MARR AREA partnership

Pathways to advance a robust third sector

Background paper 2: Financing third sector bodies

Writing of rural Aberdeenshire, Robert Smith has argued that "issues of community entrepreneurship and development are central to our understanding of enterprising communities, peoples and places."[1] For the third sector to become a potent force in place making, it must be acutely aware of the economic environment in which it operates and plan for financial resilience.

Because of its great diversity of character, there can be no simple model of how to improve the financial viability and resilience of third sector entities. Some third sector bodies, particularly well-endowed charitable trusts, such as the Robertson Trust, are extremely wealthy and develop careful strategies to guide the kind of project they wish to fund. There is a relatively strong tradition in Scotland of successful family businesses establishing foundations with charitable purposes. In North-East Scotland, examples include the Grant family (whisky), the Baxter family (food) and the Wood Foundation (oil and shipping), all of which have considerable wealth to distribute and well defined purposes on which to spend it, which often include support to third sector bodies but may also include supporting the public sector, including health and even private sector local socio-economic development. At the other extreme many local third sector bodies survive on shoestring budgets and unpaid contributions from trustees in order to deliver their charitable purposes.

The need for external financial assistance differs enormously from one third sector body to another. Some are fully funded as a result of the activities they pursue while others need to constantly seek and obtain grants in order to survive. However, the Scottish Social Enterprise Census, which very much focusses on those TSOs which are generating income, suggests that income generation from sales of goods and services is almost always insufficient to cover their costs.

The public sector is a major funder of TSOs. It funds them to deliver public goods both by supporting the organisation as an institution and by buying services such as social care or training for NEETs from them. Because public sector finances have been adversely impacted by the economic crisis and are strongly influenced by outsourcing more costly services, and because what are often described as neoliberal tendencies in political thinking in many western governments, the funding for third sector bodies can be very uncertain at precisely the time it is most needed; that is when demand is rising at the same time as public service provision is most compromised by spending cuts. The short-term nature of contracts places a further burden on third sector bodies. TSOs depend on winning contracts but are under constant pressure to reduce costs to maintain competitiveness in what can seem like a race to the bottom.

[1] Smith, R., 2012. Developing and animating enterprising individuals and communities: A case study from rural Aberdeenshire, Scotland. *Journal of Enterprising Communities: People and Places in the Global Economy*.

Revenue generation

Third sector bodies use a variety of revenue generating and fund-raising approaches. In this background paper, we explore the diverse ways in which finance can be obtained. Excepting the extremely well-endowed charities that distribute their proceeds to other TSOs, there are five main groups of revenue generating means.

- Gifts, bequests and grants
- Sponsorship
- Crowd sourcing
- Sales and rental income
- Income generation from activities and events

Recent evidence in Scotland from the Social Enterprise Census 2019[2] shows that even in the subset of social enterprises rather than all TSOs, on average only 75% of their revenue comes from trading activities. This means that it is imperative they also look to other sources of revenue. This effort can create cliff edges where the entities existence is threatened, churn of staff, a degree of flexibility in what funds to chase and a degree of deflection from core purpose.

If we are interested in the financial robustness of third sector bodies, we might be interested in how they obtain revenues to cover their operational activities. If we break down the five main groupings into a longer list of possible actions and activities, they might include the following:

1. Endowments, bequests and gifts, including creation of charitable foundations and trusts
2. Sponsorship (merges with 1. to a degree) e.g. a tree, kit for a sport's club, an event (sponsored walks, cycle rides, duck races, etc)
3. Membership, attendance or participation fees and subscriptions
4. Drawdown of grants from central and local government to deliver (quasi-) public services
5. Asset transfers from public to third sector
6. Drawdown of grants from charitable foundations
7. Sales of products and services, including event management, concerts, festivals
8. Events (jumble sales, cream teas, coffee mornings etc) (a subset of 7)
9. Upcycling – direct from those offloading products, or via council recycling depots
10. Lotteries, hundred clubs, scratch cards, raffles etc. (a subset of 7)
11. Rental income: leasing space in community-owned buildings or land for private services (a subset of 7)
12. Pro bono or reduced cost activities or services provided by individuals, businesses or other institutions to support third sector bodies
13. Volunteer days to get work done (a subset of 10)
14. Crowd sourcing of finance normally to deliver specific projects
15. Donation web-pages, collection tins and solicited financial contributions
16. Collections (of scrap metal, clothes) etc.

It should be recognised that living on the edge with dependence on short term contracts and variable success in grant applications can be extremely stressful for staff who are rarely highly salaried in their work and often work many more hours than those to which they are contractually committed.

[2] CE SG and Social Value Lab (2019) Social enterprise census

Financial planning

We might also be interested in whether a third sector body has undertaken any strategic planning and has in place any financial strategies within the organisation to increase financial resilience. Rather than wait until a financial crisis arises, it may be possible to undertake strategic planning to mitigate financial risk. This should involve a rational exploration of options and is likely to result in very different strategies for different third sector entities.

For example, running costs can be reduced by using grants to obtain capital assets (e.g. replacing oil boilers with woodchip which attracts the Renewable Heat Incentive, using grants for insulating buildings to reduce fuel bills),or using crowd funding or grants to fund capital projects which reduce running costs.

Opportunistic revenue generation

Sometimes opportunities for revenue generation present themselves which seem too good not to apply for. They can be used opportunistically to either broaden the portfolio of activity, but it may distract a TSO from its core purpose and not result in enhanced resilience. It may put pressure on core staff and entail additional costs in training temporary staff in other cases. Where such opportunities allow investments in training or capital items cognate with core purposes, they may more closely fit with core purposes.

Reducing operating costs

Reduction of operating costs may allow groups to attain financial resilience. Such cost cutting need not entail loss of service. For example, different energy providers offer different tariffs but organisations and households both tend to stick to particular providers. The same applies to internet service providers.

Summary

It is absolutely essential that in a volatile business and political environment, where funding streams are uncertain, that TSOs build strategies to enhance their financial resilience. There is no easy-fix solution. It is essential that those responsible for strategic planning recognise the need for financial resilience, and plan and act accordingly. Ideally, a long-term relationship with a durable revenue generating enterprise is the preferred option. Of such durable enterprises, renewable energy has offered many communities a very important income stream to allow them to pursue a wide range of social economic and environmental developments. Equally, a well-endowed locally focused trust can provide similar financial security. Outwith these privileged examples, the earlier-identified recipe book of possibilities needs to be explored and choices made which seek to meet the specifics of the financial need. Uncertainty of funding is often the norm even for charities with large endowments, as they can be subject to the vagaries of investment returns.