

## Briefing Paper 47

### A comparative study of changes in earned income among third sector organisations in England and Wales, and the United States

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Drawing on data from England and Wales<sup>1</sup> and the United States, this research tests the assumption that social enterprise is an important revenue stream for third sector organisations (TSOs),<sup>2</sup> and examines the extent to which this is a recent phenomenon. The findings will be compared with similar research undertaken in the US to enable comparative learning and strengthen theoretical understandings.

Nonprofit scholars have noted an increased tendency for TSOs to adopt commercial activities. There have been many different theories put forward to explain this 'changing nature' of the third sector in the US, particularly with regards to a perceived increased reliance on 'earned income', that is revenue generated through trading. For example, institutional theory has been drawn upon to suggest that market disciplines have permeated civil society to the extent that social enterprise has achieved moral legitimacy, that is the language and practices of the

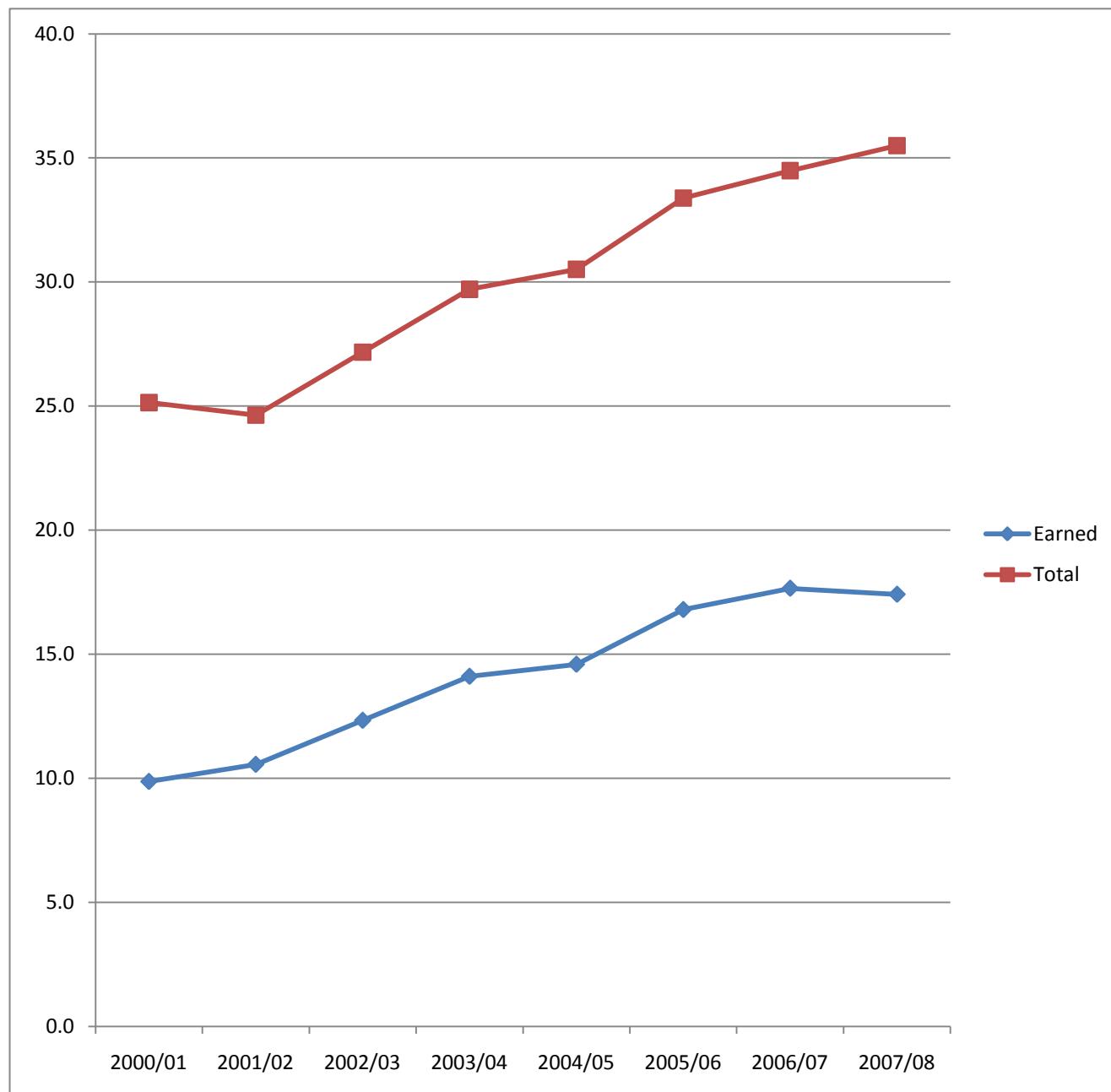
market have become accepted by TSOs as a preferred way of 'doing things'. An alternative perspective draws upon resource dependency theory to suggest that a decline in state funding, and private giving by individuals, to the third sector, combined with an increase in the number of TSOs has led them to seek alternative market-based income streams. In the UK the impact of these compelling stories can be seen at ground level as umbrella organisations 'representing' the third sector offer their members advice and support to adapt to a 'new' reliance on earned income.

