling Commission and Camelot to assist Lottery distributors in their planning; and
- work done by distributors to model the impact of reduced Lottery funding on their ability to meet spending commitments.

4 Our investigation covers the six distributors with the largest share of Lottery income in 2016-17. These received a total of 94% of Lottery income for good causes in 2016-17 and held 91% of the Fund balance at 31 March 2017. Our work does not assess the value for money of Lottery distributors' expenditure.

5 Our investigation covers the period from 2004, when we published our report on the management of Fund balances. Key events and the trends in Lottery income for good causes since 2004 are set out in **Figure 1** on pages 5 and 6. Appendix One sets out our methodology.

Figure 1
Timeline of key events and total National Lottery income for good causes since 2004

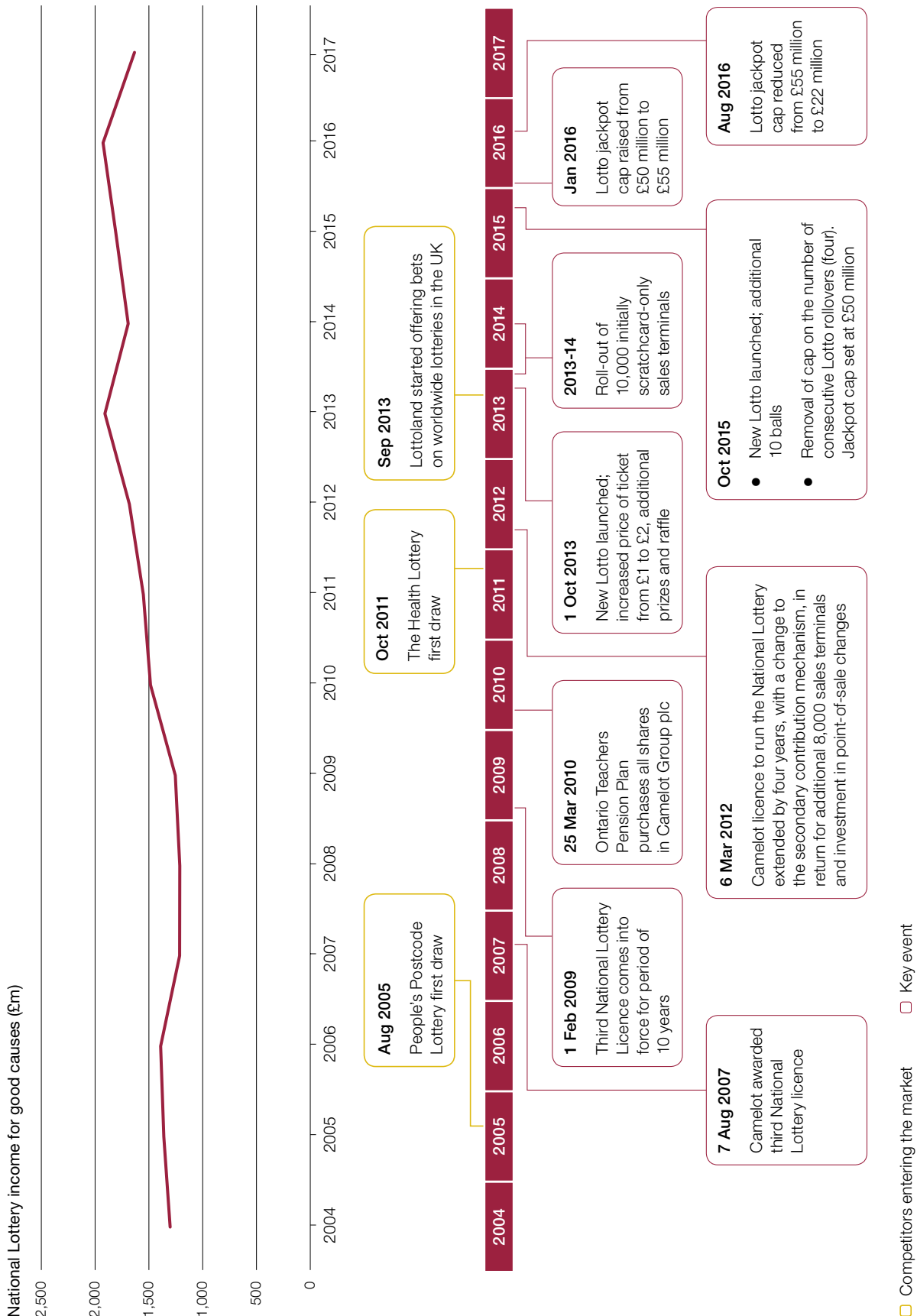


Figure 1 *continued*

Timeline of key events and total National Lottery income for good causes since 2004

Notes

- 1 The graph shows National Lottery Distribution Fund account figures for National Lottery income for good causes and excludes investment income. Economic factors influence investment income, which was £156 million in 2003-04 and £5 million in 2016-17.
- 2 Secondary contribution relates to Camelot's profits. When Camelot makes a profit greater than the one that it had predicted in its bid, it will share this profit with the good causes.
- 3 Most of the terminals rolled out in 2013-14 have recently been upgraded to offer some draw-based games, but do not offer the full range of games offered by Camelot.
- 4 Figures are expressed in nominal terms and therefore not adjusted for inflation.

Source: National Audit Office

Summary

Key findings

Income for good causes

1 National Lottery (the Lottery) income for good causes increased between 2004-05 and 2015-16, but fell in 2016-17. Lottery income for good causes rose by 42% from £1.36 billion in 2004-05 to £1.93 billion in 2015-16. However, in the 12 months from 1 April 2016, income for good causes fell by 15% to £1.63 billion at the same time as Lottery sales fell by 9% to £6.93 billion, compared with the previous year. Camelot predicts a further fall in sales and income for good causes in 2017-18 (paragraph 2.7 and Figure 8).¹

