Understanding Social Enterprise: A Case Study of the Child-Care Sector in Scotland

by

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Abstract

Defining social enterprise is a challenging task even for experts in the field, and doing so operationally in a way that would enable a commercial bank to offer credit to businesses in the social enterprise sector is even harder. To throw light on this issue, a survey of child-care businesses in Scotland was carried out, excluding as far as possible both local authority and private providers. Based on around 80 questionnaire responses, the paper studies the diverse legal form of child-care businesses and staff perceptions of their business form; the management and governance of these businesses; their pricing and credit management strategies; and various other issues. In addition, the complex policy environment in which these businesses operate was also investigated. Based on the survey findings, it proved possible to distinguish between ‘non-bankable’, ‘near-bankable’ and already ‘bankable’ types of childcare business, the middle category being of most interest. These terms are defined in relation to loans and investment rather than the provision of risk-free simple bank accounts. Much of the study findings should be capable of generalisation across the social enterprise sector.

Key words: social enterprise, childcare, Scotland

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1. Introduction
According to the DTI, “Social enterprises are businesses with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners.” DTI (2002) sees such businesses as contributing to the economy and society in several ways:

- raising productivity and competitiveness;
- socially inclusive wealth creation;
- enabling individuals and communities to foster local regeneration;
- demonstrating new ways to deliver public services; and
- fostering an inclusive society with an active citizenship.

However, the same report also notes various obstacles that limit what social enterprises can do, and discusses ways in which their contribution to society can be enhanced, identifying three key areas for government action:

- creating an enabling environment for social enterprise;
- making social enterprises better businesses;
- establishing the value of social enterprise.

In contrast to voluntary sector organisations that are set up as charities, and which are principally funded through membership fees, donations, grants (both general and project-related) and (occasional) bequests, social enterprises operate as businesses that sell a ‘product’, the net revenues from this providing the financial means to enable social objectives to be pursued. In many cases, a social enterprise might simply be the trading arm of an established charity, such as the organisations that sell products through catalogues, linked to larger charities like Oxfam, RSPB, and so on.

Social enterprises, of course, come in many shapes and sizes, just like more conventional, profit-motivated businesses. Also like the latter, they enter and leave the (social) market, and of those that survive for long, many achieve a certain size and then cease to grow any further, while a few continue to grow and develop. Interestingly, though, we appear to lack detailed statistics on birth and death rates, and survival rates, for firms in the social enterprise sector. Both from the standpoint of supporting policy towards the sector more effectively, and from the more intellectual standpoint of understanding its functioning and behaviour better than we do, improved statistics on the social enterprise sector would be very valuable.

For the study undertaken here, an important starting point was to clarify and develop some of the ideas about social enterprise that can be found in the general literature on the subject, both official and academic. In addition, though, we carried out a study of social enterprise in the childcare sector in Scotland partly as a case study to help elucidate our thinking about social enterprise; partly to help us develop a practical model for analysing such firms, one that can be helpful for banks and other financial institutions that might be in a position to offer credit. At present, social enterprises are frequently disadvantaged when they seek credit, because banks frequently do not understand ‘the nature of the beast’ or regard such firms as inherently ‘high risk’. Either way, these firms find it hard to secure enough funding on good terms. Thus one of our more practical aims in pursuing this research was to assist banks wishing to fund investments in the social enterprise sector.

Accordingly, in subsequent sections of the paper we proceed as follows. Section 2 reviews the concept of ‘social enterprise’, while Section 3 then goes on to review particular features
of the childcare sector, both in general, and specifically in Scotland where our survey was carried out. The importance of the sector, in policy terms, has been acknowledge through several recent official reports, notably a report of the National Audit Office published in 2004 (see NAO, 2004). Section 4 reports on our own survey of child-care ‘businesses’ and summarises our principal findings. Last, Section 5 elicits findings of more general interest and applicability, both for the child-care sub-sector itself, and for social enterprise as a whole.

2. The Concept of ‘Social Enterprise’
The notion of the social economy is the latest in a long line of attempts to come up with a universal term describing socio-economic organisations and activities that exist in that sphere of human organisation and interaction between the purpose, norms, values, mission(s), rights, responsibilities and actions of the public and private sectors (Spear, 2001) (parts of this Section draw heavily on Jones and Keogh, 2006). Previous terms sought to differentiate these organisations and their activities from private and public organisations. They did this by erecting conceptual barriers concerning certain types of organisation, and certain types of voluntary activity, organised by freely associating individuals operating privately for some form of public good. These conceptual barriers are concerned with four major issues:

- Voluntary participation
- Independence from the state
- The concept of profit: profit making per se, the appropriateness of profit making from certain activities, profit maximisation and profit distribution.
- Ownership and corporate governance

The term, ‘social economy’, seeks to improve upon earlier terms (Frumkin, 2002) such as ‘the non-profit or not for profit sector’, ‘the voluntary sector’ (Hussey and Perrin, 2003), ‘the third sector’ (Hudson, 1999; see Spear, 2001), the ‘charity sector’ (Philips, 2003) and ‘the non-governmental sector’ (Kanter, 1999). These earlier terms failed the universality test because they were unable to describe and connect the entire range of types of organisation and their activities that operate in the ill-defined area between the state and the private sector. Despite that, these terms continue to be used and their meaning(s) can be ‘an all things to all men’ view or belief. This has resulted in social economy leaders shying away from conceptual rigour and from trying to define exactly what the social economy is.

