

Earned income, trading and enterprise

This briefing explores issues around earned income, highlighting areas for enterprising charities, social enterprises and support bodies.

Information sources:

- [SCVO Sector Forecast for 2017](#)
- [SCVO income and spending 2014](#)
- [Social Enterprise in Scotland Census 2015](#)

Importance of earned income to third sector

2/3rd of third sector's £5 billion turnover comes from selling goods and services:



3 in 5
charities have
trading income

11,000 charities sell goods
or services

1 in 5
charities are
social enterprises

5,199 social enterprises
identified in Census

of which 3,500
are also charities

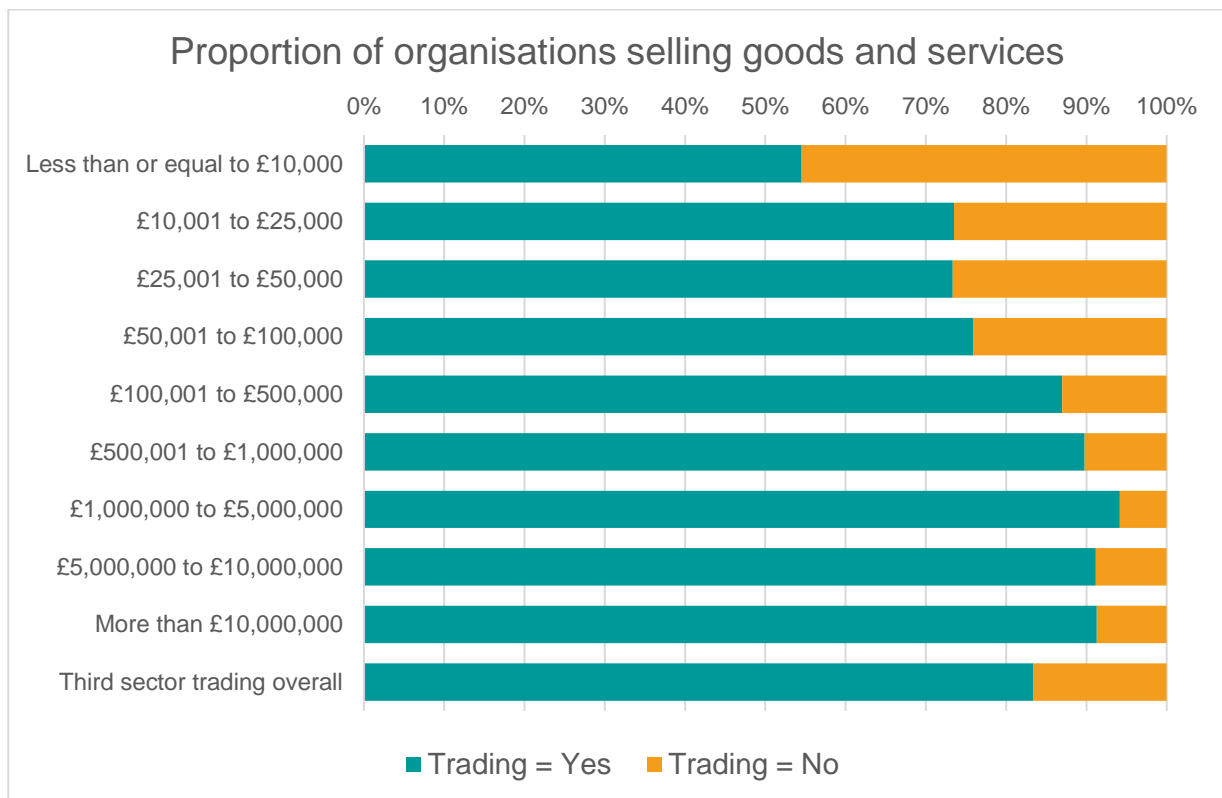
7000+
charities get
more than half
their income
from trading



‘Earned’ Income in the third sector

There are 19,635 ‘third sector’ charities in Scotland. Based on analysis of sample accounts, an estimated 7,500 of these charities generate more than 50% of their income from some form of **trading, contracted services, sales, fees or rental income**. A further 3,500 generate between 10-49% of income from trading.

