Making the case for unrestricted funding

A summary of key points for foundation staff and Boards

May 2023

Contents

What is unrestricted funding?

The terms 'unrestricted funding' and 'core funding' are often used interchangeably, but they aren't the same. We use:

- Unrestricted funding to describe no-strings funding that funded organisations can use for anything within their charitable objects.
- Core funding to mean grants restricted to either a specific element of overheads (for example, rental costs or the director's salary) or available to be used for essential running costs more broadly.
- Project funding to mean grants restricted to the delivery of a specific project or defined set of activities, often (but not always) including a percentage contribution towards general running costs.

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The purpose of this briefing

This briefing is for foundations who are interested in unrestricted funding – whether you are unsure about if or how much to restrict grants, through to those who are convinced of the benefits of unrestricted and want to equip themselves to advocate to others.

At IVAR, we believe that unrestricted should be the starting point of every fund – with each restriction having to justify its place. We recognise that some boundaries to funding can be important – for the funder, the funded organisation, or both. But the difference that unrestricted makes to the organisations who receive it is becoming hard to ignore:

> *'Unrestricted funding is the single most powerful thing that funders can do to support charities. It enables us to be agile and decisive in dealing with the ever-changing demands of the current uncertainty, while planning as best we can for whatever the future holds.'*

Restricted funding can be the right choice – but it has not earned its place as the dominant model. There are no definitive answers here, but each thread of evidence – whether from funders, charities or broader research – raises challenges to the idea of restricted funding as a 'more proven' or 'safer' approach. And each identifies ways in which unrestricted funding can deliver benefits that matter to both charities and their funders.

This view is based on over 20 years of research, and reinforced by our growing Open and Trusting community of over 100 funders committed to introducing more flexibility to their funding. In this piece, we consolidate findings from our recent research to support constructive interrogation of how you fund. We draw from:

- **The experience of foundations:** *The holy grail of funding: Why and how foundations give unrestricted funding* shares the practical experience of trustees and senior staff from 12 trusts and foundations, exploring the value of unrestricted and how to overcome common challenges.
- **The voice of charities**: *Get the basics right: findings from the Funding Experience Survey* captures what more than 1200 funded organisations think about how funders can reduce the time, effort and stress of applying for and managing grants. And *In the face of overwhelming need* shares charity leaders' experience of the cost of living crisis.
- **The existing body of research evidence:** *Evidence Review: Why restrict grants?* considers the strength of the evidence in support of the contrasting rationales for restricted and unrestricted funding.

We hope that this briefing strengthens the hand of the many champions of unrestricted funding across the trust and foundation sector. And that it encourages those who are less convinced of the benefits, or wary about perceived risk, to look at the current evidence with an open mind, asking the question: Can we go further?

Unless otherwise stated, all quotes in this briefing are taken from the IVAR publications referenced above.

Why now?

For decades, charities have been telling funders that more flexible, longer-term funding will help them to do a better job. Unrestricted funding is the most flexible form of funding and, for charities, the most precious.

Despite the efforts of pioneers, it has proved remarkably difficult to persuade the majority of funders to move away from restricted project funding and give charities greater control over their own spending. But the Covid experience has turbocharged the momentum for change. And it is maintained by pressing concerns about what it takes for us all to do our best work under the pressure of continuing social disruption, injustice and uncertainty.

Charities' views are clear. 88% agree or strongly agree[1] that:

> *'Giving us unrestricted funding – money that we can spend on anything within our charitable objects – would make a huge difference to our ability to respond to changing circumstances and the things that matter most to our community/cause.'*

And there is increasing recognition of the damage that the dominance of restricted funding is doing to the charity sector's collective contribution both to meeting immediate needs and to delivering longer-term solutions:

> *'Less restrictive and longer-term funding can provide charities with more flexibility and security to invest in better technology, greater levels of innovation, improved management, and development of their workforce. Increasing the quantity and quality of this type of financing is therefore a fundamental first step to boosting charity productivity.'* (Pro Bono Economics)[2]

Many funders are rising to this challenge: more than 100 have joined the Open and Trusting community; flexible funding sits at the heart of their commitments to change.

[1] Based on 1,200 responses to the Funding Experience Survey
[2] (2023). Unleashing the power of civil society. London: Law Family Commission on Civil Society facilitated by Pro Bono Economics.

Why offer unrestricted funding?

