

# SURPLUSES AND DEFICITS – SOME KEY RESOURCE MANAGEMENT DILEMMAS FOR HUMAN SERVICES NONPROFITS

Ian Bruce, Director, Centre for Charity Effectiveness, Cass Business School, City University, London, UK

[i.bruce@city.ac.uk](mailto:i.bruce@city.ac.uk)

## Introduction

Mr Micawber in Charles Dickens' novel David Copperfield observed

*"...if a man had twenty pounds a year for his income and spent nineteen shillings and six pence he would be a happy, but if he spent twenty pounds and one penny he would be miserable.."*

This reflects experiences for many human services non profits, especially those which have low reserves to fall back on in times of deficit. There is much discussion in the sector and beyond of sustainable funding and the dilemmas that waxing and waning income generate. It is widely assumed that nonprofits which attract significant non- tied or non earmarked income from sources such as bequests or legacies are in more advantageous positions to withstand pressure on fee and fundraised income through the use of cushions of reserves built up over years of surpluses. Although this will be true in many cases, apparent superfluity produces its own dilemmas. This paper chronicles and explores the financial resource management in one leading UK nonprofit, in this position, the Royal National Institute of the Blind (RNIB). It presents a chief officer's perspective on the RNIB' strategy over time, (the author was Director General between 1983 and 2003); identifying distinct phases in the development of the RNIB resource management strategy; and considers wider learning implications for the nonprofit sector.

## The Royal National Institute of the Blind: its organisation, purposes, finance and context

The Royal National Institute of the Blind is among the larger UK charities with approaching 3,000 staff, over 400,000 volunteers running 60 different services on 42 different sites across the four countries of the United Kingdom. Annual expenditure in 2003/04 was around £90 million (\$160m US or \$211m Ca). It reaches around 400,000 blind and partially sighted people with services. It has a membership of blind and partially sighted people and there is a legal requirement for more than half of its elected Board of 24 people to be blind or partially sighted.

The RNIB's philosophy is to try and base everything it does on the needs and wishes of blind and partially sighted people. (Bruce, 1998) This is largely delivered through the governance structures described above; also through extensive consumer research, and through interest shown in the views of frontline staff. Interactions between these inputs have established RNIB's vision and mission. Its vision is : *" a world where people who are blind or partially sighted enjoy the same rights, responsibilities, opportunities and quality of life as people who are sighted"*. Its consequent mission is *"to challenge blindness by empowering people who are blind or partially sighted, removing the barriers they face, and helping to prevent blindness"*

RNIB's key activities can be divided between direct services to blind or partially sighted people, indirect services which try and influence other service providers who impact directly on blind or partially sighted people, political lobbying and campaigning, and voluntary fundraising. Its direct service roles include provision of schools, colleges, and libraries on tape and in braille and electronic format. ('RNIB Talking Books' is probably one of its best known brands.) Other services include residential homes, over 600 different technical aids to support daily living, rehabilitation services (primarily for people losing their sight), social rehabilitation and employment rehabilitation. Examples of indirect services are consultancy and training, offered to statutory social welfare services and to commercial organisations (banks, supermarkets, public utilities) on subjects ranging from accessible web design through to braille statement production.

In its lobbying and campaigning work, the RNIB is active in the UK parliament and the civil service, at the European Union level, and the international level via a number of international fora on subjects such as IT and copyright. Its credibility in these areas is established through its long – claimed political, social and technical legitimacy (Taylor and Warburton 2003) In voluntary fundraising it is one of the largest legacy generators, charity direct mail operators, raffle/lottery operators and big gift fundraisers in the UK.

In its income breakdown: approximately 40% of income comes from fees for services primarily paid by statutory authorities on behalf of blind and partially sighted people, but paid also to a small degree by its own beneficiaries as well. Approximately 57% of income comes from what in the UK is called voluntary fundraising including bequests/legacies (32%) and the remainder from other forms of fundraising (25%), primarily big gift fundraising from rich individuals and trusts; sponsorship from corporate firms; a telephone-recruited raffle/lottery; and direct mail. Investment income comprises 2%