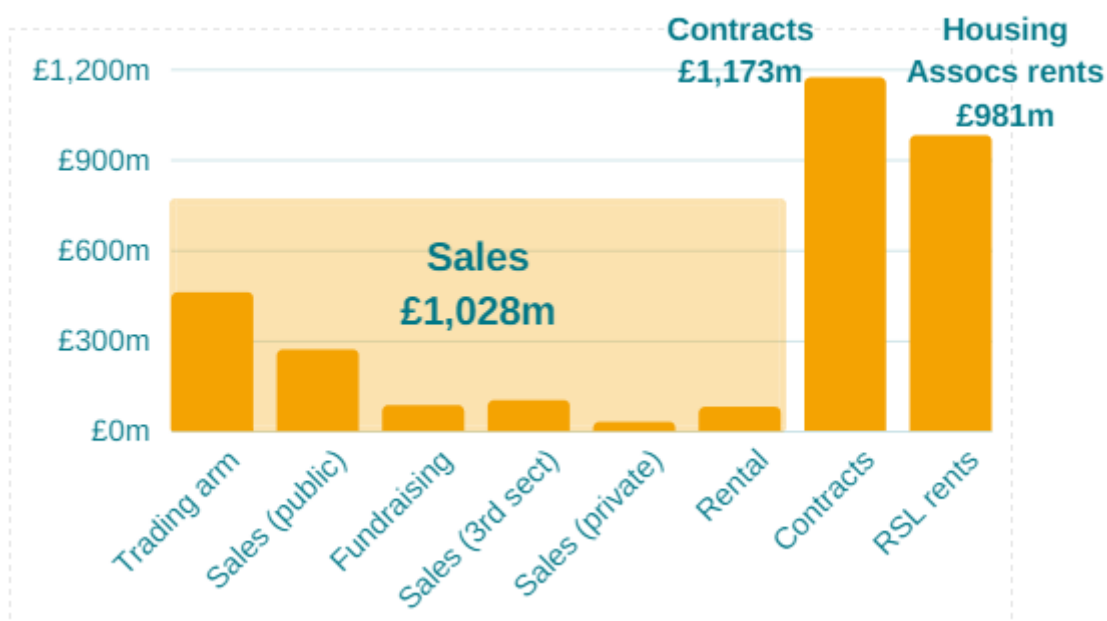
While larger organisations are more likely to derive income from contracts, charities of all sizes derive at least some of their income from selling goods or services:



The third sector’s earned income is derived from sales (£1,028m), contracts (£1,173m), and housing association rental income (£981m).

Types of services and goods sold might include:

- **Public sector contract income, e.g. social care, health services, recycling**
- **Fees paid for services e.g. care homes, childcare, classes, counselling**
- **Membership fees e.g. for sports clubs**
- **Rental income: housing association rents, community hall lets, office space/ room hire/ sub-letting**
- **Ticket sales, e.g. museums, theatres, fundraising events**
- **Shop and café income**
- **Sales of publications, merchandise etc.**
- **Training fees, course fees, consultancy work**



Social enterprise

The 2015 Social Enterprise Census identified 5,199 social enterprises, of which 3,500 are also charities. While there is significant overlap between charities and social enterprises in terms of what they do and the principles that underpin their activities, the main difference is in whether the organisation sees trading as simply one way of bringing in funds to support their work, or whether it aspires to be a business with social aim. Lines are however often blurred, e.g. even the most ‘traditional’ charities sell goods and services or have trading arms, and some social enterprises don’t describe themselves as such. The key characteristics are outlined in the table below.

Key characteristics	Third Sector	Social Enterprise
Public, social or environmental benefit	✓	✓
Organised, ie have a clear constitution	✓	✓
Non-statutory, ie independent from state	✓	✓
Significant degree of voluntarism, eg Led by an unpaid, voluntary board	✓	✓
Non-profit distributing, i.e. ‘Asset lock’: a) if body is wound up, assets are transferred to a similar body b) All/majority of profits are reinvested in the organisation	✓	✓
Aspire to financial independence through trading	Various models	✓

Issues for charities wanting to increase trading



Two in five respondents to SCVO's recent Sector Forecast told us that they plan to focus on business development in 2017. One in three organisations told us that they think that 'Income from self-generated & enterprising activities' will increase in 2017. Trading was mentioned in some form or another by around a tenth of respondents when asked what opportunities they saw for their organisation in 2017:

"Opportunities to grow existing social enterprises, replicate services that work well in other geographies and seek out innovative new social enterprises within our target areas of service."

"Managing our growing social enterprise activity."

"Key opportunities are to look at generating income in new ways - reinvigorating a dormant social enterprise, looking at new projects and trying to diversify funding."

A number of respondents highlighted that trading was a key way to, for example

- **diversify income**

"We must maintain the viability of our Social Enterprise Community Cafe and the support needed during this period of uncertainty"

- **generate unrestricted income**

"Developing some key service areas and increasing unrestricted income, potentially developing social enterprise model"

- **make up short-falls in public sector funding**

"We are hoping that our trading activity through new social enterprise arm will mitigate shortfall."

