

The three articles that follow by **Sarah Smith**, **Daniel Jones** and **Abigail Payne** are about the inter-relationship between different types of income for charities. Specifically, they look at the extent to which government and grant funding substitute for other forms of income.

Grants and other income

- The first paper focuses on the effect of National Lottery funding through grants made by the Community Fund (the predecessor to the Big Lottery Fund). It finds that being awarded a grant has a positive effect. For medium-sized charities, each £1 of grant money increases their incomes by more than £1.
- The second paper looks at the effect of government grants to charities in Canada. Here, grant income crowds-out other income – by roughly 83 cents for every \$1. Direct donations respond positively, but charities reduce their fundraising efforts, with a knock-on effect on income, and money from other charitable foundations falls.
- The third paper also looks at the effect of lottery money, but focuses on education lotteries run by US states. It finds that the introduction of these lotteries did cause donors to reduce giving to education causes.

On the face of it, these findings appear contradictory, but digging deeper, some common themes emerge that can explain the differing headline results.

First, the importance of government funding varies across charities. Receiving a grant has a more positive effect for smaller charities. For major charities, not only is a single grant a relatively smaller part of their total income, but they are also likely to have a much richer set of alternative funding options.

Second, it matters whether the money is for core activities or for new work. The National Lottery funding is often for new projects which the charity may simply decide not to pursue if the funding doesn't come through. If the funding is for core activities, the charity may try harder to find the funding from elsewhere if they don't receive a grant.

Third, it matters whether or not donors

know about the government grant. The most likely explanation for why the education lotteries had a negative effect was that they were widely advertised: donors responded negatively to a perceived increase in funding for education charities by reducing their donations to this cause. By contrast, the National Lottery funding – and government grants more generally – are widely dispersed so that donors do not know where the money is going.

What does this tell us about the effects of the current public spending cuts? We cannot predict with certainty, but here are some pointers:

- smaller charities are most vulnerable to a cut in spending;
- organisations may fight hard to deliver core services, but sacrifice new projects;
- finally, individual charities should signal loud and clear when they are being hit by cuts in order to attract more donations.

Charities need to signal loud and clear when they are being hit by cuts to attract more donations.

Crowding-out: if a charity receives a grant from the government or another organisation then other donors will react by reducing their donations.

Crowding-in: the opposite effect where government grants attract more income for charities.



DID THE GAMBLE PAY OFF FOR CHARITIES?

THE EFFECT OF NATIONAL LOTTERY GOOD CAUSES FUNDING

The National Lottery widely trumpets the amount of money that is channelled to charities and other good causes; £35 million is allocated to good causes each week, equal to 28 pence out of each £1 spent on the lottery. The overall level of funding is impressive; but what is the net effect of this income on the organisations? **Sarah Smith, Jim Andreoni** and **Abigail Payne** analyse whether lottery funding simply substitutes for other sources of funding, or has a positive effect on total income, helping charities to survive and thrive.



Since the National Lottery began, the good causes funding has played a prominent role. It is distributed by independent bodies across a wide range of projects in the arts, sport, heritage and voluntary sector. For charities, lottery funding is a sizeable source of grant income – they received £0.5 billion in 2010-11 from the National Lottery good cause funding, compared to £3.0 billion in grants from the government.

One strand of the theoretical economics suggests that if a charity receives a grant – from the government or a National Lottery good cause distributor – then other donors will react by reducing their donations.

This may occur because donors respond directly to an organisation receiving a grant, seeing less need for their own funding. An alternative mechanism is that the charities may cut back on fundraising, preferring to devote their effort and resources to their main activities.

The empirical evidence, primarily from the US and Canada, lends support to there being such ‘crowd-out’ from grants to other donations. In order to gain some further insight into this issue in England and Wales, we analysed information on applications that were made to the Grants for Large Projects programme administered by the Community Fund, one of the independent bodies responsible for allocating National Lottery funding (the predecessor to the Big

Lottery Fund). By comparing outcomes among charities that successfully applied for grants with outcomes among charities that applied but were unsuccessful, the research provided new evidence on the impact of lottery funding.

The applicants

The research analysed a sample of 5,000+ applications made to the Community Fund’s Grants for Large Projects programme between 2002 and 2005. This programme was open to all charities seeking funding of £60,000 or more (the mean award in our sample was £151,295). The money typically funded specific projects (i.e. in each case the application described a discrete set of activities to be funded); these could be for the continuation of existing work or for completely new activities. (See box for examples of the types of projects for which funding was sought.)

