Income Diversification

Voluntary Impact Northamptonshire
Executive Membership

The aim of this guide is to help VCSE organisations to consider how the spectrum of income streams available can be used as part of a sustainable funding approach.

What is a sustainable funding approach?

Sustainable funding means not relying on a single income stream, but exploring opportunities to generate income from a mix of sources, and by a variety of means, from donations, via grants, Service Level Agreements and contracts, to earning income through trading. It does not mean you have to do all of these: proportionality is key. A small organisation may well diversity into two or three different 'donation' streams, or a mix of donations and small grants; a large one may have contracts and earned income in their mix.

Diversifying income can reduce or spread risk, and help organisations being more financially robust and able to ensure their future without mission drift, or loss of independence.

This approach to sustainable funding for any organisation must be underpinned by thorough planning, an assessment of the impact of diversifying your funding streams, full cost analysis and understanding of when social investment, including loan finance, may be appropriate.

What does this mean in practice?

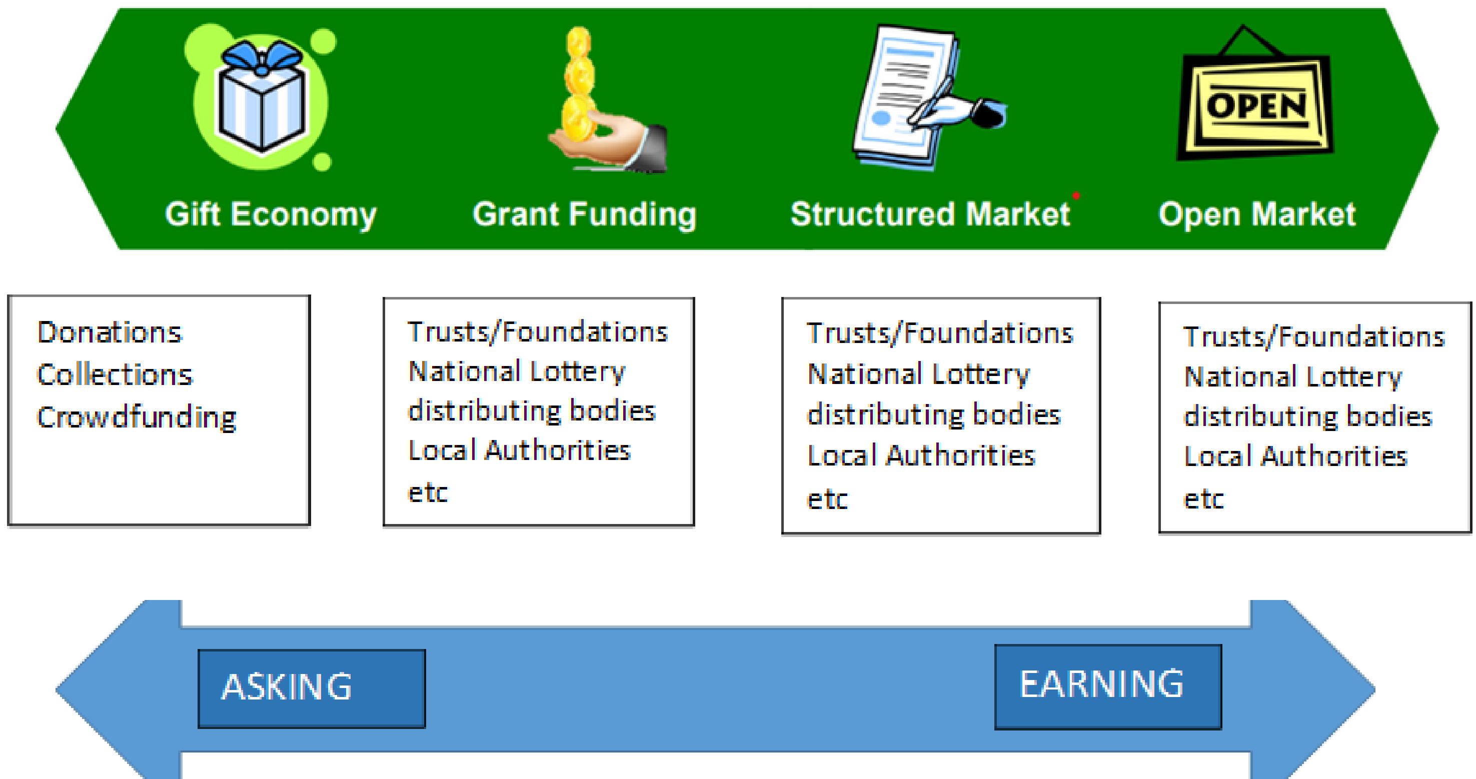
Before you can consider income diversification, and what streams may be appropriate and feasible, organisations need to know exactly what they are trying to achieve: what their mission, vision and aims are, and how they plan to work towards delivering these.