Contracted services

One of the key concerns for many Forecast respondents was the reduction in the number and value of public sector contracts:

“Increasing pressure from cuts to local authority budgets resulting in reduced commissioning of services and contracting in existing services”

“Our centres have seen a reduction in contracts for the services they are funded to deliver through social care at local authority level.”

A number of respondents raised concerns that as money becomes tighter, funders will simply focus on the cheapest option and award contracts to large private sector providers: *“The only way the public sector, and in particular Local Authorities will be able to meet its statutory duties will be to collaborate with others. The procurement system as applied mitigates against achieving the maximum benefit for collaborating and may force greater straight competitive tendering leading to more contracts going to for profit providers which will mean poorer services.”*

Respondents were keen to ensure that they did not do service-users a disservice by getting drawn in to a race to the bottom: *“New and increased market opportunities via tenders. Biggest challenge - not to be caught up in the 'race to the bottom' on price within tender bids.”*

However, a number of respondents were more positive, and felt that difficult times might mean less competition from a private sector that doesn't see much profit to be made, and (less positively) that *“Some organisations will not survive and we will be in a position to pick up these contracts”*.

While most respondents refer to public sector contracts, some organisations mentioned that the tight funding environment in the third sector had led to a *“loss of contracts from third sector”*.

Increasing trading and sales

Many respondents to the Sector Forecast spoke of their desire to increase their market share, move into new markets, or help fill local market gaps. While many of these organisations were, or had already started, looking at ways on which to do so, some were concerned both about the risks and capacity issues, while others were concerned about people's abilities to pay for certain services.

Some key issues raised in responses are listed on the following page:

- **Business development**

Many respondents mentioned that their boards and staff had already been working on new business plans, often investing in bringing specialist staff:

“Undertaking the development of the retailing side by appointing a manager starting in January 2017. Already have a graduate in place for 1 year to develop IT / Marketing side”

However, no-one mentioned seeking support from support bodies such as Just Enterprise. In more traditional organisations, awareness of the support available seemed to be low, perhaps because they do not view themselves as social enterprises.

- **Capacity**

While some organisations had increased their capacity to take on more business or were in the middle of doing so, others were concerned that a lack of funding meant that they were effectively unable to develop in the way they wanted to.

- **Cash-flow**

“Increased need to manage cashflow, restructure and deliver with minimal staffing.”

Medium-sized and smaller charities were concerned that a lack of cash flow and current assets meant that they were unable to take on new business opportunities that would mean a high rate of debtors, or contracts where payments are made retrospectively.

- **Sustainability**

Respondents for the most part felt that by increasing income from trading they would increase their organisation’s sustainability, by being less dependent on grants and other types of funding. However, some were concerned that trading would open them up to new risks.

- **Compatibility with aims**

While most respondents were keen to increase the proportion of their income coming from the sale of goods and services, some noted that it was challenging to develop income streams that would fit well with their organisation’s aims. Linked to this, many felt that their target market, for example, low income families, would not be able to pay fees at market rates. They were wary of developing business models that would look at trading and enterprise purely in order to generate funds, as this would take them away from their core mission. However, some hoped that by creating **social enterprise arms** they could keep these two factors in balance.

Issues for enterprise support bodies

“Demand for our services is growing but we may not have the capacity to meet this demand.”

“Key opportunities: business support from our investor”

“Opportunity - Capital investment opportunities to grow our commercial income”

The need remains for support for organisations across the whole spectrum of enterprise – from small organisations wanting to diversify income, to larger charities setting up trading arms to those becoming full-blown social enterprises.

There is also a continued need for funding which helps build capacity and investment in new ideas, alongside business loans and financial support to enable charities to overcome cash-flow issues and make the most of all opportunities.

Key issues summary

- Public sector contracts – respondents are wary of being drawn in to a ‘race to the bottom’ and do not want to see service quality drop. This raises some thorny questions for organisations 1) if they continue to provide the service, will they have to subsidise with their own funds to ensure quality of service? 2) if they pull out of a service are they then exposing their clients to a lower quality service?
- Social enterprise activities – a number of respondents spoke of already having increased their trading activities in response to the need to increase and diversify funding. Others were keen, but worried about a lack of capacity. Another issue was the feeling that there was a lack of appropriate options for their organisation
- Social enterprise support - many organisations would benefit from discussing their options with specialist advisors e.g. Just Enterprise, but awareness of these services seems low among small and medium-sized charities outside the normal social enterprise landscape. Continuing to raise awareness of support bodies, and the many options and models available to charities wanting to trade would be good, emphasising that support is also out there for those who just want to increase sales of goods and services in a small-scale way, or use their assets more effectively.