2 In 2016-17, Lottery sales decreased by 13% on draw-based games and 2% on scratchcards and instant-win games (instants). The Department for Digital, Culture, Media & Sport (the Department), the Gambling Commission (the Commission) and Camelot have identified some possible reasons for the fall in sales, including consumers' reaction to recent changes to Lottery games, increased competition and consumers moving away from playing draw-based games. They have not been able to establish the financial impact of these individual factors (paragraphs 2.7 and 2.14, and Figures 7 and 8).

3 Returns for good causes are higher from sales of draw-based games. The rate of return for good causes varies across different Lottery games. As at February 2017, for each pound spent on the Lottery, the approximate returns for good causes ranged from 34p for draw-based games bought online to 10p for scratchcards, with some scratchcards returning as little as 5p. Camelot told us that instants return less to good causes due to the need to offer a higher proportion of proceeds as prizes for instants to encourage consumers to participate. In 2016-17 the prize fund accounted for approximately 68% of gross sales for scratchcards, compared with 49% for draw-based games. The calculation of the amount that goes to good causes is set in Camelot's operating licence and depends on a number of factors including the level of sales, what is paid out in prizes, Camelot's retention and retailers' commission (paragraph 2.8 and Figure 9).

¹ Throughout this report we use Camelot to refer to both Camelot UK Lotteries Limited and the former Camelot Group plc. Camelot UK Lotteries Limited has been the operator of the National Lottery since 2010 following the purchase of Camelot Group plc by Ontario Teachers' Pension Plan.

4 Increases in Camelot's profits have been proportionately greater than increases in both Lottery sales and returns for good causes. Camelot's accounts show that, comparing 2009-10 and 2016-17, Lottery sales increased by 27% (£1.5 billion) to £6.9 billion. Comparing the same dates, returns for good causes increased by 2% (£31 million) to £1.5 billion and Camelot's profit attributable to its shareholders increased by 122% (£39 million) to £71 million.² The amount that Camelot keeps to cover costs and profit was set in 2009, in the third operating licence, and is a percentage of both gross and net sales, rather than a direct linear relationship to what has been raised for good causes (paragraphs 2.4, 2.10 and Figure 6).

