

With key public services increasingly delivered by the third sector, government now provides 37 per cent of charities' income. Consequently, the sector is becoming increasingly commercial in its finance, with goods and services set to overtake donations and grants as charities' major source of revenue in coming years.

Yet the steady increase in charities' statutory income conceals the inadequate and wasteful way in which government funds charities. Contracts and service level agreements are routinely unstable, undervalued and insufficiently forward-looking.

The system suffers from endemic insecurity. Although many charities cater to service users on a long-term basis, funding remains tied to an annual cycle, so that 93 per cent of Acevo members have annual contracts. In the most extreme cases, charities have to issue redundancy notices every January, only to rehire staff in April when funding decisions are made.

Similarly, government bodies strive to shift as much funding risk as possible onto voluntary providers, regardless of the impact on performance. Those providing employment training, for instance, often find funding depends on the number of referrals made by Job Centre Plus, a factor over which they have no control. So while overhead costs remain relatively stable, income fluctuates wildly. This makes for an unhappy combination.

But the most important point is that these shortcomings actually result in higher costs for the taxpayer. The insecurity forced onto charities through public funding results in unreliable services and escalating costs for the sector's funders.

For this reason, the government's Efficiency Review in 2004 accepted the four key principles outlined in Acevo's *Surer Funding* report: longer-term contracts; full cost recovery; shared risk between funder and provider; and less waste through unnecessary bureaucracy. Yet little progress has been made. Acevo's own research suggests funding practice is actually deteriorating in three of the four key areas, and the forthcoming National Audit Office report on the government's relationship with the third sector is likely to be scathing about this.

So is Compact Plus the answer? To an extent it should address the deficiencies of the Compact Funding Code, which has suffered from a lack of real teeth to improve funding practice. To address this, *Surer Funding* called for new measures from government which would provide real incentives for underperforming funders. These would include an independent champion to identify, criticise and penalise parties for poor practice in contracting, and an accreditation body to kitemark funders that conform with principles for better funding.

Compact Plus proposes both these mechanisms, which have the potential to make a real difference. It also streamlines the Compact commitments, focusing closely on the funding relationship. Still, as drafted, the proposals do not go far enough.

This is because funders will need to opt in to the scheme. Since they will potentially incur costs by doing so, and then face the possibility of being embarrassed in a Compact Champion report, there is little incentive for them to do so.

The obvious answer is to make the proposals universal: they should apply to all funders regardless of whether they opt in.



Taking them on

In March the government launched its consultation on Compact Plus, designed to bolster the Compact. All well and good, says Nick Aldridge, but charities' solution to poor funding practice lies closer to home

Only through universal application, backed by the Efficiency Review, will Compact Plus reach those statutory bodies that have little interest in improving their practice – precisely the ones that need to be targeted. There must also be real penalties for funders that waste public money through poor procurement.

In the meantime, though, the charity sector would be ill-advised to rely on central initiatives to improve local funding practice. Although Compact Plus will apply to local authorities and primary care trusts, it will take time for a “top down” message to bring change. Charities themselves must take charge of their negotiating strategies and get tough with their funders.

Mental health charity Sane, which recently threatened to sue the Department of Health for late payment of a service contract, is not alone in considering legal action against the department.

Many Acevo members are now doing the same, and some do so routinely. Many funders appear not to regard contracts with the third sector as legally binding, regardless of what has been agreed. In these situations, charities must take a firm line.

Of course, negotiation encompasses far more than looking to the courts. Many charities are adopting other “commercial” techniques, such as offering funders a discount for early acceptance of new terms, or raising service quality in return for a longer-term funding commitment. These strategies take time to develop, but offer significant gains for charities and their users. Encouragingly, three quarters of Acevo members now report that government funders are willing to negotiate contracts. And central government itself is also supporting negotiation, with Futurebuilders now beginning to provide training in negotiation skills for successful applicants.

This emphasis is welcome. Contract negotiation is a key skill – and one that needs development. After all, charities that fail to actively secure the best possible contract from their funders ultimately are failing their users.

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