If you don't already have a strategic plan, do take a little time to develop one which includes a funding strategy.

Over recent years, VCSE organisations have been encouraged to move away from grant dependency – and it's good practice not to be reliant on a single grant funder, anyway – and consider other forms of financing their work, such as delivering public services. It's vital, however, to understand your costs, so that you can assess accurately whether contracts and trading will actually bring in income, or cost money, or whether grants will cover the cost of delivering a service.

Having a mix of income streams means that if one reduces or ends, it doesn't threaten an organisation's viability or survival, and it also allows organisations to plan with a higher degree of confidence. However, it's important that there is match between what an organisation does (or plans to) and the sources of funding – mission drift from chasing money should be avoided.

The Income Spectrum



Source: CVS Bedfordshire

It is worth taking some time to consider if you need to diversify your income. Broadly, if you have only one source of income, or if any one funder or activity makes up the majority of your funding, you should think about increasing your income streams.

The key to sustainability for organisations is knowing which streams are the right ones to explore and to develop the capacity to manage.

It may not be possible, or appropriate, for an organisation to diversify across the full spectrum, but diversifying within a particular stream (eg, having more than one grant funder, or a mix of contracts with different agencies) or across just two (eg a mix of donations and grants, or grants and trading) should be considered.

Unrestricted income

It is important to consider a good level of unrestricted income (that is income that is not given to an organisation for a specific project or activity, as much grant funding is) as this gives an organisation increased independence both for delivery and core costs, and can be used to build up reserves as a financial cushion. Most donations are unrestricted income, although some donors may specify what they want their money used for. Earned income is generally unrestricted (unless, for example, an organisation sells a product that is marketed as 'all profits to a named project').

Trading

Trading has always been an important source of funding for the VCSE sector, used to generate additional income. It often relates to an organisation's charitable purposes, but this doesn't have to be the case: it is quite feasible for organisations to set up business which is purely to generate income to invest in their charitable aims, but which is not connected to them. Our information sheet on trading (hyperlink please to the relevant document) has more information on all aspects of trading.

Full cost recovery

When you are working out the cost of a project or activity, organisations need to understand what support and resources it needs from the rest of the organisation (support costs), not just the obvious costs of the project itself (direct costs).

Direct Costs	Support Costs
Relate directly to the project Examples include • project staff salaries • equipment • expenses • monitoring and evaluation of the project	The project costs to the whole organisation Examples include: • rent • utilities • insurance • management time • administration or other staff costs • fundraising

Adding these two types of costs together will evidence the full cost of the project. It is vital that organisations understand their running costs, and the real cost of providing services. Full cost recovery is when an organisation recovers all those costs, whether that is from a contract or a grant. While full cost recovery is not easy, it's essential that funding bids or contract negotiations cover all these costs, and pricing for traded products and services reflects the full cost of producing and providing the goods or service.

If an organisation can't get the full cost of a project from funders or those letting contracts, senior staff have to make a decision about whether it is an activity that they still want to do. There can be very good reasons for taking on projects that aren't fully funded, but organisations should only do this with a clear grasp of the implications,