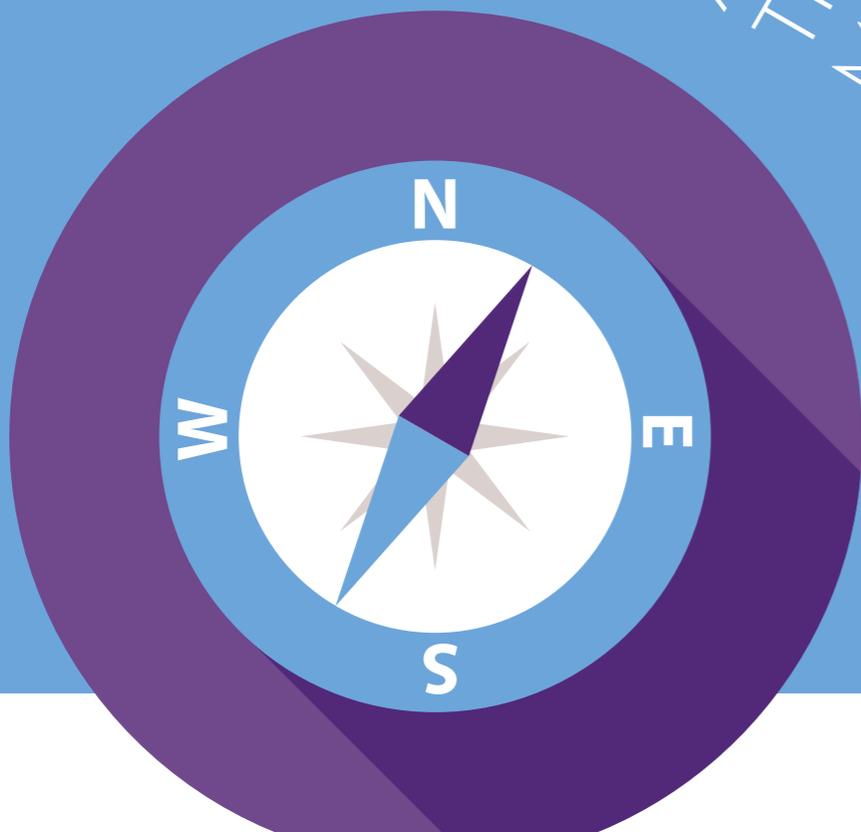


NAVIGATING CHANGE

AN ANALYSIS OF FINANCIAL
TRENDS FOR SMALL AND
MEDIUM-SIZED CHARITIES



CONTENTS



EXECUTIVE SUMMARY 3

1. SETTING THE SCENE 4

1.1 Our approach 5

1.2 The policy landscape 6

2. THE BIG PICTURE: AN OVERVIEW OF SMALL AND MEDIUM-SIZED CHARITIES 9

2.1 Characteristics of small and medium-sized charities 10

2.2 The number of small and medium-sized charities 11

3. A TYPOLOGY OF INCOME TRAJECTORIES 14

3.1 Characteristics of small and medium-sized charities by type 16

3.2 Case exemplars 17

4. AGGREGATE FINANCIAL DATA – INCOME 20

4.1 Overall income 21

4.2 Changes in income mix of small and medium-sized charities 22

4.3 Comparison of changes in income sources across income band 23

4.4 Income breakdown by region 27

4.5 Income breakdown by activity 29

5. AGGREGATE FINANCIAL DATA – SPENDING 31

5.1 Overall spending 32

5.2 Charitable activities and generating income 33

5.3 Spending by activity 34

5.4 Staff costs 35

CONCLUDING REMARKS 36

APPENDIX 37

1

2

3

4

5

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The Lloyds Bank Foundation for England and Wales is one of the UK's leading community grant makers. An independent registered charity funded by the profits of Lloyds Banking Group.

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EXECUTIVE SUMMARY

The past several years, encompassing the global financial crash and reductions in public spending, have provided considerable financial challenges for small and medium-sized charities. This summary outlines the key findings from a research project commissioned by Lloyds Bank Foundation for England and Wales and carried out by NCVO (National Council for Voluntary Organisations) examining the finances of these organisations between 2008/09 and 2013/14.

Voluntary organisations experienced substantial income fluctuation over time.

There are over 40,000 small and medium-sized charities with an income between £25,000 and £1m, accounting for one third of the voluntary sector in England and Wales. The income of these organisations is relatively unstable; up to a third or more moved in and out of Charity Commission income bands between 2008/09 and 2013/14. In addition, nearly 18,000 new voluntary organisations were created and over 23,000 disappeared, the majority of which had an income under £500,000.

Smaller charities experienced higher income volatility than larger charities.

Between 2008/09 and 2013/14 over half of all charities experienced rises or falls in income of more than 20%. For charities that were in the income band £100k–£500k in 2008/09, 23% moved into a lower income band by 2012/13 compared with 8% that moved into a higher income band in the same period, meaning that more of these organisations lost than gained income. In general, organisations under £1m appeared particularly affected by insecure income, with information from charity accounts suggesting that a major cause could be dependency on single sources of income. By contrast, organisations over £1m predominantly experienced stable or rising income trajectories.

Small and medium-sized charities lost more income proportionally than larger charities.

Between 2008/09 and 2012/13 the income mix of charities with an income below £1m shifted from one in which government and individuals contributed to overall income in roughly equal measure to one where the majority of income came from individuals. These organisations experienced proportionally bigger losses in government income and smaller increases in income from individuals than charities with an income above £1m. In addition, increases in income from individuals were insufficient to offset losses of government income for small and medium-sized charities, resulting in an overall shortfall. Central and local government income decreased for all income bands except the largest (over £100m), which increased both sources of income.

OVER HALF OF ALL CHARITIES EXPERIENCED RISES OR FALLS IN INCOME OF MORE THAN 20%.

CHARITIES IN THE INCOME BAND £100K-£500K NEARLY HALVED THE PROPORTION OF THEIR SPENDING THAT WENT TOWARDS STAFF COSTS.



Patterns of income generation and spending changed following government funding cuts.

Between 2008/09 and 2012/13 small and medium-sized organisations increased their earned income through fundraising and charitable trading by up to 60%. They decreased their overall spending and, in general, increased the amount that they spent on generating funds. Charities in the income band £100k–£500k also nearly halved the proportion of their spending that went towards staff costs.

Income loss was uneven across individual geographic regions and sectors.

Small and medium-sized organisations in the North East, North West and West Midlands lost the highest proportion of overall income. However, the North East and Wales saw the biggest cuts in government funding as well as the largest increases in income from individuals. By sector, health, social services and law and advocacy lost the highest proportion of overall income and reduced their spending the most. However, almost all sectors lost around 40% of government income, with education and research experiencing the smallest cuts of 18%.

Charities employed a diverse set of strategies to cope with funding changes.

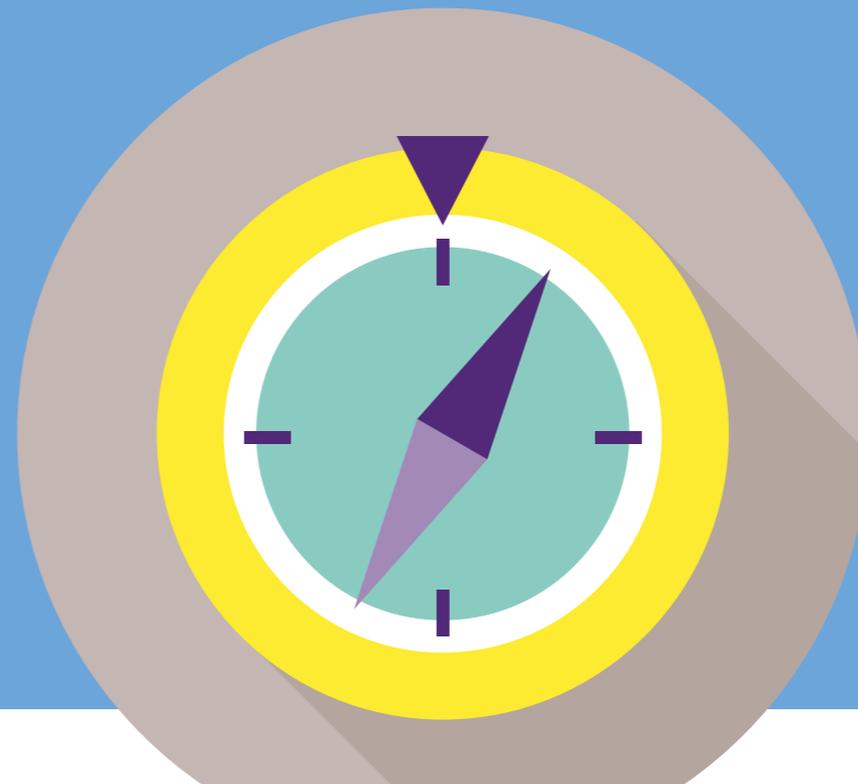
Information from the written text of charity accounts indicated that small and medium-sized charities adapted to a new financial landscape in a number of ways. These included mergers and takeovers, staff redundancies and reducing staff hours, reducing services to core activities, diversifying income sources, and increasing partnerships and joint ventures with other voluntary organisations.

Implications for the future funding of the voluntary sector.

Instability associated with short-term funding streams appears to be a more critical issue for smaller charities, for whom the removal or retention of single funding awards can be the difference between survival and closure. The funding environment for small and medium-sized charities therefore needs to be reviewed to improve and/or increase long-term, stable funding sources. In addition, these organisations need support to find alternative strategies to cope with an uncertain financial future.

1

SETTING THE SCENE



1.1

OUR APPROACH

The past several years have been ones of financial upheaval, encompassing both the global financial crisis in 2007 and 2008 and cuts to public service spending under the Coalition government from 2010. Ongoing reductions in public spending have affected the voluntary sector as a whole; the most recent UK Civil Society Almanac showed that it lost £1.9bn from government between 2009/10 and 2012/13.

The 40,000 small and medium-sized voluntary organisations in England and Wales, with an income of between £25,000 and £1m, have not been immune to these changes in the funding landscape and are operating in an increasingly challenging environment. These organisations account for nearly a third of the sector and one fifth of the sector's total income (around £7bn) and play a key role in the delivery of services to communities across the country.

This research project, commissioned by Lloyds Bank Foundation for England and Wales, aims to explore how small and medium-sized charities have been affected by and navigated the changing financial landscape over recent years, drawing on NCVO's unique historical dataset of charity financial accounts, compiled in partnership with the Third Sector Research Centre (TSRC). It seeks to improve understanding of the challenges and opportunities these charities face so that future policy interventions and funding decisions are better adapted to their needs.

THERE ARE OVER 40,000 VOLUNTARY ORGANISATIONS IN ENGLAND AND WALES WITH AN INCOME OF BETWEEN £25,000 AND £1M.



The report provides a detailed analysis of where small and medium-sized charities get their money from, how they spend it and how their finances have changed since the recession.

In line with Lloyds Bank Foundation's priorities it examines charities with an income of between £25,000 and £1m in England and Wales. It focuses on the years between 2008/09 and either 2012/13 or 2013/14 for which there is the most robust data and as this time period also captures possible impacts of the recession and cuts to public spending.

THE REPORT INCORPORATES THREE MAIN APPROACHES:

1.

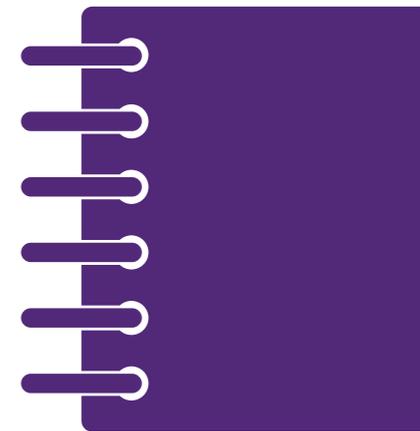
The first provides a high level overview of the voluntary sector, including the number and key characteristics of different sized organisations. The income trajectory of all c.140,000 individual organisations was also tracked from 2008/09 to 2013/14, in order to see how the income of individual organisations has changed over time. This was designed to provide a unique perspective on the 'churn' of the voluntary sector that is not available from aggregate financial data.

2.

For the second, all income trajectories were classified into a new 'typology' that assessed the proportional change in income that charities experienced between 2008/09 and 2013/14. This measure facilitated comparison of changes in income across different sized organisations. The typology was also used for a more detailed examination of the income of a subset of small and medium-sized charities for which either four or five years' worth of continuous data was available, and whose activity broadly matched Lloyds Bank Foundation's priority area of working with individuals over 17 years old facing multiple disadvantage. The text in the annual accounts of these organisations was also scrutinised in order to identify qualitative, real-world examples of how charities have dealt with a changing financial landscape.

3.

The final approach comprised an analysis of detailed aggregate financial statistics on both income and spending for the voluntary sector as a whole between 2008/09 and 2012/13, based on a sample of charities, broken down by income band. This analysis follows the method used for NCVO's UK Civil Society Almanac (see Appendix for a detailed methodology). In addition, the data was analysed by region and activity type of organisations; these figures represent aggregate combined data for the income bands £25,000 to £1m.





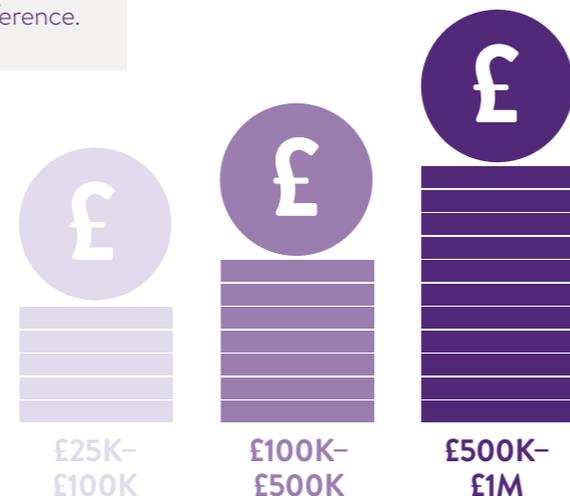
DEFINITIONS

General charities

Within this report voluntary organisations are defined according to the 'general charities' definition in order to enable comparison over time for this core part of the sector. This definition includes registered charities that meet the following criteria: formality, independence, non-profit distributing, self-governance, voluntarism and public benefit.¹ This produced a usable population for England and Wales that formed the basis for all analyses.

Income bands

The sample aggregate financial data was gathered in nine bands to accommodate Charity Commission registration thresholds. Voluntary organisations with an income of between £25,000 and £1m fell within the middle three of these bands (Table 1, shown in bold). The nine bands were divided into three groups of three (lower, middle and upper) in order to help differentiate those that were the focus of the report (the middle-income band) and those that provided comparison (lower and upper). It should be noted that for NCVO's UK Civil Society Almanac, the nine bands are aggregated into five, which are also shown in Table 1 for reference.



References :

1. NCVO 'UK Civil Society Almanac 2015: Big picture'. data.ncvo.org.uk/a/almanac15/big-picture (accessed January 2016)
2. Office for Budget Responsibility (2015) *Economic and Fiscal Outlook*. London: Office for Budget Responsibility.
3. Institute for Fiscal Studies (2015) *Post Autumn Statement Briefing*. London: Institute for Fiscal Studies.

Table 1. Income band definitions

Income bands	Income	Abbreviated income	NCVO category
Lower	Zero income	No income	Micro
	£1 – £10,000	Under £10K	
	£10,001 – £25,000	£10K-£25K	Small
Middle	£25,001 – £100,000	£25K-£100K	Medium
	£100,001 – £500,000	£100K-£500K	
	£500,001 – £1,000,000	£500K-£1M	
Upper	£1,000,001 – £10,000,000	£1M-£10M	Large
	£10,000,001 – £100,000,000	£10M-£100M	Major
	Over £100,000,000	Over £100M	

1.2

THE POLICY LANDSCAPE

The years since the financial crisis of 2007/08 have been difficult for the government, public and voluntary sectors alike. Billions were wiped off the value of investments, the country experienced a deep recession and unemployment rose significantly. Although stock markets have rebounded, growth has returned and employment has risen to pre-crisis levels, the recession has cast a long shadow of reductions in public spending.

Cuts to public service spending of £39bn under the Coalition will be followed by a further reduction of £10bn of departmental spending cuts by 2019/20² in addition to an average 18% cut to the spending of unprotected departments between 2015 and 2020.³ Even beyond this parliament, there is little prospect of the kind of expansive public-sector spending seen in the first half of the last decade. Efficiency, value for money and prioritisation will remain government watchwords for the foreseeable future.

CUTS TO PUBLIC SERVICE SPENDING OF £39BN UNDER THE COALITION WILL BE FOLLOWED BY A FURTHER REDUCTION OF £10BN OF DEPARTMENTAL SPENDING CUTS BY 2019/20.



£39bn

THE ROLE OF THE VOLUNTARY SECTOR

The voluntary sector is a vital element of the wider societal safety net. Whether directly delivering public services, shaping them or otherwise providing support to individuals in need, charities have distinctive but aligned concerns to government, with both in the business of public benefit. It was inevitable therefore that public-sector austerity would feed through to the voluntary sector. Peaking at £15.2bn in 2009/10, government funding had fallen to £13.3bn by 2012/13⁴ and the pattern is likely to continue.

Reduced funding is not the only challenging trend that the public and voluntary sectors are facing together. As with most of the western world,

Britain has an ageing population. Falling fertility rates, rising life expectancy and the retirement of the baby-boom generation will reduce the ratio of working age people to pensioners from 3.2:1 in 2012 to 2.7:1 in 2037.⁵ With the elderly being the fastest growing age group in Britain, increasing pressure is being put on healthcare and social services.

Long-term demographic pressures have been exacerbated by short-term demand increases stemming from the financial crisis and subsequent austerity.⁶ Child protection cases, for example, are at a five-year high⁷ whilst the number of people sleeping rough is up 55% since 2010.⁸ With some services closing or continuing with reduced capacity, additional pressure has been placed on those remaining.

WITH THE ELDERLY BEING THE FASTEST GROWING AGE GROUP IN BRITAIN, INCREASING PRESSURE IS BEING PUT ON HEALTHCARE AND SOCIAL SERVICES.



PEAKING AT £15.2BN IN 2009/10, GOVERNMENT FUNDING HAD FALLEN TO

£13.3bn

by 2012/13



CHANGES TO COMMISSIONING PRACTICE

For those charities in receipt of public funding, current commissioning practice can be challenging and the problem is particularly acute for smaller organisations.⁹ As commissioning and procurement teams have lost staff and seen their own budgets cut, many have sought to reduce their costs by aggregating outsourced services into a smaller number of larger contracts. Whether or not public bodies set turnover requirements for bidders, bigger contracts favour bigger organisations.¹⁰

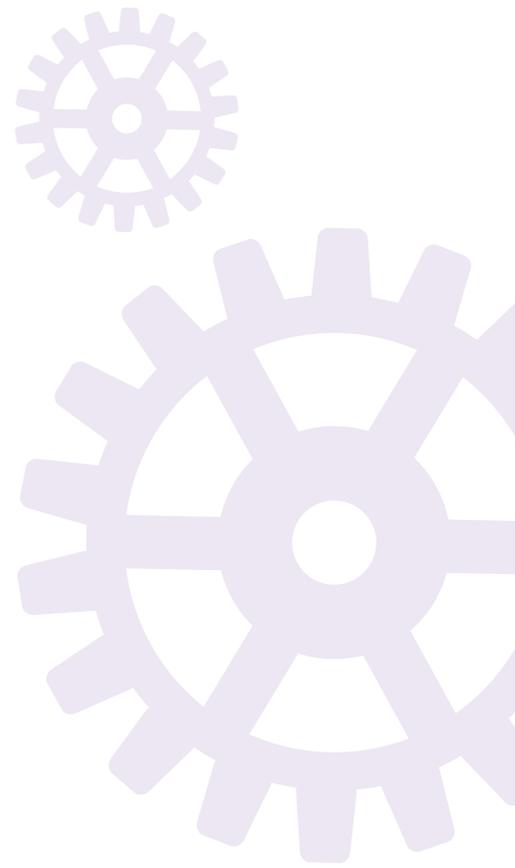
As a result, both nationally, through programmes such as Transforming Rehabilitation, and increasingly locally too, the voluntary sector is finding that it must operate as a subcontractor if it wishes to contract at all. Such a model can be highly successful, combining the scale, financial stability and contract management skills of large organisations with the nimbleness and specialist frontline expertise of smaller charities. Such advantages, however, have regularly been negated due to poor relationships between primary contractors and subcontractors, inappropriate transfer of risk down supply chains and lack of clarity about referrals.¹¹

CHALLENGES TO ENGAGEMENT

Where contracts are broken down, barriers still remain. Limited pre-procurement dialogue, disproportionate bidding and reporting requirements, short timescales, prioritising cheapest price and the transition from grants to contracts can all prevent smaller voluntary organisations from engaging and commissioners from achieving value for money.¹²

The increasing dominance of contracts¹³ is part of a wider recent evolution in funding mechanisms. Austerity has accelerated public and commissioner demands for greater accountability in how government money is spent. Payment by Results contracts, which pose particular challenges to smaller organisations,¹⁴ have proliferated. The expanded use of personal budgets, initially in adult social care but more recently for children's services too, will require many charities to alter their business model drastically. Similarly, social investment and social impact bonds introduce a third party into the commissioner-provider relationship, complicating financial management for voluntary organisations funded in this way.

THE INCREASING DOMINANCE OF CONTRACTS IS PART OF A WIDER RECENT EVOLUTION IN FUNDING MECHANISMS.



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5. Office for National Statistics 'Projections of the dependency ratio of the number of people of working age to the number of people of state pension age'. www.ons.gov.uk (accessed January 2016)
6. PWC (2015) *Managing in a Downturn*. London: PWC.
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8. Department for Communities and Local Government (2015) *Rough Sleeping Statistics England: Autumn 2014 Official Statistics*. London: Department for Communities and Local Government.
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10. VONNE, Newcastle CVS and partners (2013) *Surviving or Thriving: Tracking the impact of spending cuts on the north east's third sector*. Newcastle upon Tyne: VONNE and Newcastle CVS.
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12. NCVO (no date) *Ten Procurement Barriers Affecting Charities and Social Enterprises*. London: NCVO.
13. NCVO 'UK Civil Society Almanac 2015: Income from government'. data.ncvo.org.uk/a/almanac15/government/ (accessed January 2016)
14. Sheil F. and Breidenbach-Roe R. (2014) *Payment by Results and the Voluntary Sector*. London: NCVO

THE CITIES AND LOCAL GOVERNMENT DEVOLUTION BILL ALLOWS FOR CITY REGIONS TO TAKE CONTROL OF SERVICES AS DIVERSE AS HEALTH AND SOCIAL CARE, HOUSING, PLANNING, TRANSPORT AND SKILLS.

GREATER LOCAL POWER

The decisions made by those in power will, however, increasingly differ between localities. The Localism Act 2011 provided councils with a general power of competence and the Cities and Local Government Devolution Bill allows for city regions to take control of services as diverse as health and social care, housing, planning, transport and skills. The new Public Contract Regulations 2015 also provide significant discretion to public bodies in deciding their own approach to procurement.

These powers can be used to choose from an expanding list of public service approaches and structures. Whether through commissioning or collaborating, bringing services back in-house or spinning out public service mutuals, local authorities have case studies they can learn from. In addition, a plethora of initiatives such as Whole Place Community Budgets and Our Place have combined elements of decentralisation, citizen participation and pooled budgeting.

Bringing budgets and decision making closer to communities could be a great opportunity for small and medium-sized voluntary organisations, if commissioners choose to engage the sector in these conversations. With their roots and reach in these communities, they are well placed to provide user voice, helping shape services to meet specific needs.