The reason for the failure of earlier terms is that we have been unable to agree on what is required to be part of the social economy. This is because this is a highly contested debate reflecting philosophical, political, cultural and social differences between organisations, their leaders and other stakeholders. The very concept of a sector itself is disputed but as it is a commonly used term, proponents of this view need to accept that every sector has boundaries – even if they are not permanently fixed (Frumkin, 2002). The trouble with this concept of a sector is that no one can define exactly and/or agree on what these boundaries are. Instead, for practical purposes, what we are left with is the views of governments and the legal and tax systems. These allow for tax breaks and exemptions and the delineation of types of organisations, and activities, deemed to operate between the public and private sectors. The qualification for favourable treatment is that these organisations and what they do are seen as benevolent, or charitable or serving a public or membership good.

A further complication is that charities often use the terms ‘charity sector’ or ‘voluntary sector’ synonymously, both internally and externally. However, many organisations that require charitable status for tax breaks, exemptions and funding, such as universities, are not included in most people’s notions of the charity sector (though legally that’s where they belong).
The relationship between volunteers in the voluntary/charity sector and volunteers operating in the commercial arena is another difficult issue. The relevant commercial arena here includes co-operative retail societies (Spear, 2001; Thornton, 2003). Further distinctions are occasionally made concerning the few remaining mass mutuals in the financial services sector. In the retail co-op movement, volunteer directors are usually paid, albeit small sums, and these organisations have become massive commercial concerns. Trying to discern what their core social mission is and whether it has altered from its original roots is problematic. Fundamentally, however, these volunteers describe their activities in philosophical and political terms that reject profit as the purpose of their businesses. For these volunteer directors it is a means to an end and they differentiate themselves and what they do from capitalist businesses.

The diversity of social economy organisations and what they do is difficult to encapsulate in a single phrase. For some practitioners there is little merit in attempting to write an accurate definition. Academic investigation and rigour are seen as being largely irrelevant to the task of doing ‘good work’. The view often expressed by many social economy practitioners is that “Trying to define a Social Enterprise can be like trying to define an elephant – very difficult and not much point, because you know one when you see one” (Social Enterprise London, cited by Cabinet Office, 2002b; see also Cabinet Office, 2002a).

The following figure, Exhibit 1, illustrates the complexity and diversity of organisations involved in the social economy:

<table>
<thead>
<tr>
<th>Art &amp; Sport Institutions.</th>
<th>Universities &amp; Colleges</th>
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<tr>
<td>Charities &amp; organisations with charitable status</td>
<td>Non-Governmental Organisations (NGOs)</td>
</tr>
<tr>
<td>Churches</td>
<td>Scottish Private Schools</td>
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<td>English “Public” Schools</td>
<td>Unincorporated Organisations</td>
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<td>Incorporated Organisations and The Formal Voluntary Sector</td>
<td>Social Enterprises</td>
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<td>Mass Mutuals and Retail Co-ops</td>
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Social Enterprise
With the term social enterprise, the problems of ambiguity and imprecision are similar. For many people, the organisational terms: social enterprise, community enterprise, social firm, ethical enterprise, and non-profit enterprise are readily interchangeable. Where sub-sectoral claims are made for one particular term, this does not prevent continuing ‘mis-usage’. An example of this is the term ‘social firm’ which according to the ‘social firm sector’ is a social enterprise that creates supported employment opportunities for people with a disability such as a mental health problem. That distinction can easily be lost in conversation with the range of people operating in the social economy. A narrower compromise definition has,
however, been adopted by social entrepreneurs who trade in markets and make profits, though profits themselves are usually referred to as surpluses. That said, this approach does take the view that social enterprises are indeed – or should be – businesses.

However, different definitions and interpretations continue to be developed and used. For example (Birmingham Social Economy Consortium, 2001): “Social enterprises

- are not-for-profit organisations;
- seek to meet social aims by engaging in economic and trading activities;
- have legal structures, which ensure that all assets and accumulated wealth are not in the ownership of individuals but are held in trust and for the benefit of those persons and/or the areas that are the intended beneficiaries of the enterprise’s social aims;
- have organisational structures in which full participation of members is encouraged on a co-operative basis with equal rights accorded to all members”

Another example is from Evans et al. (2000):

“Social enterprises try to make a profit, but they operate on a not-for-personal-profit basis, applying any surplus they create to furthering their social objectives. They put people first and, through their economic activities, seek to deliver employment opportunities and other social, environmental, or community benefits”.

The major differences appear to be the nature of the intent to make, maximise and distribute profit and how committed organisations are to active participatory forms of corporate governance. Other authors attempt to clear up the confusion through the classification of defining characteristics and values of the social enterprise model. For Pearce (2003) these are:

- Having a social purpose;
- Engaging in trading activities to achieve their social purpose (at least in part);
- Not distributing profits to individuals;
- Holding assets and wealth in trust for community benefit;
- Democratically involving members of its constituency in governance of organisation; and
- Independent organisation with accountability to defined constituency and wider community.

