



articles

This article - by =mc's commercial awareness and earned income expert, Bernard Ross - gives you 7 key considerations if you're thinking about developing an earned income strategy

Commercial awareness:

## Earned Income – Seven Key Considerations Before you start

**This article draws on =mc's consulting work with national and local charities - from the National Theatre to the RSPCA and from NSPCC to the Crossroads Care. We have also carried out major programmes for local authority leisure and museums functions to help them become self-**

The economy seems to be in recovery but continued cuts in local authority spending and donations have left many third sector organisations struggling to fill income gaps. Increasingly, these organisations are looking for new ways to generate income, and at the same time reduce reliance on donations or grant-aid funds. One avenue that a number of charities have begun to explore is to charge for services that have previously been provided for free or develop new services to drive unrestricted income. (And of course some organisations have even been set up as social enterprises, consciously avoiding grant aid income altogether.)

But what seems easy in spirit needs some practical and pragmatic thinking. =mc's experience of developing earned income strategies has taught us that there are seven practical questions you need to consider before launching your 'get rich quick' scheme.

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## 1. Where's the focus – mission or money?

There is one overarching conflict that needs to be resolved. Put simply, this is whether the earned income service is primarily aimed at delivering mission or returning money. Charitable objectives and profit can co-exist but it's harder than it might seem at first.

Our experience has shown that earned income services can, and do, deliver on both mission and money but one of these needs to be prioritised for real success. The question is... which one? Our suggestion is to ensure you **can** make money first

Sometime charities seem to have a confused Robin Hood-type approach. (So the 'savvy' Robin fundraiser began by stealing from the rich and then helping the poor. A 'confused' one would have been so obsessed with developing processes to give away to the poor that he forgot to steal from the rich. Result: the poor let down.)

A child protection agency had to play 'hardball' with a number of commercial firms – holiday companies, football clubs, etc – to insist they paid for child protection training. (Donor money subsidising commercial companies wasn't right). The charity wanted to build good practice across organisations – but had to make money. And it had to make the organisation value the work.

Decide on your focus. Make sure you can make the money first before factoring in how to spend it.

## 2. Where's the added value?

If your organisation is moving from providing free or subsidised services to charging for them there will be pressure to distinguish the added value that users/customers are likely to get in the new situation.

You will need to be able to show that your service is worth paying for and be prepared for the fact that users/customers will become more demanding. For example, as a result of moving from a free to a paid-for service a carers' charity found that customers/service users began expecting a much higher quality service – even though the service was already fantastic value. But the introduction of payment changed perceptions. Managing these perceptions is a key marketing skill.

Simply offering the same service for money will go down badly – you need to change the proposition

## 3. There may be a gap in the market but is there a market in the gap?

You will need to conduct some research into the feasibility of your proposed services to ensure that there is a market for them. Ideally do this by conducting a small scale market test with potential customers to determine whether there is interest in your service and what the likely price point is. You can do this by trialing an experiment in one area, or with one cluster of customers.

A note of warning: simply asking people for their opinion in focus groups or surveys isn't enough. You often get a false or unreal answer to a hypothetical question – either positive or negative. A real 'test' is necessary.

You also need to ensure that there is a market for your service at a price that makes it worthwhile to you. (Make sure you include the full cost of service delivery in your calculations). One way to summarise this approach is in the phrase: 'there may be a gap in the market but is there a market in

## 4. What are the start-up costs and how will you meet them?

You'll need to understand and work out the likely initial costs of setting up a service and establish how you can meet these costs. It can take several years to make a real profit or surplus, especially if you need to put capital into the set up. So while you can show a profit on a rolling basis the capital challenge may have to be addressed in some kinds of projects, for example setting up a café, or providing social housing. There may be significant capital needed, your profits should cover this cost over a 3–5 year period.

Alternatively, there may be opportunities to access capital funding from external agencies and you should explore this potential. There are a number of potential sources such as foundations, government funds, EU, and even the national lottery. An animal welfare charity we worked with were able to attract a grant as capital from a progressive foundation allowing them to set up an award and accreditation scheme. The foundation was happy that the service would be sustainable after the initial grant.

