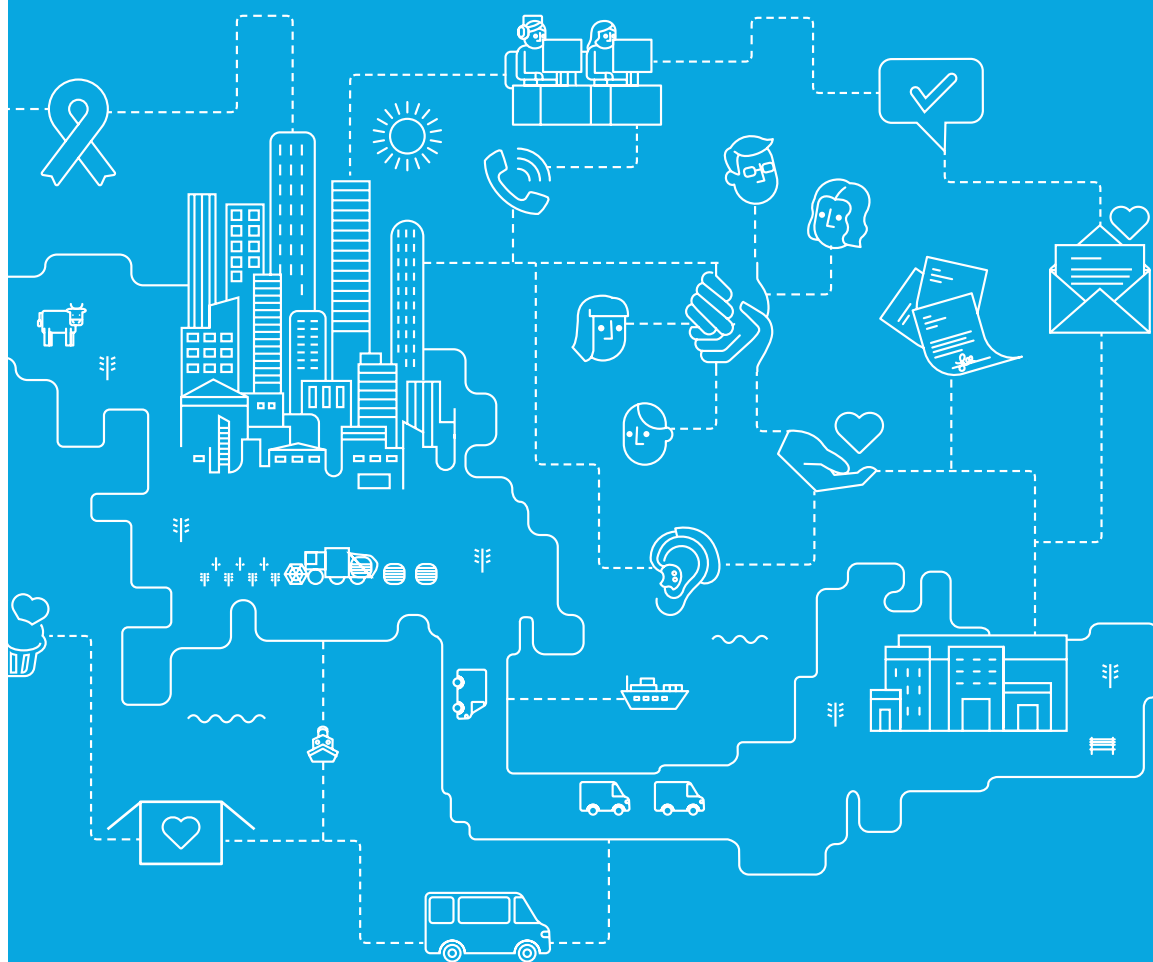


The funding of charities in 2020

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Foreword

It is over ten years since RSM began tracking how charities meet the funding challenges they face.

At that point in time, the specific issue charities were battling was the recession, and operating in an environment where they were expected to meet their objectives by assisting more beneficiaries, while simultaneously witnessing increased competition for donations, and a squeeze on statutory funding.

Indeed, the words of the then Charity Commission CEO, Andrew Hind, in RSM's 2009/10 report in [Managing charity finances through uncertain times](#), are as pertinent now as they were then: "While charities have no control over the funding environment, it's the steps they take now that can even the odds when meeting the challenges ahead."

As we enter the new decade, a sense of uncertainty remains. Brexit may be 'done' in a basic sense, but the terms of the UK's future relationship with the EU remain unclear, as do the longer-term economic consequences. And while we now have a government with a clear majority, its position on social policy and commitment to the charity sector is unknown.

Over the last ten years a number of themes have remained constant. Robust financial management and effective internal controls are vital to the success of a charity. Timely and appropriate financial information is key to making the right decisions and best enabling a charity to meet whatever funding challenges the wider economic position throws up.

An essential part of this is how charities tackle the issue of reserves. It is critical that shortfalls are tackled. In turbulent times, financial resilience will help charities stay flexible and adaptable so they can continue to fulfil their commitments to beneficiaries. A well-thought-out reserves policy is now more important than ever before.

Governance has always been a key consideration, but the focus has sharpened with the introduction of the Charity Governance Code in 2017. Last year's RSM research in how charities are complying with the Code has found that only 44 per cent acknowledge it in their annual reports. This suggests there is much room for improvement in striving to hit the aspirational standards that the Code highlights and in improving governance standards across each of the seven principles of the Code.

Over the years we have consistently been struck by the charity sector's resilience and ability to react positively to the challenges it faces. And we are confident it will continue to do so. But organisations need to remain mindful of the importance of informed financial decision-making, and strong governance, when planning ahead. It is only by doing so that they can achieve the maximum impact for beneficiaries and build strong foundations for the future.

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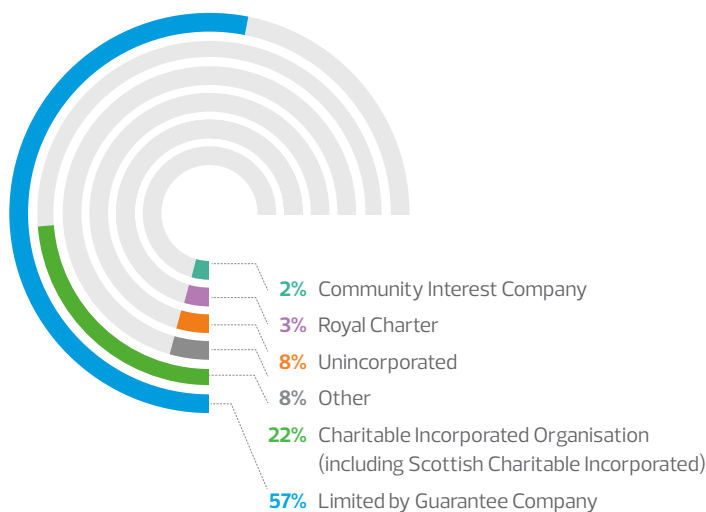
Our survey 2020

The survey was completed by senior managers, including finance directors, trustees and chief executives, from the full range of different-sized UK charities in Winter 2019.

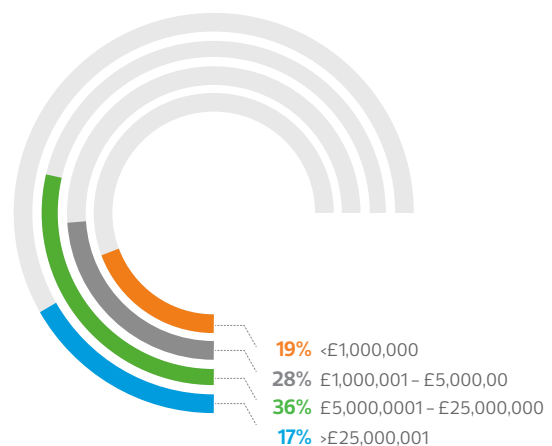
We received almost 100 responses to our questions about the realities of the last 12 months, and expectations for the next 12 months. The spread of respondents by income and area of operation is in line with previous years' research. But it's interesting to see that the use of the Charitable Incorporated Organisation as a legal form has increased since 2017, from under one in five to almost a quarter of respondents.

Due to rounding or to questions where respondents could give more than one answer, not all percentages will total 100.

