Charity Finance Group Written Evidence

Apprenticeships Inquiry

18th March 2016

Introduction

About CFG

Charity Finance Group (CFG) was founded in 1987. It is the charity that works to improve the financial leadership of charities, promote best practice, inspire change and help organisations to make the most out of their money so they can deliver the biggest possible impact for beneficiaries.

CFG has over 1300 members and they manage nearly £20 billion in charitable income. Its members work at the heart of the strategic development of their organisations, and are at the forefront of delivering a sustainable and efficient charity sector.

Finance professionals, with whom CFG have a close relationship, are often responsible for HR issues as well as managing the finances of their organisations. In our last survey of CFG service users 34% of respondents said that they were responsible for HR in their organisation.

Motivation for responding to the inquiry

CFG is pleased to submit this written evidence to the Sub-Committee on Skills, Education and the Economy on the important issue of apprenticeships. This submission focuses on:

- The target of three million apprentices by 2020, how the Government proposes to achieve this and how this may affect the 'skills gap'.

- The proposal for an apprenticeships levy and how this may be implemented.

CFG are submitting written evidence following consultation with our charity members on the existing plans for the Apprenticeship Levy. In January 2016 CFG hosted a roundtable with 35 of our charity members and representatives from BIS. This was followed by a further roundtable with the Minister for Skills, Nick Boles MP, in March.

Both meetings highlighted overall support for driving up skills and attracting people to work in the charity sector. However, there are a number of unique pressures that the Apprenticeship

Levy will place on charities, undermining the aim of the levy to increase the number of apprenticeships, and the charity sector's ability to engage effectively in it.

This briefing highlights these challenges and our recommendations to mitigate them.

Background to the Charity Sector

It is estimated that 1200 charities will be subject to the Apprenticeship Levy collectively costing an estimated £70m.

The charity sector is a major employer: according to the latest data, 821,000 people were employed by charities in March 2015 across the UK with 497,000 employees on a full-time basis.[1] This is bigger than the agriculture, mining, quarrying, utilities and property sectors.

The charity sector also mobilises 13.8 million regular volunteers, which is worth nearly £24 billion each year.

Summary

CFG supports the Government's commitment to increase skills across the economy through the introduction of the Apprenticeship Levy.

Charities have shown that they are committed to creating new opportunities for skills development. For example, a number of international development charities have partnered with City and Islington College in London to establish international development sector apprenticeships.

However, as this submission sets out, there are a number of challenges that limit the charity sector's ability to engage effectively with the Apprenticeship Levy, thereby undermining the levy's capacity to drive up skills across all sections of the economy.

These challenges can be summarised as follows:

- The expectation that charities allocate as much of their income to the front line as possible.
    - For many charities much of their income is restricted and so under charity law can only be spent directly as determined by the restriction rather than on core costs.
    - Spending money on core costs such as salaries, 'back office' staff and training (including apprenticeships) can attract criticism from the media and donors thus can pose a reputational risk for charities.

- The lack of existing training schemes, capacity and investment will mean that charities have a long way to go before they are able to use the funds in their digital accounts on training. To build capacity will take both time and additional funds.

[1] All data relating to the charity sector's workforce has been taken from NCVO's *Civil Society Almanac 2015* unless otherwise stated. http://data.ncvo.org.uk/a/almanac15/workforce/

    - Under existing plans, if charities do not spend the funds in their accounts this money will be directed to other employers. **This poses the risk that money allocated for charitable purposes will be redirected out of the charity sector to subsidise the cost of training in private businesses.** This poses a reputational risk to charities that could subsequently lead to fewer donations.

- Loss of key infrastructure – specifically the Third Sector Skills Council – means there is a lack of strategic oversight regarding skills and training in the sector.

- The additional investments or unintended consequences for charities such as additional expenditure to create opportunities for apprenticeships or the potential to suffer additional VAT.

Apprenticeship Levy: challenges for the charity sector

1. Financial challenges for the sector

1.1 The charity sector is in a precarious financial situation. The sector's income has fallen by £1.7bn since 2009/10 and according to the cross-sector financial sustainability review carried out by NCVO, Charity Finance Group and other sector bodies, the charity sector has barely recovered from the recession with an estimated income growth of 0.1% in 2013/14.

1.2 Moreover, unlike private businesses, many charities have high levels of restricted income and so under charity law this can only be spent directly as determined by the restriction rather than on core costs, such as the Apprenticeship Levy.

1.2.2 When it comes to paying the Apprenticeship Levy and the associated costs (see section 2), the lack of unrestricted funds will cause significant challenges for those many charities that receive funding purely to cover the cost of delivering their front line services.

1.2.3 For those charities that predominately deliver public services, the issue of unrestricted funding is particularly acute.