Some innovative charities are issuing charity investment bonds, which pay interest to donors as a way to raise funds for their earned income strategies. So in a recent example a disability charity

## 5. Business to Business (B2B) or Business to Consumer (B2C)?

You will need to decide whether the services that you offer will be primarily provided to 'businesses' (B2B) – including other charities – or to individuals (B2C). This choice will help you target your services and set up business processes according to different needs. B2C selling – for example 'selling' care services to elders – will require a larger volume of invoicing and will also involve a higher number of relationships to manage. So any charity or public agency will need to ensure that they have the resources and processes to manage this.

B2B relationships are likely to mean fewer, larger invoices, and fewer, more important relationships with key decision-makers. An example of a B2B business was the theatre that sold presentation skills training – delivered by actors – to management consultancies. The theatre was able to charge higher fees, but needed to deliver an exceptional high impact experience for a small number of people.

## 6. Existing or new legal structure?

There are two ways to organise your service from a legal point of view.

One is to fit it into your existing legal structure. Setting up an earned income function within the existing structure can be relatively simple and straightforward (the one big issue might be VAT registration). You may only need to designate some staff time and create some new budget codes. But there are concerns – if the service runs into trouble the main legal structure could be at risk – and Board or trustees may be liable. Note that the 'risk' is contained in the main structure so if anything goes wrong the whole organisation could fold.

The other option is to have an external freestanding service contained in a separate legal entity – typically a community interest or guarantee company. This could also involve having different branding and staff. This approach is more complicated financially and legally with more bureaucracy. But it's much safer if anything goes wrong either financially or reputationally.

## 7. Do you have the people and skills needed?

Staff may need a different set of skills to be effective in an earned income setting, different from those needed to simply to deliver a free or subsidised service. So, for example, if you run a free funding advice service for small voluntary organisations then the key issues are simply being able to offer good advice, to manage your time, and customer care.

But the skills to 'sell' such a service and generate income might include marketing to key audiences, the ability to work within customers' different requirements, pricing skills to cost work, timekeeping skills to cost time, and competitor analysis to decide a price point against other paid-for services. You may even need a skill such as debt management if people are poor payers!

You also have to decide if the best way to acquire these new skills is to train existing staff or to hire new staff. Training is an investment in people so it may seem obvious. But you may encounter some resistance as existing staff react to the new approach compared to the more comfortable previous way of working. ("I didn't join this museum to be a salesperson.") On the other hand hiring new specific staff can be really expensive.

We've run a number of commercial awareness programmes for agencies – especially local authorities – that focus on making sure everyone understands the importance of 'commercial awareness'. That tends to put any sales, etc into context.

And here's a bonus consideration...

## 8. Does your plan pass the stress tests?

After you have gathered all the information described above, you'll want to make a business plan. This is generally a very pretty shiny thing full of excel sheets...and good to do. But it's only a plan – and our key message is that things change. So you need to undertake a risk and sensitivity analysis.

The purpose of this analysis is get an understanding of what might change in the plan, how likely these changes are to happen, and what kind of impact, + or – , these changes might have on your earned income.

Examples of risks might include: changes in the cost of providing your service – such as petrol, rents etc, changes in the ability of your customers to meet your charges such as reductions in benefits, or changes in the demand for your service such as growth in numbers of older people.

Running a business is in many ways more complicated than running a charity – it's not an easy option. But, thought through, it does represent an exciting new approach to sustainability

## What's next?

If you would like more information on this article, or are thinking of setting up a earned income service in your organisation please don't hesitate to contact Bernard Ross, Director, on 020 7978 1516 or email [b.ross@managementcentre.co.uk](mailto:b.ross@managementcentre.co.uk). We can help with:

- auditing your commercial potential – so you get a clear picture of what you can achieve and what investment is needed
- developing a commercial strategy – so you know what to do and can share it with everybody involved
- commercial awareness training – so your staff and managers can develop the skillsets and mindsets needed to win new, and retain existing, customers