At first glance it would appear that a long tradition of policy transfer from the US to the UK is continuing albeit at the level of civil society. However, there is little empirical evidence to support the underlying assumption that earned income strategies are the most important source of revenue for nonprofits, and that their relative importance is increasing over time. This is because existing,

studies have drawn on small samples focused on limited subfields within the sector, or relied on changes between two time points rather than attempting to show trends. Moreover the academic literature relies almost exclusively upon data from the US as until recently this

was the only large country with sufficiently robust data sources to draw upon. Since then headline trend analyses by NCVO would seem to support the assumption that charities earned income has increased over time in England and Wales (See Figure 1).

**Figure 1: Charities earned and total income since 2000/01 (£ billions)<sup>3</sup>**



Since 2002, analysis of charitable returns in England and Wales enables us to distinguish between different sources of charities income. Guidestar UK has collated data for the period 2002-2008 and from this we constructed a dataset that allows detailed analysis for England and Wales. In the US the equivalent data is that drawn from US Internal Revenue Service (IRS) Statistics of Income (SOI), which in turn draws on Annual Returns by charitable organisation to the IRS. Georgia State University has obtained this data deriving from 1982-2008. Thus the two datasets are well suited for comparative analysis. We draw upon these sources to show trends in earned income among charities in the US and in England and Wales since 2002. This enables us to determine the proportion of charities revenue derived through earned income in both countries, and examine how this has changed over time. In turn this helps us understand how the sector is changing. Comparing England and Wales with the US develops our understanding of the extent to which these changes (if any) are country specific, or occurring across similar welfare regimes.

## Methods

The SOI data relies on a sample of non-religious 501 nonprofits with annual revenue over £25,000, stratified by asset size with higher sampling rates for larger organisations. The datasets for each year have been weighted and calculated to adjust for inflation. Hospitals and higher education institutes have been excluded as

outliers as they have traditionally relied heavily on earned income. The TSRC dataset contains the full population of 70,000 charities submitting annual returns to the Charity Commission in England and Wales. We also exclude hospitals and higher education institutes for comparative purposes.

We undertake trend analysis of both the US and England and Wales datasets to compare changes over time between the two countries. We then break down the aggregate data into field specific trends, categorised according to the International Classification of Nonprofit Organisations (ICNPO) - for example, health; social services; and environment. This enables us to understand whether the trends are common across the whole sector or are specific to certain subsectors. Breaking down the data by field also helps us speculate on different reasons for changes in the different countries.

Informed by academic work seeking to explain TSOs increased reliance on earned income, we undertake panel and regression analysis of the England and Wales dataset to identify variables correlated with an increase / decrease in earned income among TSOs stratified by (for example) size and field. Next we will undertake panel analysis of the US dataset to understand the relationship between government grants, private donations and earned income (statistical analysis of the US dataset is problematic given the variation in IRS sampling methods from

year to year). At this stage it is not possible to state with any degree of accuracy how many organisations have been sampled in enough different timeframes to enable the construction of a panel. However we expect it to be possible to explore the impact on earned income of a) a decline (or increase) in government grants of 5% or more, and b) a decline (or increase) in private giving of 5% or more.

## Who is this research of use to?

It is expected that the provision of robust data to academics in the field will contribute an empirically informed underpinning to theoretical understandings of earned income strategies among TSOs in England and Wales, and in the US. It will also improve policy and practice through comparative learning.

Our trend analyses will provide robust evidence of the relationship between earned income and other sources of revenue for charities and nonprofits at an aggregate level over time. This will be of use to current and potential donors and investors in the sector. Our panel analyses will investigate relationships between different funding sources at a field level. This will inform governments wanting to support growth of the sector through the tax system, and will also help inform the policy work undertaken by a range of organisations providing support to, and advocating on behalf of TSOs.

Perhaps of most practical significance, our research will be of use to organisations that are concerned about future revenue sources, and want to understand relationships between sources of funding. Our analysis of comparative revenue sources for different categories of TSO will permit individual charities to compare their revenue sources with similar sized organisations in the wider field in which they operate. This may offer opportunities for organisations to target particular revenue streams in the future.

## When will our findings be released?

The data for England and Wales has recently been analysed. In April 2011 analysis of the US data will enable a comparative picture to be painted. The findings will be distributed through freely accessible working papers on the websites of TSRC and Georgia State University. TSRC's Knowledge Exchange Team will maximise user engagement with the research.

<sup>1</sup> Since devolution in the United Kingdom, the different countries have collated charitable data in different ways. This makes it difficult to collate a dataset covering the whole United Kingdom.

<sup>2</sup> In this proposal we use the term TSO when referring to charities in England and Wales, and Nonprofits in the US. However we recognise that our research covers only a sub-set of TSOs.

<sup>3</sup> Figures sourced from NCVO's UK Civil Society Almanac 2010

This paper is part of the Third Sector Research Centre – Briefing Paper Series see [www.tsrc.ac.uk](http://www.tsrc.ac.uk) for more details and a copy of the full Working Paper 47

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