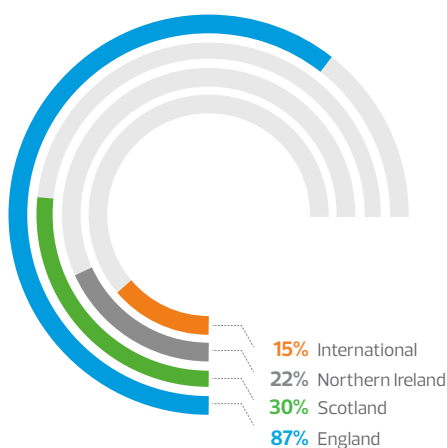
Type of charity



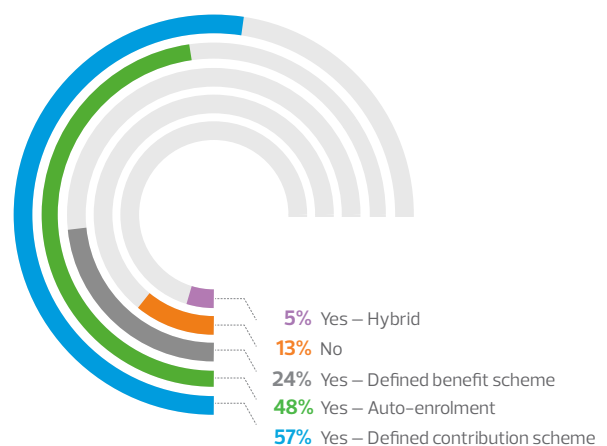
Annual total income



Area of operation



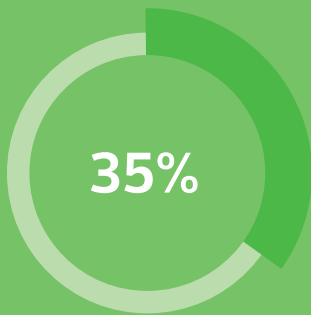
Type of pension scheme



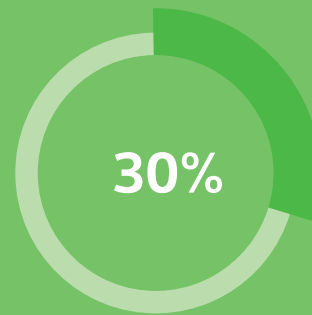


The funding scene

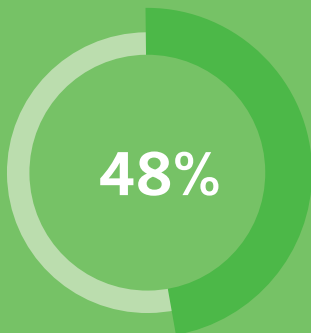
Key findings:



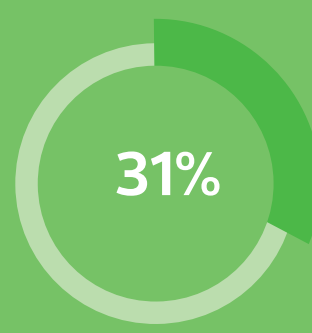
35 per cent of respondents have enjoyed an **increase in donations** over the last 12 months.



30 per cent see the need to demonstrate **social impact** as a big change in how funding is obtained.

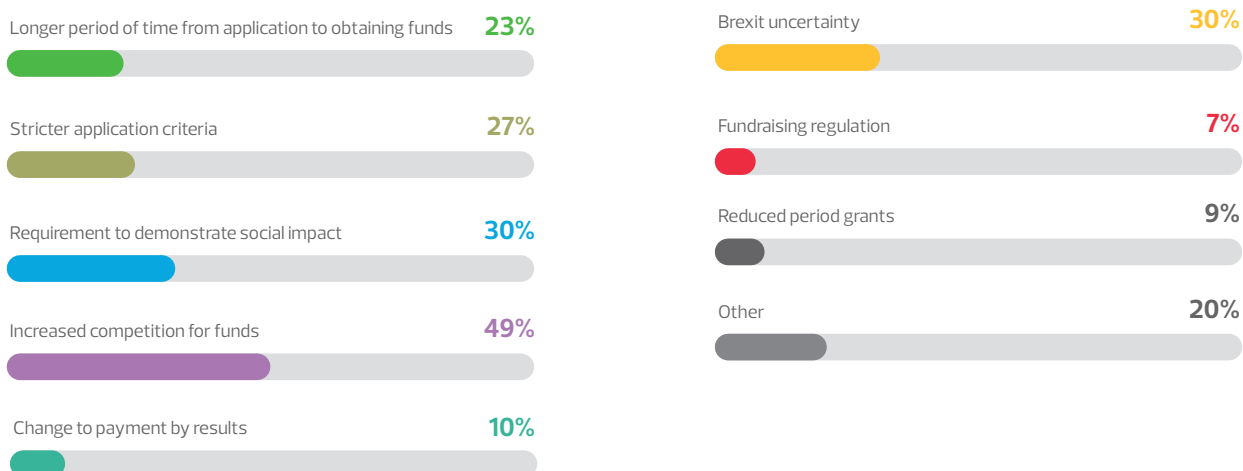


48 per cent say **full cost recovery** remains a funding challenge, down from 52 per cent in 2017.

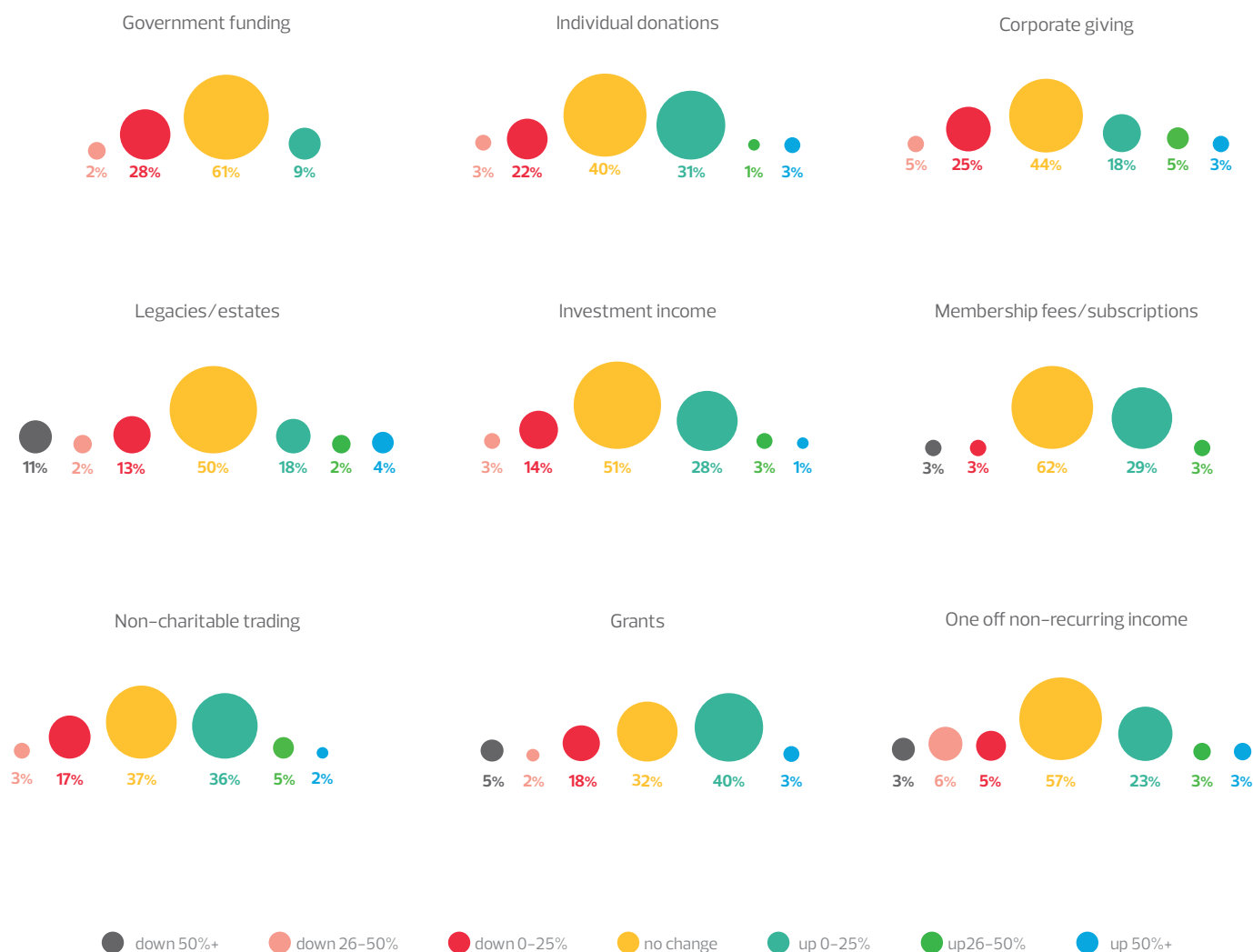


31 per cent said **raising money for capital projects** is a challenge, up from 27 per cent in 2017.