There is, however, a concern that the speed with which local devolution deals are being struck means that councils have not fully engaged voluntary organisations in the design of new local arrangements. Similarly, this historic decentralisation, combined with another tough funding settlement for local government, may see further aggregation of contracts, this time at a wider geographical level, shutting out smaller charities.

INDIVIDUAL GIVING

Finally, while statutory income is important, the life-blood of the voluntary sector is still income from individuals. Giving has remained strong despite a sustained fall in real wages,¹⁵ yet here too the sector faces challenges. Questions about campaigning, fundraising and chief executive officer (CEO) pay have strained the crucial relationships between the sector and donors. Public trust in the sector has fallen to its lowest level since 2007.¹⁶ While much of this may be driven by perception of larger charities (and wider public discontent with big institutions) the impact will still be felt by those in lower income bands.

HISTORIC DECENTRALISATION, COMBINED WITH ANOTHER TOUGH FUNDING SETTLEMENT FOR LOCAL GOVERNMENT, MAY SEE FURTHER AGGREGATION OF CONTRACTS, THIS TIME AT A WIDER GEOGRAPHICAL LEVEL, SHUTTING OUT SMALLER CHARITIES.

References :

15. NCVO 'UK Civil Society Almanac 2015: Income from individuals'. data.ncvo.org.uk/a/almanac15/individuals (accessed January 2016)

16. nfpSynergy (2015) *Trust in Charities Now at Lowest for Eight Years Scotland and Northern Ireland have Higher Trust in Charities than rest of Great Britain*. London: nfpSynergy.



2

THE BIG PICTURE: AN OVERVIEW OF SMALL AND MEDIUM-SIZED CHARITIES



2.1

CHARACTERISTICS OF SMALL AND MEDIUM-SIZED CHARITIES

This chapter provides an overview of the voluntary sector in terms of numbers and key characteristics of organisations and provides context for understanding the journey of small and medium-sized charities.

The voluntary sector is a large and diverse sector that has experienced significant recent change in response to financial events both at home and abroad. Whilst this is generally acknowledged, it is rarely reflected in long-term financial analyses of the sector. This report for the first time ventures beneath the high-level, aggregate figures in order to understand how the sector has evolved by following individual organisations through time. This has allowed for an investigation of the change and churn that it has experienced in response to an ever-fluctuating funding landscape, both at a sector-wide level as well as on an individual organisational level.

Figure 1 presents a breakdown of the number of charities within each income band in 2008/09 and 2013/14. It highlights that the larger the income size, the smaller the number of charities in that income band. Indeed, the voluntary sector predominantly comprises micro, small and medium-sized charities.

THE VOLUNTARY SECTOR IS DOMINATED BY A HIGH NUMBER OF SMALL AND MEDIUM-SIZED CHARITIES.

A HIGHER PROPORTION OF SMALL AND MEDIUM-SIZED CHARITIES ARE REGISTERED IN RURAL AND SEMI-URBAN AREAS THAN LARGER CHARITIES, WHICH ARE MOSTLY REGISTERED IN URBAN AREAS.

Charities are not evenly distributed geographically across England and Wales. This is to be expected, since human population and therefore social need are also unevenly spread. However there is a pattern related to the size of organisation, whereby smaller charities are predominantly located in rural areas and larger charities in urban areas. It is likely that many charities are in major cities for administrative and practical purposes (similar to public- and private-sector organisations) and as they work with more people. However, it also probably

reflects the less connected nature of rural areas in comparison with urban areas. In regions with limited public transport provision and accessibility it makes sense to have more charities that can meet needs locally, rather than create a situation where people are forced to travel longer distances in difficult circumstances to access services.



Figure 1. Number of charities within each income band in 2008/09 and 2013/14

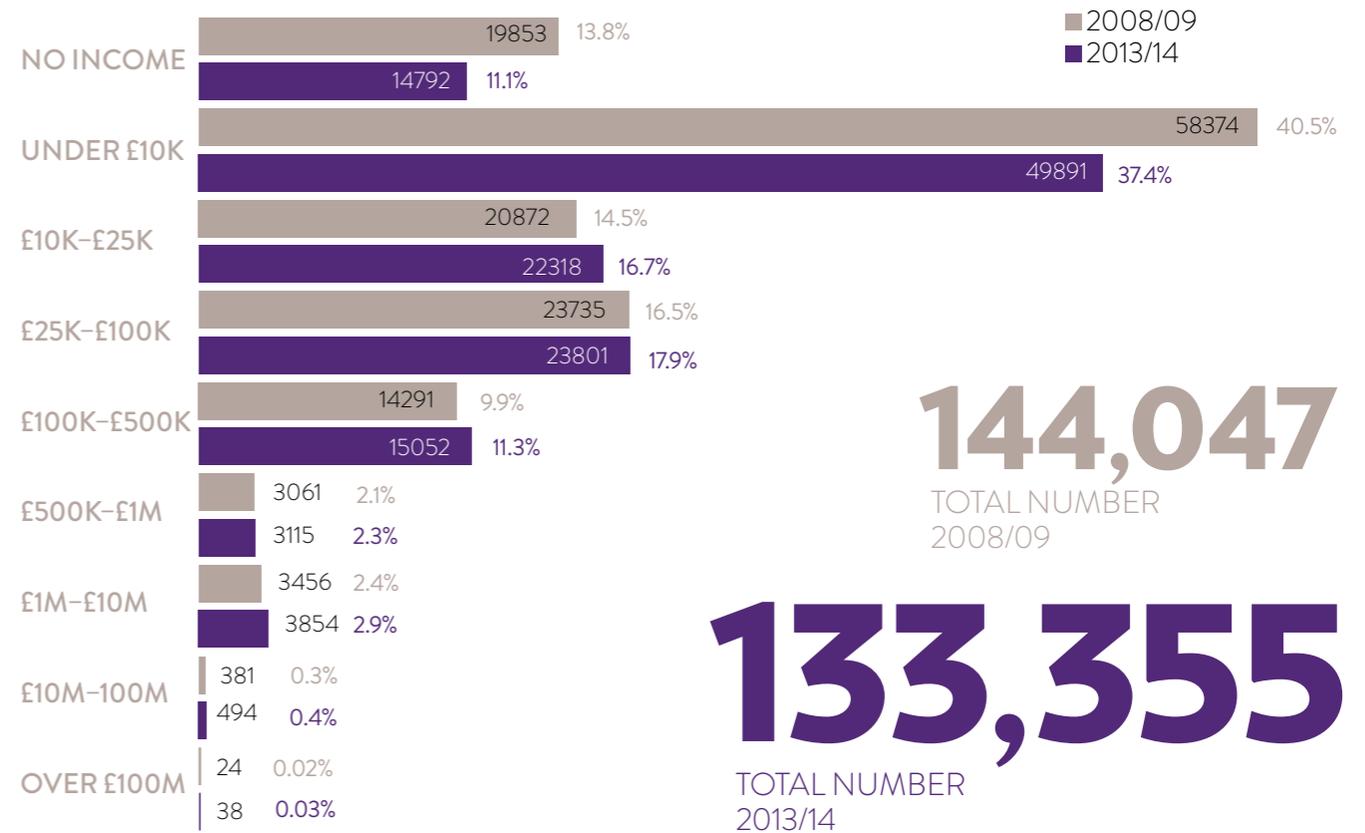
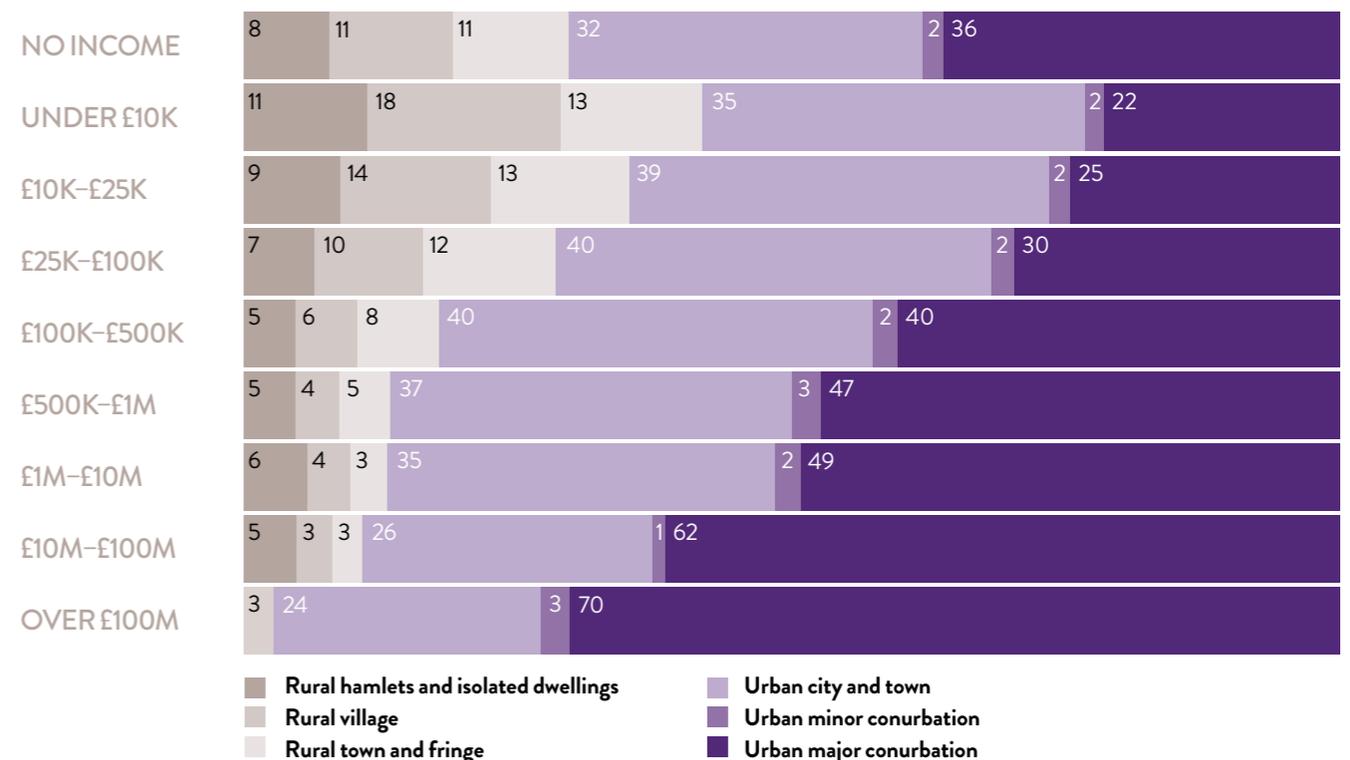


Figure 2. Proportion of charities in rural and urban areas by income band, 2013/14 (%)



Similar to the size pattern of rural-urban areas, charities are unevenly distributed according to wealth. The fact that small charities are more likely to be located within less deprived areas, whilst large charities are more likely to be located in more deprived areas partly reflects the rural-urban split of small and large charities, as areas of high poverty also tend to be associated with higher levels of urbanisation. The large number of very small, or micro, charities also includes many community organisations such as village halls and parent teacher associations which are not generally associated with deprivation or poverty alleviation. In chapter 4 more detailed breakdowns of income are also analysed by region, based on data available from the UK Civil Society Almanac.

A HIGHER PROPORTION OF CHARITIES WITH AN INCOME UNDER £500K ARE REGISTERED IN LESS DEPRIVED AREAS THAN LARGER CHARITIES, WHICH ARE LIKELY TO BE LOCATED IN MORE DEPRIVED AREAS. HOWEVER, THE HIGHEST PROPORTION OF CHARITIES REGISTERED IN THE MOST DEPRIVED AREAS WAS FROM THE £500K-£1M INCOME BAND.

Figure 3. Proportion of charities in areas of deprivation, as defined by the Index of Multiple Deprivation (IMD), 2013/14 (% in deciles)



2.2

THE NUMBER OF SMALL AND MEDIUM-SIZED CHARITIES

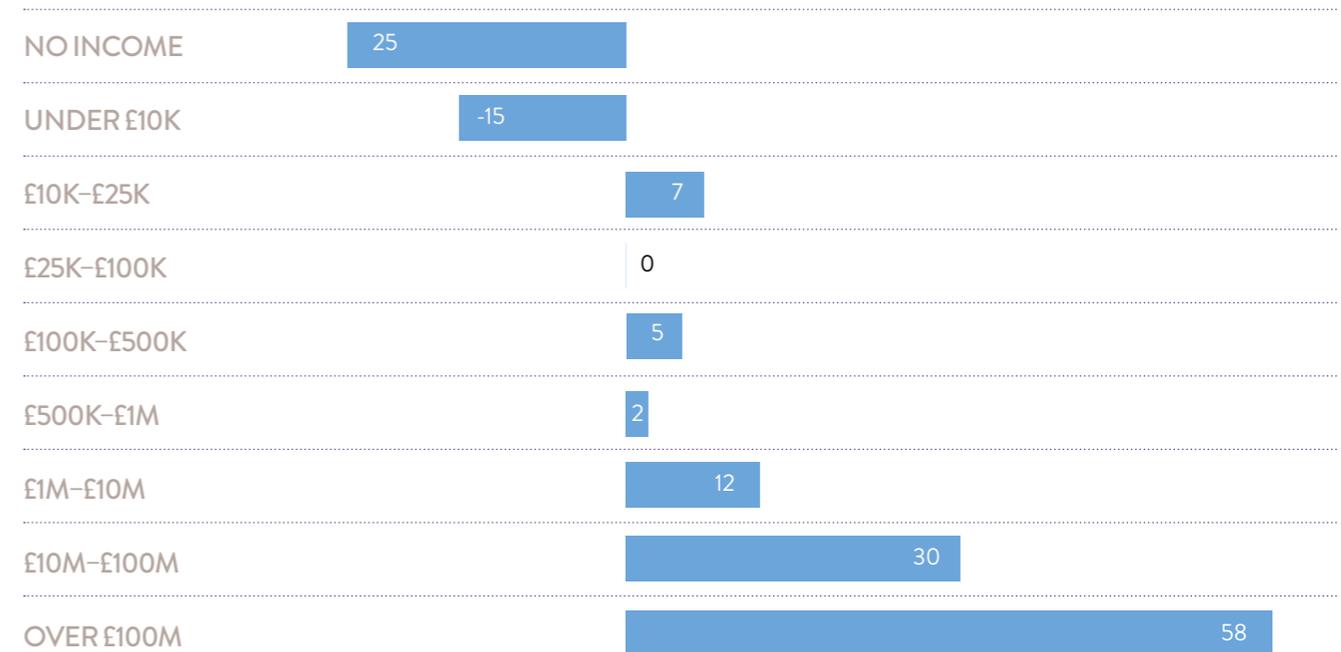
THERE WAS A DECREASE IN THE NUMBER OF THE SMALLEST CHARITIES AND AN INCREASE IN THE NUMBER OF LARGER CHARITIES BETWEEN 2008/09 AND 2013/14. NUMBERS OF MIDDLE-INCOME CHARITIES (£25K-£1M) APPEARED THE MOST STABLE.

Whilst in general the overall number of charities has remained relatively stable over time, the makeup of these organisations by size has changed. In general, the larger the income band the greater the relative increase in the number of charities. Charities registering no income decreased by one-quarter between

2008/09 and 2013/14 whilst the number of charities over £100m increased by nearly 60%. Those in the middle three income bands (£25k-£1m) only increased by between 0.3% and 5%. However, in terms of absolute numbers, the £10k-£25k income band increased by the most, with nearly an extra 1,500

charities operating in 2013/14, whilst charities with no income or under £10k together decreased by nearly 13,500. By contrast, the number of over £100m charities increased by 14. Therefore, the biggest absolute changes are occurring among the very smallest charities.

Figure 4. Change in number of charities in each income band, 2008/09 to 2013/14 (% change)

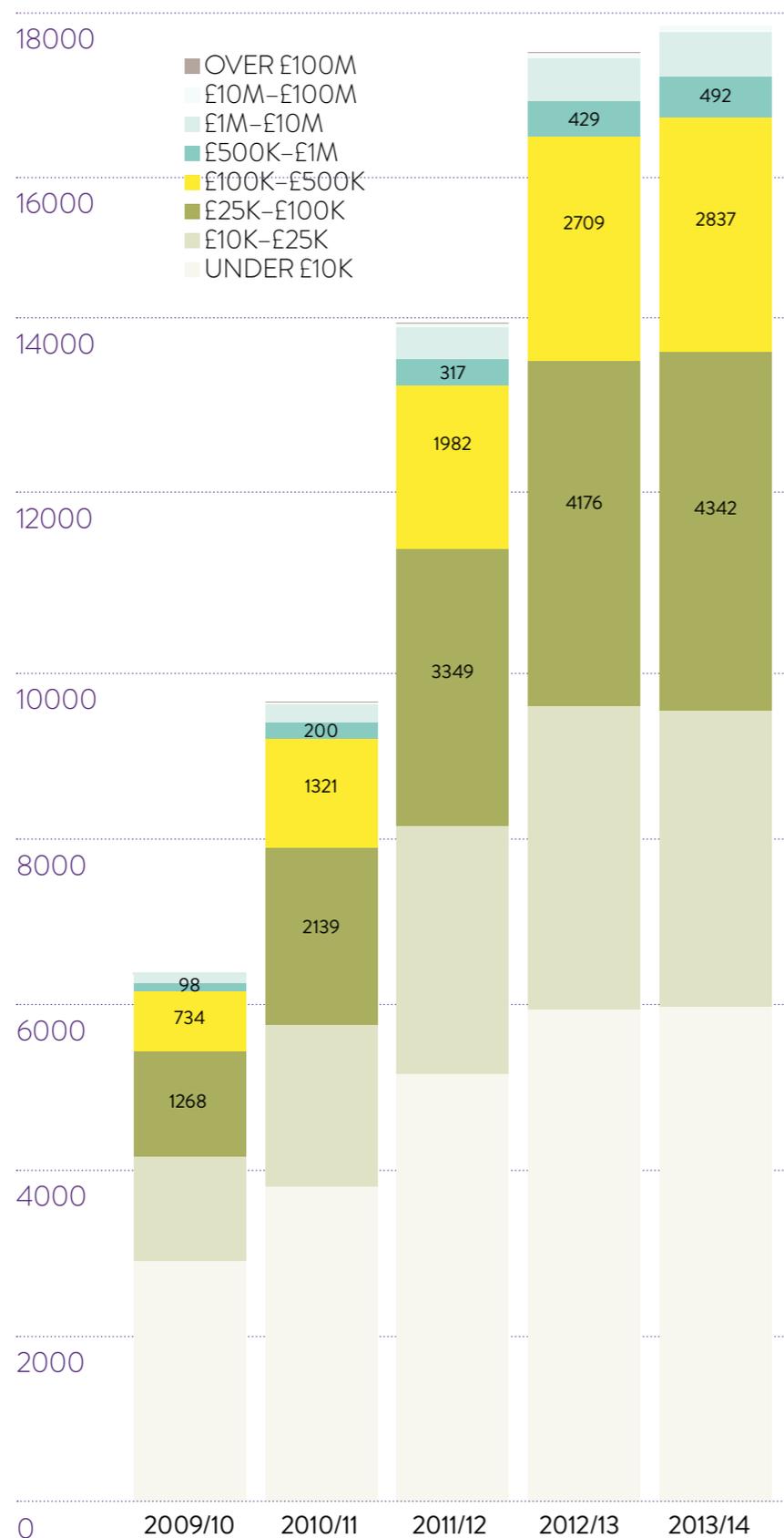


However, do these numbers represent individual organisations being formed and lost, or the same organisations undergoing change and moving between income bands? The two following charts suggest that both scenarios may be at play.

CONSIDERABLE NUMBERS OF NEW ORGANISATIONS WERE REGISTERED BETWEEN 2008/09 AND 2013/14; THESE WERE PREDOMINANTLY MICRO AND SMALL CHARITIES.



Figure 5. Number of new charities that had either zero income or were not in existence in 2008/09, by income band, cumulative increase



18,000

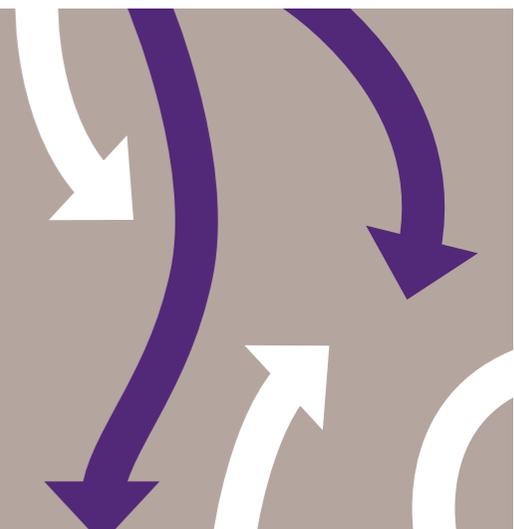
CHARITIES WERE OPERATING IN 2013/14 THAT WEREN'T ACTIVE IN 2008/09

- Nearly 18,000 charities were operating in 2013/14 that weren't active in 2008/09, constituting a sizeable chunk of the overall voluntary sector. The vast majority of these were small and medium-sized charities. However, despite a large number of new, very small charities being established, far more were lost as shown in Figure 4, an indication of

the level of movement among micro charities.

It should be noted that figures for new and missing charities are not adjusted to reflect re-registrations of organisations, so some of these organisations may represent pre-existing organisations now under different registrations.

THERE IS A HIGH AMOUNT OF MOVEMENT IN THE VOLUNTARY SECTOR, WITH INCOME FLUCTUATION CAUSING CHARITIES TO MOVE IN AND OUT OF INCOME BANDS OVER TIME. OF ORGANISATIONS THAT WERE IN THE £500K-£1M INCOME BAND IN 2008/09, MORE HAD LOST INCOME BY 2012/13 THAN GAINED INCOME.



Static income bands can mask considerable changes in income that charities experience over time. Following the fate of individual organisations instead illustrates that in addition to charities being created and lost, many charities frequently moved between income bands. Figure 6 provides a high level overview to indicate the degree of movement of charities between income bands. It shows all charities that were in the middle-income band £100k-£500k

in 2008/09 and the income bands that these same charities were in during previous and subsequent years. In 2006/07, 33% of charities were in different income bands and by 2012/13, 39% had moved again. This approach clearly demonstrates that the income of many charities fluctuates considerably from year to year.