In our past research, we have heard from very different foundations about the value of unrestricted funding. Together, they believe that a more trusting and flexible approach to funding helps them to do a better job as funders, and supports better outcomes for the causes and communities they care about.

The 12 foundations who took part in *The Holy Grail,* for example, identified seven distinct but related ways in which giving funded organisations greater control over their own spending adds value:

1. **Better use of expertise.** It respects the experience, skills, and knowledge of funded organisations, freeing them to make informed judgements about the best use of funds.
2. **More flexibility and agility.** It recognises that the future is unpredictable, and it enables funded organisations to manage well in uncertainty, responding quickly to changing circumstances and needs.
3. **More effective work.** It maximises the chances of delivering the greatest positive impact for the communities and causes that the funder seeks to support.
4. **Better relationships.** It helps towards levelling the power relationship and opens the way for greater mutual honesty between funded organisations and their funders.
5. **Building confidence.** A more supportive, less transactional funding relationship delivers a significant boost to funded organisations.
6. **Lighter processes.** It reduces bureaucracy for both funders and funded organisations.
7. **Reduced organisational risk and greater resilience.** It gives funded organisations much greater scope to cover all essential costs, deal with challenges quickly and effectively, and experiment.

By bringing together the experience of those funders with the input of charities and the findings from our review of evidence, we can add depth to four core arguments for unrestricted funding.

Charities understand what's needed

Funders develop strategic priorities so that they can target their efforts on causes they care about or where they feel they can make the most difference. The question is why, having chosen charities who share these priorities, so many then limit their activities through restricted funding. The assumption seems to be that charities are less effective than funders at determining which activities are likely to produce the best outcomes. But, the Evidence Review makes it clear that funders' preference for restricted funding 'because it delivers' rests on familiarity, not on evidence.

By contrast, unrestricted funding represents a shared effort towards a common goal, not *'a purchase of outcomes'.*

'Trustees' fundamental belief is in valuing the expertise of people doing the funded work. Then the question for us is "how do we help them to do what they do and do it better".' (Philippa Charles, Garfield Weston Foundation)

Both funded organisations and funders experience unrestricted funding as helping to level the power dynamic between them. It is seen by funded organisations as an expression of confidence and trust in their experience, skills, knowledge and integrity. And in their ability to manage effectively, spend money wisely and deliver as much benefit as possible:

'It means the relationship feels respectful, equal, stable and empowering – enabling us to get on with the vital work we do.'

When charities feel trusted by their funders, they are *'in the driving seat'* and have *'freedom to act'*.
Research shows that unrestricted funding gives organisations the time, resources and freedom to engage in strategic thinking, leading to improved planning and a stronger focus on making decisions in line with their charitable mission.
Charities report that all of this enables them to make better use of their resources, to be more forward-looking and to achieve better outcomes in a complex and changing environment:

'Ultimately it means that we achieve more, help more people, and make more of a difference.'

A stronger voice for stakeholders

In their assessment processes, many funders look for evidence that organisations are mission-led, collaborative, connected and accountable to their beneficiaries and causes. Some have a strategic commitment to more equity in their grant-making and hearing the voices of people with lived experience. The Evidence Review suggests that *restricted* funding may work against all these aims because charities can experience it as reinforcing an unhelpful power dynamic that privileges funders' concerns over those of other stakeholders.

By contrast, *unrestricted* funding:

- **Devolves power to charities:** This creates more space for them to engage with the beneficiaries and communities directly affected by their work and to make strategic decisions based on <u>their</u> views and priorities, rather than being funder-led.
- **Creates a better environment for collaboration:** Charities that depend heavily on project funding are less able to free staff up to engage in explorative collaborations or sector networks. Organisations are more willing to share ideas and outcomes without feeling pressure to claim credit in reporting on restricted grants.

Agility and adaptability enable effective action

The evidence is clear. Restricted funding can slow down and even prevent charities from adapting as circumstances change, whereas unrestricted funding enables funded organisations to be more agile and adaptable, whether this is in response to new opportunities, changing needs or unexpected events:

> *'Unrestricted funding gives our partners the freedom to be outcomes-focused and community-led. They can do their best in the best way; it enables them to plan and allows them the discretion to stop what is not working and adapt to new realities.'* (Eleanor Harrison, Impetus)

The body of research generated in relation to Covid-19 has considerably strengthened evidence of what can be achieved when small and medium-sized charities are given scope to respond and adapt to changing circumstances and need.

