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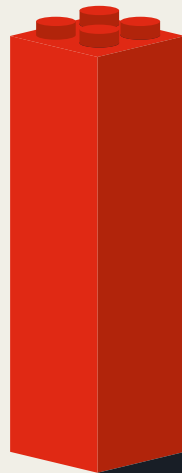
*The Royal Society
of Edinburgh*

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Report

The economic contribution of the third sector in Scotland

The RSE Economy and Enterprise Committee



Executive summary

- The third sector – which includes charities, community, and voluntary groups and other non-profit distributing organisations – primarily provides services which are important in reducing inequality and disadvantage and improving health, wellbeing, housing, and community cohesion.
- Despite the inherent complexity of the third sector highlighted in this report, its economic contribution, through employment, purchasing and commercial activities, remains substantial with many analyses showing it to be greater than other sectors including health and life sciences and creative industries, which enjoy considerable Scottish Government support
- By contrast, the third sector is often overlooked as a source of wealth generation and seldom included in national or local growth strategies. The RSE believes this could mean opportunities to enhance regional and national economies are missed.
- The purpose of this paper is to highlight some of the barriers to a wider recognition of the third sector's economic contribution and to stimulate debate on how these blocks might be overcome.
- This paper was based on interviews with and contributions from a number of participants in third sector organisations and followed by a roundtable discussion hosted by the RSE.

Problem of definition

1. Despite work by voluntary sector organisations like the Scottish Council for Voluntary Organisations (SCVO) and public bodies like the National Audit Office, there is a lack of consistency in applying definitions of what constitutes the third sector. Some organisations have charitable status and so file accounts with the Charities Regulator (OSCR in Scotland). Some organisations (including some charities) are constituted as companies limited by guarantee and are obliged to file accounts at Companies House. But there are many community and voluntary groups which have no formal legal or charitable status.

2. This is not just a Scottish issue. Professor Mairi Spowage, Director of the Fraser of Allander Institute (FAI) at the University of Strathclyde, singles out the problem of the UK National Accounts definition of Non-Profit Institutions Serving Households (NPISH). In the rest of the UK, this sector is made up of universities and colleges, trade unions, political parties, and all charities, which generate less than 50% of their income from trading and so are dependent on donations. Charities which fail this test are treated as private-sector organisations.¹

3. We understand the inclusion of universities is being reviewed by the Office of National Statistics (ONS) and the situation in Scotland is different because colleges are considered public bodies, and thus not included in NPISH. Another problem identified by Professor Spowage is that the data used to classify (and quantify in GDP estimation)

charities come only from England and Wales. There has been no work to ascertain whether including Scottish data would lead to different outcomes.

4. FAI and SCVO have started to look at the charity registration list to see how the charities registered express sales or their economic case. This was then linked to industrial codes standard industrial classification of economic activities (SIC) in an attempt to see which organisation passed the market test. Good progress was made, and there was much interest in looking at the economic contributions at the UK Government level.

5. This has led the ONS and the Department for Culture, Media and Sport to explore the potential of creating a Satellite Account similar to the Tourism and Household Accounts. Satellite economic accounts consider other factors that traditional economic accounts would not usually include and expand the definitions to fit the specific sector.

6. Much of the discussion has been on defining the sector, and there have been a number of strands of work by the Economic Centre for Excellence looking at the practical issues and how we should link the sector to the impact measurements normally used when looking at the economic accounts of other sectors. However, this has proven difficult.

7. There is clearly a need for more research, and FAI is currently exploring funding options with collaborators across the UK and internationally to invest in this work. It is also actively seeking to discuss the importance of better measurement of the sector with policymakers in Scotland and across the UK.

¹ Spowage, M. (2022) 'The challenges of measuring the economic contribution of the third sector' SCVO [online] Available at: <https://scvo.scot/p/49011/2022/02/28/the-challenges-of-measuring-the-economic-contribution-of-the-third-sector>

Problem of measurement

8. If the third sector cannot be adequately defined, it cannot be properly quantified, let alone measured. Professor Spowage says third sector organisations contribute significantly to most sectors of the economy. FAI has estimated the economic impact of some individual organisations, and there have been studies (of varying quality) carried out by other universities and consultancies to measure the impact of particular charities. Yet in Scotland, there has so far been no attempt to estimate the overall economic contribution of the third sector. Professor Spowage asks: *“What would our economy look like without third-sector organisations?”*²