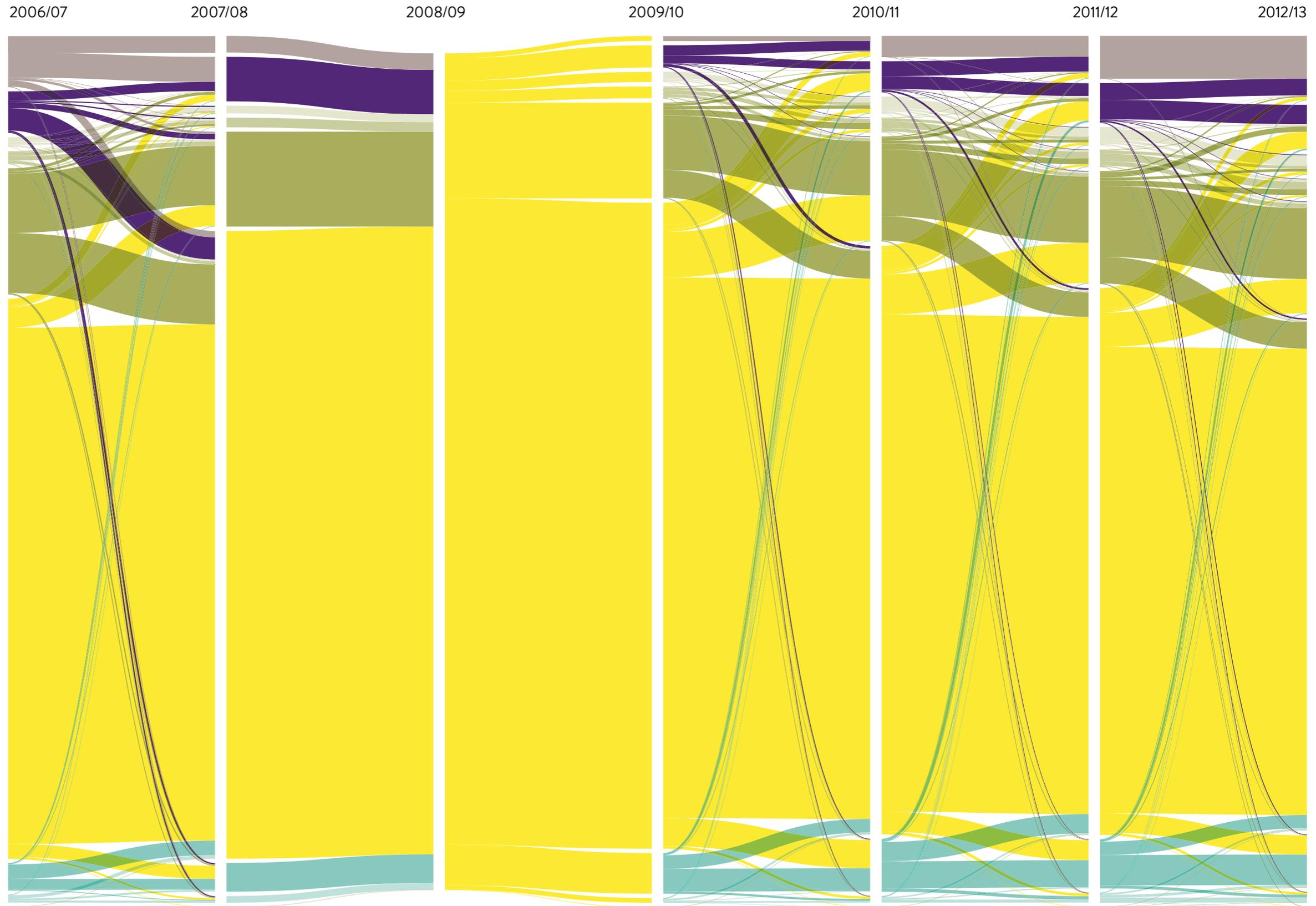
In addition, of charities that were in the income band £100k-£500k in 2008/09, 23% moved into a lower

income band compared with 8% that moved into a higher income band, meaning that more organisations lost than gained income between 2008/09 and 2012/13. These could partly account for the numbers of charities increasing in the £10k-£25k income band, in addition to new charities.

Figure 6. All charities that were in the £100k–£500k income band in the year 2008/09 and their income bands two years previously (from 2006/07) and in subsequent years (to 2012/13).

The height of the bands is proportional to the number of charities in that band. The top band represents 'missing' charities – those that did not register an income that year.

- MISSING
- NO INCOME
- UNDER £10K
- £10K–£25K
- £25K–£100K
- £100K–£500K
- £500K–£1M
- £1M–£10M
- £10M–£100M
- OVER £100M



3

A TYPOLOGY OF INCOME TRAJECTORIES

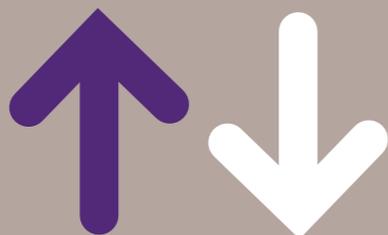


As demonstrated in chapter 2, the ability to explore and compare financial changes between different charities is somewhat limited by static income bands, as the amount that defines the jump between different income bands ranges from £10,000 to £90m. For example, the loss of £250,000 in income could represent the difference between survival and closure for a medium-sized organisation but only a relatively small loss for a larger organisation. Therefore a new classification of all organisations into a 'typology' was developed that described the trajectory of all individual organisations based on the proportional change in their overall income between 2008/09 and 2013/14. The new typology helped overcome the limitations of pre-defined income bands and facilitated comparison between the income trajectories of different sized organisations.

Table 2. Definition of typology categories for all charities based on the change in their income between 2008/09 and 2013/14

Typology category	Definition	Percentage of charities
Missing	Income was zero in 2013/14	18%
Up then down	The upper income reached was more than double the largest income in both 2008/09 and 2013/14	7%
Big fall	Income halved or more between 2008/09 and 2013/14	9%
Little fall	Income fell by one-fifth or more between 2008/09 and 2013/14	10%
Ticking along	Income in 2013/14 was within 20% of the income in 2008/09	22%
Little rise	Income rose by one-fifth or more between 2008/09 and 2013/14	14%
Big rise	Income doubled or more between 2008/09 and 2013/14	8%
Down then up	The lower income reached was less than half the smallest income in both 2008/09 and 2013/14	7%
From nothing	Income was zero in 2008/09 and greater than zero in 2013/14	4%

OVER HALF OF ORGANISATIONS EXPERIENCED A RISE OR FALL IN INCOME OF MORE THAN ONE FIFTH BETWEEN 2008/09 AND 2013/14.



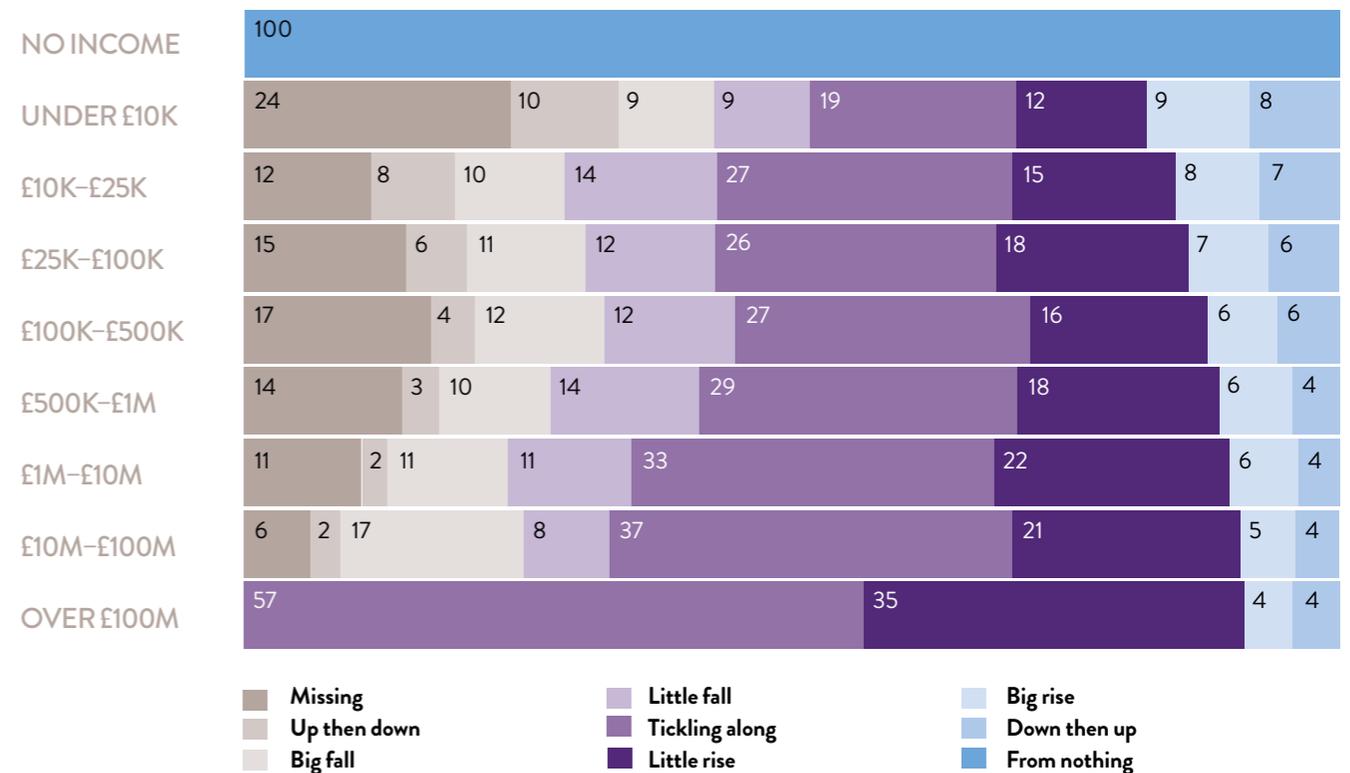
Nearly half of charities across all income bands were classified as either 'ticking along' or experiencing only a 'little rise' or a 'little fall' (Table 2), suggesting some level of stability in the sector. However, this also means that just over half experienced substantial income change between 2008/09 and 2013/14. This includes nearly one-fifth of organisations (18%) that were defined as 'missing', and a further 17% that saw a 'big rise' or 'big fall'.

Consistent with the findings in chapter 2, the typology helps to demonstrate that instability within the voluntary sector is not equally spread between different sized organisations. Figure 7 shows that smaller charities generally fell within every category of the typology. In addition, they occurred within the different categories in increasingly equal measure the smaller they became, meaning that the smallest experienced downward trends

almost as frequently as upward trends. By contrast, the larger charities were more likely to predominantly or solely fall within one of the middle three 'stable' categories ('little fall', 'ticking along', and 'little rise'). In other words, the smaller a charity is, the less resilient it is to change, and vice versa.

SMALLER CHARITIES WERE MORE LIKELY TO EXPERIENCE INCOME VOLATILITY THAN LARGER CHARITIES.

Figure 7. Proportion of charities within typology categories (%)



BEHIND THE DATA: 'MISSING' CHARITIES

In addition to new organisations being formed, substantial numbers of charities cease to exist every year. This occurs for a number of reasons, but all help to highlight the changeable nature of the sector from the perspective of

small and medium-sized charities. For example, one advisory service for young people in the south-west of England dissolved following financial difficulty; a crime prevention charity in Wales was unable to repay a large loan; one charity that carried out business training for people with mental health problems in the east of England closed due to cuts in statutory funding and

grants; an educational trust in the north-east of England closed due to local authority cuts. These examples taken from an analysis of charities' annual accounts represent only a sample of the financial problems that middle-income charities have faced in recent years, but demonstrate the diversity of challenges that the sector faces.

3.1

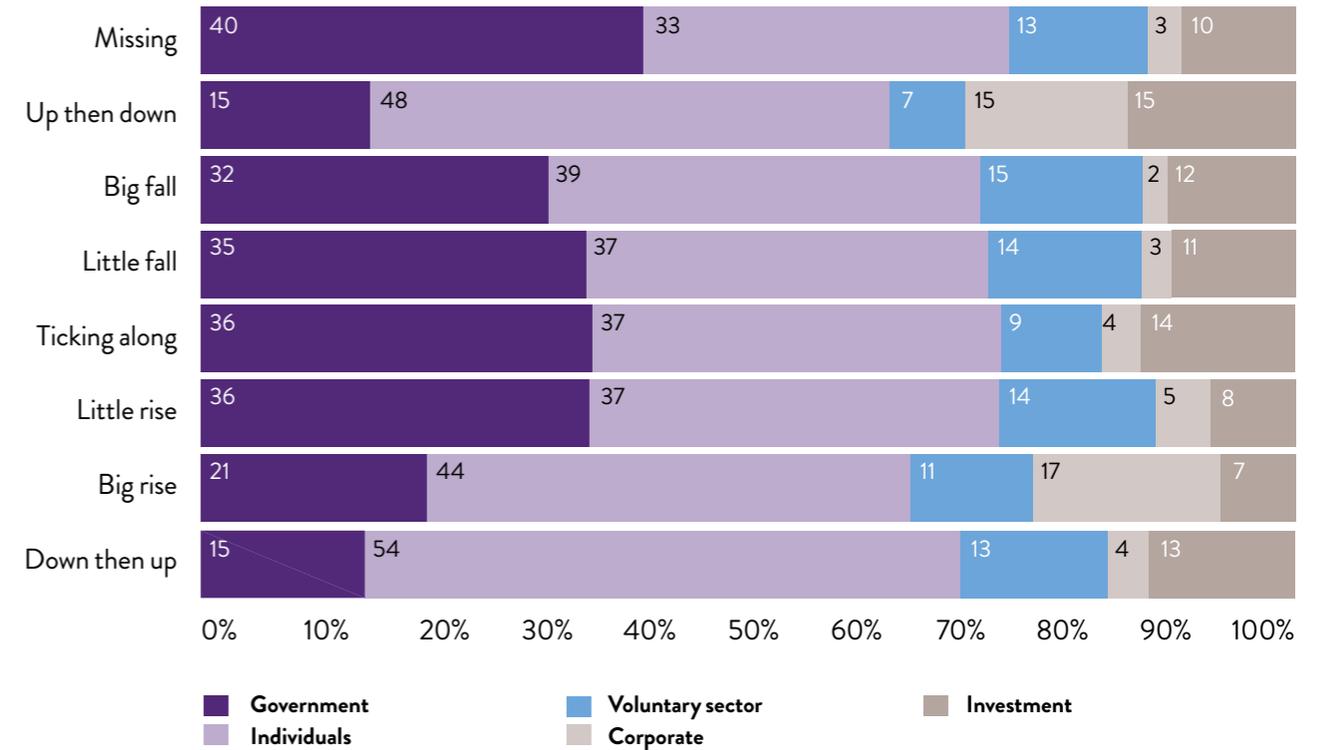
CHARACTERISTICS OF SMALL AND MEDIUM-SIZED CHARITIES BY TYPE

This section investigates income according to type in more detail solely for middle-income charities (£25k–£1m) whose activity encompassed those working with individuals over 17 years old facing multiple disadvantage (in line with Lloyds Bank Foundation’s priorities). Due to the focus here on detailed financials such as income by source, only data up to 2012/13 was used.

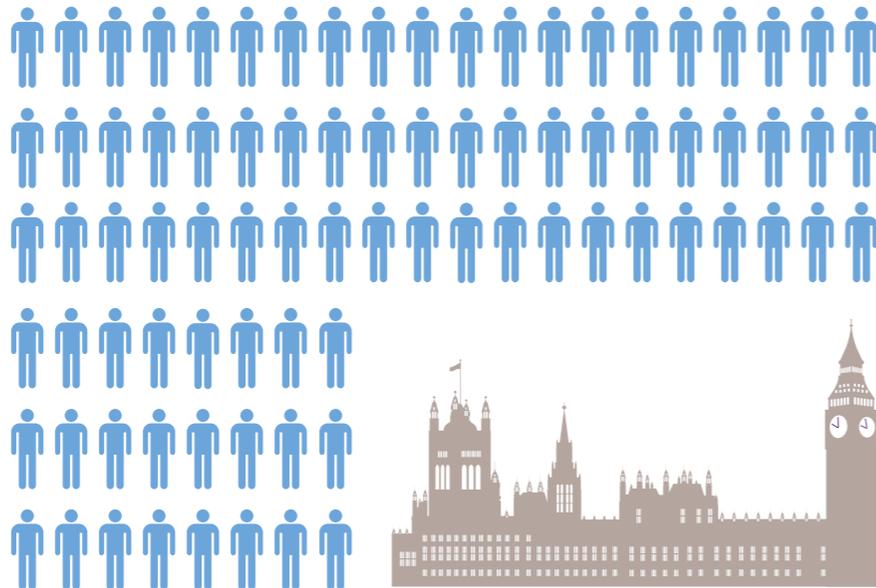
Figure 8 shows the income sources for the different categories of the typology for middle-income charities. Although there is no huge variation in funding sources between typology categories, it appears that those organisations that experienced a ‘big rise’ are more likely to end up with a much higher proportion of income from individuals. Income from individuals also seems to be associated

with the volatile income categories (‘down then up’ and ‘up then down’), as does income from investments (which is probably a result of investment performance over the period). Moreover, these patterns are broadly consistent with those in 2008/09, emphasising that a prerequisite for growing fast over this period was to not start with a lot of income from government.

Figure 8. Income sources of charities with income between £25k–£1m in 2012/13, by type (%)



MIDDLE-INCOME CHARITIES THAT INCREASED THEIR INCOME SINCE 2008/09 HAVE A HIGHER PROPORTION OF INCOME FROM INDIVIDUALS THAN GOVERNMENT.



We know from the rest of the dataset that the sector as a whole was able to replace some of the lost government funding with funding from individuals. But the question remains whether this was done at a sector level (with some organisations losing funding from government and other organisations gaining income from individuals) or at the level of individual organisations (with the organisations themselves able to replace lost government funding with new income from individuals).

Figure 9 shows that there is some evidence to support the latter. Of those middle-income organisations that saw a decrease in government

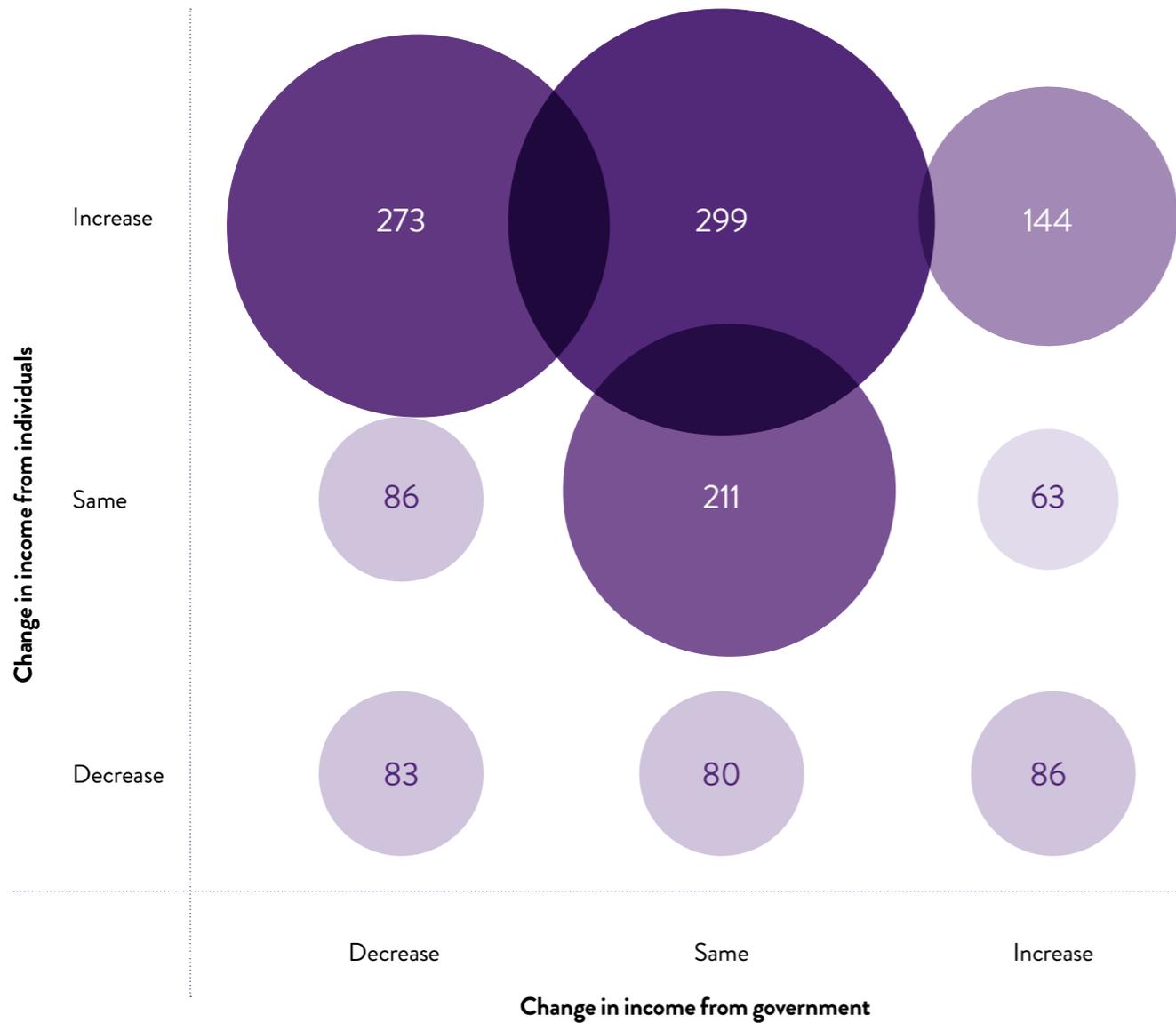
funding of more than 20% between 2008/09 and 2012/13, 62% had an increase in income from individuals, compared with under half of those that saw government funding increase or stay the same. Overall, organisations were more likely to experience an increase in income from individuals if their income from government either decreased or stayed the same.

Some caution needs to be exercised around this data, however. There may be a survivorship bias – those organisations that returned data for all four years are more likely to be those that had successful funding strategies.

CHARITIES THAT INCREASED THEIR INCOME FROM INDIVIDUALS THE MOST WERE THOSE WHOSE INCOME FROM GOVERNMENT HAD EITHER STAYED THE SAME OR DECREASED.



Figure 9. Number of charities with an income between £25k–£1m and their change in income from government and individuals between 2008/09 and 2012/13 (increase = more than 20% increase, same = within 20%, decrease = more than 20% decrease)



3.2

CASE EXEMPLARS



The following section details four examples of how individual charities have fared between 2008/09 and 2013/14 in terms of their income generation, using information taken from the text in charities' accounts. The examples focus on three different categories of the typology: one organisation that experienced a 'big fall' in income, one that broadly maintained its income 'ticking along', and two that experienced a 'big rise' in income.



BEHIND THE DATA: DEPENDENCE ON FEW RESOURCES

For many small and medium-sized charities it was clear that their annual income depended very much on the success of individual bids and continuous funding of often single projects that placed

them in a very precarious financial situation. For example, one mental health charity in south London experienced a 'big rise' in income that was as a result of one successful bid from a local clinical commissioning group. Likewise a heritage trust in the West Midlands experienced a 'big rise' in income as a result of a single legacy donation and one successful lottery bid.

By contrast, a penal reform charity in London experienced fluctuation in income due to the end of a Big Lottery Fund grant which accounted for over 40% of its income. This dependency on single sources of income is likely to account for the fluctuation of organisations under £1m across income bands through time.

'BIG FALL'

A London-based charity that works to combat in-work poverty for families suffered a big fall in income between 2008/09 and 2013/14. In 2009 its income decreased from £820,000 to £670,000 and it predicted a small deficit in the following year as well. In both years' accounts it noted that income loss was largely due to the fact that 'funding from individual supporters, from corporate sponsorships and from sales to employers continued to be affected by the recession'.

As a response to this situation it revised its business plan 'to concentrate on core activities around a reduced core cost base, since the risk remains high that the charity will not meet its reserves target'. It experienced small income fluctuations in the next three to four years, largely driven by earned income. It noted that earned income from sales (largely membership and marketing) did well but that it struggled to establish training and consultancy as a core income stream.

It managed to maintain funding from grants despite the fact that 'fundraising from Trusts and Foundations was increasingly competitive'.

Its strategy in the face of falling income then also shifted to decreasing spending, by 'controlling costs' and 'reducing overheads by moving to cheaper, serviced offices'. A 'tightening [of] corporate budgets', particularly around sales and membership, was mirrored by a final fall in recorded income in 2013/14.