Again these are idealised characteristics and there are major problems in defining the term ‘community’ and presenting participatory forms of governance as active and significant features of these organisations. Social economy organisations may claim good governance structures and systems, and they may meet de jure conditions, satisfy regulators and keep a committed core of volunteers happy. However, there is the problem that in practice, democratic governance is failing because of our society’s declining rates of participation in electoral and governance processes.

How does a social enterprise grow? Much of the academic literature on firm growth is devoted to a variety of so called ‘stage’ models, usually identifying three to five stages, occasionally as many as ten. The best known of these models is probably that of Churchill and Lewis (1983) which distinguishes five stages: (i) existence; (ii) survival; (iii) success (with sub-stages, (a) success-disengagement; (b) success-growth); (iv) take-off; and (v) resource-maturity. This is not the place for an extensive review of such models, except to note that they commonly suffer from a lack of empirical testing and can also appear rather mechanistic. For in practice, many firms will never pass through all stages, firms can move back and forth between stages, and the stages might not even occur in the specified
sequence. Hence the model can provide us with an appealing picture of a possible growth process, but most likely it is not one that will often be observed. However, it is a useful starting point.

Other models focus on the entrepreneur, an even more hazardous notion since we still have such a limited conception of entrepreneurship in general and ‘the entrepreneur’ in particular; however, see Chell et al. (1991) for an example of this approach, with some useful critical discussion. It is fairly clear that we cannot pin down with any precision those characteristics that mark off ‘the entrepreneur’ from other people. This probably explains why more descriptive models of the sort developed in Storey (1994) became quite popular, with their focus on clusters of factors related to: (a) initial resources; (b) the firm; and (c) strategy.

For a social enterprise, the growth process is likely to be more complex, and quite possibly more difficult, than it is for a conventional, profit-oriented firm, whatever particular model of the latter one might adopt. For one thing, it will often be the case that in a given line of business a social enterprise will be operating in competition with conventional firms seeking to make money for owners rather than for the pursuit of social objectives. To succeed, therefore, not only in the basic sense of surviving but in the more important sense of being able to attract funding for investment and expansion, a social enterprise has to offer society (or ‘the market’, if we take a narrower viewpoint) something ‘different’ or ‘special’. What can this be?

First, if an organisation is explicitly devoted to the maximisation of profits, then it will not be able to draw on a pool of volunteer labour, since everyone associated with such a business will expect to be paid the established ‘rate for the job’. However, this attitude is far less likely to apply to a social enterprise. So one potential strength of a social enterprise will be its ability to attract and make use of volunteer labour, provided by people who support the objectives of the organisation in question. Along similar lines, many people are willing to engage in what might be termed ‘self exploitation’ by working for a social enterprise whose goals they approve, for a lower wage than they would seek from a mainstream capitalist firm.

Second, while a social enterprise will not normally have shareholders in the conventional sense, it will often be able to establish a network of supporters, sponsors, members and the like, people and organisations willing and able to contribute funding on terms that would never be offered to a profit-making firm. Hence a social enterprise can benefit from a network of funders who are not looking to make a profit for themselves. These might be ethical investors of various sorts, for instance.

Third, the goods and/or services provided by a social enterprise will often be purchased by customers in preference to similar items from competing profit-oriented firms precisely because the customers support the social goals of the enterprise. An obvious example of this is the charity Christmas card business which earns surpluses for charitable and social causes by attracting millions of willing customers who would certainly not be lining up to buy the identical products from profit-seeking firms. Hence to some extent, it can be stated that social enterprises benefit from a loyal, and to some extent captive market. This does not mean, of course, that a social enterprise can survive by churning out any old rubbish and assuming that its loyal followers will buy more or less anything. There are still quality standards to achieve, and the market environment is always going to be harsh and competitive. Hence by referring to a ‘captive market’, we are merely indicating a way in which a social enterprise can enjoy a slight ‘edge’ over a corresponding profit-seeking firm. The social enterprise still has to work hard to sustain its initial market advantage.

Returning to the growth process, for a social enterprise this will naturally include all the elements that are important for a conventional profit-seeking firm. However, the success - and hence growth - of a social enterprise will also depend on how effectively it is able to
capitalise upon the three factors just mentioned, namely volunteer labour and the self-exploiting workforce, a network of funders, and a captive market. These are the features that make a social enterprise different from a standard commercial entity.

These features and others also imply that evaluating the performance and results of a social enterprise is a more complex task than in the case of a profit-seeking firm. This is why notions of social audit, and ideas regarding double or even triple bottom lines have gained currency in recent years. For present purposes, the double bottom line that supplements the standard financial accounts of a firm with indicators of its social impact is probably as far as we need to go in the context of our investigation of the childcare sector in Scotland. However, there is some anecdotal evidence that managing the environmental impact of nappies and waste materials, etc., is a feature of some providers' services and the cultural norms they display.