5 The method of calculating returns for good causes was set in Camelot's 2009 licence and does not reflect subsequent changes in sales across different types of Lottery games. The Lottery's overarching objective is to maximise returns for good causes through selling Lottery products in an efficient and socially responsible way. The relative decline in sales of draw-based games compared with instant games has led to a lower rate of return to good causes. The licence terms were set in 2009 and Camelot's current licence term ends in 2023. Any changes to the basis for calculating returns for good causes prior to 2023 would need to be agreed by the Commission and Camelot (paragraphs 1.2, 2.3 and 2.9 and Figure 10).

Management of balances in the National Lottery Distribution Fund

6 Half of the six largest Lottery distributors increased their grant commitments in 2016-17 at the same time as Lottery income fell. Funding liabilities of the six largest distributors increased by a total of £88 million compared with the prior year. At 31 March 2017, distributors' liabilities as a percentage of their National Lottery Distribution Fund (the Fund) balance ranged from 19% for UK Sport to 342% for the Big Lottery Fund. Distributors often have commitments spanning many years, so it is likely that commitments will exceed their Fund balance at a given date. However, between 2009-10 and 2016-17, the total available Fund balance increased by 18% (to £1.54 billion) while total grant liabilities increased by 37% (to £3.04 billion) (paragraphs 3.4, 3.6 and Figures 12 and 13).

7 The Fund balance at 31 March 2004 was sufficient to cover 96% of total liabilities raised by distributors; at 31 March 2017 this figure had fallen to 51%. At 31 March 2017, Fund balances were £1.5 billion compared to distributors' grant liabilities of £3.0 billion. In July 2005, the Committee of Public Accounts recommended that the Department should set a target to reduce the Fund balance (which stood at £2.7 billion at 31 March 2004). Fund balances are determined by how much money is raised by the Lottery for good causes and how much is paid out by distributors. Since distributors have no control over Lottery income, they manage their balances by planning their grant awards using available information on future Lottery income (paragraphs 3.2, 3.4, 3.7 and 3.8).

² Camelot account figures of funding for good causes exclude income from unclaimed prizes.

8 Since the fall in Lottery income for good causes, distributors have been given more sophisticated information, including short-term forecasts from Camelot. In June 2016, Camelot began to provide distributors with short-term, commercially sensitive forecasts of future Lottery income for good causes. Prior to this, until October 2015, the Department shared with distributors projections of future income for good causes based purely on projecting historical trends. In June 2017, the Department gave all distributors an external consultancy's analysis that modelled future income for good causes up to 2019-20. Distributors have raised concerns that the modelling makes no adjustment for the impact of any structural changes in the Lottery, such as game changes to address the recent fall in sales. The Department told us that the modelling work will be repeated following Camelot's recent strategic review of its business and it did not believe it would have been helpful to model the impact of potential game changes prior to Camelot's review, given the wide range of potential variables. The six largest distributors have modelled different scenarios of potential income when setting future years' grant budgets. Many distributors continue to use their own estimates of future income for good causes informed by the data sources available, causing some duplication (paragraphs 3.11 and 3.14 to 3.16).

9 The Department gives distributors information to help them manage their balances; but distributors told us they do not get all the information they need. The Department can request any data it wishes from the Commission, in accordance with its management agreement, and receives detailed information, including weekly sales by game and monthly returns for good causes. The Department does not give the distributors weekly sales figures split by game, even though they have asked for them. Distributors have told us that prompt sharing of such data allows them to spot declining or increasing income early, helping them to plan their future grant awards. The Department believes that weekly sales data does not provide a clear indication of trends due to the range of factors that may cause Lottery sales to fluctuate from week to week (paragraph 3.18).