'TICKING ALONG'

A charity based in the West Midlands that provides support for carers was one example of a charity that was defined as 'ticking along' – in other words it did not experience large fluctuations in income. From 2008/09 its income remained just over £500,000.

The majority of its income was derived from grants from a major funder and the local county council, the latter in 2010 providing nearly three quarters of its income. As this was a three year grant it provided a solid income source and gave it time to investigate alternative sources of funding when this came to an end.

The main reason for its ability to retain a steady income appears to be the diversity of funders that it applied to, with several different foundations and organisations providing grants in the year that it lost council funding. However, it also appeared to maintain a positive relationship with the council as it was confident that a grant would be renewed in 2013/14, with no indication that council cuts would impact this.

'BIG RISE'

(CHARITABLE TRADING)

One alcohol and drugs abstinence service charity in the north-west of England grew its income rapidly from nearly £900,000 in 2008 to over £1m in 2009 and then nearly doubled its income in the following year to £2.5m. By the end of 2013 its income was over £3m.

This huge income increase was driven solely by earned income, specifically from charitable trading, meaning that it related to its core charitable activity. It actively embraced the new 'Payment by Results' model of funding despite it being 'an anathema to the majority of providers for many years' by diversifying its services and entering

into partnerships with other agencies in order to be able to bid for a wider range of contracts. It also explored new funding mechanisms such as Social Impact Bonds which it argued 'enabled [it] to expand in a climate of public-sector cuts'.

Finally in 2013 it had grown its services to such an extent that it negotiated a merger with a larger organisation in order 'to strengthen the general administration of the charity' and to reflect the widening scope of its charitable activities. It specifically attributed its growth to 'developing partnerships with larger organisations that wish[ed] to

subcontract our services'. It acknowledged that the local authorities' demand to get 'more for less' has devastated many agencies but stated that it provided 'several opportunities'.



'BIG RISE'

(FUNDRAISING TRADING)

Another charity based in the east of England that works on inclusion and independence for disabled and disadvantaged people also experienced a huge rise in income from £900,000 to £2m from 2008/09 to 2013/14, propelling it out of the middle-income bracket.

Its accounts show that it experienced a large jump in earned income from around £17,000 to nearly £600,000 from 2007/08 to 2008/09. This figure continued to rise steadily year-on-year, while its voluntary income fluctuated and then declined substantially from 2011 onwards. However, in contrast to the previous charity, the rise in earned income was predominately attributable to fundraising trading, in other words through activities unrelated to its main

charitable purpose. This was in the form of two successful social enterprise subsidiaries set up by the charity, in one year earning them £1.6m, and it commented that 'the Social Enterprise sector is a key driver in strengthening an inclusive and growing economy'. It also received a grant that contributed towards the salary of a business development manager, reflecting the increasing commercial approach of the charity towards income generation.

This move was explicitly motivated by concern at 'changes in local and central funding and other organisational agendas' and it proactively 'had to look for alternative revenue streams and develop new services and introduce new ways of working'. For example it also 'identified the need to invest in

maintaining and establishing constructive and positive relationships with cross sector agencies', which resulted in securing extra revenue as a subcontractor.





THE BIG PICTURE: POLICY COMMENTARY

One of the first documents published by the Coalition government, just one week after its formation and two days before the release of its programme for government,¹⁷ was called *Building the Big Society*.¹⁸ Drawing inspiration from the 18th century statesman Edmund Burke, who wrote of the ‘small platoons’ on which civil society is based, the document set out a vision in which greater power and responsibility were placed in the hands of communities, including local charities.

The figures in this report show that the voluntary sector largely embodies this vision. Almost half of all registered charities have an income below £10,000 and over 99% meet the EU definition of an SME.¹⁹ Yet, despite David Cameron periodically returning to the *Big Society*, under the Coalition it was the ranks of the largest organisations that grew the most. In 2013/14 there were 30% more charities

with a £10m–£100m turnover and 58% more with income over £100m than there were in 2008/09. By contrast, the number of medium income organisations grew only a little whilst there was a significant thinning of groups with a turnover below £10,000.

Looking just at the static income bands, however, only tells half the story. For the first time, this research has uncovered the scale of ‘churn’ within the sector. Large numbers of charities are moving between bands on an annual basis and the movement is greater the further down the income spectrum you go.

Smaller organisations experience much greater income volatility: they are significantly more likely to experience big rises or big falls or go out of business. (A similar dynamic occurs in the private sector where almost 60% of new businesses go out of business within five-years).²⁰ In many ways this is unsurprising. Larger organisations will, in general, have a greater number of income streams. As a result, their overall income will be determined less

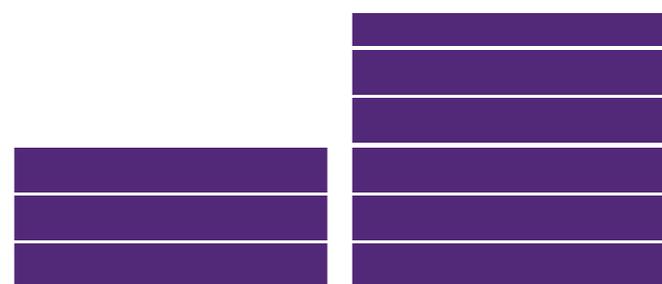
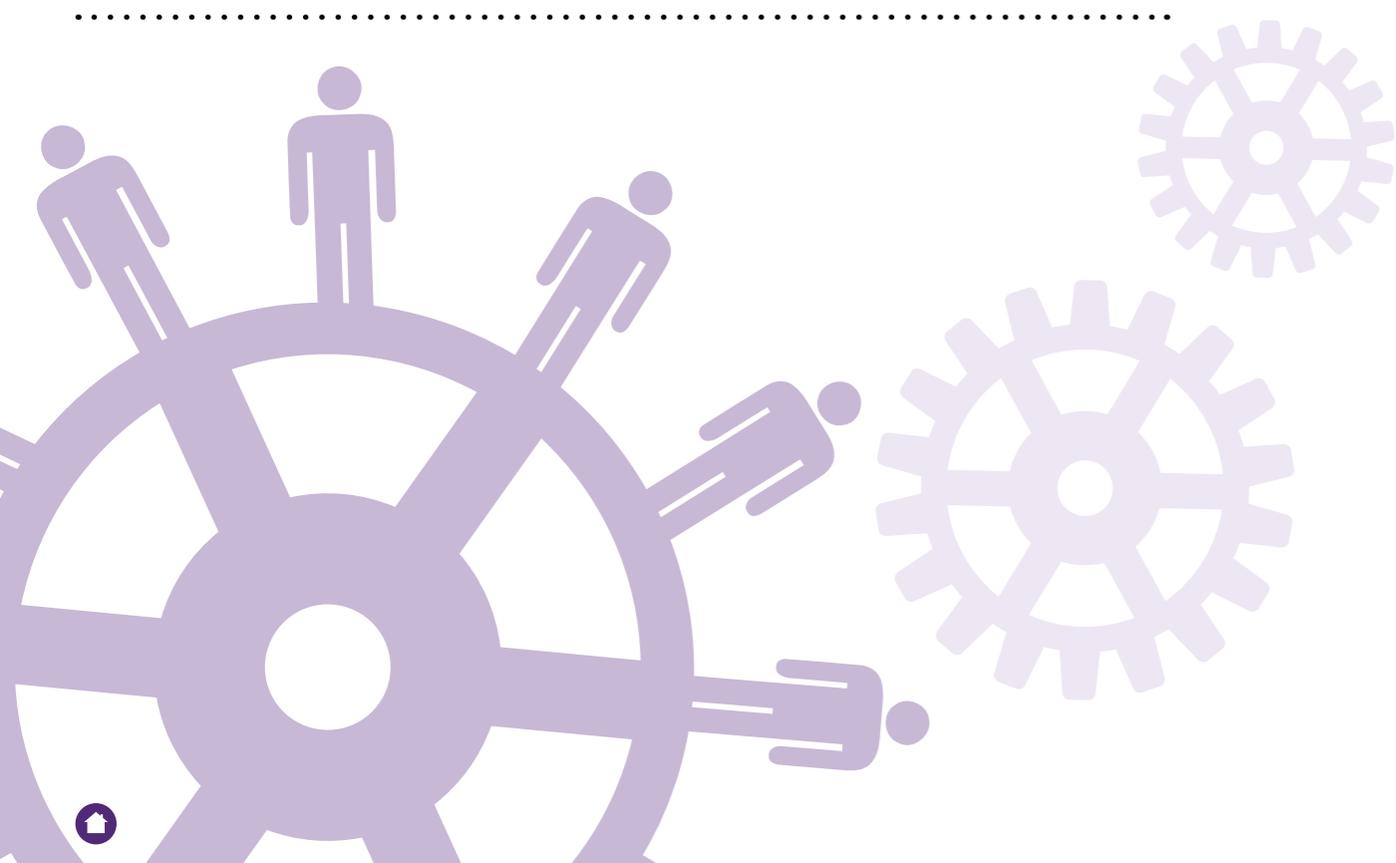
by changes to a single source, leading to a more stable income profile.

This does, however, have implications for funders. The uncertainty associated with short-term grants or contracts, unpredictable referrals and delegated personal budgets will be far more critical for smaller charities. The removal or retention of a single funding award is more likely to be the difference between survival and shutdown. Once gone, the additional resources attracted by that organisation – for example donations or volunteer capacity – may be difficult to get back.

References :

- 17. <https://www.gov.uk/government/publications/the-coalition-our-programme-for-government>
- 18. <https://www.gov.uk/government/publications/building-the-big-society>
- 19. A turnover of less than €50m and fewer than 250 employees
- 20. Office for National Statistics (2014) *Business Demography*, 2013. Newport: Office for National Statistics.

THE UNCERTAINTY ASSOCIATED WITH SHORT-TERM GRANTS OR CONTRACTS, UNPREDICTABLE REFERRALS AND DELEGATED PERSONAL BUDGETS WILL BE FAR MORE CRITICAL FOR SMALLER CHARITIES.

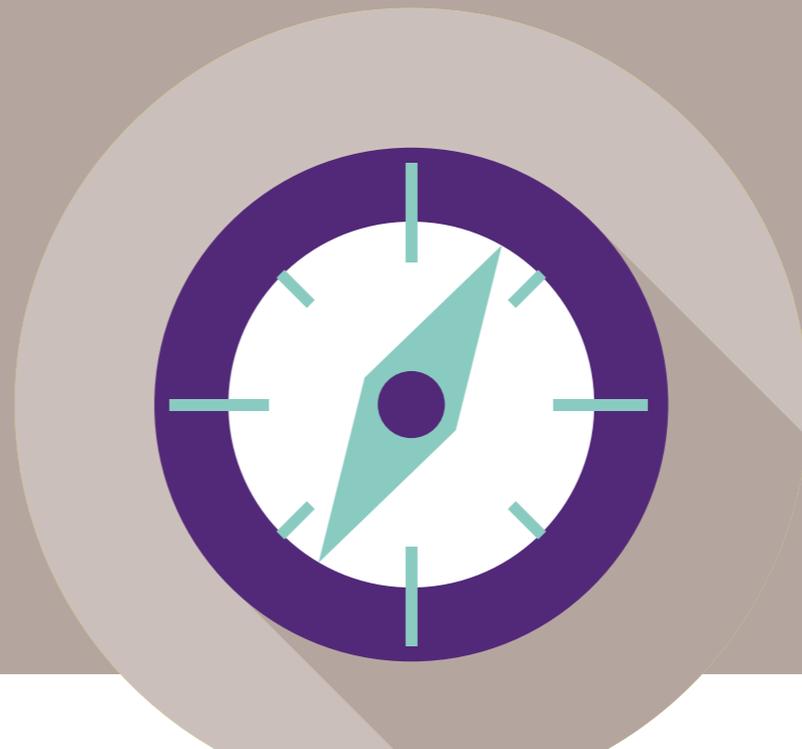


IN 2013/14 THERE WERE 30% MORE CHARITIES WITH A £10M–£100M TURNOVER AND 58% MORE WITH INCOME OVER £100M THAN THERE WERE IN 2008/09



4

AGGREGATE FINANCIAL DATA INCOME



The following two chapters focus on detailed breakdowns of aggregate income and spending for the voluntary sector based on the UK Civil Society Almanac methodology (see Appendix). Due to the fact that the aggregate data relies on a sample of organisations, it is less robust for the very smallest charities (£0–£25k) as there are proportionally fewer smaller charities represented in the sample. Therefore, analysis in these chapters is restricted to the middle (£25k–£1m) and upper (£1m–over £100m) income bands.



SOURCES OF VOLUNTARY SECTOR INCOME

1. Income from government:²¹

The definition of government covers any statutory body, including central government departments, local authorities, devolved and regional government, the EU and international governments, town and parish councils, NHS trusts and a range of non-departmental public bodies (NDPBs). This report focuses predominantly on central and local sources of government income.

Although most transactions occur between the statutory authority and the voluntary organisation, more complex relationships such as subcontracting, match funding and direct payments also occur. However, in general income from government is received as either voluntary or earned income in two main forms:

- Voluntary income: as **grants**.
- Earned income: as **contracts** or fees.

2. Income from individuals:²²

This is also received as either voluntary and earned income, but each comprises two main forms:

- Voluntary income: as i) **donations** (an amount of money given to a charity) and ii) **legacies** (an amount of money or property left to someone in a will).
- Earned income: as i) **charitable trading** (also known as fees for services) that provides services that the charity was set up to deliver eg rent for accommodation, fees for adult social care, training course fees and membership subscriptions, and ii) **fundraising trading** that provides services outside those that the charity was set up to deliver eg the sale of donated goods in charity shops and admission fees for fundraising events¹.

References:

21. NCVO 'UK Civil Society Almanac 2015: Income from government'. data.ncvo.org.uk/a/almanac15/government/ (accessed January 2016)

22. NCVO 'UK Civil Society Almanac 2015: Income from individuals'. data.ncvo.org.uk/a/almanac15/individuals (accessed January 2016)



• These different sources and forms of income can be broken down and analysed to ascertain where charities are receiving their funding from. The balance of these different income sources can also tell us something

about the 'health' of the sector, for example, in challenging financial times charities need to look for new ways of generating income, which may be reflected in an increase in earned income from individuals.

4.1

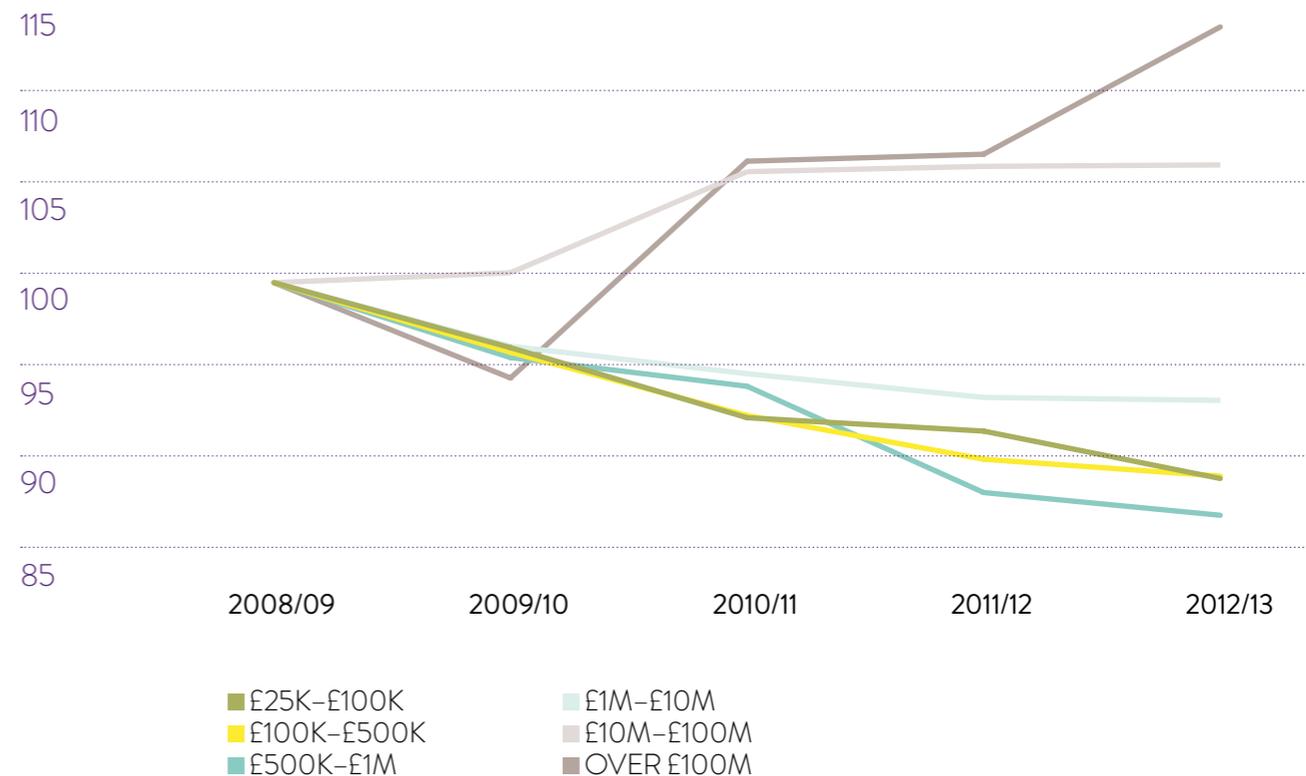
OVERALL INCOME

Overall losses and gains in income were not experienced equally across different income bands. All three middle-income bands (£25k–£1m) experienced a decrease in overall income between 2008/09 and 2012/13. The three middle-income bands lost a higher proportion of

their income than all the upper income bands, the top two of which actually increased their income over this time. This suggests that larger charities have been able to better navigate the changing financial landscape between these years than middle-income charities.

MIDDLE-INCOME (£25K–£1M) CHARITIES LOST A HIGHER PROPORTION OF THEIR INCOME THAN UPPER INCOME (£1M–OVER £100M) CHARITIES.

Figure 10. Overall income by income band, cumulative change, 2008/09 to 2012/13 (2008/09 = 100)



4.2

CHANGES IN INCOME MIX OF SMALL AND MEDIUM-SIZED CHARITIES

This section provides a breakdown of income sources for middle-income charities and how these have changed over time.

For all middle-income bands, the pattern of income change was broadly similar and consistent over time. This comprised a year-on-year loss of both government grants and contracts. In terms of voluntary income from individuals, income from donations remained stable whilst legacy income rose. Both forms of earned income from individuals (charitable and fundraising trading) also increased. Overall, the major shift in income was from one dominated by government grants and contracts to one in which earned income from individuals made up a higher proportion of overall income. The smallest income band (£25k-£100k) provided the only exception, for which government contracts increased over this time.

BETWEEN 2008/09 AND 2012/13 THE INCOME MIX OF MIDDLE-INCOME CHARITIES (£25K-£1M) SHIFTED FROM ONE IN WHICH GOVERNMENT AND INDIVIDUALS CONTRIBUTED TO OVERALL INCOME IN ROUGHLY EQUAL MEASURE TO ONE WHERE THE MAJORITY OF INCOME CAME FROM INDIVIDUALS.

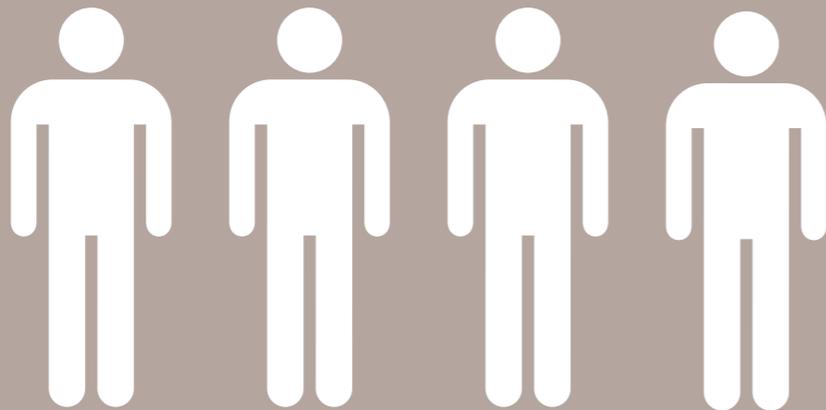
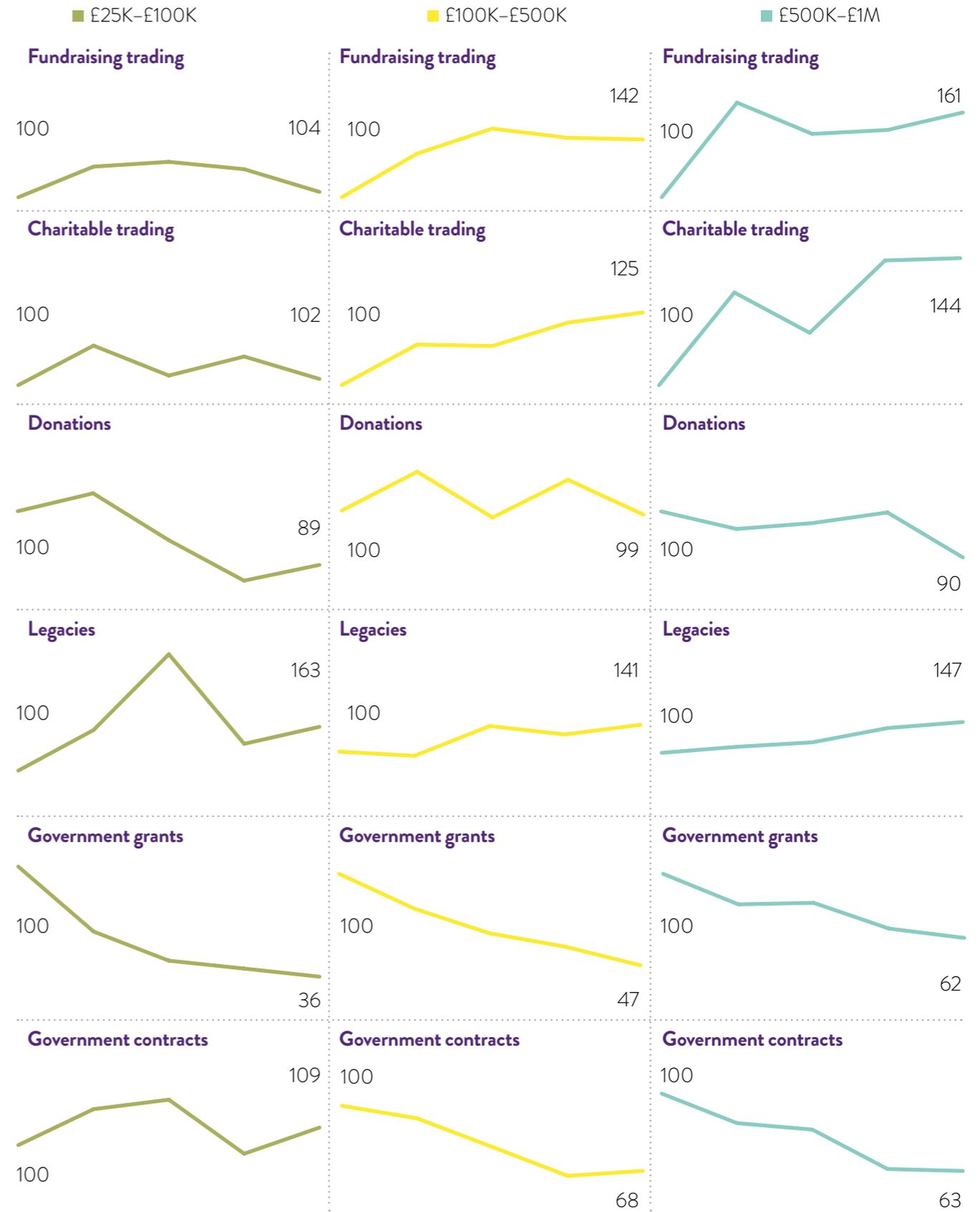


Figure 11. Sources of income for income bands £25k-£100k, £100k-£500k and £500k-£1m, cumulative change, 2008/09 to 2012/13 (2008/09 = 100)





INCOME MIX OF SMALL AND MEDIUM-SIZED CHARITIES: POLICY COMMENTARY

The increase in government contracts for the £25k–£100k income band is striking. Although income from this source is below the peak achieved in 2010/11, the financial year before the Coalition’s Spending Review came into effect, by 2012/13 it was still 9% above the 2008/09 level. Indeed, this was the best performing income stream for this band over the period.