Between 1982/3 and 2002/3 expenditure rose from £15.5 million to £90.8m or in real terms (2003 prices) from £33.5m to £90.8m. Expenditure thus more than doubled in real terms. (Up by 171%) Income in that same period increased in 2003 prices from £37.5m to £84.8m also more than doubling in real terms (up by 126%) As can be seen 02/03 was a deficit year of £6m on expenditure of £90m. This deficit was anticipated, although not the degree, and the following year

(2003/04) was £2m with a surplus predicted for 04/05. There was one other period between 83 and 03 when deficits were reported, namely in the economic downturn of the early 90s

### **Three phases of resource, activity and policy planning and implementation**

Over a twenty-year period there have been three distinct strategic phases of resource and activity planning and review in RNIB, with implementation a continuous process. The internal documentary materials cited in the references, on which this work is based, are in the public domain via the RNIB Reference Library. The first strategy period was ten years, shortened to nine years by trustees, was approximately 1985 through to 1994; the second six years, 1994-2000; and the third six years, 2000-2006. (The technical change over date was 31 March in the start and finish year of each period.).

#### **The first strategic period**

This started with approximately two years of review of existing areas of work and potential new ones. By 1986 major conclusions had been drawn and by 1987 these were codified into a strategy entitled "Meeting the Needs of Visually Handicapped People – RNIB aims and strategy" (1987). This appears to have been one of the first conscious and overt exercises in strategic planning in the UK voluntary and community sector, and the first that involved staff at all levels, publishing the results for all to see. As such it attracted a considerable interest among other nonprofits. It had nine policy and service orientated directives and five resource orientated directives. These were fairly open ended i.e. of the "more should be done" variety. This followed the structure of organizational development proposed by Newman (1971) of the need to balance objectives, activities and resources.

The resource objectives were prefaced by a recognition and imperative for growth in order to meet the policy and service (activity) objectives. The resource objectives were comprehensive and demanding. They looked to: raising more government/service income; raising more voluntary/donated income; raising the competence of staff, committee members and other volunteers; developing the organization structure and processes; developing internal and external communications channels; and the development of qualitative and quantitative target setting and review. The organization thus had a broad view of resources, not just money but also people, structures, processes, communications channels and plant.

By 1988 a detailed development programme with closed objectives was voted upon by the Board and agreed. Although it was a nine year strategy period there were major reviews after four years and eight years which resulted in significant revisions to the resource and activity programme. The first four years were ones of substantial surpluses, the next four ones of breakeven/deficit and the final two, ones of significant surpluses

#### **The second strategic period 1994- 2000**

In this period, the strategy took the form of identification of five strategic priorities which constituted twelve service objectives and sixteen resource objectives. These were less prescriptive on method/activity than the first strategy's development programme but did set closed targets – in

other words a typical mechanistic strategy approach. (Hatch 1997) The first period of the strategy was marked by significant financial surpluses consolidated in the second period by breakevens. These positive signs along with a strong stock market, encouraged significant investment decisions in organisational growth and renewal, in particular a new digital system for Talking Books costing £15m ( \$26m US or \$35m Ca).

### **The third strategic period**

This started in 2000 and is due to finish in 2006. This strategic period has also identified relatively few priorities; with "six strategic directions" set out. However, this time, there was no attempt to set a list of closed ended objectives at the outset, except to honour the decisions of the last strategy. This approach aimed to achieve a more summative or bottom up strategy- process within RNIB. This took the form of asking for, and encouraging activity units to put forward their objectives and activities to contribute to the six priorities, deliberately enabling an emergent strategy approach. (Hatch 1997) For reasons of resource constraint (primarily money) and a newly elected Board with new approaches, this was modified after two years to identify around 30 priority activities or areas where the corporate centre of RNIB has a major role to prioritise and encourage; while the remaining unprioritised strategic areas and activities continue to provide a bottom up contribution. Unexpectedly severe bequest/legacy falls combined with the dramatic stock market falls in the early 2000s depleted reserves at a time when earlier commitments to capital investment in services came to fruition, made their mark. After more than a decade of annual revenue surpluses the years 02/03 and 03/04 had revenue deficits but 04/05 will see a return to surplus and the reserves have risen back up to policy levels through stock market recovery.