1.2.4 CFG's benchmarking survey recently found that large charities – those likely to be subject to the levy – are making an 11% median loss on government contracts. Those that deliver public service contracts will find it difficult to find room in their unrestricted funds to cover the direct and associated costs of the levy as well as the necessary investment to prepare for its introduction. **(See section 6.2 for CFG's recommendation to mitigate this risk).**

1.3 Even where money is not unrestricted, charities have a duty to allocate as much of their income to the front line as possible. Spending money on core costs such as salaries, back office staff and training – including apprenticeships – can attract (and has attracted) criticism from the media and donors thereby posing a reputational risk for charities.

1.4 Charities are also concerned that the cost of irrecoverable VAT will compound the cost of the levy.

1.4.1 Under the VAT system charities are, effectively, treated as a final consumer. This is because charities typically provide services that are exempt from VAT and as such they cannot claim back the VAT that they pay on the costs of delivering their charitable aims.

1.4.2 Irrecoverable VAT is estimated to cost charities £1.5 billion. This is money that could be better spent on delivering public benefit.

1.4.3 The government has shown that it is possible to address this issue for a chosen few charities, such as air ambulances, military charities, blood bikes and so on.

1.4.4 The European Commission has made clear that it is within the power of the UK government to create a refund mechanism to tackle this problem for charities. (See section 6.7 for CFG's recommendation to address this challenge).

2. Lack of sector skills infrastructure and existing apprenticeships

2.1 Some charities have taken the lead in developing apprenticeships for their sector. Christian Aid, ActionAid and PlanUK have developed an international development sector apprenticeship with City and Islington College in London.

2.2 However, in response to the volatile funding environment (as outlined above), charities have cut back on training and development.

2.2.1 The UK Commission for Employment and Skills (UKCES) survey 2013 found that 17% of voluntary organisations not investing in training cited lack of funds as the reason, compared to 10% in the private and public sectors.

2.2.2 An indication of the scale of this retrenchment can be seen in the fall in trading between voluntary organisations – most of which is spent on training and development – by 43% between 2007/08 and 2012/13.

2.3 Charities often work with vulnerable people and in challenging circumstances. 52% of the charity sector's workforce is employed in social work and residential car activities. As such, having the right skills within their workforce is essential.

2.4 However, the sector lost its skills council in 2013. It is therefore difficult for the sector to identify where the sector's skills gaps are.

2.4.1 In comparison, the industry sector has 6 Sector Skills Councils and 5 Sector Skills Bodies who work with over 550,000 employers to define skills needs and skills standards in their industry. This is in addition to 19 National Skills Academies, which lead the development of the infrastructure needed to deliver specialist skills in individual industries and sectors of the economy.

2.4.2 The Apprenticeships Levy in and of itself will not achieve the Government's aim of improving the UK's skills base – at least in the charity sector which is a major employer in the UK – unless there is investment in high quality sector-specific apprenticeship courses **(see recommendation 6.3)**. This is compounded by the increased financial burden that the levy will pose on charities outlined in Section 1.

2.4.3 Moreover, given the limited resources available for charities to develop training opportunities in the sector, and the lack of a skills council to provide strategic oversight of skills development and standards, the sector will be on the back foot when the levy is introduced in April 2017.

2.4.4 Charities are concerned that the 12 months until the levy's implementation is too short a timeframe in which to address the issue of a lack of sector-specific skills infrastructure and training **(see recommendation 6.6)**.

2.5 Given the continued pressures on the sector's finances and the policy of funders in the charitable and public sectors to reduce the amount of core funding given to charities, it is likely that the number of charities unable to invest in staff development will only increase.

3. The Levy risks redirecting funds away from charities to private businesses

3.1 Existing guidance states that if employers do not spend the money in their digital accounts the funds will be redirected to other employers. This poses the very real risk that charitable funds could be redirected out of the organisation to subsidise private businesses to train their apprentices.

3.1.1 This opens the wider question of how the levy interacts with the principles which underpin the use of charitable resources. For example, redistribution outside of the charity sector of apprenticeships levy funding could call into question whether money given for public benefit should be allowed to leave the sector in order to subsidise private sector employers and support private benefit. Should funding given to one charity by a funder or donor should be allowed to leave that charity in order to subsidise another charity's operations which were not their intention?

3.2 If it is found that charitable resources are being redirected to subsidise training in private companies, this could undermine public confidence in the policy. Moreover, this could lead to a reduction in donations as people question how much of their money is going to good causes.

3.2.1 There are a number of steps the government could take to mitigate these risks, **see section 6, specifically 6.4, for CFG's recommendations**.

3.3 The Skills Minister has indicated that employers will be given a year or so to spend the funds in their digital accounts after April 2017. However, given the funding challenges in the sector, and the lack of existing apprenticeships across much of the sector, there is significant risk that many charities will struggle to spend their funds within that time frame.