Information on charity incomes for 2002-2008 was obtained from the Charity Commission register. Given the timing of grant applications, this means that we can follow charities for up to four years after the committee decision. The Charity Commission register covers all charities in England and Wales with annual incomes of £5,000 or more but, in practice, there is a lot of missing information, particularly on sub-components of income. This guided us to looking at the

overall effect of being awarded a grant on charities’ incomes, rather than at specific components of income, such as donations.

Comparing like with like

The effect of receiving a grant on charities’ incomes was measured by comparing the change in income before and after

Examples of projects for which lottery funding was sought

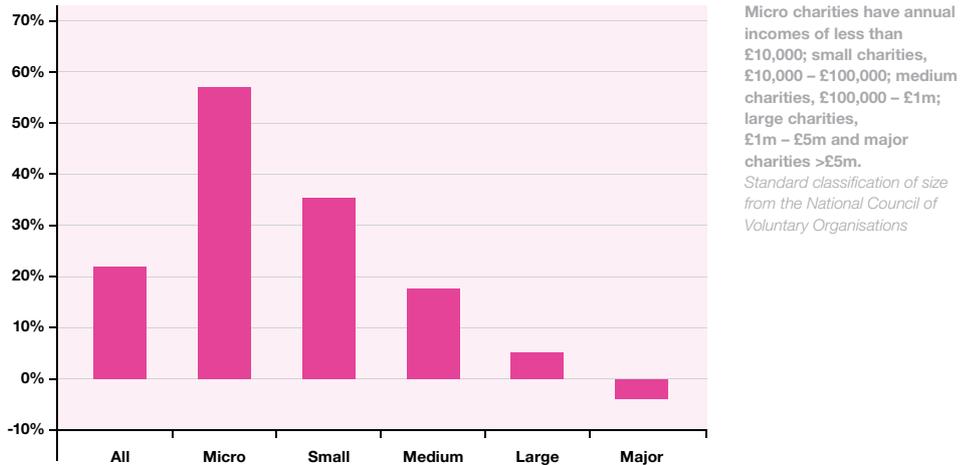
Services: “The project aims to provide a volunteer bureau service for the people living in [the town] and surrounding areas, which will also support people with learning disabilities, excluded young people and older people.”

Staff/training: “[the advice centre] wants to employ a diagnostic interviewer and receptionist to screen and signpost clients to decrease waiting time and increase capacity. Training will be provided to all staff on diagnostic interviewing.”

Capital: “The project will replace a well used Brownie and Guide headquarters. The project will increase and improve activities for children and young people who access the centre.”

National Lottery funding doesn't substitute for other money.

Figure 1
Change in income among successful applicants (compared to unsuccessful)



the committee decision for successful and unsuccessful charities – all of which had chosen to apply for funding and had passed an initial eligibility screening process. This allowed us to compare outcomes for charities that, apart from receipt of a grant, are otherwise very similar.

Looking at this kind of sub-sample is important because charities that chose to apply for a grant are systematically different to the general population of charities. We know this because charities that applied for a grant, but were unsuccessful, experienced significantly higher income growth than a randomly selected group of non-applicant charities from the general population. This means that it is not possible to learn about the effect of lottery funding by comparing outcomes among successful charities with a wider sample of all other

charities. The results in this summary, therefore, compare all successful charities with all unsuccessful charities.

Findings
Receiving a grant makes it more likely that a charity survives

Being awarded a grant directly affects a charity's survival. Although there is no explicit information on charity deaths, "charity exit" can be measured as sustained non-missing income (i.e. a charity for which there is no subsequent income information after the first observed period of missing income data). Controlling for charity size (mean income prior to the award), region and the score awarded by the Community Fund to the application, the exit rate among charities that received a grant was significantly lower than among those that were not awarded a grant.