9. Recently, FAI has been working towards an answer by trying to use the national economic accounts to quantify the sector and to estimate the economic value in terms of jobs and gross value added (GVA). An article for the Scottish Council for Voluntary Organisations (SCVO), outlined some of the problems involved in this work.³

10. The lack of an agreed definition leads to some wide variations in estimates of the economic contribution of the sector. The 2021 Social Enterprise in Scotland Census, for example, estimated that there were over 6,000 ‘social enterprises’ in Scotland, providing nearly 90,000 full-time equivalent jobs and adding £2.6 billion in Gross Value

Added (GVA) to the Scottish Economy. It provides a definition of ‘social enterprise’ and a justification for that choice.⁴

11. But SCVO’s Sector Stats for 2022 adopted a wider definition. It estimated that there were 46,500 charities, community groups and social enterprises active in Scotland and that between them, they had income of £8.5 billion and spent £7.9 billion. They employed 135,000 paid staff and were supported by 1,182,000 volunteers. Small charities (under £100k and new charities) make up 80% of the charity sector in terms of number of organisations, but account for only 4.5% of its annual turnover – a large social impact but only a small financial footprint. Large charities, with incomes over £1m make up only 3.5% of the sector, but these 843 charities account for 80% of the sector’s annual income. Social Care and Housing account for over half the Scottish charity sector’s income (£3.6bn).⁵

12. Despite the pandemic impacting negatively on many organisations, the charity sector saw a small 2% (£148m) rise in income between 2020 and 2021. However, in real terms, this results in a -3.3% drop in sector income due to rising inflation rates.⁶

13. The RSE argues that it is possible that both the Social Enterprise Census and SCVO’s estimates are reasonable and consistent with each other. Still, without further work, it is impossible to state definitive numbers for the contribution the sector makes.

² ibid

³ ibid

⁴ Social Enterprise In Scotland (2021) ‘Census 2021’ [online] Available at: <https://socialenterprisecensus.org.uk/wp-content/themes/census19/pdf/2021-report.pdf>

⁵ SCVO (2022) ‘SCVO Sector Stats 2022 – key stats’ [online] Available at: [0693z00000YRi7XAAT-SectorStats2022_keyfigures.pdf](https://storage.googleapis.com/0693z00000YRi7XAAT-SectorStats2022_keyfigures.pdf) (storage.googleapis.com)

⁶ ibid

A significant contribution

14. If either of these estimates are anywhere near accurate, then the third sector is a significant player in the Scottish economy. By comparison, Health and Life Sciences, a sector strongly supported by the Scottish Government, public agencies, and universities, is estimated to employ 40,000 people and contribute £2.6 billion to GVA. The Creative Industries and Gaming are estimated to employ 90,000 and contribute £4.4 billion, and Chemical Sciences employs 11,000 and contribute £1.4 billion.⁷

15. Some of the ways in which the third sector contributes to the economy are obvious – as an employer, through its purchases of goods and services and as an investor in buildings and equipment. Some large charities hold significant reserves, which may be on deposit with banks or invested with financial institutions. The retail contribution of charities and community groups is more noticeable, and some charities have large retail businesses. The number of charity shops on the high street is sometimes seen as a sign of economic distress, yet many are in affluent or high-footfall locations. The traditional image of a charity shop is also being challenged. Some are specialising – in books, videos and DVDs, or recorded music, for example – or moving upmarket by selling designer clothing.

16. Other contributions by the third sector may be less apparent, but still make significant contributions to the 'GDP economy' and, more widely to the 'wellbeing economy.' Many organisations

enable people to enter the workforce by providing skills or workplace training or enable them to remain employed by providing support at times of personal or community difficulty or by providing childcare. Volunteering in a charity or community organisation helps people gain skills and confidence that they may use to get paid work elsewhere.

17. The third sector can also act as an enabler of other organisations' economic activity. By helping to provide settled and viable communities, they can help to provide an environment in which purely commercial activities can flourish. Their partnerships with commercial organisations can help to demonstrate social impact to their customers and staff.