### **Some key dilemmas in these strategic periods**

Financial resource management is demanding and complex for virtually any organization; nonprofits are no exception, where the imperative to 'do good' as well as to 'do well' is ever-present. In its management accounts RNIB has reached its surplus/deficit and reserves targets or thereabouts, in 17 out of the last 20 years contained in these three strategic periods. Despite this success, certain financial resource issues have been hard to manage. From a close review of the three strategic periods, four themes are particularly prominent. These are : planning and delivery on the size of cushioning reserves; whether and how to invest surpluses in revenue as well as capital; seeking one leading income stream or several; and how to avoid becoming financially over-dependent on powerful ,monopolistic commissioners of services . These themes are now discussed in turn, setting out the RNIB experience and reflecting on relevance for other nonprofits.

#### **'the size of cushioning reserves'**

In 1990 RNIB set its first explicit reserves policy, setting its "free" reserves (ie only counting assets which were liquid or easily disposed of) at 21 – 25 weeks of annual expenditure. In the light of experience that target has been incrementally lowered to 11 – 14 weeks but at their nadir in 2003 reserves were at 7.5 weeks returning to 12 weeks in 04. Looking a different way, in 1983 total reserves were the equivalent of 1.6 years of annual expenditure while in 2003 they were 0.9 years.

Some nonprofits have far lower reserves levels than these, but RNIB found them challenging. Why is this? It is especially strange because on the two times in the 20 years they dropped significantly below target, they were built up again rapidly ie within a year or so. One explanation is that a shocked reaction is at best encouraged and at worst necessary to make the organization at all levels realize that decisive and unpalatable action has to be taken to replenish reserves up to levels required by policy. Another explanation may be that members of trustee boards who are ultimately legally responsible, especially trustees with financial roles, are particularly sensitive to adverse signs in the external environment (eg the 1990s the economic downturn and the stock market plateauing) and that the missing of targets is seen as an additional blow to the organisation rather an effect or impact from the external environment

### **Whether to invest surpluses in revenue as well as capital?**

RNIB, as a growing organisation, needed to do both but the rationale and impact were challenging to manage

The seemingly easiest decision for organisations is to invest revenue surpluses in capital projects because they are time limited, do not become part of the continuing revenue commitment; and the organisations have already "saved" the money through surpluses. Often being bricks and mortar, capital projects are eminently "fundraisable". High quality service buildings are attractive to beneficiaries, staff and volunteers, and to commissioners of services contracts. At their best, investments in capital service provision operate both as a resource magnet and a resource generator, driving and supporting revenue based services operating from within them ( eg libraries, schools, service centres ).

Yet in human services organizations, people are the biggest cost and they are revenue not capital. In a needs -led organization overseen by trustees elected from the beneficiary group, there is also a real and continuing push to expand 'people services' to meet unmet need. RNIB would not have more than doubled in service delivery capacity simply by investing surpluses in reserves and bricks and mortar

However, are surpluses used for future revenue expenditure, sustainable? If they are not, or at least the organization is unsure, what ways are there of limiting risk? One way is to create time limited revenue interventions of 3 or 5 years. This caps financial risk but often creates other problems. One is the difficulty of maintaining service quality throughout because staff on 3 year contracts often leave during year three to secure their futures in another job. A second challenge is implementing what often turn out to be optimistic continuation or exit strategies. Either the hoped for income stream to guarantee continuity of the project after the third year has not been secured, or the need which was seen to be solvable/curable within 3 years has proved obdurate. Expectations have been raised among beneficiaries which are shattered by closure of the project and this distress is picked up by donors who become disaffected. In RNIB's case these challenges were infrequent because it had continuously increasing revenue income and so was able to convert projects into permanent services through absorbing them into the main revenue budgets.

But improving revenues were not certain at the time of decision and across the full swathe of nonprofits are frequently not delivered.

### **Seeking one leading income stream or several?**

The traditional or conventional (and sometimes idealised approach) is for organisations to generate several income streams to reduce over-dependency on any one. (Alcock, Harrow et al, 1999) In 1983 RNIB had two major streams, legacies and fee income for services delivered. It had two minor ones, investment income and other fundraising. Over the 20 years there has been a major push and associated investment to grow the two big ones steadily but to help other fundraising catch up. In 1983 other fundraising was 17% of all income, it is now 25%.