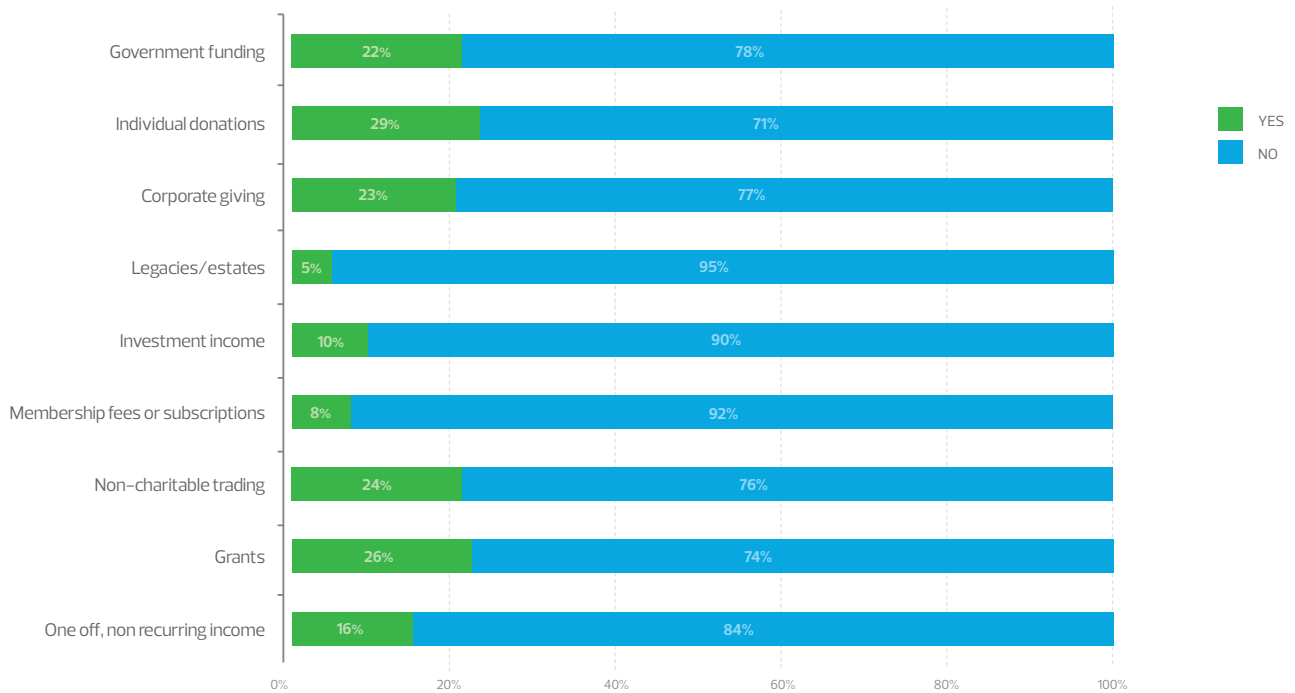
What are the biggest changes you have experienced in the way that funding is obtained in the past 12 months?



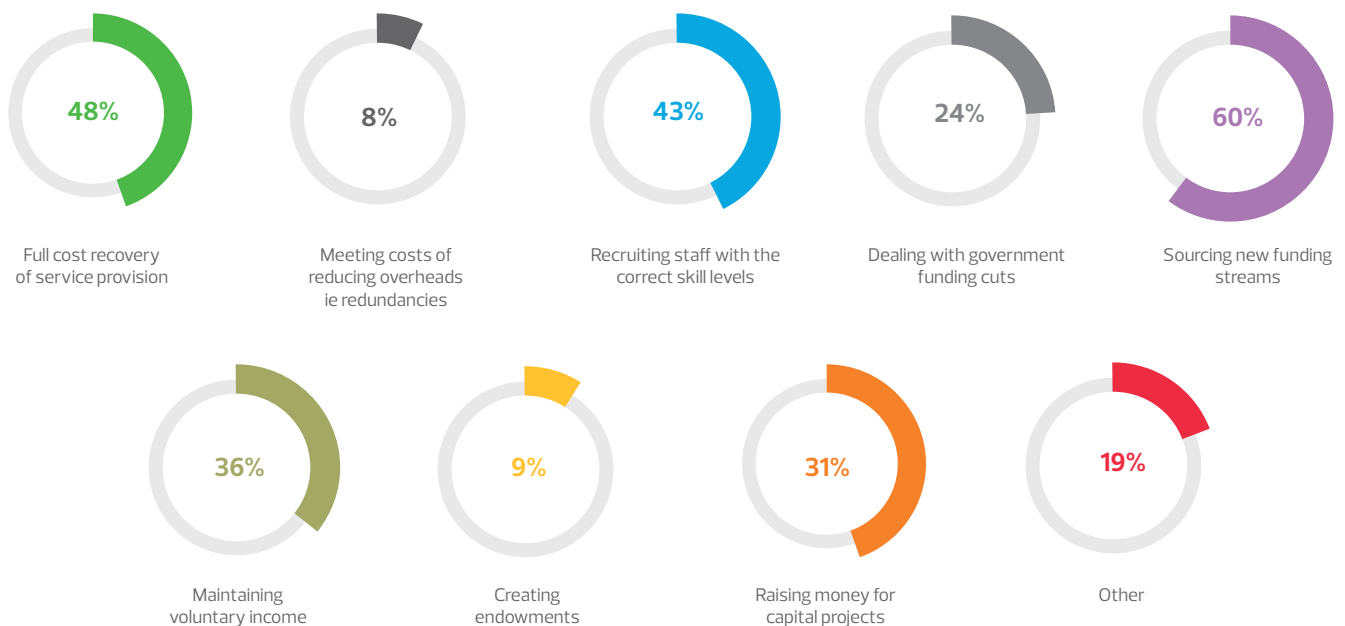
How much has your funding income changed in the last 12 months from the following sources?



Do you anticipate significant changes in funding over the next 12 months in the following areas?



What are your biggest funding challenges?



To make a difference and have an impact, charities rely on vision, passion, hard work – and funding. Funding, as we'll see, is an ongoing challenge.

Charities exist to fulfil their mission and meet their charitable objectives. So, it's slightly concerning that 12 per cent of respondents said they have no mission statement.

Two years ago, we found that donations were holding up well, despite the fundraising scandals of 2015. But a third of 2017's respondents still thought that maintaining voluntary income would be one of their biggest funding challenges in the next couple of years.

Were they proved right? In our latest survey, 22 per cent said they've seen a small drop in individual giving, 40 per cent reported no change, and 31 per cent a modest increase. However, corporate giving has for the same period dropped by 30 per cent.

In most other income streams, a significant proportion of charities saw no change. But grants, investments, and non-charitable trading saw increases of 43, 32 and 43 per cent respectively.

Some 48 per cent of respondents are worried about recovering the full cost of service provision, a slight improvement on the 52 per cent reported last time. However, recruiting staff with the correct skills is a concern for 43 per cent, marginally higher than what was predicted.

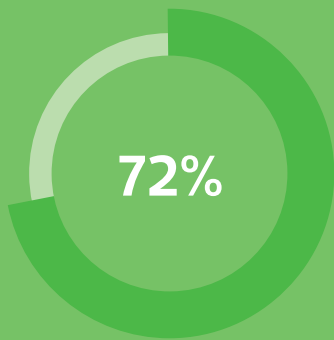
When asked about changes to obtaining funding in the last 12 months, 49 per cent of charities said there had been increased competition for funds. In 2017, the figure was 60 per cent, which we put down to stricter application criteria and a longer period from applying to receiving funds. Once again, these are significant obstacles. The need to demonstrate social impact is back up to 30 per cent after falling in the last survey, and is perhaps due to the renewed focus on proving impact.

How to improve on funding:

- 1 Regularly review your fundraising model and check your compliance with codes of practice.
- 2 Take steps to improve the diversity of your income streams.
- 3 Implement a strategy for recruiting and retaining good quality staff.
- 4 Ensure you demonstrate your social impact when bidding for funding.