Of course, even in a framework in which social and environmental dimensions of a business are to be examined, it will remain the case that to survive, the business must be financially viable. Hence a core concern of this study, both for understanding the dynamics of the social enterprise sector and for enabling us to provide well formulated guidance to banks on how to assess and support firms in the sector, will necessarily lie with the financial performance indicators of such businesses.

3. The Childcare Sector in Scotland

Overview of the UK

In a recent article on their website reviewing the childcare industry in the UK, Childworks¹ report that there are 11.5 million children under the age of 16 in the UK. Furthermore the article goes on to highlight the findings of The Family Policy Studies Centre who estimate that 7.6 million of these children live in households where both parents work. Hence, the article concludes that around two-thirds of children at some point may be cared for by an outside party.

In Scotland there are just over one million under 16s, accounting for around a fifth of the total Scottish population². Scotland also has the highest percentage of lone parents in the UK and the number of children living in lone parent families has more than doubled between 1981 and 2000 (NCH, 2004, pp7-8) The NCH (2004, p52) report also finds that “a lack of affordable, high quality childcare is one of the key reasons for relatively low employment rates among lone parents”³

As part of the National Childcare Strategy launched in 1998, the Government committed itself to improving the access and affordability of childcare services, including pre-school and after school provision in deprived areas supported by funding via the Neighbourhood Nursery Initiative and the New Opportunities Fund, together with £203 million worth of funding from the Department of Education and Skills. In total, the government invested £3.6 billion during 2002-03 in childcare provision, and has invested around £14 billion in the sector since 1998.

Despite the considerable amount of funding available, it is reported that “There is only one registered childcare place for every seven children under eight in England” (Wilkinson, 2001 p10). In addition, NAO (2004) highlights that high staff turnover and finding suitable premises

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¹ www.childcareworks.co.uk/newspub/story.cfm?ID=7
² Figures are taken from NCH Factfile 2004, Facts and figures about Scotland’s children
are major threats to the sustainability of childcare provision. A lack of demand is a particular problem faced by playgroups and childminders. It may seem odd that there appears to be both a lack of supply and not enough demand at one and the same time. But it makes sense since the supply (e.g. a particular childcare establishment) always has a very specific location, and many parents – especially those less well off – are unwilling or unable to travel far to ‘deliver’ their children. Thus it is perfectly possible for parents to report insufficient supply of services while spaces might be available at a facility only half a mile or a mile away.

In addition to the above points, organisations find themselves weighed down by paperwork and chasing parents for payment, as is confirmed by some of our survey evidence reported below, discussing credit control policies and practices, and the like. New legislation and regulation over the coming months, together with insufficient business planning, may lead to a number of child-care organisations closing. The National Audit Office report suggests that less than half of the organisations they surveyed were able to cover their (full) costs or indeed understood their cost structures and issues affecting their viability.

**The future of childcare**

With such a high proportion of lone parents, if employment targets in Scotland are to be met then accessible and affordable childcare must be made more widely available. Mothers are increasingly returning to the labour market, with the proportion of women with under fives engaging in paid work rising from 28% in 1980 to 58% in 2001 (SEL, 2002, p23). In addition, mothers are also returning to work sooner (within the first year) after giving birth than they did previously, the share of early returners rising from 24% in 1979 to 67% in 1996 (SEL, 2002, p23).

Traditional working hours are also less common now as more and more firms seek to employ labour outside the standard hours of Monday to Friday, 9 to 5. This creates a demand for more flexible childcare provision both in terms of opening hours and the facilities/services provided (SEL, 2002, p23).

The face of childcare provision has been changing, too, with a decline in local authority provided facilities – down to 6% of all childcare places compared to a third a decade ago (SEL 2002, p25) – and a huge rise in private sector day nurseries. This is now one of the fastest growing sectors in the UK with demand reportedly far exceeding supply (SEL, 2002, p26).

**The childcare market in Scotland**

The Scottish Executive (2005) estimates that there are 263,000 children in Scotland aged 0-4 years old and this number is expected to decline modestly to 248,000 by 2010. Recent statistics published by the Executive report that there were 4717 childcare and pre-school education centres in January 2005, employing 11,905 full time staff and 16,208 part time staff. The number of childminders working in Scotland has fallen slightly and only 25% of these have any formal childcare qualifications.

The day care of children describes services which care for children outside the home for more than 2 hours per day for at least 6 days a year; many groups that operate within this definition are not required to be registered and are not subject to the Care Commission regulations and inspections. Nurseries, crèches, after school clubs (also known as out of school clubs) and playgroups are included in the childcare sector, and may operate on a private, public or voluntary sector basis. Sports clubs and uniformed activities such as scouts/brownies are not included as part of childcare.

Across all types of childcare provision, there were 2517 establishments providing nursery services, 1079 offering Out of School Club services, 368 Breakfast Clubs and 62 offering
Gaelic Provision. The majority of the service providers offer multiple services and operate between for varying periods during a typical day, depending on the service being offered.