However gaining significant voluntary income is in tension with raising fee income from government commissioners and beneficiaries. Both groups may easily say, if you are raising all this "charity" money why should we need to pay "so much" or even "why should we pay at all." Also staff and volunteers, passionate towards the cause, also argue for (greater) subsidy of services "from all this money" so that beneficiaries are not excluded either because they cannot pay or because the government commissioner is not paying enough for a high quality service. The volunteers and staff blame the nonprofit for underinvestment, not the commissioner of services for their under-payment. On the other hand nonprofits with high fee income and low voluntary income may be more driven to negotiate hard and cut service cloth to meet the price. They can also expand faster because they do not build up repeating requirements for charitable subsidy per additional unit of service which drain away precious fundraised income which can rapidly be used up. For example RNIB used to subsidise talking book member subscriptions heavily which meant every new member "lost" money which the charity could not afford. This meant that for a while RNIB could not afford to promote the service to people who needed it for fear it would be oversubscribed with more members than it had the money to subsidise. (RNIB's answer was to move talking book membership fees up, and costs down, towards breakeven levels so that additional members did not require subsidy)

### **Avoiding becoming financially over-dependent on powerful, monopolistic commissioners of services .**

A major and continuing debate of resource management in the UK is that nonprofits are losing their independence and thus their critical and wider contribution to civil society (Salamon and Anheier 1998; Kendall 2003) by becoming over dependent on government money. For some, accepting more than 50% of organisation income from the state is seen as triggering subservience. However there are UK nonprofits which accept resources levels far higher than 50% from government, yet still appear to retain their ability to challenge and critique government . Two examples are Mencap for people with learning disabilities and Leonard Cheshire for people with disabilities, both of which receive over 80% of their income from government sources and still manage to lead challenge and criticism of government policies and programmes where they see this as needed. For RNIB with "only" 40% of its income coming from government bodies, this has not been a problem. In addition the strong stream of fundraised income has paid for the research and staff so essential in vigorous lobbying. So independence may not be constrained by significant payment from government but may be encouraged by significant fundraised income.

One way to attempt to reduce risk of being dominated by the (government) commissioner is perhaps to avoid the large centralised highly monopolistic commissioners in favour of multiple commissioners independent of each other (This has comparisons with commercial companies and their suppliers). However the UK government over the last 40 years has been centralising on many fronts and any major service expansion funded by the state through commissioning from nonprofits is increasingly likely to be through centralized commissioning. This trend increases the power of the commissioner to have undue influence as in "he who pays the piper, calls the tune"

## Conclusions

Drucker (1990) has argued that the multiple constituencies of nonprofits make their work particularly challenging. Nowhere is this more evident than in the area of financial resource management. Meeting the various and often differing needs of beneficiaries, commissioners and donors in the field of resource management is especially challenging for nonprofits. This review of one major UK charity's strategic responses to those challenges is intended to give an insight into their implications for nonprofit organisation strategy generally. The paper has drawn on a unique chief executive perspective over a key and substantial period of the organisation's life, as supplemented with reference to senior-level organisation documentation. It reflects necessarily, the strategic thinking paradigm of the author, as director-general of the RNIB throughout this time. It also therefore begs questions as to the extent to which the analysis would be shared or interpreted differently by board members, donors, services commissioners and users with needs, both met and unmet. This suggests further work, and in particular, analysis rooted in multi-stakeholder theory, as underpinning nonprofits' strategic decision-making; as advocated and exemplified by Bryson (2004). At a wider level, it also follows that an increase in interdisciplinary focus of study on nonprofits' financial resource dilemmas from economists, accountants, marketers, psychologists and others, as well as strategic management thinkers would be especially welcome.

In the current political and social context of non profit working in many countries, beneficiaries have higher expectations and governments (certainly the UK government) are paying more to, whilst demanding more from, nonprofits. Businesses are both concerned about the competitive advantage they perceive some nonprofits enjoy, while bemoaning what they see as the amateur approach some nonprofits take. The donor is also expecting 'more'. In the meantime nonprofits have to struggle through the challenges described above and more. For those practitioners and leaders in the nonprofit field who seek to take the best learning from cross-sectoral management thinking, much theory and practice still appears unsatisfactory. Increased theoretical as well as practice inputs of financial resource management dilemmas for nonprofit leaders is therefore sought. Nonprofit leaders need more predictive capacity. Hindsight is too gratuitous and too late.

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