Understanding finances

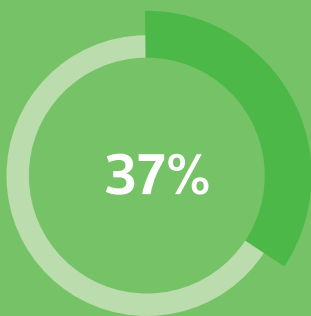
Key findings:



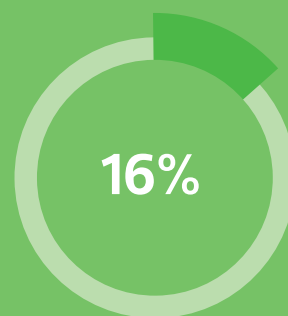
72 per cent of charities
**produce monthly management
financial reports**



53 per cent use **reserves** to
control costs.

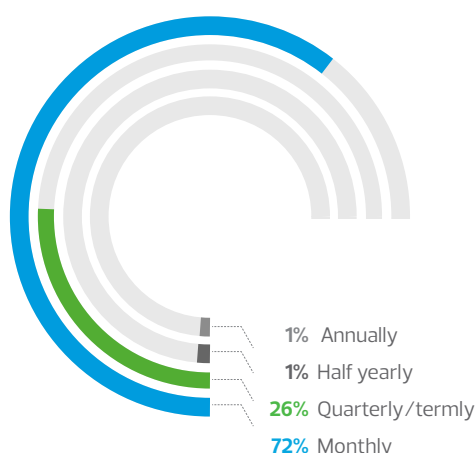


37 per cent of respondents
have between **0–3 months’
expenditure in reserve**



16 per cent have seen a
**significant decrease in their
reserves** over the last two years.

How frequently are management reports produced?



For a charity to get the most from its funding, it needs to be well managed. This relies on a competent and efficient finance team, and on timely and accurate financial information.

It also requires a trustee board that's knowledgeable enough to both understand and react to the data.

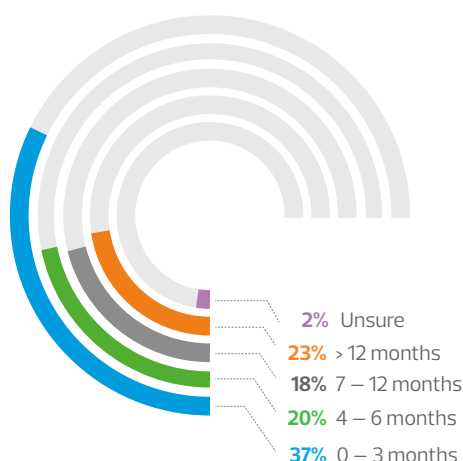
It's encouraging then that management reporting is becoming more frequent, with 98 per cent now reporting at least quarterly and termly and 72 per cent now producing monthly.

But regular reporting is only a positive if it contains the right information. A third of respondents' reports do not provide financial projections, while almost half don't include information on KPIs or impact analysis measures.

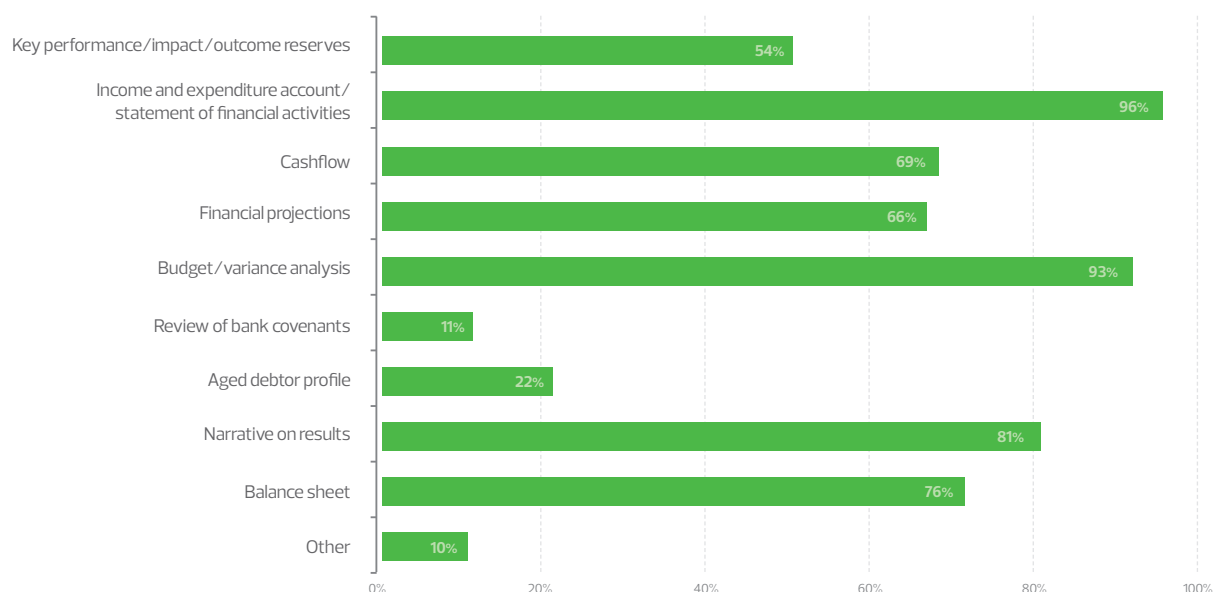
Most worryingly, over 31 per cent make no mention of cashflow analysis despite it being vital to controlling costs.

There are some interesting comparisons to 2017 around ways to control costs. Fewer charities are choosing to freeze staff pay (down to 11 per cent from 21 per cent in 2017), which is welcome given the sector's concerns over staff retention. Procurement and contract review continues to rise, now up to 34 per cent (from 30 per cent in 2017). And 26 per cent are deferring new projects (up from 21 per cent in 2017), possibly due to general uncertainty made worse by Brexit.

How many months' costs did you have in reserves at the end of your last financial year?



Do financial management reports include the following?



Reserves

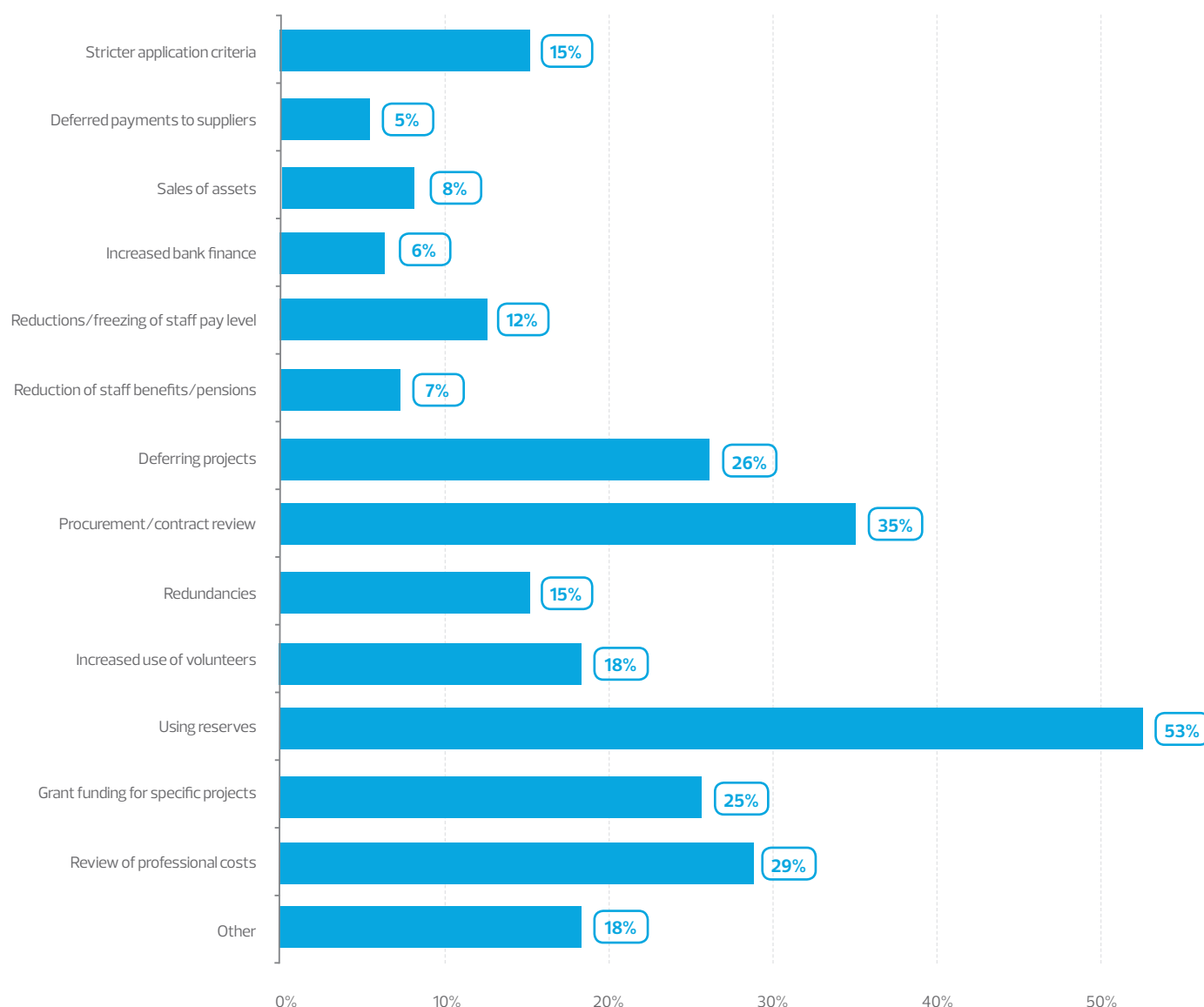
The most common method of subsidising costs is dipping into reserves, which 53 per cent of respondents said they've done. This is a small but worrying increase since 2017, and something we've consistently warned against as a long-term strategy.