Local authorities run 1984 childcare and pre-school education centres, 1037 are operated by the private sector and 1345 are run by the voluntary sector. Just over half of all nurseries in Scotland are managed by the local authority and approximately 50% operate within school premises. Breakfast clubs and Out of School Clubs also tend to operate in school premises. It was estimated that there were 861 playgroups operating in 2005, with 596 of these being run by voluntary committees and over a third are run in church or village halls.

4. Survey and Major Findings

The Survey
In late 2005 and early 2006, we carried out a postal survey of 300 childcare organisations selected from a list of registered organisations in Scotland provided by the Care Commission. Within the Care Commission list of 4414 organisations, we first picked out those classified as ‘voluntary’ (the other categories being ‘private’, ‘local authority’, ‘other’), giving us an initial dataset of 1502 organisations from which our sample of 300 was selected randomly. This approach meant, of course, that our research could not pick up the possibly large number of unregistered organisations operating in the childcare sector (and this is why the numbers in this paragraph differ from those reported in the previous section). The survey questionnaire was formulated following extensive discussions with stakeholders in the childcare sector, and it was piloted on 10 childcare groups who either offered to assist our research, or who were suggested to us by other contacts. The pilot enabled us to clarify some questions, and generally to improve the final survey instrument (see Appendix 1 of forthcoming complete project report for the final version of the questionnaire).

A total of 81 organisations have been included in our analysis. An additional 9 surveys were returned but were not been included in our statistical analysis as too many sections were incomplete. Within the 81 that are included there are also some organisations that did not complete all the sections. However, it was felt that some missing information was not detrimental to the overall analysis and that such organisations provided enough useful data to justify their inclusion.

Survey Results
Number of sites and closures
The vast majority (about two-thirds) of the organisations surveyed operated at just one site, as one would expect given the large number of playgroups that responded. Playgroups tend to be locally based groups operating in relatively small geographical areas, although there may be many within large towns and cities.

Just fifteen organisations operated at more than one site and two-thirds of these multi-site organisations had between two and five sites in total and only 3 organisations indicated that they had more than 10 sites. Our results show that very few organisations (less than 5%) have experienced any site closures within the past year, although lack of finance is cited as the key reason for site closure when it does occur. Most organisations liaise with their local Childcare Partnership, with 68% of all organisations that responded to the question stating that they belong to their local organisation.

5 The organisations listed on the Care Commission database were not classified by the Care Commission itself; rather, organisations chose for themselves which category was ‘suitable’ for them, so we expect that there is some degree of mis-classification.

6 Childcare Partnerships were set up in every one of the 32 local authority areas in Scotland. Their initial tasks were to carry out an audit of childcare supply and demand in their area and based on this draw up plans for expansion, integrated with plans for the expansion of early education.
Almost 70% of the organisations surveyed are not managed by the same people who set them up originally, not too surprising since the mean lifetime of an organisation in this survey was 18 years 5 months. Several organisations had existed since the late 1970’s or early 1980’s. Somehow, childcare businesses manage to survive, despite the concerns about their sustainability that we come to later on.

Enterprise Ethos
When asked whether childcare should be free, responses were fairly evenly distributed from strong agreement to strong disagreement. 44% of the organisations that gave a positive response to this question suggested that they were responding to the lack of provision by the local authority, 36% were neutral and 21% disagreed. 68% of the organisations that answered the question also considered that the local authority should fund childcare, with 45% strongly agreeing with this statement.

Funding
On external sources of funding and the problems related to these, the majority of respondents agreed that childcare services are unsustainable without external funding. In this context, sustainability is not, of course, the same as self-sufficiency. The former term means that an organisation is able to keep going, but this may be with the help of various grants (including direct local authority funding), and sub-commercial contracts – often with local authorities or Childcare Partnerships – known as Service Level Agreements (SLAs). The latter term, self-sufficiency, would imply that an organisation had the financial means to keep going without such external supports. In practice, many social economy stakeholders use language ambiguously, and would often use the term ‘self sufficiency’ more like our ‘sustainability’. Grants/funding/investment, etc., from the state (in whatever guise) are treated as ‘gifts or discretionary finance’ rather than a purchase of services.

Furthermore, short term funding in particular was not judged to be conducive to sustainability. Interviews and informal discussions with organisations had raised this issue on numerous occasions. Short term funding does not give organisations the opportunity to plan for the future as their survival is reliant on a succession of successful grant applications which require a great deal of time and effort. This imposes a vast administrative burden on what are mostly quite small organisations and which enjoy, in many cases, very modest managerial capacity.

Changing the structure of grants – mostly only offered for one to two years at a time – will not happen overnight and so alternative means whereby groups can access long-term finance are needed. One of the areas in which the financial institutions could perhaps assist is through loan finance. However, the survey responses suggest that this is not widely regarded as a good way forward: nearly a third of those who responded to the question disagreed with the statement that long term loan finance would improve sustainability and only a quarter of respondents agreed with it. There is a high degree of aversion to loan finance on the part of many organisations operating in the childcare sector; at the same time, even if they desired it, many childcare businesses in the social economy are not ‘investment ready’, that is, they would be unable to service a loan offered on normal commercial terms. Thus in a recent study of the social economy, McGregor et al. (2003) found that “almost three quarters of the smallest organisations are not prepared to consider loans” and very few small organisations indicated that they would seek to obtain loan finance.