> *'During a period of crisis and rapid change, many small charities have demonstrated incredible resilience in responding to an array of challenges. This resilience has seen small charities first demonstrate absorptive capacity by "soaking up" the unprecedented impact of the crisis on their work, operations, and the individuals and communities they support; and then show tremendous adaptive capacity by responding rapidly and flexibly through incremental adjustments and innovations that have been introduced on an ongoing basis.'*[3]

Charities desperately needed a more settled period as the emergency response to Covid wound down, but instead found themselves coping with the consequences of continuing economic, political and social volatility for the communities and causes they serve – and for their own organisational resilience. Many now see little prospect of an end to this instability. They are weary of short-term, tightly restricted funding when the problems everyone is facing will clearly call for action over the long term. For any funder who wants to equip funded organisations to respond well to volatile and uncertain environments, the argument for unrestricted funding is compelling.

Stronger organisations do better work

> *'When we fund an organisation, we say "we back you and we stand beside you" – and that means their Board, their staff, their strategy, their infrastructure.'* (Dame Rennie Fritchie, Former Chair of Lloyds Bank Foundation for England and Wales)

The argument that unrestricted funding supports stronger organisations stands on a firm footing. There is good evidence that it:

- Improves their strategic planning and helps them to implement their plans, leading to improved performance and delivery against objectives.

[3] C. Dayson, L. Baker, J. Rees et al. (2021). The Value of Small in a Big crisis. London: Lloyds Bank Foundation for England and Wales.

- Enables them to invest in management and administration and to make their own judgements about priorities in these areas.
- Helps them cope with fluctuations in project income, practise strategic reserves management[4] and become more financially stable.
- Gives them more scope to use their staff and volunteers efficiently, to manage them well and invest in their development.
- Reduces the costs of funder compliance and allows them to focus on more meaningful data collection and reporting.

All these benefits are most clearly seen in multi-year unrestricted funding. All are indicators of organisations well positioned to do good work.

> *'If we want to receive applications in future from an agile, creative and resilient third sector, learning and innovating its way towards ever more effective solutions to stubborn social and environmental problems, then we need to see contributing to core costs, working capital and reserves as part of the cost of doing business with it, just like paying the profit margin priced-in by the private sector.'* (Nick Addington, William Grant Foundation)

Challenging the barriers to action

We know enough about the potential of unrestricted funding to give assurance to any funder that it is a responsible choice to make. The next questions to be asked are practical ones: Is it within our powers? Can we afford it? What are the risks? How will we know about the difference it has made?

Managing legal constraints and strategic choices

There are (almost) no legal barriers to unrestricted funding. Foundations can make unrestricted funding to any organisation that is itself a charity and does not have legal objects that are wider than their own. When legal objects are not fully aligned, funders can use light-touch restrictions (ideally jointly agreed) that give charities the freedom to spend within their areas of common concern.

Many funders have strategic priorities that are narrower than their legal powers. But this doesn't mean they have to make restricted grants. They can, for example, rely on their application and assessment processes to determine whether there is a fit with strategic priorities. Again, they can use very light-touch restrictions to focus the grant on their priorities without further constraining charities' freedom to spend it as they see fit. They can even ask a charity to report on a specific project or activity that they are interested in without restricting their money to that piece of work.

[4] Mills, C., Hopgood, R. and Cairns, B. (2022). Thinking about charity reserves. London: Institute for Voluntary Action Research.

Managing costs

Unrestricted funding saves money and time for both funders and charities simply because it lifts the burden of managing restrictions. But funders often assume that it also means exchanging a relationship grounded in formal reports about spend against budget, or activities against plans, with a much more intense – and potentially costly – relationship with funded organisations. This view is not supported by the evidence.

Some unrestricted funders do enter into close partnerships with the charities they support, but many do not. This is a strategic choice, not an essential feature of unrestricted funding. Whatever approach funders choose, evidence shows that unrestricted funding helps to make the funding relationship more open and less stressful for charities. They are more comfortable speaking to funder staff and more likely to have honest conversations with them, and to find these interactions helpful. Charities value unambiguous relationships with their funders but do not expect them to be all the same. The key to unlocking the benefits of an unrestricted funding relationship is to be crystal clear about the nature and limits of the relationship on offer, and to manage it reliably and respectfully.