While there's no one-size-fits-all figure for how much charities should hold in reserve, 37 per cent are operating with no more than three months' expenditure in the bank – up from only 28 per cent in 2017. A fifth of respondents have reserves of between four and six months' expenditure, and just over 40 per cent have more than half a year in reserve.

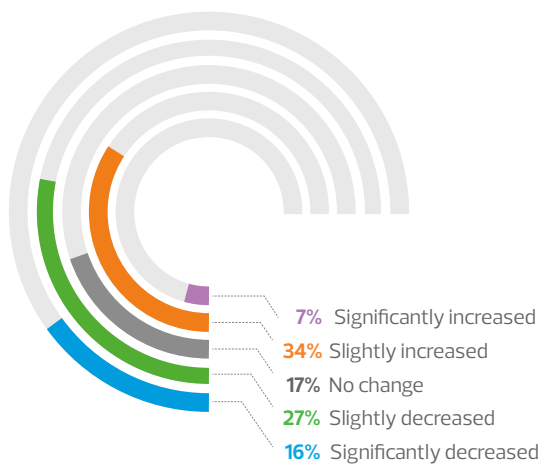
Has this changed since 2017? For 17 per cent of respondents, reserve levels have stayed the same and 41 per cent have even seen an increase. But 43 per cent have seen a slight or significant fall in reserves in the last two years, up from just 33 per cent for the period 2015–17.

And that seems to be affecting charities' optimism. Some 44 per cent expect their reserves to fall in the future and 10 per cent expect the fall to be 'significant' (up from three per cent in 2017). Just 30 per cent expect reserves to rise, which is down from 41 per cent in 2017.

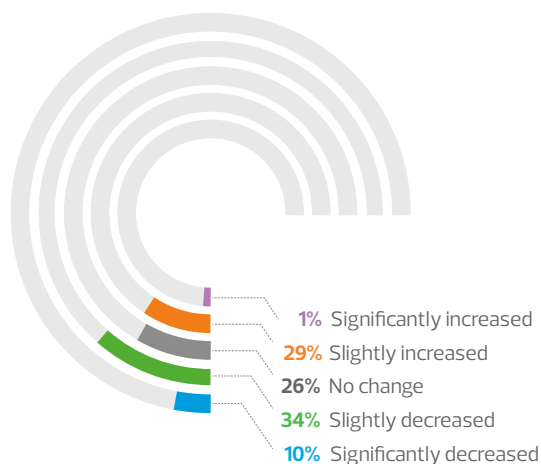
How are you managing your costs/cashflow?



Have you seen a change in your organisation's reserves in the last two years?



Where do you anticipate your organisation's reserves being in the next 12 months?



It is also important for planning that charities know how much of their reserves are held as unrestricted cash. 48 per cent of respondents hold between one and 25 per cent of reserves as restricted funding, while four per cent aren't sure.

RSM's research, 'Charity Reserves: Resilience in 2018', found that 22 per cent of charities surveyed required significant improvement in formulating and implementing an effective reserves policy. Reserves are much more than a statement about the financial health of your charity. Amid growing media and public interest in fundraising practices, a robust reserves position will send a clear message to funders and beneficiaries that you are well-led, well-managed, and well-run.

As that report concluded: "Ultimately, it is up to trustees to work out how much your charity needs to keep in reserves. A balance must be struck. Too little, and you could be exposed to shifts in donor contributions, contracts or fundraising. Too much, and questions could be asked about whether you are managing resources in the best interests of beneficiaries".

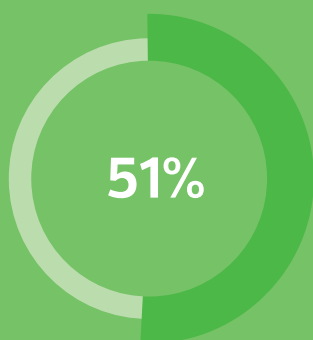
To view a copy of the report please visit <https://www.rsmuk.com/ideas-and-insights/charity-reserves-resilience-in-2018>.

How to improve on reporting and reserves:

- 1 Produce detailed monthly financial management reports.
- 2 Report on all metrics that are essential for financial decision-making, including non-financial KPI's.
- 3 Assess your use of reserves for controlling costs and cashflow.
- 4 Review and monitor your reserves policy and levels, particularly the proportion that is unrestricted funding.

Taking action

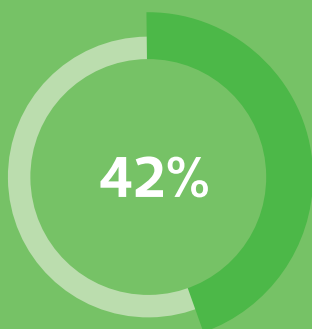
Key findings:



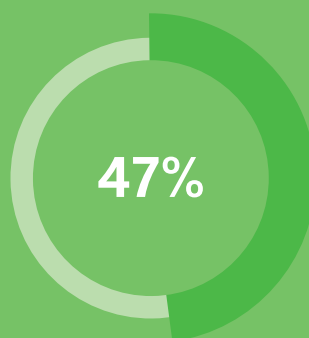
51 per cent of respondents have sought **new sources of funding or commercial activities** over the last 12 months.



15 per cent have experienced **fraud or been offered a bribe in the last year.**



42 per cent of known fraud is committed by **employees.**



Just 47 per cent can prove they comply with the **Charity Governance Code's diversity principle.**

