9 Social Accounting and Third Sector Organisations

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Introduction

In recent years, much attention has been paid to the roles and the responsibilities of not-for-profit or charitable organisations. These mission-based entities seek social impact rather than profitability for shareholders and comprise what is known as the third sector (TS) of economic activity (Lindsay *et al.*, 2014). Even though the origins of third sector organisations (TSOs) are associated with the birth of the big cities and the industrial revolution in the UK (Emmanuel, 2014), focus on these socially-driven entities and their performance has increased over recent years, primarily due to the alleged failure of not-for-profit organisations to efficiently deploy financially sustainable services and achieve associated programmatic goals.

Like public sector entities, TSOs are under pressure to be accountable for delivering value added services to their constituents. However, the way TSOs are held accountable is different; they are expected to manage a 'double bottom line,' in that they must deliver a measurable and meaningful social impact for their beneficiaries, while also responsibly and transparently accounting for the financial resources entrusted to them by their donors (The Scottish Government, 2011). The TS accounts for a substantial part of many countries' economies. In England and Wales, for example, the TS annual income is estimated at £75 billion, which renders it vulnerable to fraudulent activities and potential misuse of financial resources. Third sector trustees therefore have a duty to manage and protect their organisation's financial resources responsibly; ensure that funds are accurately accounted for and to ensure delivery of their mission as providers of social care and welfare to those in need.

This, however, is not always enacted and has attracted considerable media attention and negative perceptions of TS service social accountability. Indeed, following some recent TS scandals, (such as the Kids Company[1] which collapsed in 2015 triggering a financial and child abuse investigation, Rotherham Children's Services who were accused of a lack of social care and child abuse, and the Cup Trust tax avoidance[2] scandal), the Charities Commission[3] reported "our trust in the third sector has hit an all-time low". This has led to more robust reporting; governance and accountability structures being demanded within this sector.

After introducing the TS in more detail and discussing its nature and purpose in society, this chapter will define what accountability means in this arena and will investigate TSO accountability through three key lenses: reporting frameworks, the 'not-for-profit starvation cycle' and TSO governance. The reporting framework applied by TSOs focuses on the illustration of a not-for-profit organisation's sources and uses of funds, but it fails to highlight how activities performed by the organisation create measurable and meaningful social impact for program beneficiaries. With regard to the 'not-for-profit starvation cycle', donors expect charities to deliver more with less and tend to penalise those charities with high overhead costs. This often results in the delivery of fewer services and an undermining of the organisation's ability to create meaningful and measurable impact (Bedsworth *et al.*, 2008). The manner in which the organisation is governed has a direct impact on its ability to achieve financial and social objectives. Multiple governance methods exist in this sector, which is plagued by poor management, weak control over decision-making and the need to satisfy the interests and expectations of multiple constituencies (Caers *et al.*, 2006). This culminates in agency problems and accountability failures as well as the loss of organisational legitimacy and the erosion of financial support. (Cordery *et al.*, 2017). Following this the chapter will discuss the three forms of accountability typically found in TSOs: upward, downward and holistic. The chapter ends with important remarks, conclusions and critical takeaways.

The nature and purpose of third sector organisations

Using a broad definition, the United Nations (UN) defines the 'civil society' as the 'third' sector (TS) in terms of economic activity, placing it alongside the first and second sectors, or the public and private sectors respectively. Third Sector Organisations (TSOs) are unique in that they do not aim for profit and profit distribution; rather they are self-governed, driven and measured by their social

1 https://www.theguardian.com/uk-news/2015/aug/21/kids-company-faces-investigation-over-financial-collapse

2 http://www.thirdsector.co.uk/commission-easily-detected-cup-trust-scandal/governance/article/1184746

3 http://www.managementtoday.co.uk/why-weve-lost-faith-charities/reputation-matters/article/1369094#vKxPBKb7HgYRsTyL.99

impact, and fuelled primarily through gifts of time, insight and capital (Kelly, 2007; Lindsay, 2013). In fact, unlike first and second sector organisations, many consider TSOs to manage a double bottom line (DBL), in that while the achievement of fiscal goals is, of course, essential to the organisation's viability, advancement in its mission is the primary objective.

For these reasons, such organisations are defined as the 'voluntary', or the 'independent' or the 'not-for-profit' sector. Civil society rests upon the community and civic engagement.

> *Civic engagement means working to make a difference in the civic life of our communities and developing the combination of knowledge, skills, values and motivation to make that difference. It means promoting the quality of life in a community, through both political and non-political processes.*
> (New York Times, 2000).

Third sector organisations, therefore have a strong social orientation. An example of which is that of the Gavi-Vaccine Alliance (GVA). The mission of the GVA is to "sav(e) children's lives and protect people's health by improving the availability of vaccines in lower-income countries". GVA is a charity that was launched in 1999 with the mission of immunizing children in poor countries and is funded both by the public and private sources. Civil society organisations play a key role in advancing GVA's vision and mission; and working in partnership with governments in poor countries, they deliver up to 65% of immunization services, helping populations in remote areas and minorities gain access to vaccines.

In general, TSOs aim for sustainable social growth and the advancement of citizens' well-being; and, rather than distributing their profits to shareholders, they reinvest them in pursuit of their mission. This sector consists of community groups, voluntary organisations, charities, social enterprises, co-operatives and individual volunteers, business forums, faith-based associations, labour unions, philanthropic foundations and think tanks. The main sources of funding for TSOs are voluntary donations from gifts-in-kind and financial contributions, grants from government agencies, membership dues, income from fundraising events, sponsorships, donated goods, as well as income from investment activities in the form of dividends, interest and rent (The Charity Commission – GOV.UK; see also Emmanuel, 2014).

The importance of TSOs in the modern economy

The size, composition and scope of TSOs varies across countries and regions. In terms of size, the third sector is largest in Western Europe and in the United States, while it is much smaller in Latin America and in Central and Eastern Europe, with cultural, religious, economic and prevailing political structures driving these differences (Lester *et al.*, 1999). The demand for a social safety net, especially in Northern European countries, has driven civil society organisations