The contrast with the £100k–£500k and £500k–£1m bands, which both saw falls in government contract income of over 30%, is stark. Although we can’t say for certain what caused this performance gap, it may not

be coincidence that the various EU procurement thresholds, above which more onerous regulations apply, were over £100k between 2008/09 and 2012/13 (replacement public contract regulations with new, higher thresholds came into force in 2015).

It would make sense that charities with a turnover higher than £100k, competing for bigger contracts which attract larger bidders and entail more complex bidding processes, would struggle more than smaller charities bidding only for smaller, potentially less competitive contracts. Indeed, of all three middle bands it was the highest (£500k–£1m) and most likely to bid for above threshold contracts which saw the biggest drop in government contract income. Perhaps commissioners feel able to adopt more flexible procurement approaches below

EU threshold which favour smaller, local charities for specialist services.

There may also have been a process of substitution in action. For while the £25k–£100k band saw the best contract performance, it also experienced the biggest drop in government grant income: almost two-thirds. It is possible that, in addition to grant cuts, some public bodies chose to refund voluntary organisations that had previously been funded through grants via contracts instead. It is notable that whilst the voluntary sector as a whole lost 63% of its government grants (£6bn down to £2.2bn) between 2002/03 and 2012/13, charities in the £25k–£100k band lost 1% more in less than half the time.

THE INCREASE IN GOVERNMENT CONTRACTS FOR THE £25K–£100K INCOME BAND IS STRIKING. ALTHOUGH INCOME FROM THIS SOURCE IS BELOW THE PEAK ACHIEVED IN 2010/11, THE FINANCIAL YEAR BEFORE THE COALITION’S SPENDING REVIEW CAME INTO EFFECT, BY 2012/13 IT WAS STILL 9% ABOVE THE 2008/09 LEVEL.

4.3

CHANGES IN INCOME SOURCES ACROSS INCOME BAND

SMALLER CHARITIES LOST MORE INCOME FROM GOVERNMENT AND GAINED LESS INCOME FROM INDIVIDUALS THAN LARGER CHARITIES.

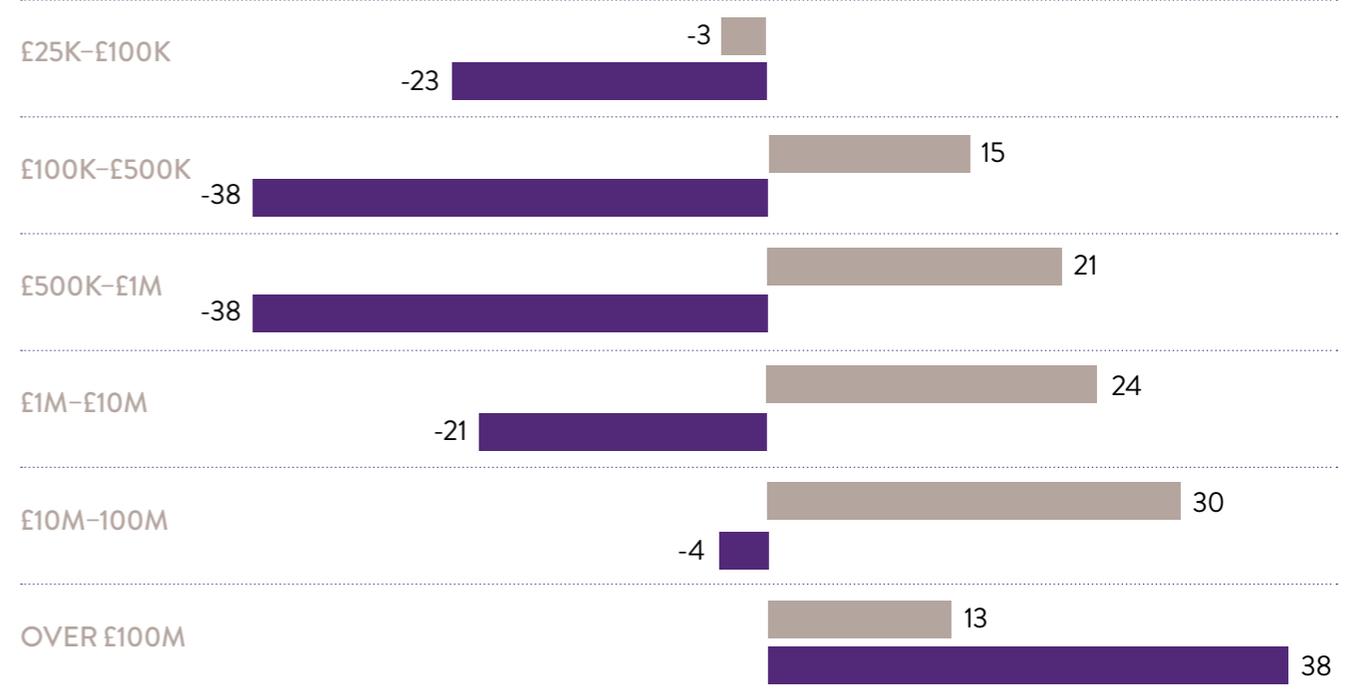
GOVERNMENT AND INDIVIDUAL INCOME

Most income bands lost government income and increased their income from individuals between 2008/09 and 2012/13. However, both these trends appeared to be compounded by size: the smaller the organisation, the greater the proportional loss of income from government, and the

larger the organisation the greater the increase in income from individuals. The exceptions were the smallest income band (£25k–£100k), which decreased both government and individual income sources, and the largest income band (over £100m) which increased both government and individual income sources.

However, the absolute numbers also show that increases in individual income did not sufficiently compensate losses of government income for the three middle-income bands (£25k–£1m), which all suffered an overall loss in income. By contrast, the shortfall was met for all three larger income bands (£1m–£100m), with the largest actually increasing both sources of income.

Figure 12. Change in income from government and individuals, 2008/09 to 2012/13 (% change)



GOVERNMENT GRANTS AND CONTRACTS

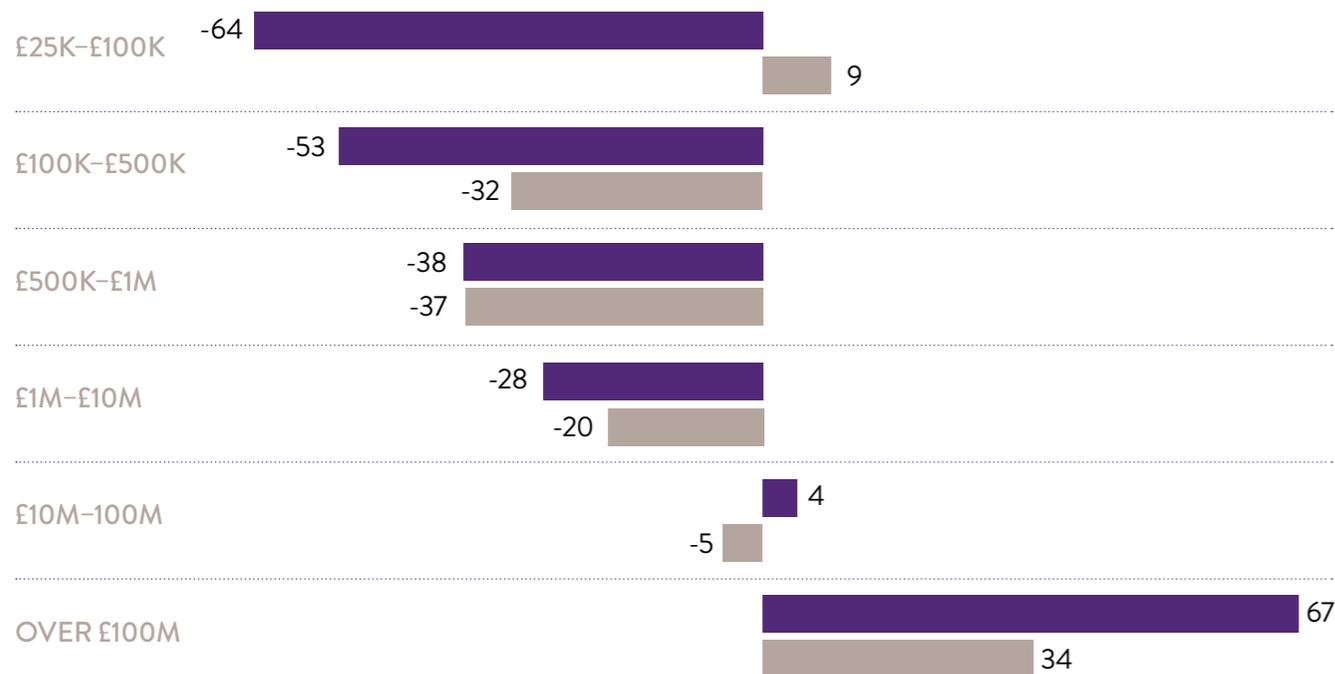
All income bands received more government money via contracts than grants, on average by a factor of 5:1. However, the three middle-income bands (£25k-£1m) relied slightly more on government grants than the three upper income bands (£1m-over £100m); they constituted around 25% and 15% of total government income respectively.

Between 2008/09 and 2012/13, the middle-income bands generally lost a higher proportion of income from both grants and contracts than charities over £1m. The only exception was the £25k-£100k income band that surprisingly increased its income from government contracts by around 9%. This rise came from central rather than local government contracts.

BETWEEN 2008/09 AND 2012/13, THE THREE MIDDLE-INCOME BANDS LOST A HIGHER PROPORTION OF INCOME FROM GOVERNMENT GRANTS THAN THE UPPER THREE INCOME BANDS.



Figure 13. Change in income from government grants and contracts, 2008/09 to 2012/13 (% change)



■ Grants
■ Contracts



MANY

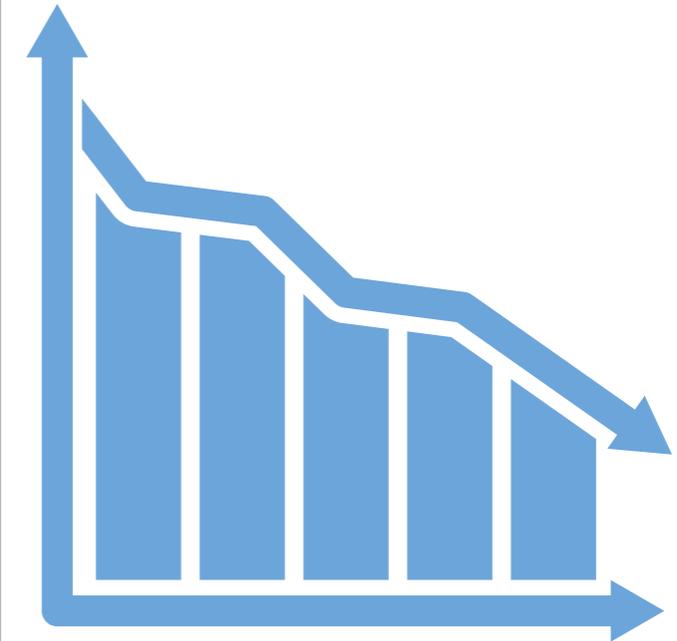
CHARITIES EXPERIENCED LARGE FALLS IN INCOME DIRECTLY AS A RESULT OF THE LOSS OF GOVERNMENT GRANTS.



BEHIND THE DATA: LOSS OF GOVERNMENT GRANTS

Many middle-income charities experienced large falls in income directly as a result of the loss of government grants, highlighting their importance as an income source for small and medium-sized charities. In an extreme case for one charity tackling poverty in the north-west of England, its annual income from government grants nearly halved between 2012 and 2013 from over £650,000 (three quarters of its total income) to £350,000 and then again in the

subsequent year to £140,000. It also noted that as a consequence it ended the financial year 'with a substantially reduced level of reserves'. Another charity championing race equality in the north-east of England described the 'funding cliff edge' that it was approaching as a number of its area-based grants that funded 'all of its project activities' came to an end, resulting directly in staff redundancies and an end to many services. Such has been the uncertainty of government grant provision that one charity working with families in London notably commented that it was 'fortunate not to depend on statutory grants'.

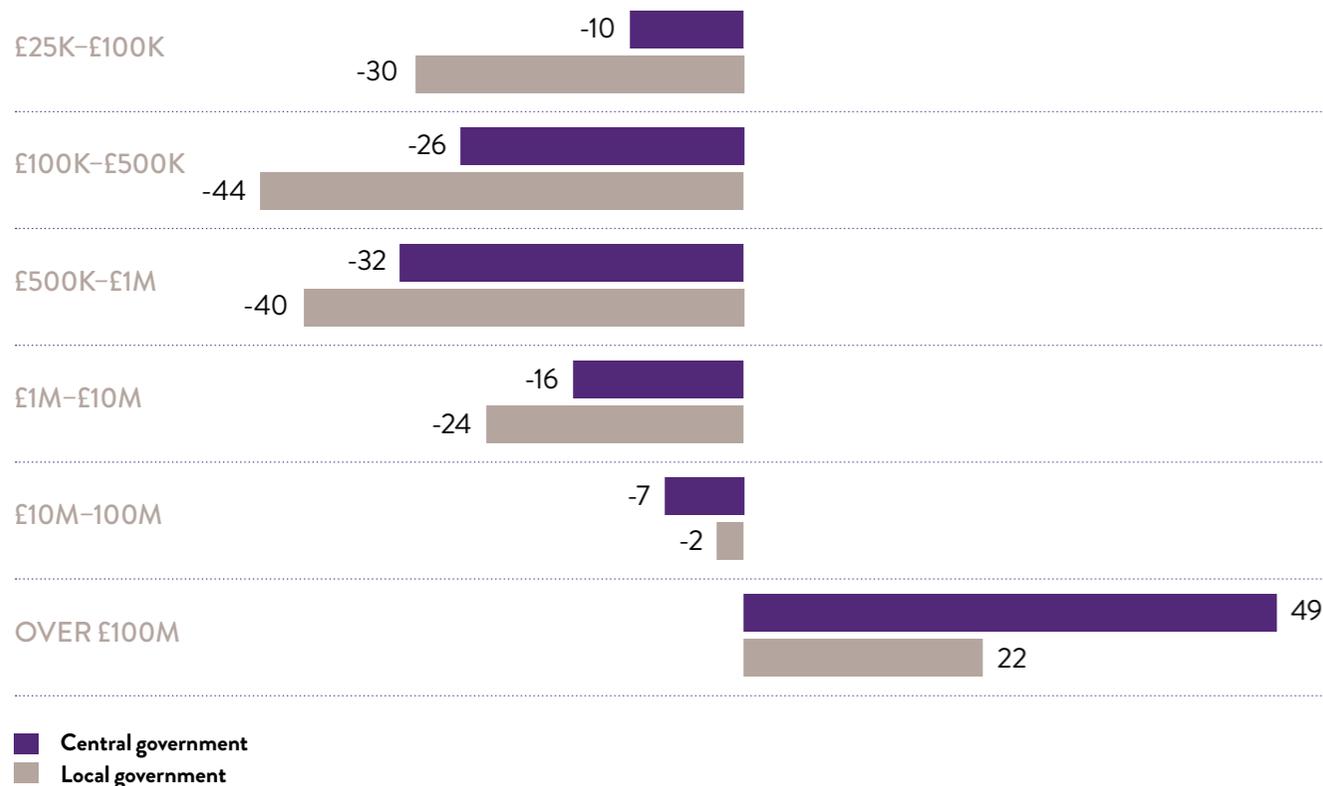


LOCAL AND CENTRAL GOVERNMENT INCOME

The voluntary sector received on average £1bn more income from local than central government every year. Again, in general the smaller the income band the more they lost in income from both local and central government. All three middle-income bands (£25k-£1m) experienced the biggest losses of local government funding.

BETWEEN 2008/09 AND 2012/13 CENTRAL AND LOCAL GOVERNMENT INCOME DECREASED FOR ALL INCOME BANDS EXCEPT THE LARGEST (OVER £100M), WHICH INCREASED BY 49% AND 22% RESPECTIVELY.

Figure 14. Change in income from central and local government, 2008/09 to 2012/13 (% change)



INCOME FROM INDIVIDUALS

In terms of voluntary income, most income bands received around 40% of their funding from donations. Legacies made up an increasingly higher proportion of income with increasing income band size. A higher proportion of earned income was raised through charitable trading than through fundraising trading, except for the largest income band (over £100m), for which this pattern was reversed.

Whilst voluntary income remained broadly stable between 2008/09 and 2012/13, all income bands increased their earned income over this time. However, in general the greater rise was from fundraising trading more than charitable trading. This means that charities have increasingly been generating income from trading that is unrelated to their core charitable activities. The only exception here was the largest income band (over £100m) which managed to earn more through trading related to its core charitable activities.

THE RISE IN EARNED INCOME WAS A RESULT OF AN INCREASE IN BOTH CHARITABLE TRADING AND FUNDRAISING TRADING BETWEEN 2008/09 AND 2012/13 FOR ALL INCOME BANDS.



Figure 15. Average proportion of income from different sources of individual income, 2008/09 to 2012/13 (%)

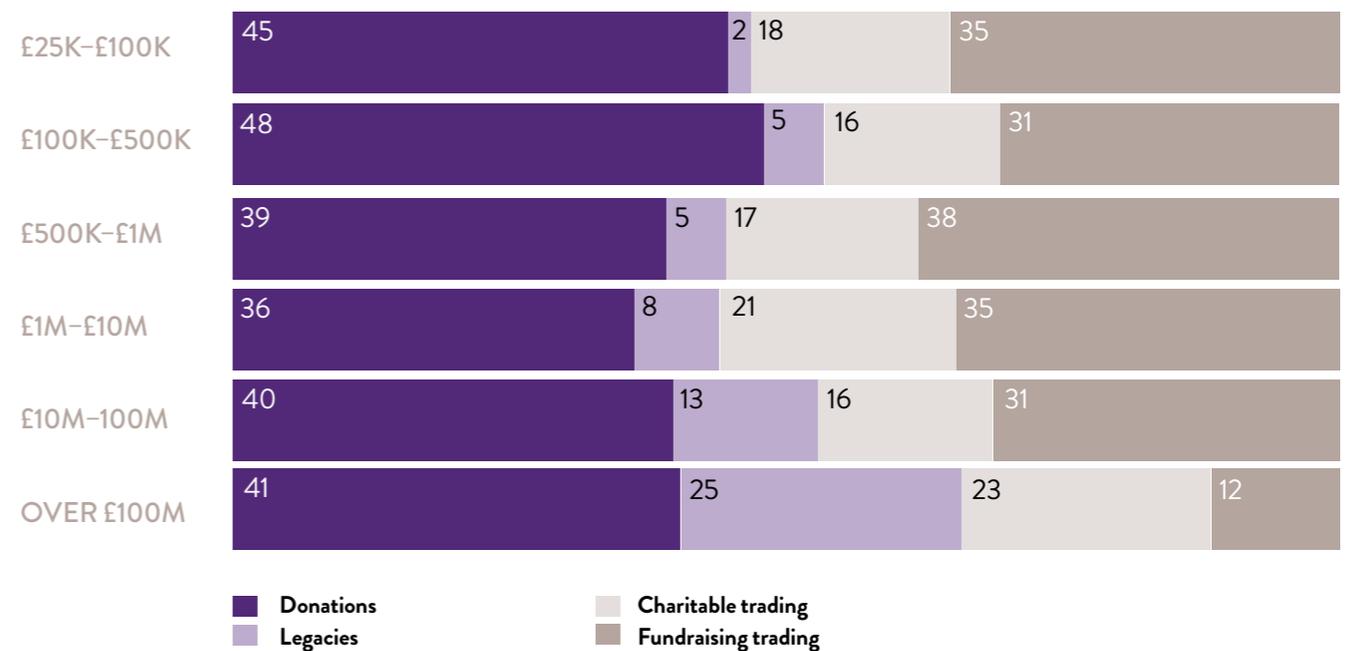
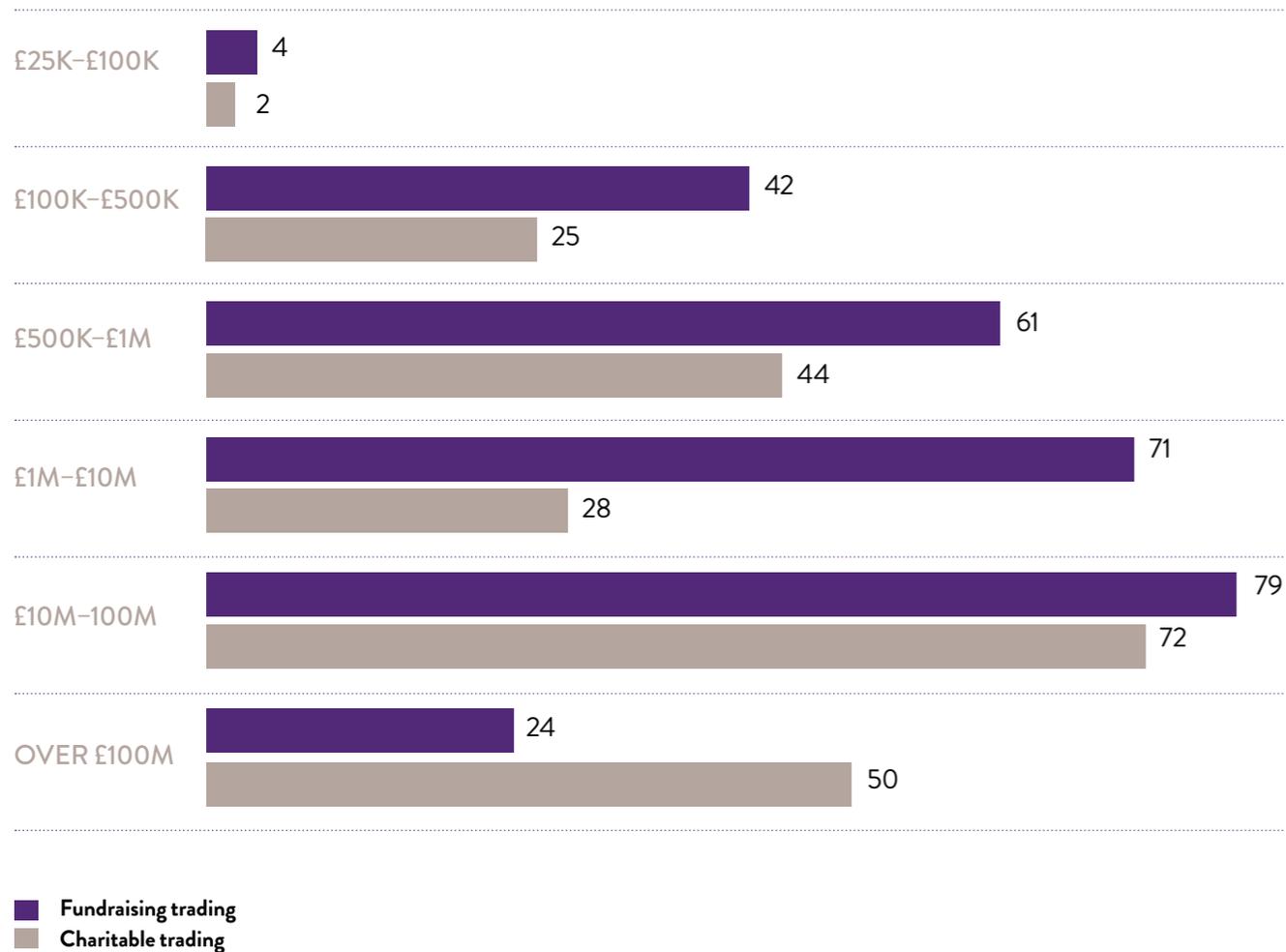


Figure 16. Change in earned income from fundraising trading and charitable trading, 2008/09 to 2012/13 (% change)



INCOME BY SOURCE: POLICY COMMENTARY

Only the over £100m band received more income from government in 2012/13 than 2008/09: the value of statutory grants and contracts increasing by 38%. It is likely that the continued aggregation of services into a smaller number of large contracts is a major contributing factor to the strong growth in contract income for these charities. This transition can be seen as an understandable response by public authorities to reduced funding and headcounts in commissioning and procurement teams, and a desire to cut the transaction costs of contracting. However, the risk is that the expertise of smaller, specialist organisations is lost as they find themselves unable to even bid to deliver services. This could be further exacerbated by devolution deals for combined authorities. Many will seek to aggregate contracts for an even larger geographical area unless central government requires meaningful onward devolution to communities.