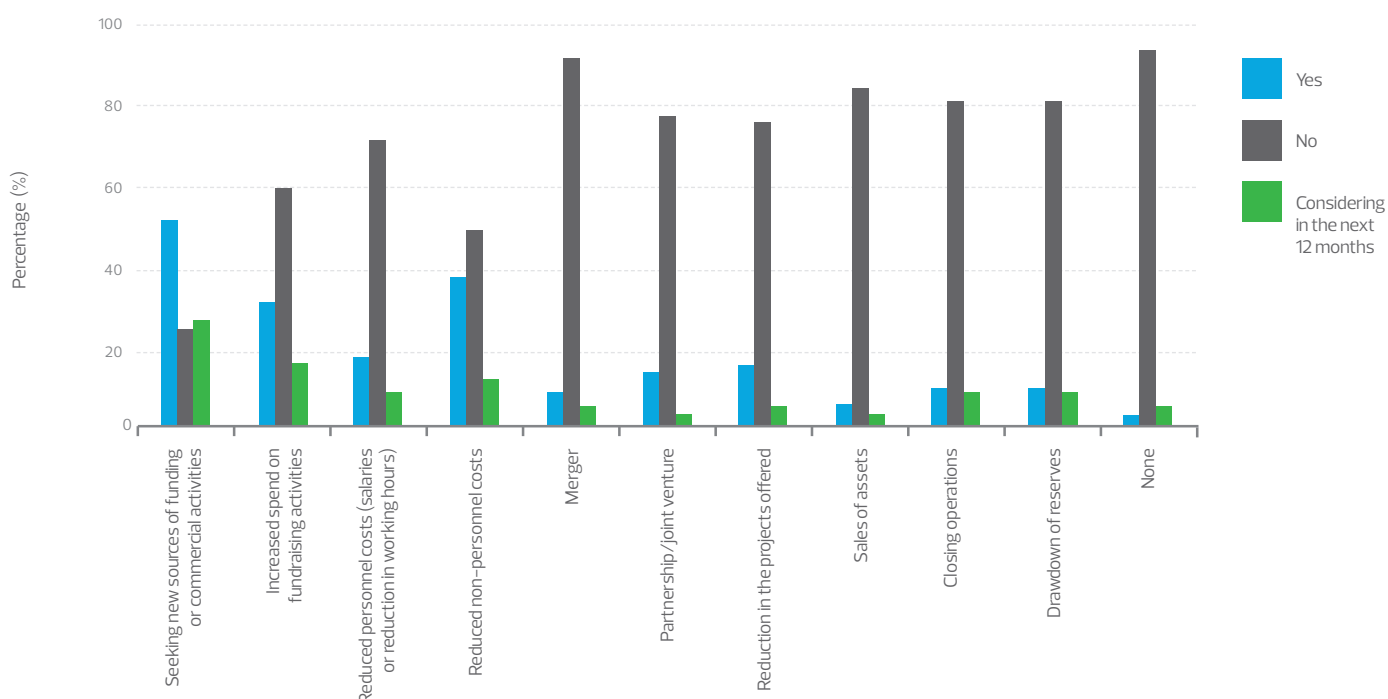
When asked what finance-related actions they'd taken in the last 12 months, 51 per cent said they sought new sources of funding or commercial activities and 26 per cent expect that to continue in the coming year.

38 per cent had chosen to draw down on reserves, and 11 per cent expect to do this in the next 12 months.

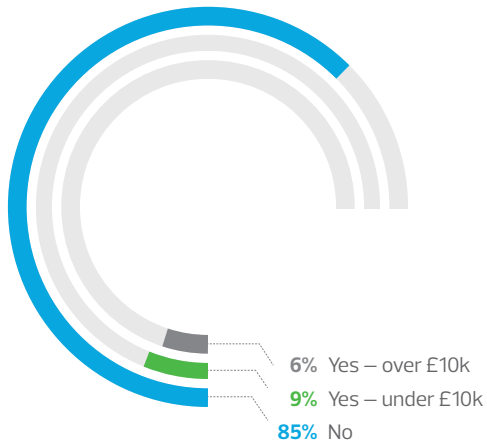
38 per cent have reduced non-personnel costs and 28 per cent have increased spending on fundraising. And while 20 per cent have been involved in either a merger, partnership, or joint venture, only nine per cent are considering this for the next year.

The technical debate around going concern continues, but 63 per cent of respondents said their trustee board formally approves a separate going concern assessment for the annual statutory financial statements. However, eight per cent simply didn't know.

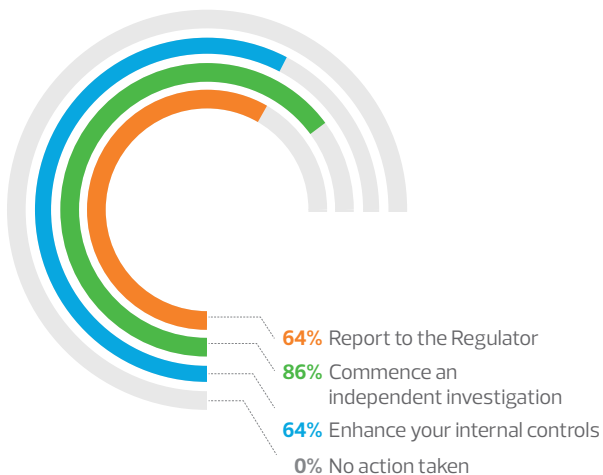
Have you undertaken any of the following in the last 12 months?



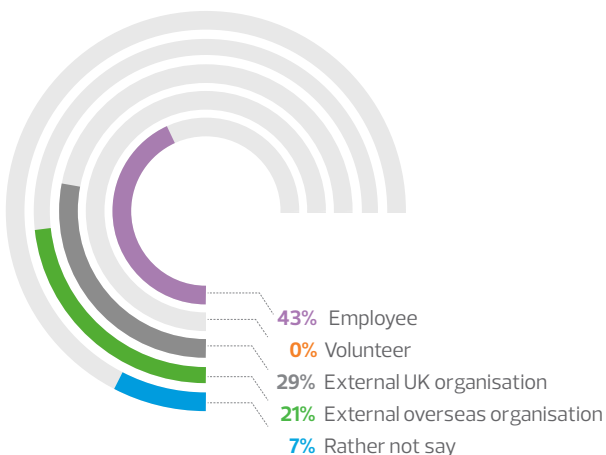
Has your charity experienced fraud or been offered bribes in the last 12 months?



For those that answered yes to experiencing fraud or bribes did you...



Who committed the attempted fraud or bribe?



Fraud

Statistics revealing true levels of fraud are always hard to obtain. So it's difficult to know whether the 15 per cent of respondents that have experienced fraud or been offered a bribe in the last 12 months are:

- showing a lack of adequate financial controls;
- making a greater commitment to transparency; or
- responding to the Charity Commission's push on serious incident reporting.

Certainly, it's a concern that only 64 per cent of charities who experienced fraud reported it to the regulator. And while the majority conducted an internal investigation, just 64 per cent strengthened their procedures as a result.

In 43 per cent of cases the fraud was committed by an employee, which is in line with the findings of other surveys.

Governance

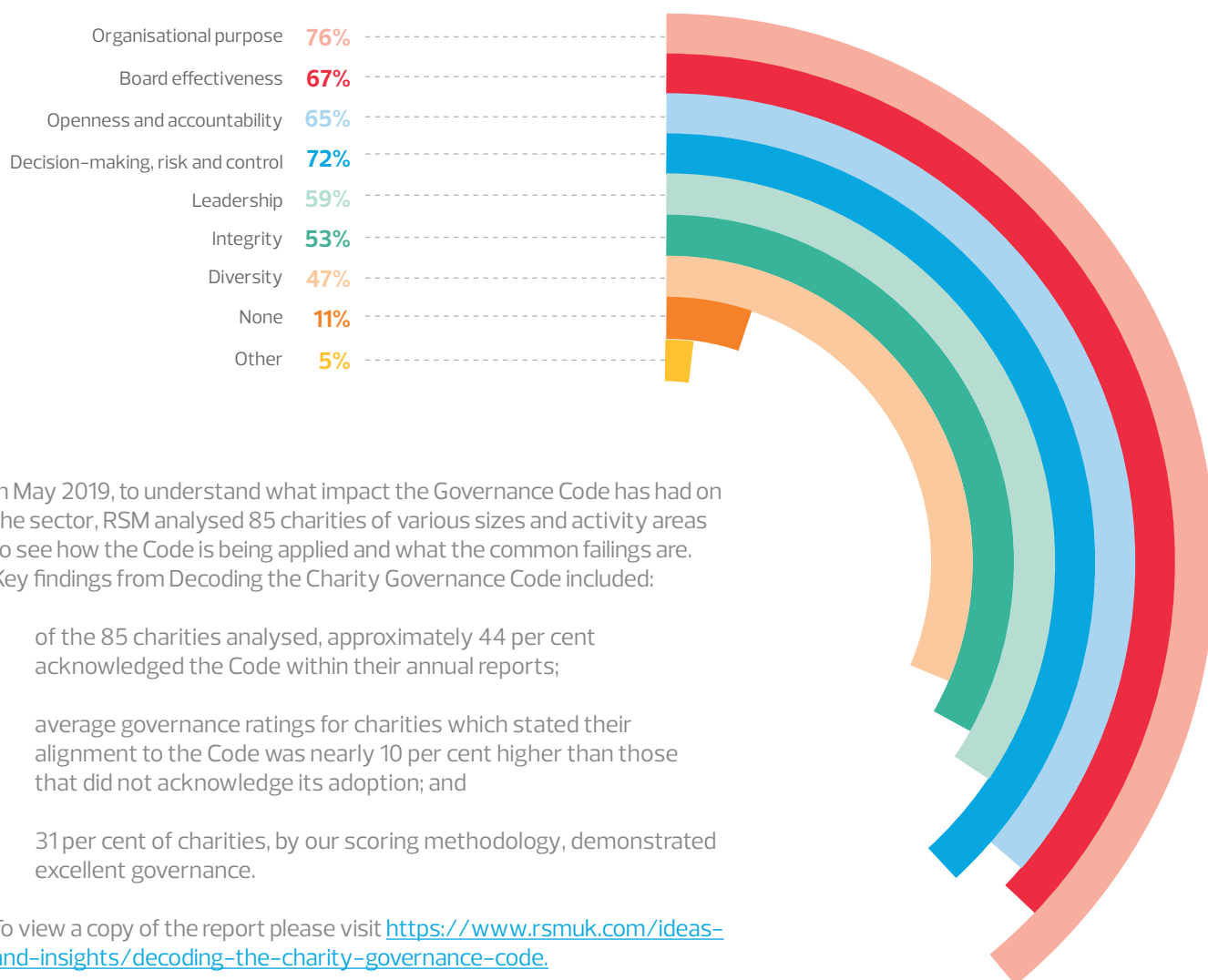
The Charity Governance Code was introduced for charities in England and Wales (Scotland has a similar code) in 2017 and, in our survey that year, 48 per cent of respondents planned to implement it in the next 12 months. But 18 per cent had no intention to, and 20 per cent hadn't even heard of it.