Looking beyond the traditional financial institutions, a significant proportion of respondents agreed that a mixed economy of customers is conducive to sustainability. During one interview, a manager of a local childcare organisation indicated that “you need to encourage
families from the more affluent areas as they tend to be the families that will pay on time and you don’t need to spend time chasing for payment”. These prompt payers therefore offset some of the cash-flow difficulties that can arise when organisations have a large number of families who require prompting for payment.

However, these social economy childcare organisations have a very different culture to typical private sector organisations. One difficulty for some of them is that because they operate in small geographical areas, once non-payment begins by some customers it can quickly become quite widespread, as there is an attitude of “why should I pay, if such and such doesn’t have to?”. Therefore, if organisations seek to have a mixed economy of customers, they must equally protect the prompt/reliable payers as these are the pool of customers who (in effect) compensate for late payments, and if this pool was significantly reduced then it could lead to financial instability. Interestingly, though, only 40% of respondents clearly agreed with the view that childcare services should be paid for by the customer at the point of delivery. Thus many of the businesses we surveyed were far from having a well developed commercial outlook.

Childcare Services Provided
Just over half of the organisations surveyed indicated that they were playgroups, followed by out-of-school clubs (OSC) who represent 35% of our sample. Breakfast and holiday clubs are often an extension of the out-of-school clubs, in fact 89% of OSCs also provided a holiday club and 36% provided a breakfast club. Less than 10% of organisations surveyed were day nurseries and 25% stated that they provided another form of childcare which had not been listed; these are most commonly créches and mobile créches.

Enterprise Type
Almost a third (32%) of organisations that responded to this question stated that they were a parent co-operative, followed by partnership (27%) and then community business (18%). 31% of the organisations who answered the question on incorporation indicated that they had some form of incorporation, with 80% of incorporated organisations being a companies limited by guarantee (CLG). Many of the surveyed organisations did not answer the direct questions on organisation type and form of incorporation, but we also asked that they describe themselves in their own words. 60% of organisations then identified themselves as something other than the terms we had provided, most of these claiming to be voluntary, non-profit or not-for-profit organisations.
The vast majority (85%) of organisations that answered the question on charitable status had charitable status and only two organisations were affiliated to another large organisation. Five organisations indicated that they were a trading arm of the local authority, but it was unclear whether the organisations were partner-providers, or whether there was some other linkage between the organisation and the local authority. Moreover, some organisations stated that they were partner-providers without also agreeing that they were a trading arm of the local authority.

Starting up
Securing initial finance was the most common problem, with just over a quarter of respondents to this question stating that that this had been very difficult for them, and nearly 50% suggesting that it created more than average difficulties. The next most common problem encountered was finding suitable premises, with 15% of those who answered this question stated that this had been a very difficult area to deal with.

The most common sources of finance used during start up were grants, with both capital and revenue grants being used in nearly a third of all cases. The use of personal funds or those of family/friends was rare. Organisations suggested that grants and loans were the most useful form of start-up finance. Organisations that had have previously received a capital grant indicated that the most common sources were their local authority and the Lottery. A few organisations did secure grant funding from the EU or the Scottish Executive. Fourteen organisations indicated that they had received funds from other sources, including charities such as Children in Need and the Scottish Pre-School Play Association. Revenue grants had a similar distribution.

Staff
Only a few organisations had qualified childcare staff working for them on a voluntary basis and the majority of voluntary staff were unqualified. As the majority of the organisations surveyed are relatively small, they tended to have few qualified staff, most only reporting between one and three paid members of qualified staff. A smaller proportion of respondents indicated that they had between four and six members of qualified paid staff and only the very largest organisations had a larger qualified workforce. The results for unqualified staff showed similar patterns, one or two members of unqualified staff being most usual.

Part-time working is more common than full-time working, as expected given the large proportion of playgroups within our sample, since these tend to operate for only a few hours in the morning. Sixteen percent of organisations did not employ any part-time childcare workers, while 64% did not employ full-time staff. The emphasis on part-time volunteering within these organisations is strong, with 38% of all organisations having at least one part-time voluntary member of staff. Almost a quarter of organisations (23%) used volunteers for non-childcare activities such as bookkeeping and other administrative roles, although 32% of organisations employed part-time staff to carry out such activities.

In recruitment, the strongest source of competition for staff was the local authorities, followed by private organisations. The information on staff turnover indicated that one-third of organisations that employ full-time staff have experienced no staff turnover in the past year and the results were similar for organisations with part-time staff, although 13.5% indicated a turnover rate of 50% and two organisations had experienced full staff turnover. However, these results should be viewed with caution as the use of volunteers, parent rotas and sessional staff (used by one-third of the organisations surveyed) would tend to lead to a greater staff turnover rate as parent volunteers leave the organisations as their own children move onto school and so forth.
Management and Board
In just under three-quarters of the organisations surveyed, the manager had a background in childcare, 30% having a professional background. Managerial tenure ranged from newly appointed managers who had been in place for less than six months to a few organisations whose manager had been in place for over 15 years, and 20 years in one case. The most common length of service for a manager was between 3 to 5 years.