This over £100m band is an outlier in more ways than one. Whilst in general the larger income bands saw the greatest overall increase in income from individuals, the very largest charities bucked this trend, with only the £25k-£100k band performing worse.

Although this data predates current controversies over fundraising, it may be tempting for some to suggest that this reflects increased public weariness towards the largest charities. Yet evidence for this is thin. The public are relatively evenly split on how trusting they are of larger charities: 37% agreeing that they trust big charities more than small ones and 47% disagreeing. Far more important is name recognition, with 82% of people reporting that they trust charities more if they have heard of them.²³ Given that larger charities will in general have higher levels of name recognition it seems unlikely that this can be the principal cause for poorer individual income growth.

A more promising explanation may lie in the proportion of individual income that charities in the over £100m group receive from different sources. For all bands, earned income (fundraising and charitable trading) grew significantly more strongly than voluntary income (donations and legacies) over the period and the largest charities received a much smaller proportion of their individual income from earned sources than others. This difference is due entirely to fundraising trading: all of the income bands received over 30% of their individual income from this source apart from over £100m organisations which received only 12%.

Yet, overall, fundraising trading was the fastest growing source of individual income. Indeed, the largest charities not only received less from fundraising trading than all other income bands, but they also saw slower income growth from this source than all but the £25k-£100k band. It may be that they prioritised earning income from government rather than individuals on the basis that whilst public-service outsourcing seemed likely to expand, the recession and falling real wages made growing individual income a riskier bet.

The other outlier is the £25k-£100k band. All income bands experienced growth of at least 30% in their earned income apart from the smallest band which saw an increase just one-tenth as big. This could be a case of smaller charities not having the skills or resources to invest in income generation. Given that this band also saw the biggest drop in voluntary income, there may be a more general trend of individual income concentrating amongst larger charities.

References :

23. Ipsos MORI (2012) *Public Trust and Confidence in Charities*. London: Ipsos MORI.



BENEATH THE DATA: INCREASING INCOME FROM INDIVIDUALS

The pressure to substitute losses of government income with increased voluntary and earned income from individuals was apparent for many charities. One charity supporting older people in the south-east of England commented that ‘trustees [felt] sure that the increased costs could be met with more aggressive fundraising’. Although voluntary

income remained down the following year it had managed to increase its earned income. A religious charity working in the north-west of England noted the increased importance of its supporters from which it ‘saw a significant rise in both individual and group donations’ that enabled it to carry out further work. For one charity that works with visually impaired people in the East Midlands, legacy donations became one of its main sources of fundraising, providing up to £200,000 in one year. In light of this, it took the initiative to open up a free will-writing

service in conjunction with a solicitors’ firm service which generated over 50 new wills.



- The next two sections examine
- breakdowns of key income sources by
- region and activity in order to identify
- any notable geographical or sector
- specific trends. Income in these sections
- represents an aggregate of the income
- of all middle-income charities
- (£25k-£1m) only (see Appendix
- for a more detailed description).

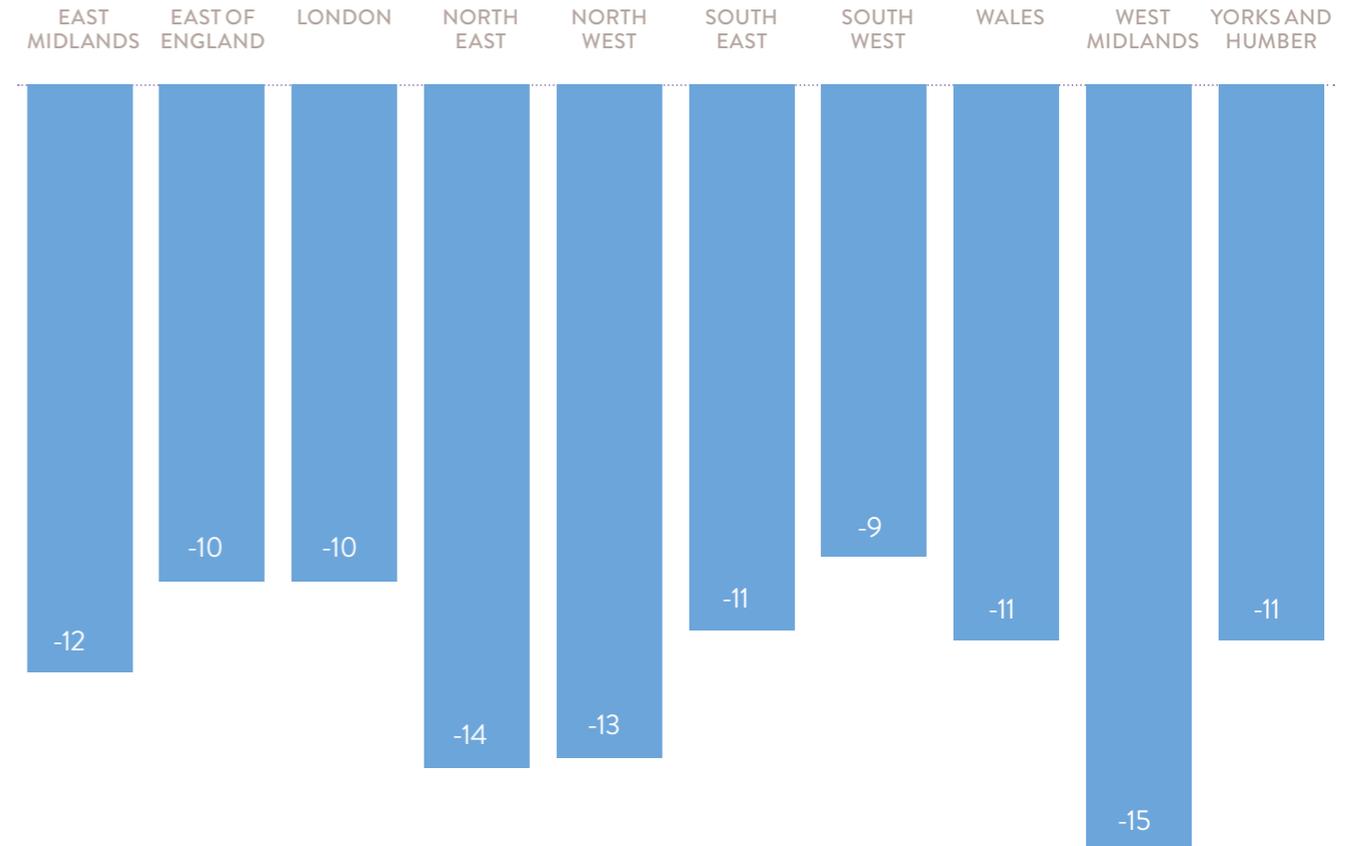
4.4

INCOME BREAKDOWN BY REGION

OVERALL INCOME DECLINED FOR MIDDLE-INCOME CHARITIES FOR EVERY REGION BETWEEN 9% AND 15%. THE WEST MIDLANDS, NORTH EAST AND NORTH WEST LOST THE HIGHEST PROPORTION OF INCOME.



Figure 17. Change in overall income by region for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)



WALES AND THE NORTH EAST SAW THE BIGGEST CUTS IN GOVERNMENT FUNDING AS WELL AS THE LARGEST INCREASES IN INCOME FROM INDIVIDUALS.

- At just over 40%, government funding made up a slightly higher proportion of income for the East Midlands, North East, North West and Wales than for other regions.
- However, the North East and Wales lost the most government funding but also increased their income from individuals more than other regions.
- Nonetheless, increases in income from individuals generally did not make up for losses of government income. Even for the North East which substantially increased its proportion of income from individuals, this still translated to a loss of over £50m in government funding and a gain of around £39m in income from individuals, leaving this region with an overall shortfall.

Figure 18. Average proportion of income from government and individuals by region for charities with an income between £25k and £1m, 2008/09 to 2012/13 (%)

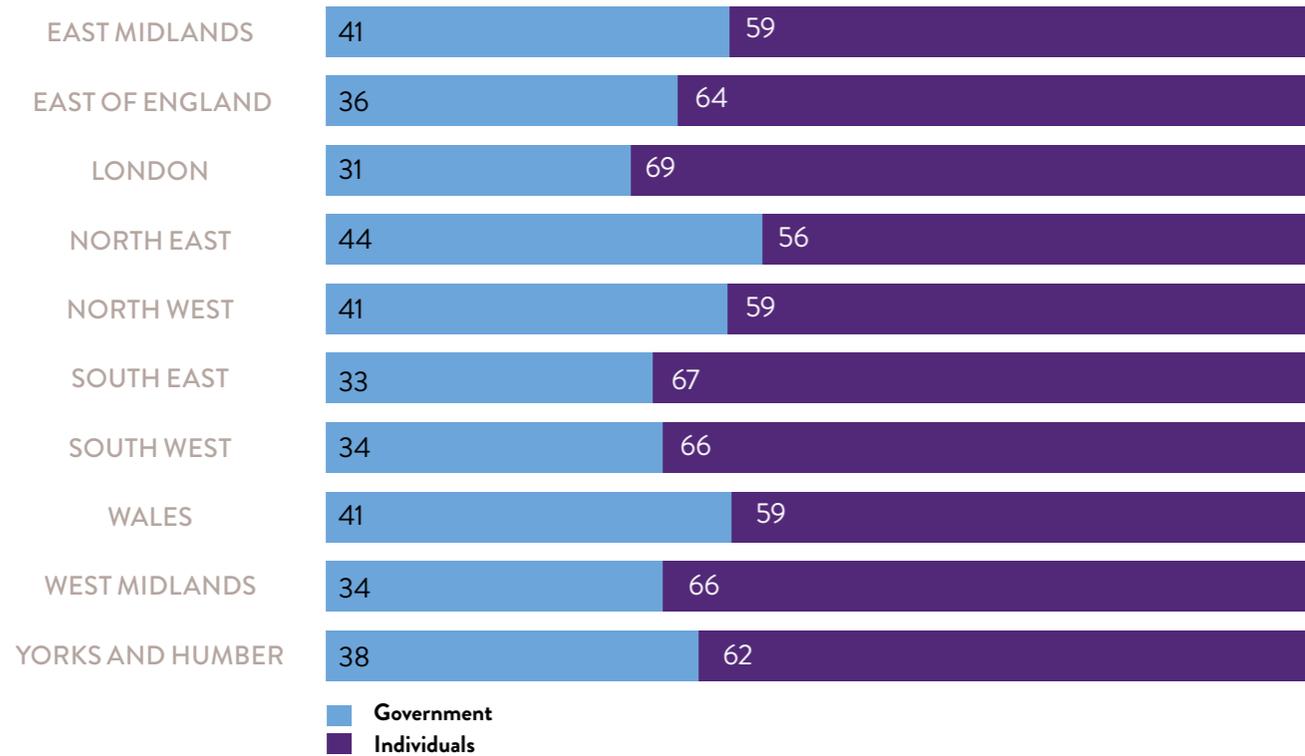
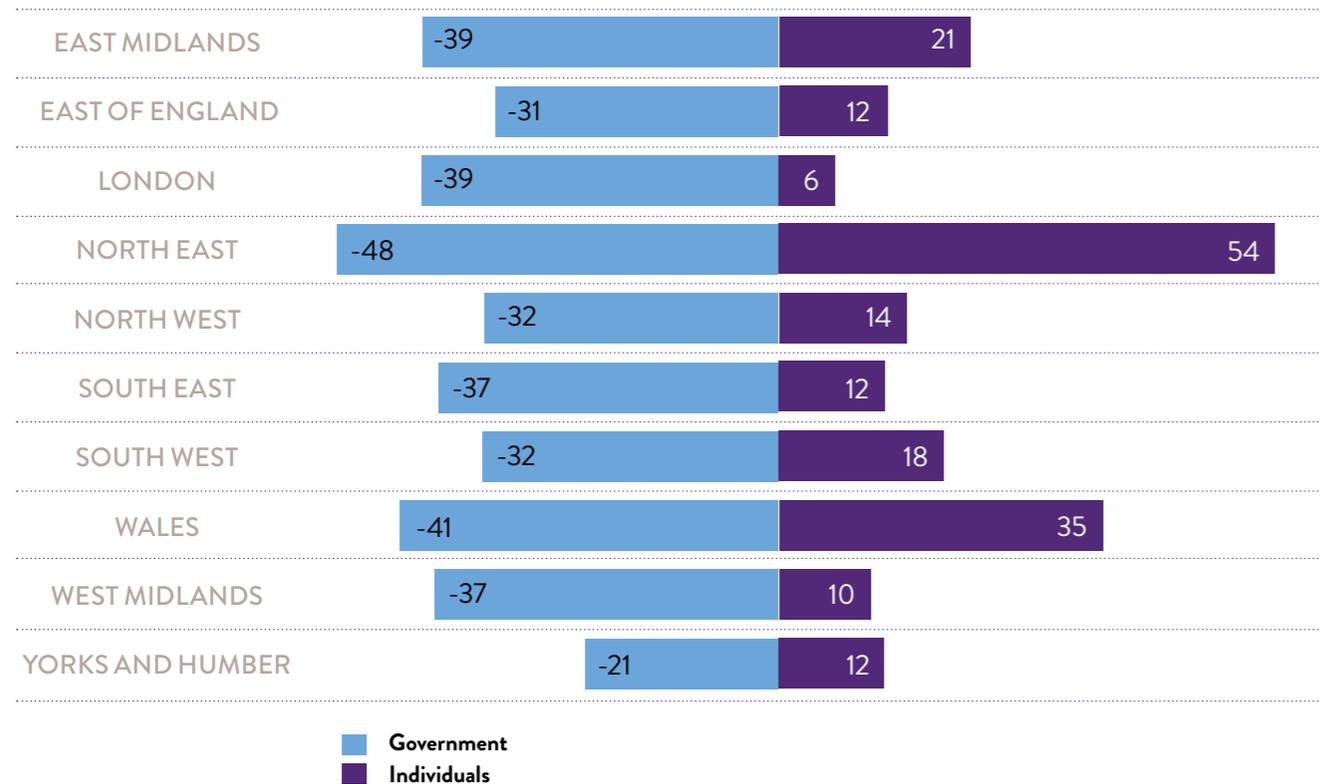


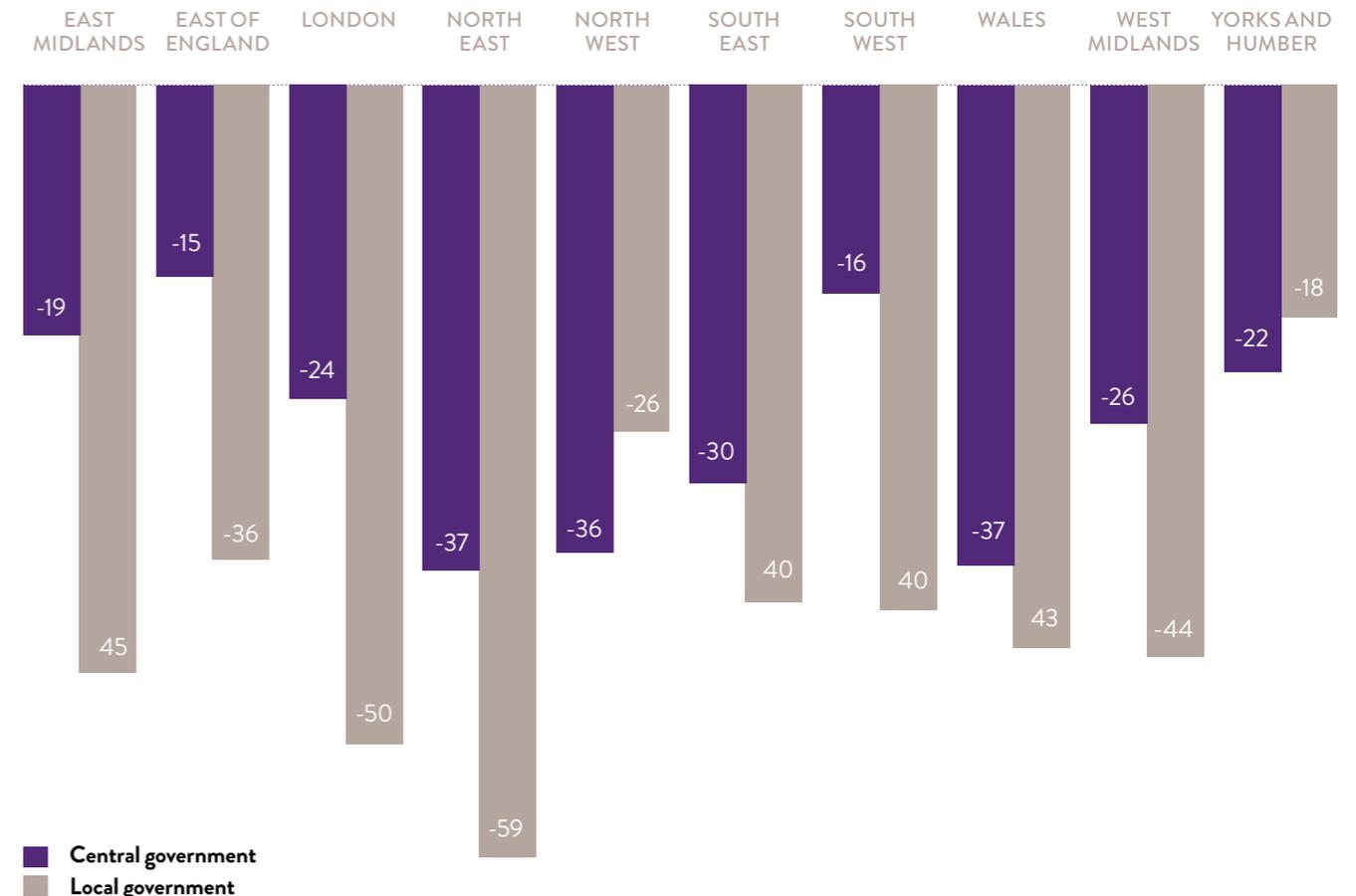
Figure 19. Change in income from government and individuals by region for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)



• All regions lost both central and local government income, but most regions lost more local than central government funding. Central government income declined in all regions, with the North East, North West, South East and Wales all experiencing particularly large losses of between 30% and 40%. Likewise, local government income declined in all regions, but the North East and London experienced the greatest losses of between 50% and 60%.

LOCAL GOVERNMENT INCOME FOR MIDDLE-INCOME CHARITIES DECLINED IN ALL REGIONS, BUT THE NORTH EAST AND LONDON EXPERIENCED THE GREATEST LOSSES OF BETWEEN 50% AND 60%.

Figure 20. Change in central and local government income by region for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)





INCOME BY REGION: POLICY COMMENTARY

There is, perhaps unsurprisingly, considerable correlation between changes in the voluntary sector's regional income - from both government and individuals - and the wider economic and public spending landscape.

The North East and London, the regions in which charities experienced the greatest loss of local government income over the period, also, according to the Institute for Fiscal Studies (IFS), saw the largest average government cuts to spending per person between 2009/10 and 2014/15. London boroughs cut spending per person on average by 31.4%, while spending per person was cut by 26.5% in the North East (compared with an average of 23.4% across England).²⁴

With regard to funding mix, there is notable variation between regions. Whilst charities in London get just 31% of their income from government, in Wales the proportion is 41% and in the North East 44%. This mirrors the

regional labour markets where London has the lowest proportion of the population employed by the public-sector, Wales and the North East the highest.²⁵

Wales and the North East are outliers in a number of respects. As well as being most reliant on government income they also saw the deepest cuts in government funding and the biggest rises in individual income. Could the two be related? There is mixed evidence as to whether statutory funding 'crowds out' private giving or vice-versa. Some evidence from the UK and the USA indicates that this is not the case and that the reverse may actually be true ie that government funding acts as a signal to the public about the quality of an organisation, crowding in private donations.^{26,27} By contrast, research from Canada has found that where government funding increases, private donations decrease. However, this is attributed to charity behaviour ie a decrease in fundraising efforts, rather than donor behaviour.²⁸ In this instance, the significant increases in individual income in Wales and North East may instead be more easily explained by

the fact that between 2011 and 2013 these regions also saw the largest year-on-year growth in gross disposable household incomes.²⁹

References :

- 24. Innes D. and Tetlow G. (2015) *Central Cuts, Local Decision-Making: Changes in local government spending and revenues in England, 2009-10 to 2014-15*. London: Institute for Fiscal Studies.
- 25. Office for National Statistics (2015) *Public Sector Employment, Q1 2015*. Newport: Office for National Statistics.
- 26. Andreoni J., Payne A. and Smith S. (2013) *Do Grants to Charities Crowd Out Other Income? Evidence from the UK*. Bristol: Centre for Market and Public Organisation.
- 27. Heutel G. (2009) *Crowding Out and Crowding in of Private Donations and Government Grants*. Cambridge, MA: National Bureau of Economic Research.
- 28. Payne A. and Andreoni J. (no date) *Government Funding and Private Charitable Donations: The Canadian experience*. Bristol: Research in Public Policy Centre for Market and Public Organisation.
- 29. Office for National Statistics (2015) *Regional Gross Disposable Household Income (GDHI), 1997 to 2013*. Newport: Office for National Statistics.