Adherence to the code is voluntary but there's anecdotal evidence that funders will increasingly see compliance as obligatory or, at least, as a sign that a charity is robustly governed.

A number of charities have chosen to focus on one or a few of the code's seven principles, rather than try to comply with them all in one go. Evidence of compliance with organisational purpose has been provided by 76 per cent of respondents. But just 47 per cent have tackled diversity and inclusion, which does seem to be the area that many charities and trustee boards are struggling to grasp.

The code will be refreshed in 2020 but the core principles won't change. An ongoing and genuine engagement with them is advised if you want to demonstrate a strong commitment to quality governance, and vital to making a full impact.

Which sections of the governance code do you evidence compliance with?



How to improve in these areas:

1

Actively explore opportunities for new funding.

2

Speak to your auditor about going concern assessments.

3

Put in place adequate systems for detecting and reporting fraud.

4

Implement one or more of the seven principles of the Charity Governance Code.

5

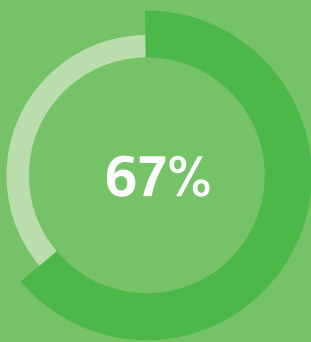
If you have experienced a fraud, have you considered the Charity Commission Serious Incident Reporting Requirements?

6

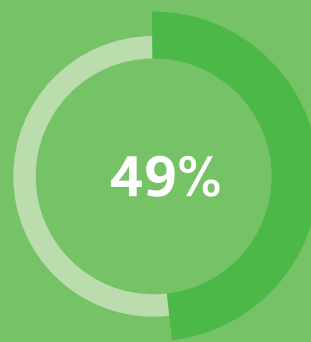
If you have suffered a fraud, have you reviewed the adequacy of your controls?

Future challenges

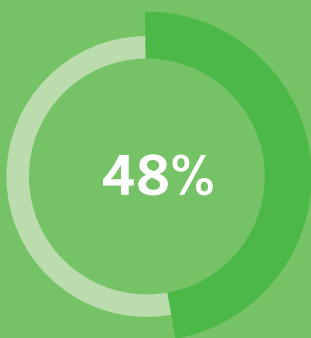
Key findings:



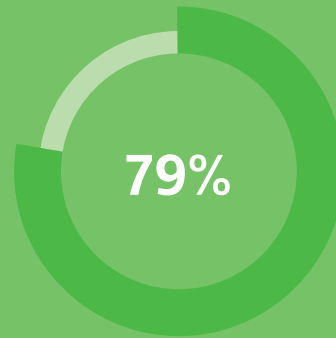
67 per cent of respondents see **new funding sources** as a challenge over the next 12 months.



49 per cent see **staff resources** as a challenge.



48 per cent measure **impact and outcomes** on beneficiaries.



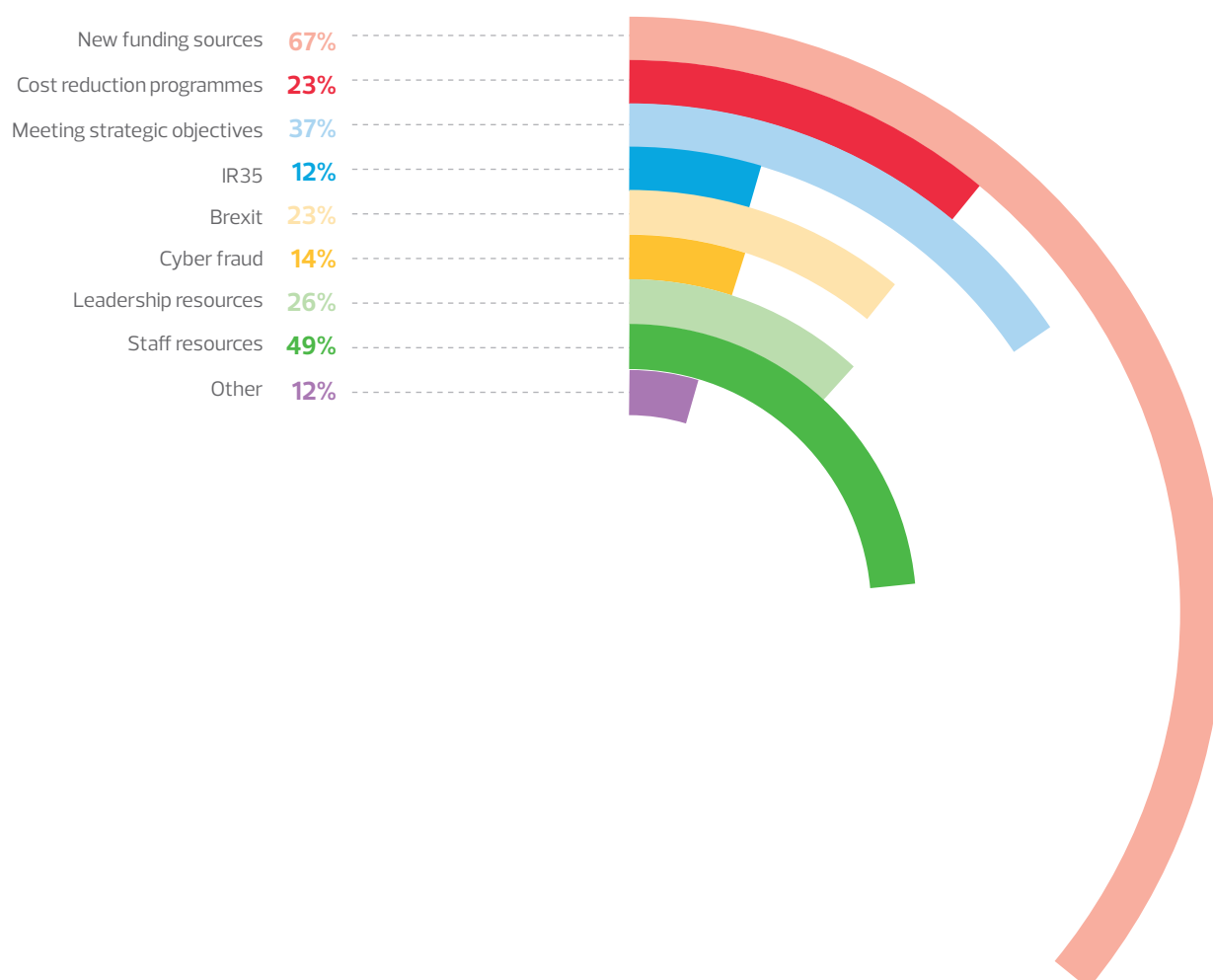
79 per cent **use their annual report and accounts** to report on impact.

While the environment has been uncertain over the last few years, planning ahead and operating in ambiguous circumstances, and on scarce resources, is nothing new for the sector.

Their biggest concern, as expected, remains new funding sources (67 per cent). 49 per cent see staffing as a challenge, both in terms of attracting and retaining new talent. And 37 per cent worry about meeting strategic objectives, which is core to running an effective charity and making an impact.