18. Lastly, third sector organisations can help to reduce public expenditure, either by providing services in health, social care, or education, which the state would otherwise have to provide or by reducing the need to use public services. Homeless people are frequent users of medical services. For example, one homeless charity's work has been shown to reduce patient readmittance to hospitals by two-thirds.⁸

19. The third sector is not homogeneous. SCVO identifies social care and housing as the two largest activities by income, followed by culture and sport, community work, education, health, and religion. The Social Enterprise Census takes a different approach, using the number of enterprises as a measure. However, these organisations can vary from small, local organisations staffed entirely by volunteers to national or international charities, employing hundreds or even thousands of people:

⁷ Figures from [Scotland.org](https://scotland.org).

⁸ Cyrenians Impact Report 2022 [online] https://cyrenians.scot/assets/000/000/955/Impact_report_2022_%28web%29_original.pdf?1665387484

	Number of Social Enterprises				% of all 2021
	2015	2017	2019	2021	
Community centres and halls	846	971	1,005	1,022	17%
Arts and creative industries	708	777	816	839	14%
Health and social care	623	659	755	795	13%
Early learning and childcare	670	708	667	604	10%
Tourism, heritage and festivals	243	361	365	363	6%
Sport and leisure	228	254	318	341	6%
Property, energy, utilities and land	238	307	315	321	5%
Information, consultancy and support	250	223	269	292	5%
Education, training and employment	222	262	297	282	5%
Housing	264	226	228	217	4%
Retailing	136	182	218	210	3%
Environment and recycling	156	153	179	197	3%
Food, catering and hospitality	78	106	138	151	3%
Transport	82	108	110	108	2%
Financial services	138	121	112	104	2%
Other	317	182	233	201	3%
ALL SOCIAL ENTERPRISES	5,199	5,600	6,025	6,047	100%

20. The RSE contends that what is clear is that third sector organisations play a meaningful part in a number of different industries, and how we capture that in a more robust and consistent way across these different industries is really important, given the huge variety of ways the sector is currently classified.

Is there an advantage to exploring the soft economy?

21. There is an important relationship between the third sector, the private sector, and the public sector. The three sectors are the pillars of society and are crucial for Scotland's success.

The third sector supports the public sector, wider society and the wider economy. Facilities such as hospices, community mental health and wellbeing initiatives, and emergency housing make potentially considerable savings to the public purse. However, it was recognised that there is a complexity in measuring this via funding streams, as third sector work can span across different government departments simultaneously.

22. The quality of third sector services is also an important reason to value its impact. Data shows that social care services regulated by the Care Inspectorate suggest that the performance of third sector care providers is usually of higher quality than social care services in the private sector.¹⁰

⁹ Table from Social Enterprise Census 2021 (<https://socialenterprisecensus.org.uk/wp-content/themes/census19/pdf/2021-report.pdf>).

¹⁰ Bach-Mortensen AM, Montgomery P (2019) 'Does sector matter for the quality of care services? A secondary analysis of social care services regulated by the Care Inspectorate in Scotland' *BMJ Open* 2019 [online] Available at: <https://bmjopen.bmj.com/content/9/2/e022975> (Accessed 02/08/2023)

23. The Community Foundation has been attempting to assess these trends throughout the Northwest of England (and has now extended into Wales) since 2008. In their November 2002 report, one of the areas of focus was the economic contributions of the third sector, and they used proxy measures for their evaluation, with the understanding that the economic impact of the third sector cannot be evaluated by traditional economic measurements such as GDP. Using these proxy values, they looked at third-sector activities and estimated its social and economic value.¹¹

24. The third sector's contribution to public service and civil society helps create an environment for business and investment. A measurement which takes into consideration the aspects of society that the third sector supports would be helpful for making the case for the sector's importance to policymakers. There are various ways to measure its impact, with hard data such as employment figures and volunteers etc., but there also needs to be a systematic means of measuring social return on investment.

Opportunities for involvement

25. The lack of an agreed definition (or even title – social enterprise or not-for-profit are sometimes used in place of third sector) and approach to measurement means that often the potential contribution of third sector organisations to national or regional economic development programmes is underplayed or overlooked altogether.

26. One of our interviewees cited a *"cultural resistance"* to involving charities and other social organisations in programmes. *"I can call up the chief executives or chairs of the national agencies, and they speak warmly to me, but when it gets to the local level, it is a different story."*

27. Another commented: *"My experience is that there is a wide range of approaches, often depending on the individual official involved. I have had some public bodies initially reluctant to work with us because we are a charity and seen as less 'serious' or 'professional' in our approach. However, this tends to come from an individual who may have limited experience or breadth of vision about the role of the voluntary sector."*

"Usually, this can be overcome by working through the relationship and helping show the degree of professionalism the voluntary sector brings. For example, some NHS colleagues are surprised by the level of regulation, scrutiny and clinical governance oversight that is directed towards charity-run healthcare services, often far more than is directed to the NHS itself. Good interpersonal relationships are key, plus a willingness to work in deep partnership."