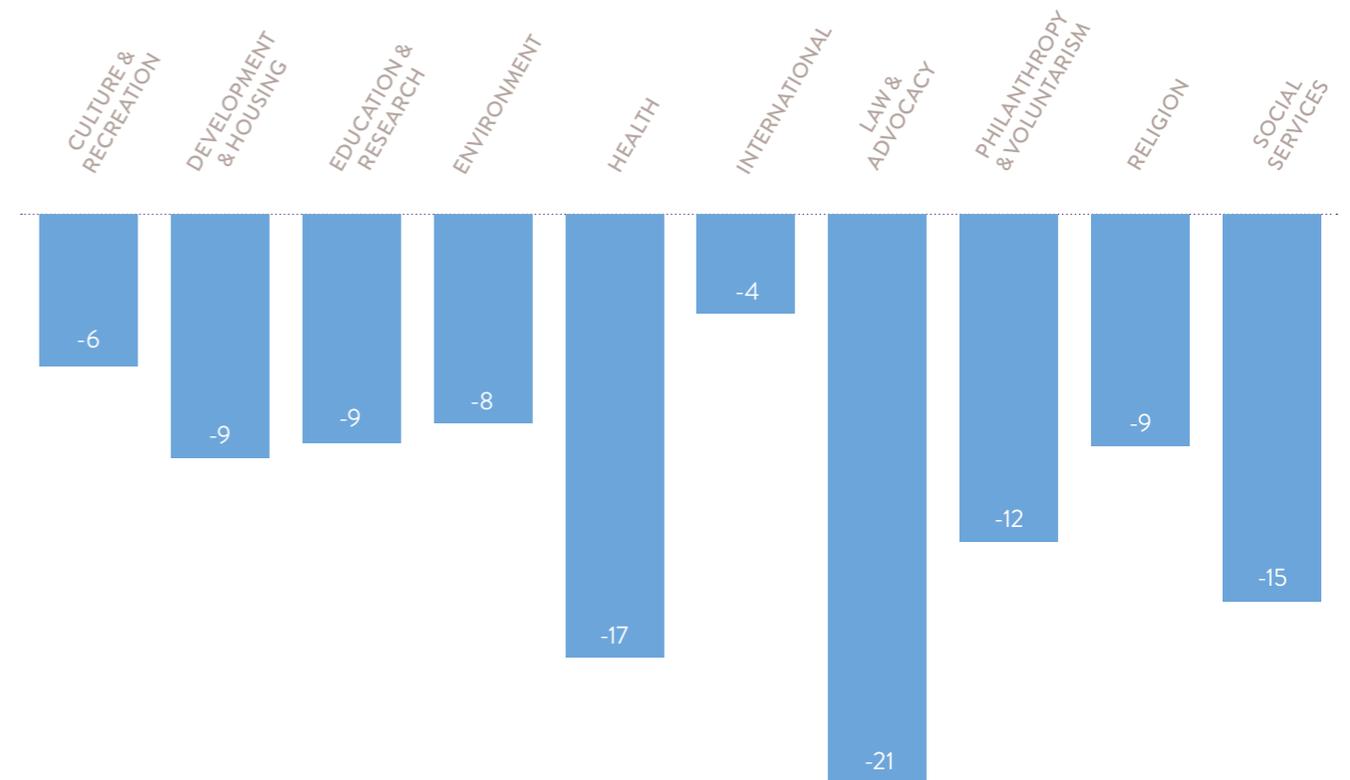
4.5

INCOME BREAKDOWN BY ACTIVITY

Losses in income were not shared equally between sectors. The sectors of small and medium-sized charities that lost the most income were arguably those most likely to be involved in the delivery of public services, namely health, social services and law and advocacy. Notably, income from government made up a higher proportion of income for these sectors, along with development and housing, than any other sector.

OVERALL INCOME DECLINED FOR EVERY SECTOR, WITH LEGAL SERVICES, HEALTH AND SOCIAL SERVICES SEEING PARTICULARLY LARGE DECREASES.

Figure 21. Change in overall income by activity type for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)



LONDON BOROUGHS CUT SPENDING PER PERSON ON AVERAGE BY 31.4%, WHILE SPENDING PER PERSON WAS CUT BY 26.5% IN THE NORTH EAST.



Figure 22. Average proportion of income from government and individuals by activity type for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)

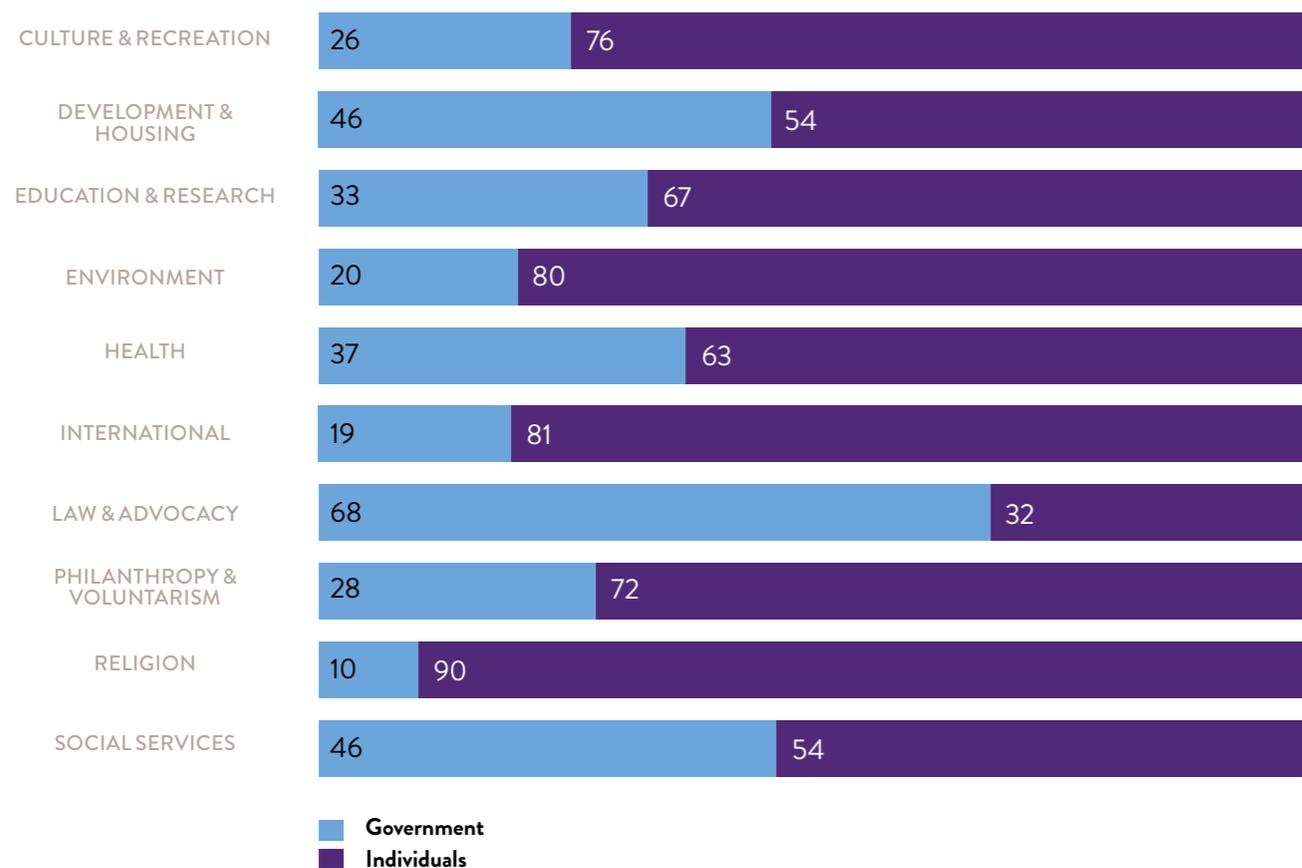
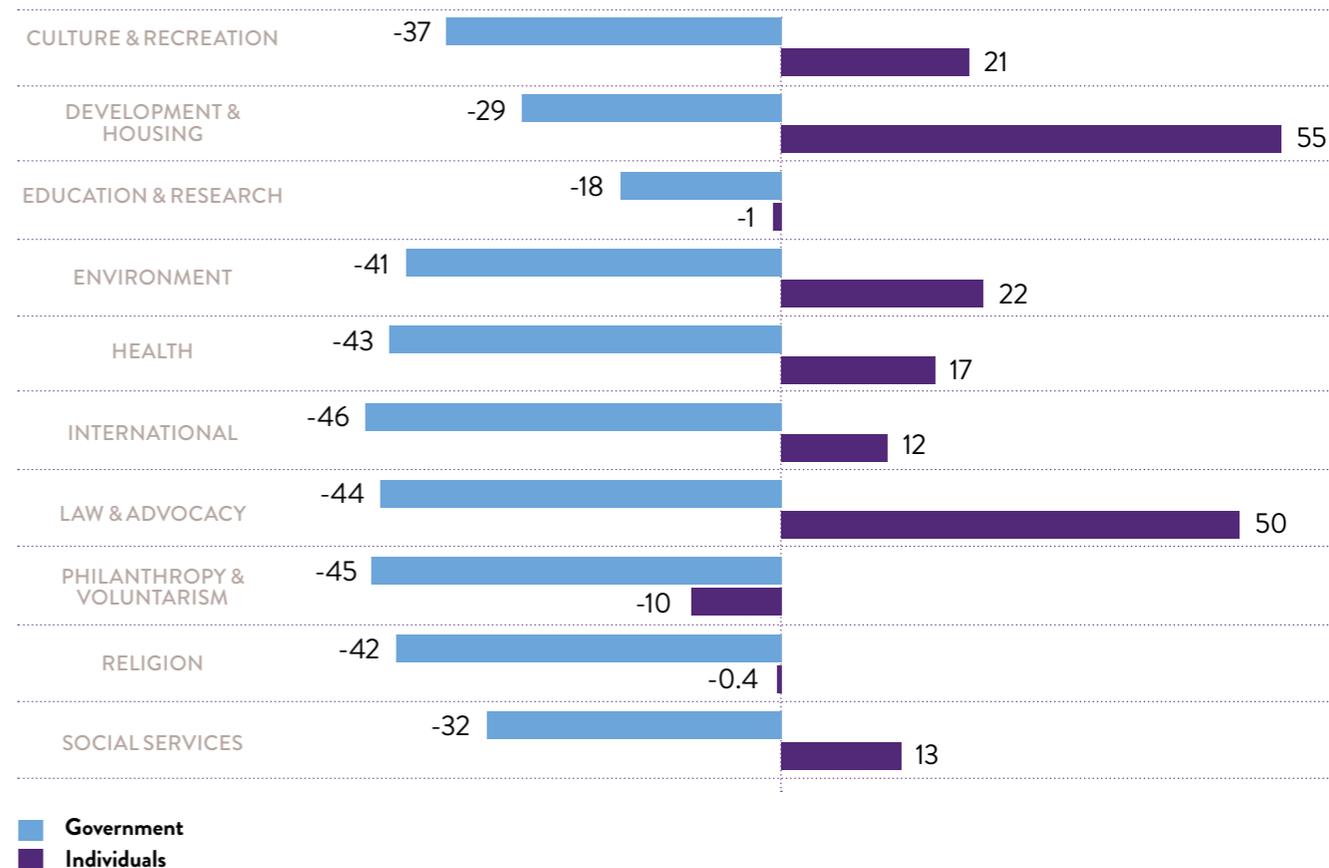


Figure 23. Change in income from government and individuals by activity type for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)



INCOME BY ACTIVITY: POLICY COMMENTARY

The three sectors with the biggest overall income falls – law and advocacy (21%), health (17%) and social services (15%) – are all areas in which the voluntary sector plays a vital role in the delivery of public services. But why should this be the case?

Each of these sectors saw significant cuts in statutory funding but this should not be put down solely to overall reductions in government public service spending, at least for health and social services. Spending by local authorities, for example, on children’s and adults’ social care has been ‘relatively protected’,³⁰ largely due to the fact that public bodies have statutory

duties that must be met in relation to these services. Meanwhile, government health spending actually increased every year between 2008/09 and 2012/13.³¹

It is, however, more likely that public service cuts are a major contributing factor to the one fifth drop in funding for law and advocacy organisations. It is difficult to get a picture for changes in overall government spending on law and advocacy as there is no single public body with responsibility for these services. This may be part of the problem. Usually seen as preventative services, spending on them is typically discretionary and therefore without the protection afforded to social care and health services.

A more important reason for the fall in government income for these sectors is

the changing public service market place. Overly burdensome bidding and reporting requirements, short timescales and the trend towards a smaller number of large contracts is benefiting larger providers at the expense of small, specialist organisations. As a result, while law and advocacy charities of all sizes lost 18% of their statutory income between 2008/09 and 2012/13, those with a turnover between £25k and £1m lost 44%. Similarly, voluntary organisations providing social services lost 11% of their government funding over this period but medium-sized organisations lost 32%. Health charities actually increased their statutory income by 5%, yet those in the £25k to £1m bracket lost 43%.³²

A final factor is that law and advocacy, health and social services are three of the four sectors most reliant on government funding. As a result, despite each increasing their individual income (law and advocacy by an impressive 50%), this was not enough to offset losses in statutory funding.

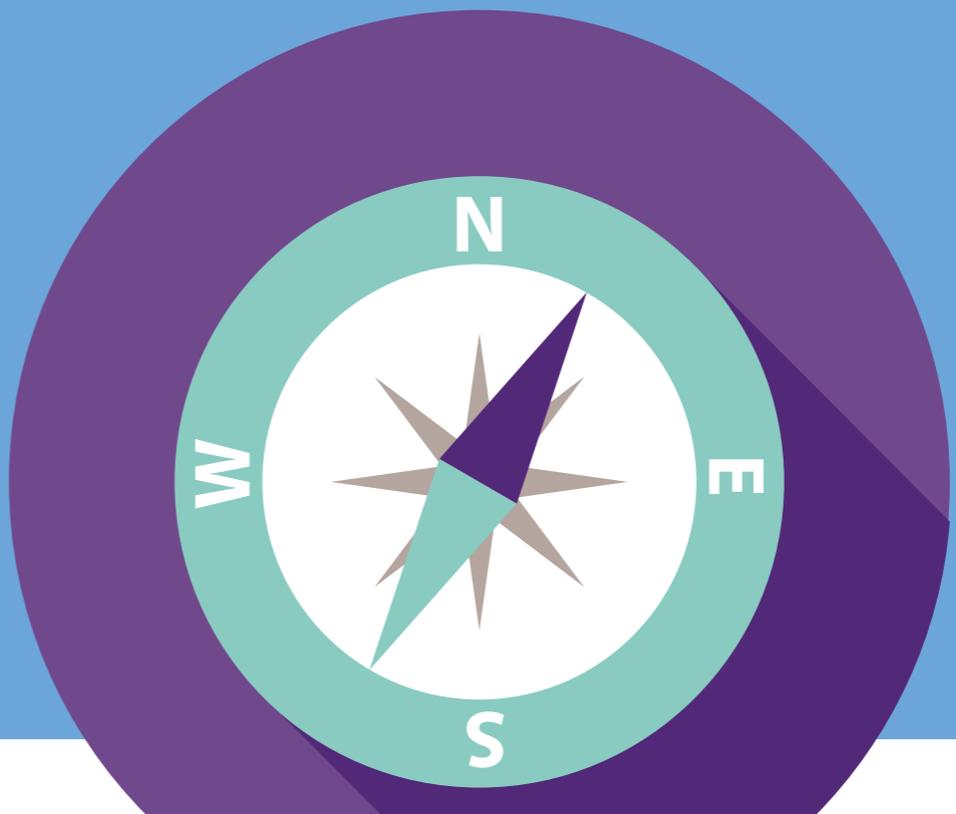
Development and housing, and law and advocacy charities saw the greatest increase in income from individuals between 2008/09 and 2012/13. Education and research, philanthropic and religious charities all experienced a small loss of income from individuals. All sectors experienced loss of government income, mostly around 40%, with education and research experiencing the smallest cuts of 18%.

References :

- 30. National Audit Office (2014) *The Impact of Funding Reductions on Local Authorities*. London: National Audit Office.
- 31. Lewis J. and Cooper J. (2015) *Expenditure on Healthcare in the UK, 2013*. Newport: Office for National Statistics.
- 32. NCVO ‘UK Civil Society Almanac 2015: Income from government’. data.ncvo.org.uk/almanac15/government (accessed January 2016)

5

AGGREGATE FINANCIAL DATA SPENDING



The following chapter focuses on detailed breakdowns of spending for the voluntary sector based on the UK Civil Society Almanac methodology (see Appendix). As with income, data are presented for middle (£25k–£1m) and upper (£1m–over £100m) income bands only.

Changes in types of income are not the only source of evidence for understanding a shifting financial landscape. Changes in spending are also a useful reflection of ways that voluntary organisations are coping with or adapting to changing circumstances. For example, an increase in the amount that organisations spend on generating income may reflect an increasingly challenging funding environment. Spending can also be a useful way for understanding how organisations compensate for losses in income, for example through mergers, redundancies and efficiency savings.

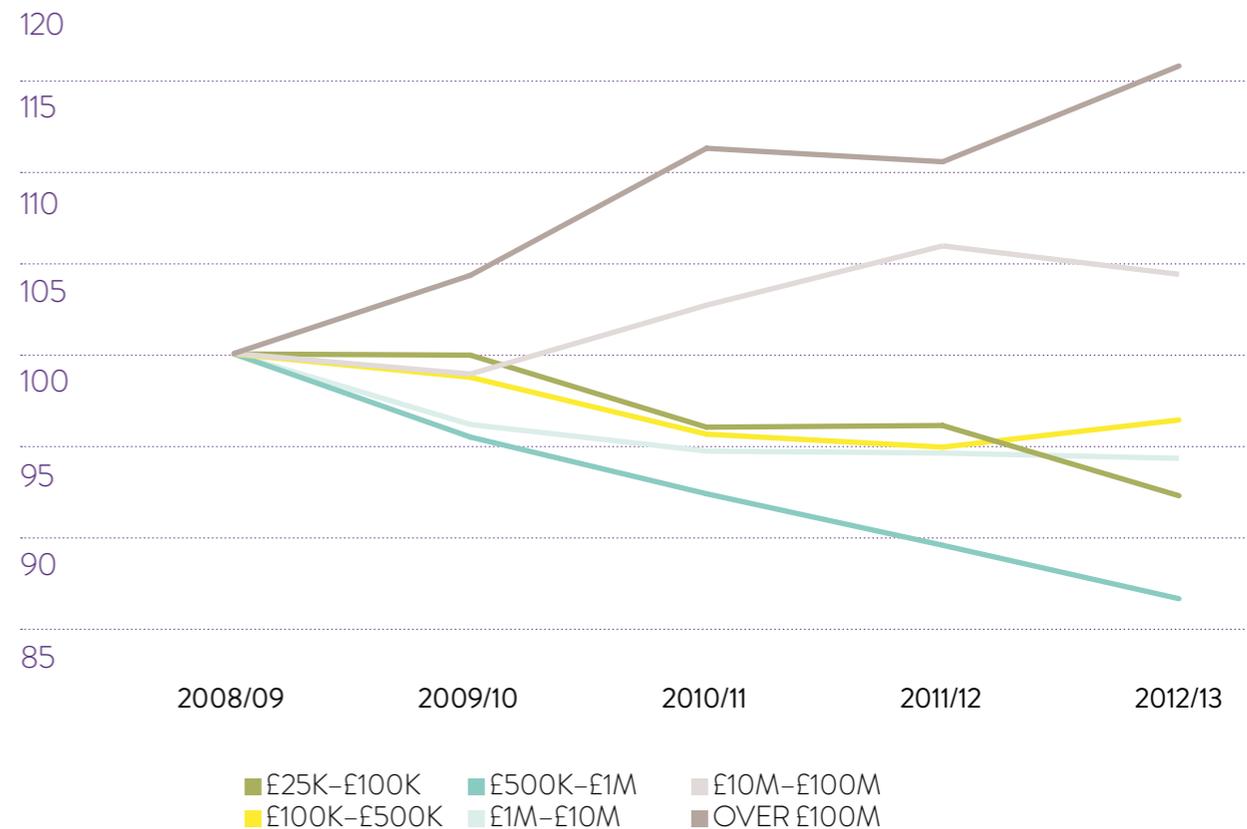
5.1

OVERALL SPENDING

ALL THREE MIDDLE-INCOME BANDS DECREASED THEIR SPENDING IN REAL TERMS BETWEEN 2008/09 AND 2012/13.

In parallel to decreases in income, all income bands decreased their spending except for the two largest income bands (£10m–£100m and over £100m). This is most probably directly related to losses in overall income.

Figure 24. Overall spending by income band (as defined at 2008/09), cumulative change, 2008/09 to 2012/13 (2008/09 = 100)



TYPES OF VOLUNTARY SECTOR SPENDING

Charities Statement of Recommended Practice (SORP 2015)³³ requires organisations with an income over £100,000 to report their spending using activity-based costing and accrual accounting. The SORP requires spending to be assigned to one of three categories, the totals of which includes all costs related to the activity, including staff costs, and management and administration.

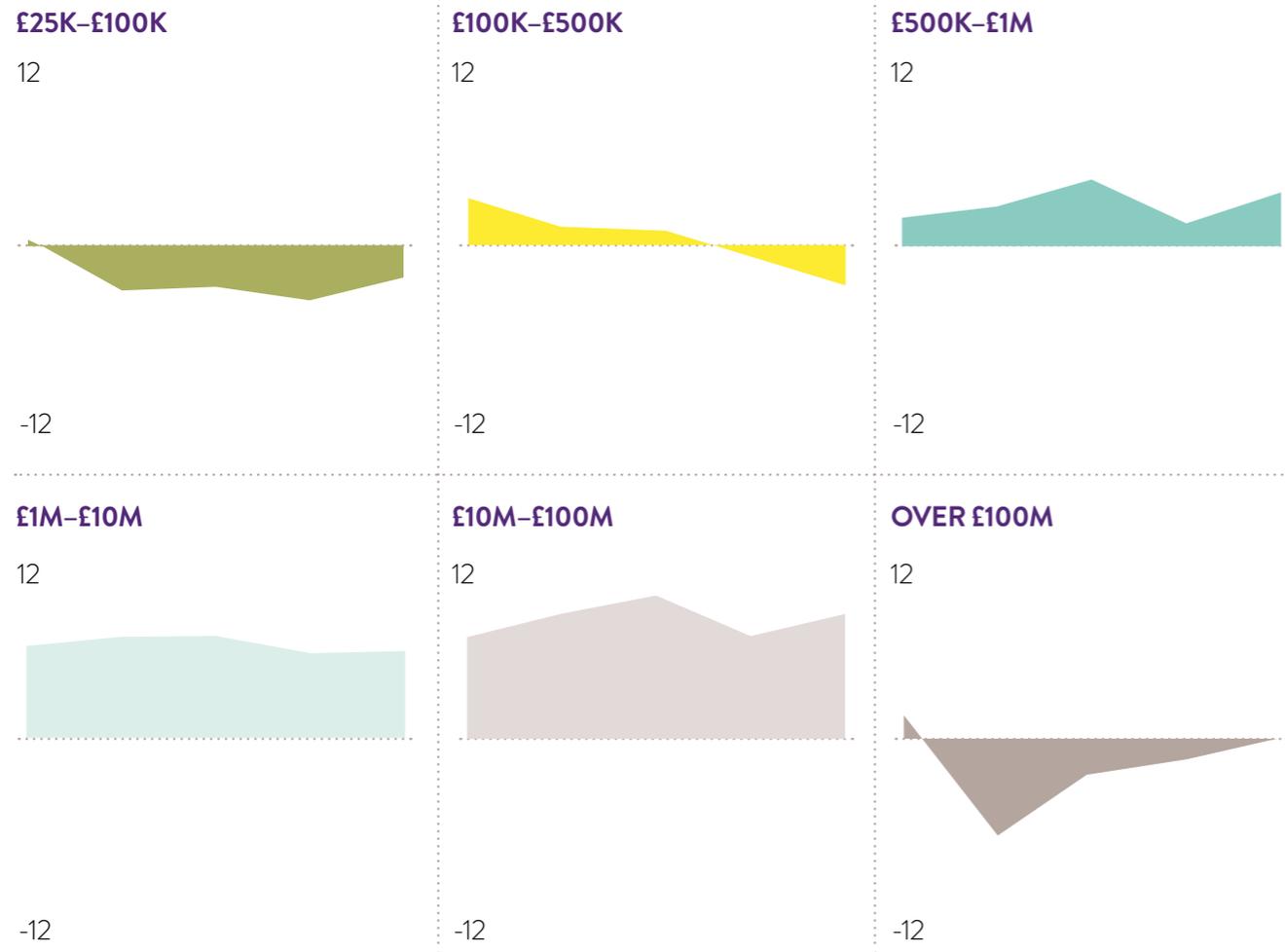
- **Charitable activities:** this includes money spent delivering the work that the organisation was set up to do, as well as grants made.
- **Generating income:** this includes fundraising and publicity, generating voluntary income and investment management costs.