Although the UK's future relationship with the EU and the longer-term economic consequences of Brexit remain uncertain, only a quarter of respondents see Brexit as a challenge for the next 12 months.

What do you think are the biggest challenges facing your charity in the next 12 months?



Impact

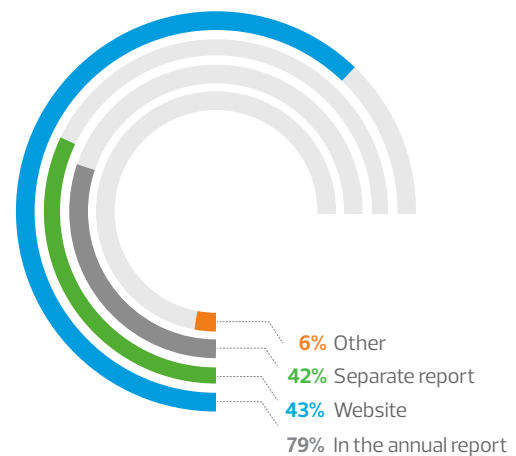
Making such an impact is one challenge, being able to demonstrate and report on it is quite another. But in order to survive, win the competition for funding, and deal with a seemingly more sceptical media and government, charities must be able to justify how they spend their money – and the difference they make.

Only 48 per cent of this year's respondents stated that they undertake impact reporting. They do this mostly with KPIs and statistics (68 per cent), case studies (63 per cent), and surveys or interviews (58 per cent).

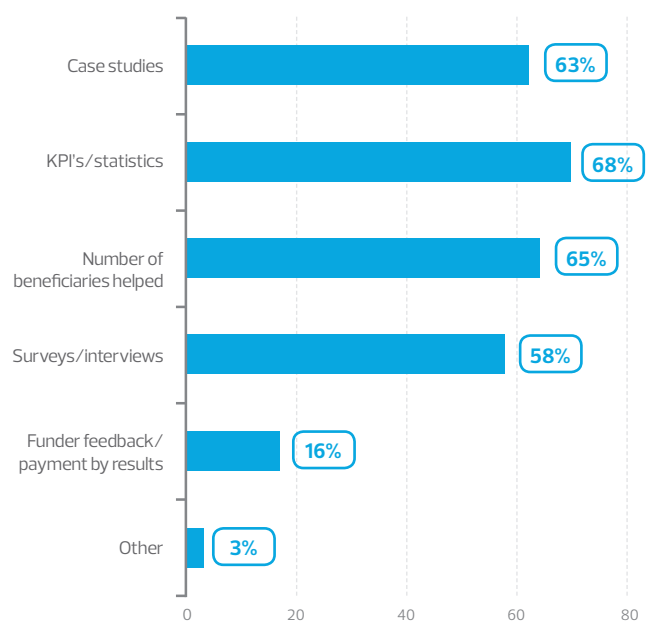
But measuring impact is only half the battle. Communicating it in an accessible, easy to interpret, and resource-efficient way is tricky too.

Unsurprisingly, 79 per cent report on impact in their annual report and 42 per cent produce a separate report. Just 43 per cent do it via their website, an obvious quick win for those looking to engage younger supporters.

Where do you report on your impact?



How do you measure your outcomes and impact on beneficiaries?



How to improve in these areas:

1

Consider the effect of different Brexit scenarios on your organisation.

2

Regularly review your strategic objectives and assess your ability to meet them.

3

Consistently and methodically assess the impact you have on beneficiaries.

4

Effectively report on that impact, using digital channels to reach new donors.



Authors

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Nick is the national head of charities and independent schools at RSM and is a client partner responsible for a portfolio of RSM's largest not for profit clients, including a number of top 250 charities and large independent schools.

Nick has responded to numerous sector consultations including the Charity Commission and OSCR on Charities SORP and the Financial Reporting Council on the Practice Note 11 Consultations: The Audit of Charities in the UK. Nick has worked with a number of boards to improve their governance and financial reporting over the past decade.

**Karen Spears****Head of Not For Profit – Restructuring Advisory****T:** 020 32018421**E:** karen.spears@rsmuk.com

Karen is head of the restructuring advisory not for profit group at RSM and represents the faculty in the firm's national cross-disciplinary not for profit steering group.

Karen has considerable experience in all types of restructuring, in particular advising trustees of charities and senior management teams in the Not for Profit sector on the strategic options available to them. This includes advising on cashflow and long-term viability, orderly wind-down of services and operations, transfer of services and mergers, and administrations and liquidations.

About RSM

RSM is an independent UK firm of chartered accountants and business advisers.

Charities

The Charities Group at RSM comprises a core team of 50 partners and managers, devoting substantial time both professionally and through personal commitments to the Not for Profit sector. Many in our core team have been awarded the ICAEW Charity Diploma. The Group's specialists include recognised national experts, renowned for their individual and team input to both the sector and government at all levels. The Group is multi-disciplinary covering a wide range of audit, tax and consultancy services. Our team has a flair for problem solving and proactive planning and believe in developing and sharing best practice by monitoring trends and emerging issues. The Group is unusual among charity professional service firms in having a truly national coverage.

The Group has strong links with the Charity Commission, OSCR and other major sector bodies such as the Charity Tax Group and Charity Law Associations as well as other sector professionals and government departments. The Group's support includes delivering seminars, publishing sector publications and sitting on various umbrella bodies' committees.

One in four of the top 250 charities use RSM as either external or internal auditors.

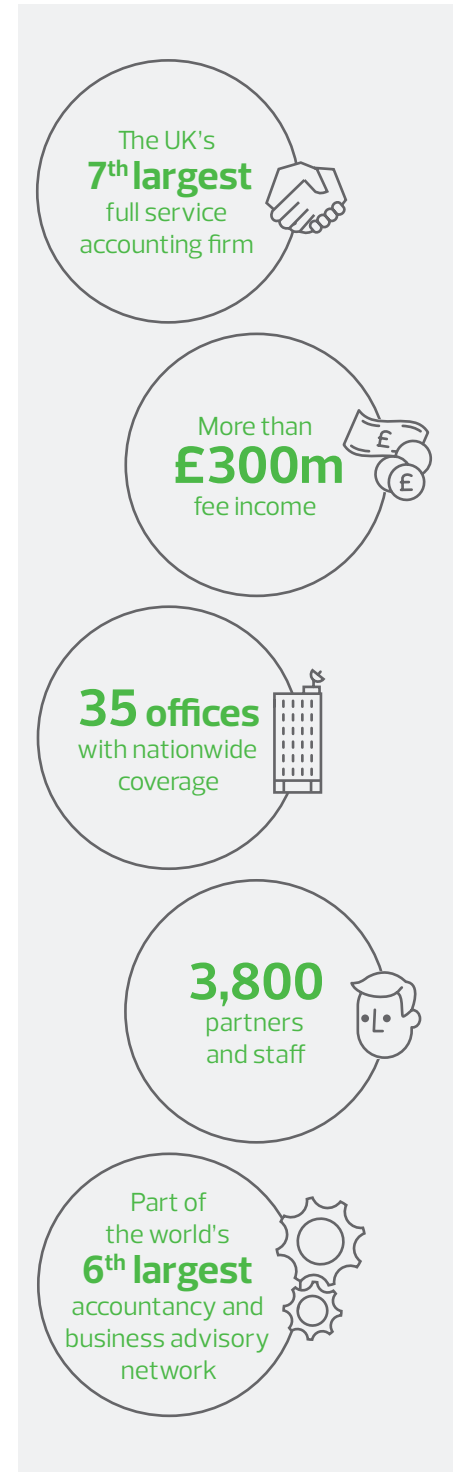
Restructuring Advisory

A dedicated team within our Restructuring Advisory service focuses on providing senior management teams and trustees of charities and Not for Profit organisations with practical expertise ranging from informal advice and support right through to formal insolvency proceedings.

The breadth of services it offers includes:

- cash management analysis;
- review of asset values and associated banking covenant issues;
- risk assessment and 'what if' scenarios;
- turnaround and recovery advice
- advice on defined benefit pension scheme deficits;
- insolvency solutions; and
- orderly wind-downs.

As part of the firm's wider Not for Profit Group, the team works alongside other advisers to ensure that the best team is assembled to provide innovative solutions to our clients. RSM Restructuring Advisory LLP is also on the Charity Commission's panel for interim manager appointments.



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