Rebalancing risk

Charities shoulder the burden of risk from restricted funding – whether this is the drain on resources from multiple different reporting requirements, the danger of funder-led planning and 'mission drift', or simply not having the flexibility to move quickly when needs change or opportunities arise. There is compelling evidence that, as a result of funder preference for project or programme grants, many charities spend too little on overhead costs. This is not about 'extras' but about doing without the basic infrastructure that keeps services running – planning time, managing and developing staff and volunteers, supporting an effective board, IT and data, office costs, fundraising, financial management, time to collaborate with others and so on. Research shows that the '*starvation cycle'* of insufficient investment in overheads weakens organisations and damages their capabilities. Enabling funded organisations to have greater control over their own spending significantly reduces the risk those organisations are managing.

By contrast, research finds no evidence that restricted funding is an effective mechanism for funders to prevent 'wasteful' spending by charities. Instead it shows that waste is inherent in some assurance processes, such as detailed reporting and spending deadlines. Foundation trustees do need confirmation that the foundation's resources are being used responsibly, but this can be achieved in a very light-touch way. Judgements about compliance risks are made during the application and assessment process, when all foundations spend time and energy doing due diligence to assure themselves that the organisations they choose to fund are appropriately managed and can do a good job. If funders have confidence in their application and assessment processes, they can have confidence in giving unrestricted funding:

> *'We simply don't see unrestricted funding as intrinsically risky. We have a robust due diligence process. It's not a free for all.'* (Paul Streets, Lloyds Bank Foundation for England and Wales)

Making a difference

There is growing evidence both that unrestricted funding supports charities in ways that increase their capacity to make a difference and that the dominant use of restricted funding across the sector constrains this potential. We cannot allow worries about how we make judgements about the impact of unrestricted funding to remain a barrier to change.

The evidence points to a simple solution. Funders can shift their focus away from project level outputs or outcomes towards the wider contribution that a funded organisation is making to the community or cause that they both care about. Becoming comfortable with the idea of 'contribution not attribution' – of playing a part in collective achievements rather than seeking to make a direct connection between 'our money and this specific result' – enables funders to think about 'assessing impact' as a forward-looking activity rather than as an audit of performance. This shift in mindset helps both funders and charities to develop indicators of progress that are more rooted in operational realities and more useful in making decisions about how best to use their resources in the future. In support of this shift, the evidence identifies two features of good impact reporting, which are:

Agreed not imposed: Funders are able to help charities develop better outcome measurement practices and to build their capacity. But this only works when they focus attention on data and reporting that is also meaningful or useful to charities themselves and to others with a stake in their performance and learning. Where funders make an unrestricted grant, they may be more willing to assess the difference that has been made against the funded organisation's goals and outcomes as set out in their own strategic plan, removing the burden of any bespoke reporting.

Recognises complexity: The success of any programme of work is a mix of what the charity does, what other partners and stakeholders contribute, what's going on in the local context or the wider environment and many other factors that muddy the water around who 'owns' what achievements. In a situation of complexity, narrowly focused project or programme reporting can skew data capture away from this bigger picture, impede learning and damage long-term effectiveness:

> *'Funders don't need to worry that they won't be able to see the difference that is being made – they just need to look in a different place. You are contributing to the totality of our impact and have a share in everything we do.'*

Download *The holy grail of funding: Why and how foundations give unrestricted* for practical experience and advice from foundations who already provide unrestricted funding.

Round up

The evidence does not offer simple answers to the question of whether unrestricted or restricted funding works best, under what circumstances and for whom. But it does make it clear that the status quo rests on very shaky foundations. As the Evidence Review concludes:

> *'Evidence for the assumed benefits of restricted funding offers an inadequate justification for the strong preference still shown by many for this funding model. On the other hand, evidence suggests that funded organisations' continuing advocacy for more unrestricted funding is not simply a matter of preference but shows promise in delivering a range of benefits that are of importance to funded organisations and funders alike. The case for funders engaging with the arguments for change is a strong one.'*

This is not to suggest that restricted funding is never appropriate or useful (nor that foundations can't contribute to core costs through other means, for example through the adoption of full cost recovery). But it has not earned its place as the dominant funding model on the basis of evidence. Charities have long argued that it inhibits their work, distorts their accountability to communities and causes, and weakens them as organisations.

Funders need to listen to what they are saying, look at the evidence and the practical experience of others and do whatever they can to respond. The current environment for social action is more challenging than ever. It calls for a new mindset – one that starts from the assumption that charities *'know their own business and can be trusted to spend wisely'*, adding constraints only by mutual agreement or where absolutely essential. For small and medium-sized organisations in particular, this change would be transformational.