• **Governance:** defining governance costs is challenging, as it is often not obvious what should or should not be included. As charities with an income under £100,000 are not bound by the SORP standard, they choose their own reporting categories and so are less easily comparable with larger charities; for example, smaller charities tend to assign more spending to governance costs so there appears to be less spending on charitable activities. For this reason, governance costs are not reported here.

References:

33. NCVO 'UK Civil Society Almanac 2015: Income from government'. data.ncvo.org.uk/a/almanac15/spending-2

Figure 25. Annual surplus or deficit as a proportion of annual income for each income band, 2008/09 to 2012/13 (%)



Overall, smaller organisations were more likely to run a deficit than larger organisations, which in general ran a surplus every year. The only exception was the largest income band (over £100m). This is probably due to the fact that as there are so few organisations in this band, this figure is dependent on the individual financial decisions of a small number of charities, many of which are grant-making foundations and so make large donations as part of their spending.



5.2

CHARITABLE ACTIVITIES AND GENERATING INCOME

On average, all three middle-income bands (£25k-£1m) directed the vast majority of their spending towards charitable activities (c.80-90%) compared with generating income and governance (both c.5-10%). In general, larger income bands increased their spending on charitable activities more than smaller income bands, most of which reduced their charitable spending.

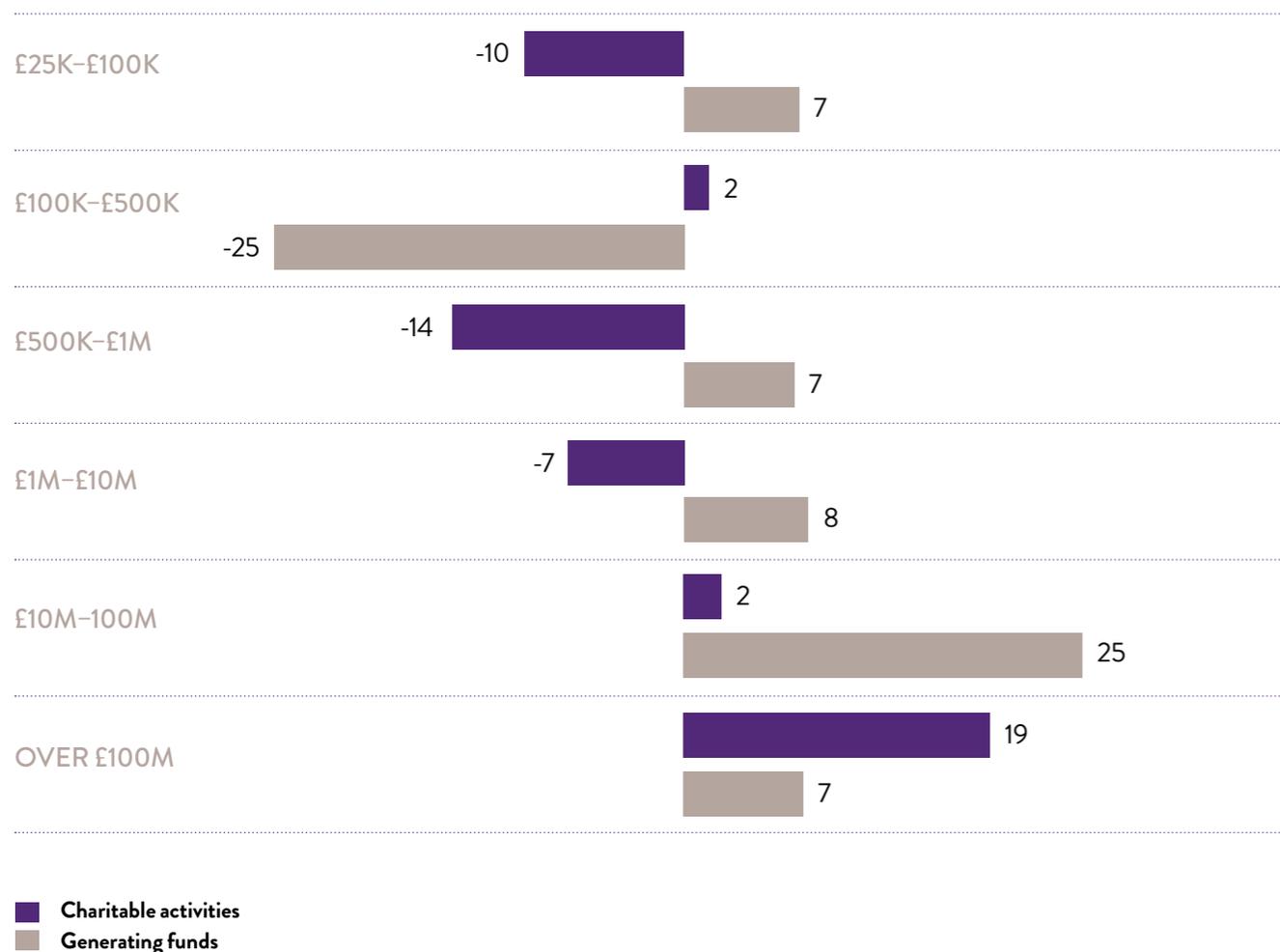
The only exception was income band £100k-£500k which increased its charitable spending by a small amount between 2008/09 and 2012/13.

Most income bands increased their spending on generating funds between 2008/09 and 2012/13, with the £1m-£10m income band increasing it by one-quarter. This is suggestive of a tougher operating

environment, where charities have had to use a greater amount of resources to generate income than before. Again, the £100k-£500k income band provided the exception, decreasing its funds for generating income by one quarter.

ALMOST ALL INCOME BANDS INCREASED THEIR SPENDING ON GENERATING INCOME. IN GENERAL CHARITIES OVER £10M ALSO INCREASED SPENDING ON CHARITABLE ACTIVITIES WHILST THOSE UNDER £10M REDUCED CHARITABLE SPENDING.

Figure 26. Change in proportion of spending on charitable activities and generating funds, 2008/09 to 2012/13 (% change)



THE £100K-£500K INCOME BAND PROVIDED THE EXCEPTION, DECREASING ITS FUNDS FOR GENERATING INCOME BY ONE QUARTER.



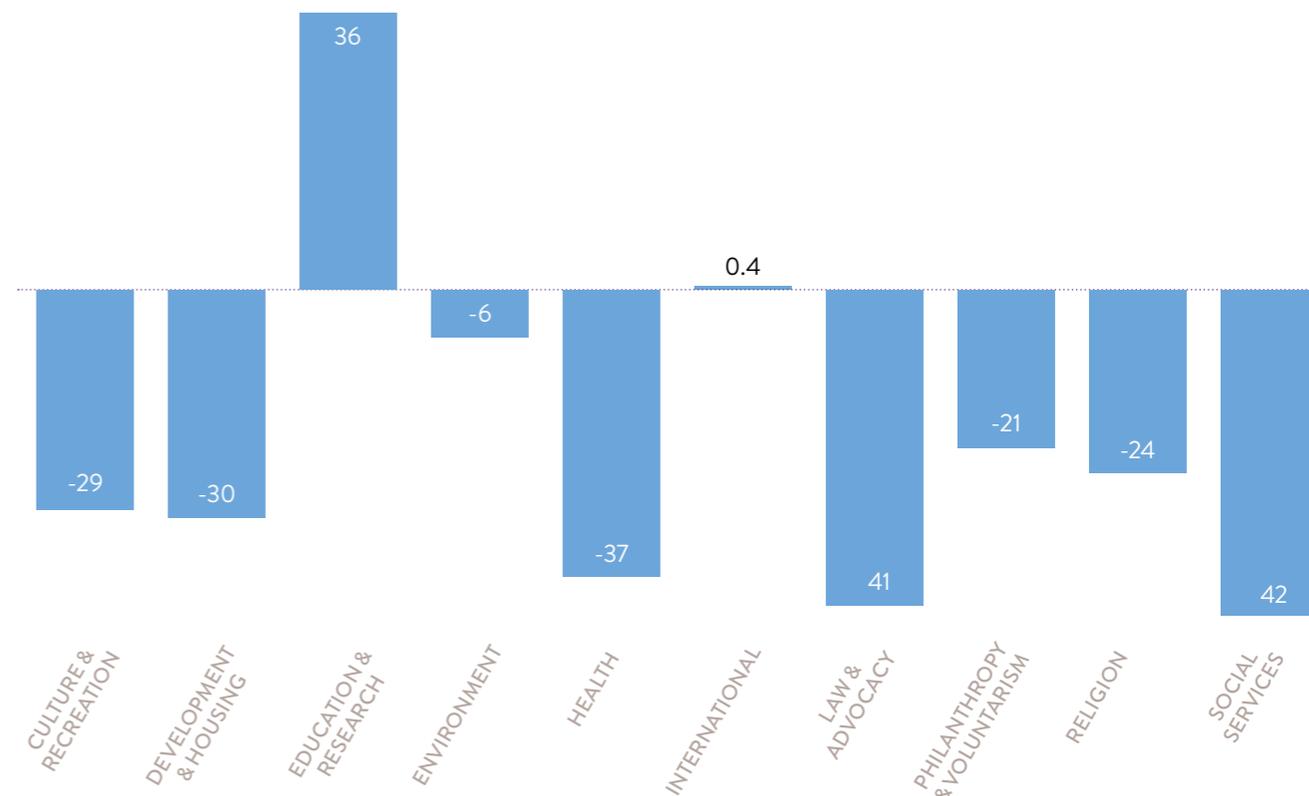
5.3

SPENDING BY ACTIVITY

Small and medium-sized charities across most sectors decreased their spending between 2008/09 and 2012/13. In line with income loss, the three sectors that decreased their spending the most were health, social services and law and advocacy. Despite a 9% loss of income education and research spending increased by 36%.

OVERALL SPENDING DECLINED FOR EVERY SECTOR EXCEPT EDUCATION AND RESEARCH; LEGAL SERVICES, SOCIAL SERVICES AND HEALTH DECREASED THEIR SPENDING THE MOST.

Figure 27. Change in overall spending by activity type for charities with income between £25k and £1m, 2008/09 to 2012/13 (% change)



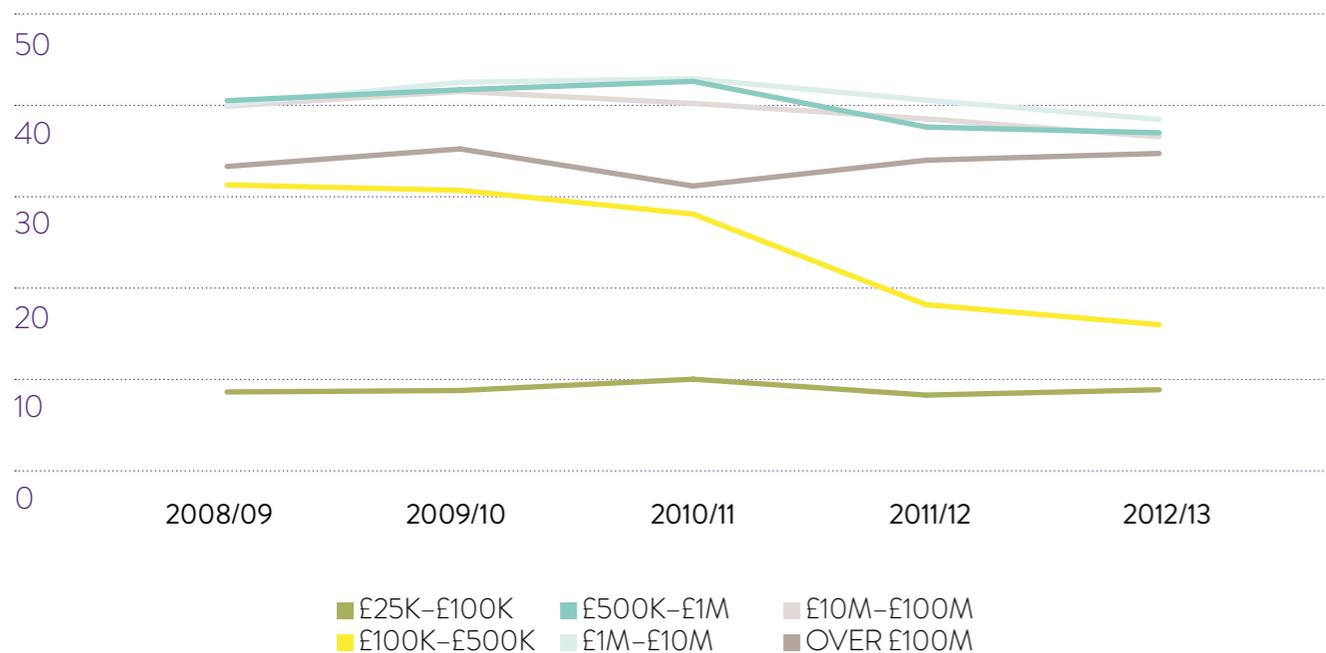
5.4

STAFF COSTS

Staff costs measure the amount spent by charities on wages and salaries, social security and pensions, spread across all three types of spending. Income bands above £100k all spent between 30% and 40% of their spending on staff costs, whilst the £25k–£100k income band only spent around 10%. Over time, spending on staff costs generally remained stable, with only small rises or falls. However, the exception was the £100k–£500k income band, for which spending on staff costs halved from 32% to 16% of overall spending.

THE £100–£500K INCOME BAND HALVED THE PROPORTION THAT IT SPENT ON STAFF BETWEEN 2008/09 AND 2012/13.

Figure 28. Proportion of spending on staff costs, 2008/09 to 2012/13 (%)



BEHIND THE DATA: IMPACTS OF SPENDING CUTS ON CHARITY SPENDING

The financial climate over the past few years has forced some charities to adapt to reduced public funding. One organisation that supports children and young people with disabilities in the East Midlands noted that ‘the well intentioned “Big Society” was meant to encourage Local Authorities to transfer some of its service delivery, and funding, to the voluntary sector who could deliver services more cost effectively. In practice service providers, like [it], have simply seen reduced funding for the services

they already provide’. As a result it had to make significant changes to its spending. It established ‘well managed cost control, against a realistic forecast’ but nonetheless had to in addition ‘implement major staff reductions [and] the remainder of [its] staff have seen no payscale increases for five years, and have, in some cases, accepted reduced working hours’. However, it noted that this has impacted service delivery due to ‘a loss of experience and expertise which will be hard to replace quickly when, or if, funding permits’. Despite this, it noted that it has ‘probably fared better than other providers’.



SPENDING: POLICY COMMENTARY

All of the bands (apart from £100k–£500k) have increased, by at least 7%, the amount that they are spending on generating funds. This is likely to reflect the increasingly tough operating environment for the voluntary sector. For both individuals and government funding there is a strong trend from voluntary to earned income. By contrast, the decrease in funds spent on generating income for the £100k–£500k income band could indicate a priority to protect spending on charitable activities, although this could have implications for the longer-term financial sustainability of such organisations.

in spending on income generation. Finally, the £25k–£100k band has run a deficit four years in a row. This helps explain why the income trajectory for smaller charities is more likely to be down than up (see chapter 3).

The biggest spending falls are in law and advocacy, social services and health. This is not entirely surprising as these sectors also saw the largest income falls, though the reductions in spending are much larger: 20 percentage points or more in each case. The apparent loss of capacity of small and medium-sized organisations in these sectors is likely to have placed additional pressure on other public services.

Success in charitable and fundraising trading has driven the growth in individual income but will generally cost more per pound earned than donations or legacies. Similarly, the transition from government grants to contracts brings with it more onerous bidding and reporting requirements. While it is in many ways positive that the sector has responded entrepreneurially to the economic downturn, seeking to earn money that was previously given, this appears to be putting upward pressure on overheads.

There has been an interesting movement in proportion of spending going on staff costs. The four income bands above £500k have gradually converged and by 2012/13 all spent between 35% and 39% on staff. The biggest movement has come in the £100k–£500k band. In 2008/09, organisations of this size spent a comparable proportion on staff to the over £100m band. By 2012/13 this had halved and is now much closer to the £25k–£100k band, which has consistently spent around 9% on staff.

The increased cost of income generation will inevitably make it harder for many organisations to stay in the black and, in general, the further down the income scale charities are, the more likely they are to run a deficit. Whilst the £1m–£10m and £10m–£100m bands have average surpluses of over 5% in every year, the £500k–£1m band has not seen a surplus of this size in any year. Meanwhile the £100k–£500k band has seen its balance worsen with each consecutive year as ongoing reductions in income have not been matched by commensurate falls in spending, despite, uniquely, a big fall

The proportion of spending that voluntary organisations devote to staff costs will reflect their operational models and this dramatic change in the £100k–£500k band suggests that charities of this size have become more reliant on voluntary action over the period. These figures indicate that there is a division between the paid employee-led organisations which dominate the higher income bands and the volunteer-led groups which populate the lower income bands. Between 2008/09 and 2012/13 this cleavage has effectively moved up the income scale.

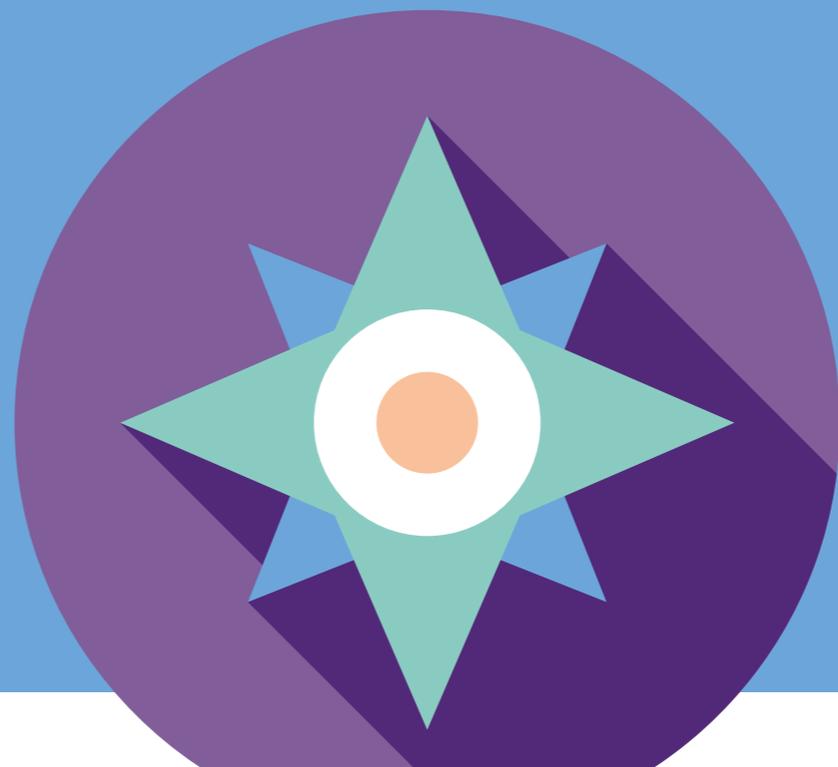
CONCLUDING REMARKS

This report explored three different approaches for understanding the financial journeys of small and medium-sized charities in England and Wales between 2008/09 and 2013/14. Two of the methodologies involved following individual organisations through time, including the development of a new typology that described income trajectories to facilitate comparison across different sized organisations. These have provided substantial new insights into the level of churn, in terms of income volatility, that voluntary organisations experience. Furthermore it has highlighted that this phenomenon is more pronounced for small and medium-sized charities with larger charities generally more resilient to external change.

There is some evidence of individual organisations weathering the storm and even thriving in the new financial landscape of reduced government funding. However, the overall picture is one in which the policy environment appears to be favouring the survival and growth of the largest organisations. These are intrinsically more stable due to their size but also have the resources to bid for and win remaining government funding in an increasingly competitive marketplace. This is of concern given that small and medium-sized charities fill vital roles in local communities and in delivering frontline public services in ways that cannot necessarily be replaced by larger organisations.

APPENDIX

METHODOLOGY



ANALYSIS OF AGGREGATE FINANCIAL FIGURES

The report used the same financial data as that obtained for the UK Civil Society Almanac. Financial information on voluntary organisations was based on their annual accounts submitted to the Charity Commission. Financial data for a sample of these organisations was obtained by entering data from the charities' annual accounts. Before use, the data was

cleaned to remove significant errors, and underwent a series of checks to ensure validity. To ensure consistency all values were converted to April 2013 prices using the Retail Price Index. Once cleaned, mean amounts were produced for all financial variables within each income band and multiplied to the population size of England and Wales by income band.

More detail on the finances of voluntary organisations is available in the UK Civil Society Almanac, available from <http://data.ncvo.org.uk/>. The latest edition of the Almanac was published in June 2015 and presented data for the financial year 2012/13.

Table 3. Number of organisations in the sample by income band, 2008/09 to 2012/13

Income band	2008/09	2009/10	2010/11	2011/12	2012/13
No income	25	11	40	1	0
Under £10k	159	203	111	24	3
£10k–£25k	248	234	145	61	5
£25k–£100k	1101	972	1085	776	943
£100k–£500k	1304	1047	1315	875	880
£500k–£1m	1306	1171	1119	895	757
£1m–£10m	2789	2878	2588	2719	2923
£10m–100m	359	387	384	403	442
Over £100m	24	29	29	31	33
Total number	7315	6932	6816	5785	5986

ANALYSIS BY REGION

In order to analyse geographical trends across England and Wales, England was split into nine regions (East of England, East Midlands, London, North East, North West, South East, South West, West Midlands, Yorks and Humber). All regional breakdowns of income represent aggregate combined values of the three middle-income bands (£25,000 to £1m).

Rural-urban classifications were defined according to the Office for National Statistics (ONS).³⁴ The Index of Multiple Deprivation (IMD)³⁵ was used to quantify levels of deprivation across the UK, which incorporates indices on areas such as employment, health, education, crime and housing. It should be noted that both the rural-urban and IMD categorisations reflect where charities are registered and headquartered, not necessarily where they operate and carry out charitable activities.

ANALYSIS BY ACTIVITY

Voluntary organisations conduct a wide range of activities, which are often grouped into sub-sectors or industries. The International Classification of Non-profit Organisations (ICNPO)³⁶ is designed for voluntary organisations and other non-profit groups, and so is the most useful for comparisons between groups of organisations. In reality many organisations undertake multiple activities (eg housing and advice), but this analysis groups organisations into a single category based upon their primary activity. As ICNPO comprises multiple categories, they were further grouped into a total of 10 in order to facilitate analysis. All activity breakdowns of income represent aggregate combined values of the three middle-income (£25,000 to £1m).

References:

- 34. Office for National Statistics (no date) *Rural/Urban Local Authority (LA) Classification (England)*. Newport: Office for National Statistics.
- 35. Department for Communities and Local Government (2015) *English indices of deprivation 2015*. London: Department for Communities and Local Government.
- 36. NCVO 'Dataset #4: ICNPO Classification of charities'. data.ncvo.org.uk/datastore/datasets/dataset-4-icnpo-classification-of-charities (accessed January 2016)