Most organisations claimed to have a management team (i.e. more than a single manager). However, this question might have been misinterpreted by some organisations as the responses were similar to those about board members. For the majority of the organisations, the Board was made up of the manager together with a mix of local parents and business professionals.

Pricing, Expenditure and Income of the Enterprise
Nearly all the organisations surveyed indicated that they set their own pricing and offered a mixture of set weekly charging and sessional based charging on an approximately equal basis. Three-quarters of the organisations responding to this question also applied a charge when a child missed a session. Less than half of the organisations offered special discounted rates for families with more than one child using a service. In addition, most charged at a single rate, unrelated to the age of the child, and 60% indicated that they did not charge separately for nappies, outings or snacks.

Price and cost data were, however, extremely limited in our survey as most respondents did not answer questions on these areas; the same was true in regard to data on their annual expenditure budgets.

Information on sources of financial support for families was also incomplete. Almost half (48%) of the organisations did not indicate how many places were funded through the Working Families Tax Credit. Furthermore, 64% of those that did respond to the question indicated that they had no funded places. The uptake of childcare vouchers was also low, with only 24% of organisations who recognised the scheme accepting the vouchers.

Capacity
The number of places that organisations offered varied a great deal from as few as 10 up to 440 places in a multiple-site case; the most common size of organisation is around 24 places.

The number of places taken up in the previous week also varied a great deal, with one organisation having no places taken up in the week prior to them completing the survey (we assume that the organisation may have been closed) to 203 places being filled in the very largest organisation. 61% of organisations indicated that they had a waiting list, although 44% indicated that they did not achieve full occupancy, which they felt created stability/sustainability problems for their organisation. The most common reason stated for operating below full capacity was lack of demand, followed by competition from other providers. The vast majority of organisations operated for 5 days per week and tend to run alongside school term times. There was, however, a great deal of variation in the number of hours that organisations operated.

Credit Policy and Action
Only a quarter of the organisations surveyed stated that they had a written-down credit policy and almost 9% were unaware whether they had a policy. Of those with a credit policy, only half enforced the policy all the time. The majority of organisations appeared to operate credit control on an ad hoc basis and most had not designated a specific member of staff to manage credit control. Issues of non-payment were most commonly dealt with via individual negotiation, emphasising the lack of any standardised credit policy.
Cash was the most common form of payment (94%), but a small number of organisations had standing order facilities set up and a significant number of organisations had contract agreements as partner-providers (22%).

Investment

Personal sources of finance or those of family and friends (includes fundraising) were rarely used for investment purposes. Nearly all organisations drew their investment funds from fee income and grants and almost a third also used their reserves for investment purposes (for a more general discussion of financing social economy organisations, see Bank of England, 2003).

Evidence from FutureBuilders Scotland shows that some childcare organisations have already benefited from the investment programmes they have in place, which aim to develop social economy organisations by helping them move away from grant funding and onto earning income.

FutureBuilders Scotland, unlike its English counterpart, supports social economy organisations through grants rather than by means of loans (see Scottish Executive, 2004). They offer three programmes of investment that organisations can access to develop their organisation. Within the investment funding programme, FutureBuilders Scotland have made 40 awards totalling nearly £6.5 million. The majority of investments are large scale projects costing between £70,000-300,000. They include refurbishment projects, purchase of new buildings and development of outdoor facilities. In addition, these new premises will also give these organisations opportunities to expand their services and in some cases expand their workforce.

The FutureBuilders programme also provides smaller awards worth up to £50,000 for business planning, specialist/technical support and some small scale investment in equipment and fixed capital. A small number of childcare providers have been successful in securing some of this funding across Scotland. This part of the programme has invested around £4.8 million in 205 organisations.

In addition, the learning component of the programme has assisted 79 organisations with around £350,000 worth of funding in management training, including strategic planning, financial management and other related business courses in several Out of School (OSC) Care clubs. Investments have also been made in leadership training courses in conjunction with the Social Enterprise Academy based in Edinburgh.

FutureBuilders have tended to provide funding for the larger childcare organisations. This suggests that scale may be an important factor for investors. FutureBuilders are clear in their mission statement that they are seeking to “make one-off investments in organisations to enable them to both expand future service delivery and improve their financial sustainability”.

Opportunities and Threats

Looking ahead at opportunities and threats it was clear that nearly three quarters of the organisations surveyed did not plan to expand the number of places currently available or increase the range of services available. The results suggested that very few organisations wished to undertake any changes to their organisation over the next 12 months, with only four indicating an intention to pursue other business opportunities in the year ahead (of which three had finance for their new activities confirmed at the time of the survey). These organisations indicated that they planned to open training centres, pursue private contracts similar to the services provided by mobile crèches, and also suggested that they would pursue other activities not related to childcare.
The greatest threat to sustainability over the next 12 months was possible reductions in grant funding, followed by changes in legislation such as the minimum qualification requirements and to some extent the recommendations of the Care Commission. Competition from other providers was also noted as an area for concern by half the surveyed providers, a point further supported by the 57% expressing concerns about reductions in their occupancy rates.