"My sense, however, is that this is not the norm, at least for us, where the nature of our work and the reputation of the organisation often open doors to create engagement with councils and public bodies. That is always helped by enlightened leadership in those bodies: the best have chief executives who actively court local charities and seek to support them."

28. The RSE highlights the importance of personal relationships in breaking down this resistance, but it is not universal. It is often easier for third

¹¹ Community Foundation (2022) 'Third Sector Trends in England and Wales 2022: Sector Structure, Purpose, Energy and Impact' [online] Available at: <https://www.communityfoundation.org.uk/wp-content/uploads/2022/11/Third-Sector-Trends-in-England-and-Wales-2022-structure-purpose-energy-and-impact-November-2022.pdf>

sector organisations to work with smaller local authorities than large ones, one respondent giving the example of a council where there is an excellent relationship with one department but indifference from another.

29. At a regional and national level, the contribution third sector organisations could make is often undervalued or overlooked. For example, the Integration Joint Boards for the Health and Social Care Partnerships require third sector representation, but the representative does not have a vote.

30. The Scottish Government's National Strategy for Economic Transformation (NSET),¹² for example, does not include any third sector organisations in its list of stakeholders for its Programme 1: Entrepreneurial People & Culture, even though there are certainly some high-profile social entrepreneurs in Scotland. Nor are any listed in Programme 2: New Market Opportunities, even though the Social Enterprise Census indicated that 7% of organisations in its sample had exported in the previous 12 months.¹³ (This compares with 16% of small businesses which export.¹⁴) The same is true of Programme 3: Productive Businesses and Regions and Programme 6: A Culture of Delivery.

31. The third sector is included in the list of stakeholders for Programme 4: Skilled Workforce, where a number of social enterprises are involved in skills training, and in Programme 5: A Fairer and More Equal Society, which underpins the activities of many social economy organisations.

32. During the engagement with third sector stakeholders, it was noted "the

appointment of a third sector leader – as one of the 11 board members of the NSET delivery board may help to bring more attention to the contribution that third sector organisations can make. But some institutional barriers: funding for entrepreneurship, for example, comes from different departments of government for the third sector and the commercial sector – that makes a statement."

33. *"Even the language we use is different. The 'wellbeing economy'" and the need for 'green jobs' are acknowledged at the policy level, but we struggle to articulate what they mean in practical terms. We need a different mindset, one that sees what the third sector does as valuable and values it."*

34. *"NSET understand that the third sector makes an economic contribution. However, the challenge is understanding what that contribution is. It was noted that one of the difficulties with attempting to gain recognition for the sector within the strategy is whether the sector has more of a supportive or core contribution to the economy."*

35. Scottish Enterprise does support not-for-profit organisations through Co-operative Development Scotland, which aims to promote employee ownership, but it is only one type of social enterprise. However, most of its programmes are aimed specifically at commercial organisations, and there is no specific mention of the role of social enterprise, even in areas such as the promotion of women leaders or inclusive growth where the third sector has something to offer. According to the Social Enterprise Census, 71% of organisations sampled are led by women (up from 50% in

¹² For more information, see: <https://www.gov.scot/publications/scotlands-national-strategy-economic-transformation-delivery-plans-october-2022/pages/2/>

¹³ Social Enterprise In Scotland (2021) 'Census 2021' [online] Available at: <https://socialenterprisecensus.org.uk/wp-content/themes/census19/pdf/2021-report.pdf>

¹⁴ Scottish Government (2023) 'Small Business Survey Scotland: 2021' [online] Available at: <https://www.gov.scot/publications/small-business-survey-scotland-2021/pages/trade-activities/>

2015).¹⁵ This compares with 14% for small and medium-sized enterprises generally in Scotland. The figures for leaders from Black or Ethnic Minorities are 5% and 2%, respectively.