Receiving a grant has a positive effect on charities' incomes

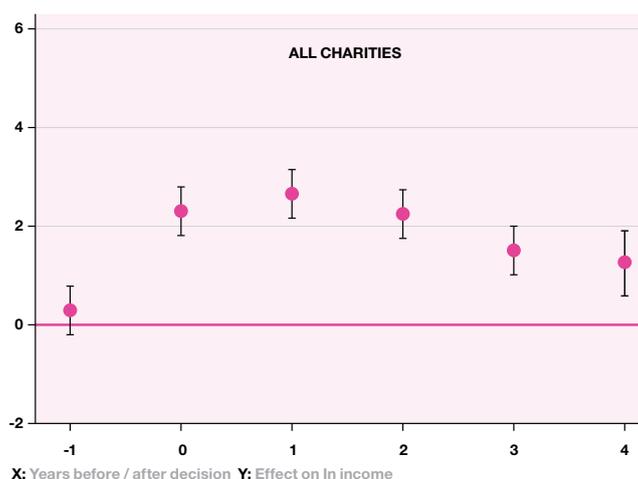
Lottery funding does not simply substitute for other sources of funding. Figure 1 summarises the change in income among charities that were awarded a grant, compared to the change in income among unsuccessful charities that applied but were not awarded a grant (looking up to four years after the grant decision). This shows that, on average, successful charities experienced incomes that were 22 per cent higher after being awarded a grant.

The positive effect of receiving a grant is greater for smaller charities

The effects of being awarded a grant are proportionately bigger for smaller charities than for larger charities, and are negative (but statistically insignificant) for major



Figure 2
Change in income among successful applicants
(compared to unsuccessful) – Individual years
before/after grant decision



Successful charities experienced incomes that were one-fifth higher after being awarded a grant.



charities. This may be because the lottery funding is relatively smaller for these larger charities and/or because they have more alternative funding sources. We return to this below.

The positive effect of receiving a grant persists over several years

Being awarded a grant has a positive (and significant) effect on income for four years. The effect is biggest in year 0 and year 1, but remains positive and significant for up to +4 years after the committee decision was made. Since the payment of the grant could be made over up to +2 years, this means that the positive effect of funding on total income persisted for at least two years after the grant payment period.

This is illustrated in Figure 2 and highlights the importance of making an assessment of the effects of grant funding over the longer-term. Whereas Figure 1 showed the overall effect on charities' incomes of being awarded a grant, averaged over (up to) four years after the decision was made, Figure 2 breaks the effect down by individual years.

Year -1 captures any difference in income growth between successful and unsuccessful charities in the year prior to the committee decision. The fact that this is zero implies that successful and unsuccessful charities were not any different in terms of their trend income prior to the award. This is a robustness check that the difference that emerges after the grant is awarded (in year 0) is attributable to the effect of the grant. It rules out, for example, that grants were awarded to charities that show better (or worse) income growth prior to the committee decision.

Each £1 of lottery funding increases incomes of medium-sized charities by more than £1

Quantifying per pound the effect of lottery funding (whether each pound of grant increased charities' incomes by more or less than a pound in total) reveals that, for small and medium charities, lottery funding crowds in other money. Looking over the longer period (from the year of the decision to +4 years after), each pound of grant increases charity incomes by £1.60 for medium-sized charities. For these charities, this means that lottery funding is actually "crowding-in" other funding and helping them not only survive but thrive.

Being awarded a grant has a positive effect on income for four years.

Why the difference?

Contrary to the North American case our results show strong evidence that lottery funding has a positive net effect on charities. It has helped charities to survive and, for all but major charities, increased their incomes relative to those that applied but were unsuccessful. It means that the lottery award was not simply a one-for-one replacement for other funding.

So, what might explain the difference between the experience of charities in England and Wales and those in North America and what might grant bodies learn that will help them design their funding programmes in order to increase effectiveness?

- **First**, we have shown that size matters. The positive effects of grant funding are driven by smaller charities. A plausible explanation for this is that larger charities can draw on more alternative sources of funding.
- **Second**, the effects of grants persist; it may take several years before the full picture emerges and this should be taken into account in any analysis.
- **Third**, the National Lottery grants examined put sizeable sums into specific (and often new) projects which may help to reduce any sense among potential donors that the money is simply going into a general spending pot for the charity and replacing funding from other sources.
- **Fourth**, because National Lottery good cause funding is widely spread across many projects and areas it may avoid any impression that any particular good cause is being adequately funded by this source. This is very different to the US state lotteries (discussed by Daniel Jones on page 9) which are targeted at one or a few specific causes.

This article summarises Andreoni, J., Payne, A., Smith, S., *Do grants to charities crowd out other income? Evidence from the UK*, CMPO Working Paper 13/301.

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