Three-quarters of the organisations responding on special funding were aware of grant funding to meet the needs of children requiring additional support, 23 organisations had previously applied for such funding; all but two had been successful. It is unclear whether new legislation in areas such as the Disability Discrimination Act was considered to create opportunities or further threats for social economy organisations, since over 40% of the respondents indicated that they did not yet know how they would be affected.

Relationship with banks
To function at all, all the businesses we surveyed needed a bank account. But most used a very limited range of banking services. Just over two-thirds of the organisations used a deposit account, almost a quarter had direct debit facilities and just over a quarter used standing orders. Other banking services such as overdraft facilities were only used by two organisations, and only one organisation indicated that it had benefited from a bank loan. Moreover, only 12 organisations indicated that they had used the business advice services provided by their bank.

Profit
Three-quarters of the organisations that responded to the question on profit were comfortable with the concept of making profit to ensure their sustainability. Organisations were then asked to indicate whether they found it acceptable to make profits from childcare, with 59% indicating that they did not find it acceptable. However, when asked whether they were comfortable with making enough profit to fulfil their needs, 88% indicated that they agreed with this sentiment. It appears that social economy organisations such as those in the childcare business are well aware that they need to cover their costs, but are frequently quite uncomfortable with such market-economy terms as ‘profits’ when this is linked to their specific business activity. It is widely considered that childcare and profits do not belong together.

5. Conclusions and Lessons
Our survey of the Scottish childcare sector presented a fairly comprehensive picture of provision by social economy businesses, though as noted earlier we left out of consideration those providers run by local authorities, and those that described themselves as wholly private providers. We now conclude by setting our study in a wider context in two senses: (a) the childcare sector as a whole, including issues at most only touched on in our survey; and (b) the social economy sector as a whole. On both aspects we must, of necessity, be very brief.

(a) Childcare sector issues
The most significant issue here concerns various aspects of childcare regulation, where a number of recent and on going developments pose a serious challenge to the sector. Existing regulation of health and safety standards (including fire regulations applied to premises), and criminal records checks on all staff working with children (through Disclosure Scotland) are already onerous enough. Plans to require childcare staff to possess certain qualifications will significantly add to the sector’s difficulties, partly because some good staff might not be willing to undertake the needed training; also, the new requirements might make recruitment more difficult. Further, once staff are better qualified, it is virtually certain
that they will expect better wages, and in our view this expectation has not been taken on board in the sector’s financial planning.

The 2005 Disability Discrimination Act (DDA) will have further consequences for the sector, some undoubtedly unintended. For example, premises used to deliver childcare services will have to comply with DDA requirements, and this is likely to require provision for wheelchair access even when the organisation concerned does not currently have a child ‘on the books’ needing this. Moreover, in the course of our research we encountered instances of childcare businesses located on school premises, where the DDA was expected to entail very substantial spending by a childcare business to meet the new rules – in a situation where neither the school nor the relevant local authority were willing to contribute anything at all. In these circumstances, it is almost inevitable that some childcare businesses would be compelled to close, since especially the smaller ones would be unable to meet the additional costs of compliance with the DDA.

(b) Social economy issues
Our final topic concerns the funding of social economy businesses, and the possible part that the commercial banks can play in that. While all social economy enterprises will have a bank account to handle their routine, day-to-day cash inflows and outflows, few are in a position to seek loans (whether on commercial terms, or even on somewhat preferential terms) to support their development and expansion; indeed surprisingly few even have a regular overdraft facility in place. In this significant sense, very few social economy enterprises would be regarded as properly ‘bankable’. However, while our own survey confirmed that such businesses are mostly non-bankable, there are a few that are large enough and sufficiently commercially minded to be clearly bankable, some of which already have experience of receiving and servicing loans as part of their business. In between these extremes lies a grey area of what we term the ‘near bankable’ firms. The interesting question, then, is what features of social economy businesses influence their position along this spectrum?

We consider three features, namely size, ethos, and goals. The first of these, size, is clearly relevant. Many social economy organisations are small, offering services in a limited area to a modest client base. To be large enough to be bankable, such a business would need to offer multiple services, possibly in different locations. This suggests there is some critical mass, some lower size limit, below which an organisation is highly unlikely to be bankable in our sense. The ethos of such an organisation is also important, since it matters whether it thinks of itself as a social service provider (often with the background idea that, really, it is doing something that the state would ideally be doing), or a commercial business (with the background idea that profits are acceptable, private sector provision is fine), or a mix of these. Last, it matters whether the organisation has a goal such as ‘getting single parents back to work and off benefits’, or something more commercial such as covering all its costs or even making profits through business growth and diversification.

Life in the social economy is not easy, perched uneasily between the state and the private sector, and often competing with both. It is therefore not too surprising that business identities often appear ambiguous or unclear, or that there is such widespread ambivalence towards commercial norms. The result, we suspect, is that only quite a small segment of the social economy sector will prove of significant interest to commercial banks.
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