36. Social enterprises and voluntary organisations are major employers and have a good record in paying the living wage, offering flexible working arrangements and employing people from other minority or disadvantaged groups.¹⁶ They are also open to employee involvement, although there are some areas where the third sector lags behind, in closing the gender pay gap, for example.¹⁷

37. However, it was welcomed to see that there was mention of social enterprises in a recent report aligned with NSET, *the Entrepreneurial Campus*, which looks to build entrepreneurial development in Scottish Universities, had a large focus on social impact.¹⁸ This is important in terms of achieving parity of recognition within the economic strategy, as many social enterprise organisations struggle to access mainstream business support and infrastructure.

Current and future challenges

38. The SCVO findings in its Spring 2023 Tracker¹⁹ revealed considerable reports of uncertainty for many third sector organisations. The top three challenges reported by charities are, rising costs and/or inflation (45%); difficulty fundraising (35%); uncertainty about the future (34%):

39. SCVO comments that more organisations are feeling the impact of rising costs, inflation, and other financial pressures. Core operating costs continue to rise, with more organisations reporting a negative impact on their ability to deliver services. In addition, difficulty fundraising continues to be a perennial issue for around a third of organisations, with over half applying for additional funding to combat rising costs.

40. Funding delays and cuts, whilst not appearing to be prevalent, cause additional financial uncertainty for organisations.

41. Two-thirds of organisations would like to see more funding made available to help with rising costs, with 40% wanting specific help with energy costs.

¹⁵ Social Enterprise In Scotland (2021) 'Census 2021' [online] Available at: <https://socialenterprisecensus.org.uk/wp-content/themes/census19/pdf/2021-report.pdf>

¹⁶ SCVO (2022) 'SCVO Sector Stats 2022 – key stats' [online] Available at: [0693z00000YRi7XAAT-SectorStats2022_keyfigures.pdf](https://storage.googleapis.com/0693z00000YRi7XAAT-SectorStats2022_keyfigures.pdf) (storage.googleapis.com)

¹⁷ Close the Gap (2022) 'Gender Pay Gap Statistics' [online] Available at: <https://www.closethegap.org.uk/content/resources/Gender-pay-gap-statistics-paper-2022.pdf>

¹⁸ For more information, see: <https://www.gov.scot/binaries/content/documents/govscot/publications/strategy-plan/2023/06/entrepreneurial-campus-higher-education-sector-driving-force-entrepreneurial-ecosystem/documents/entrepreneurial-campus-2023-ross-tuffee-professor-joe-little-higher-education-sector-driving-force-entrepreneurial-ecosystem/govscot%3Adocument/entrepreneurial-campus-2023-ross-tuffee-professor-joe-little-higher-education-sector-driving-force-entrepreneurial-ecosystem.pdf>

¹⁹ SCVO (2023) Scottish Third Sector Tracker' [online] Available at: https://storage.googleapis.com/scvo-documents-evidence/0693z00000fMjPGAA0-wave6_summary_report_final.pdf

This comes after a quarter of organisations said that the practical and financial support available to help with rising costs was not very sufficient, and an additional 15% said that it was not at all sufficient.

42. Financial reserves remain important to the survival of many third sector organisations. However, almost half of those organisations using reserves feel this use to be unsustainable. This wave also saw an increase in the number of organisations reporting that they had access to less than six months operating costs in their reserves.

43. Despite these financial pressures, 60% of organisations report reducing the cost of their services or making them free to support the communities they serve as the rising cost of living continues to have a detrimental impact on peoples' lives.

44. While financial pressures are prevalent, staffing and volunteer issues remain high too, with volunteer shortages the response option most frequently ranked as organisations number one challenge. Many organisations report increasing the pay offered to new and existing staff and offering more flexible working conditions to attract and retain paid staff.

45. In the face of these challenges, most organisations remain confident of their future survival, although the percentage of organisations that are very confident has dropped.

Next steps

46. The RSE would welcome comments, additions or criticisms of this paper and will actively seek engagement with the Scottish Government, public bodies, MSPs and other interested parties to discuss its contents. If you have any enquiries about this advice paper or if you wish to engage with the RSE, contact Stephanie Webb, Policy Advice Officer (swebb@theRSE.org.uk).



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SCOTTISH CHARITY NO. SC000470

22–26 George Street
Edinburgh
EH2 2PQ

Telephone: +44 (0)131 240 5000
Email: info@theRSE.org.uk

Discover more at rse.org.uk