3.3.1 This challenge is also specifically related to the issue that employers can only use the levy to cover the costs of training apprentices and not the costs of developing apprenticeship schemes, recruitment, or salaries etc. Relaxing this rule for charities at least in the early years of the levy will enable them to use the money in their digital accounts, and will enable the government to meet its targets **(see section 6.5)**.

4. Apprenticeships and meeting the charity sector's needs

4.1 Under existing plans employers can register to become approved trainers. However, the lack of capacity and the funding challenges that many charities face (as outlined in section 1) will mean many charities may not have the capacity to go through the process of becoming a registered training provider. This will be especially true for those charities which receive the majority of their income through public service contracts.

4.1.1 CFG members have reported that buying in external training is not necessarily the best way to develop apprentices. In some cases it might be appropriate to provide in-house training.

4.1.2 The concern that the levy will encourage an emergence of expensive training courses delivered by private business that are not necessarily effective, nor meet the needs of the charity sector, has also been raised.

4.2 Our charity members have raised their concern that the levy will not drive up productivity in the sector.

4.2.1 Volunteers make a significant contribution to the sector's productivity. Charities mobilise 13.8 million volunteers, worth £24 billion annually.

4.2.2 When looking at skills gaps in the organisation a charity's first question is often: can this be done by a volunteer? Apprentices are likely to occupy the same level as volunteers within a charity's structure and so in order to use the levy charities will be incentivised to replace volunteers with apprentices, perversely reducing productivity.

4.2.3 The charities that we have engaged with have raised their concerns that the apprenticeship levy could force them to redirect money spent on recruiting and training volunteers to apprentices **(see recommendation 6.8)**.

5. Charities will not get more out of the Levy than they put in

5.1 A driving principle behind the levy is that employers will be able to get out what they put in. However, during both roundtables participants noted that this was not achievable.

5.2 As highlighted in section 2, many charities will need to make significant investment in identifying areas within their organisations where apprentices can work and in developing a high-quality apprenticeship scheme, recruiting into the scheme and so on. This investment will be on top of the levy.

5.3 For some charities, they could have as little as £1,000 in their digital account. For example, a charity with a wage bill of £3.3 million would have only £1,500 per year to spend on training.

5.3.1 In order to get out what they put into the levy charities would need to increase the number of apprentices they employ, thereby increasing the amount that they will have to pay in the levy. However, as they recruit more apprentices to get back what they put in, the pay bill will increase which will in turn raise the cost of the levy again.

5.4 Grants from medical research charities typically cover staff costs. Conversations with the university sector have indicated that most universities would seek to recover the cost of the levy through grants. This will impact the number of grants that charities can offer.

5.5 Charities are concerned that the cost of irrecoverable VAT will compound the cost of the levy **(see section 1.4 - 1.4.4)**.

6. Recommendations

CFG proposes the following recommendations to help ensure that the levy genuinely increases skills and productivity within the sector, whilst ensuring that money given for charitable purposes remains within the cause.

6.1 **The new board of the Institute of Apprenticeships should include a charity representative.** This will not only recognise that the sector is a major employer but also that charities face unique challenges in developing and recruiting into apprenticeships.

6.2 **Existing government contracts need to be uprated and future contracts need to cover the cost of the levy**. By accounting for the costs of the levy in existing and future contracts, government departments will be in line with NAO guidelines which state that contracts should meet a fair share of a "provider's central administrative costs". In specific regard to the voluntary sector, the NAO states that charities cannot be expected to subsidise the cost of the service from donations that it receives.

6.3 **Government should provide seed funding to assist the sector in creating new standards and capacity,** to ensure that funds are used for the purposes they were given and do not leave the sector (into the private sector).

6.4 **Ring fence unspent levy funds so that they are not redirected to private businesses.** Under existing plans there is the possibility that smaller organisations that do not pay into the levy could be awarded any unspent levy funds. Inasmuch as it is typically organisations with fewer that 50 members of staff which are most likely to report skills shortage vacancies, this stipulation could be seen as a positive one.

6.4.1 However, as outlined in **section 3.1 – 3.2.1**, this could result in funds meant for charitable purposes being redirected out of the sector to subsidise private business.

6.4.2 This could be mitigated by funds in charities' accounts being ring fenced so as to only be redirected to other charities, or invested in skills infrastructure for the sector **(see section 2)**.

6.5 **Allow charities to use the Levy to cover direct costs,** such as developing apprenticeship schemes, recruitment, salaries and other non-training costs.

6.6 **Increase the time frame in which charities have to spend the funds in their digital account.** This will allow charities a longer breathing space in order to put the necessary steps in place and build up funds in their digital account. This will also reduce the risk of funds leaving the sector.

6.7 **Government should seek to minimise charities' exposure to irrecoverable VAT.** For example, grass root costs for digital vouchers.

6.8 **Government should work with the sector to explore how volunteer training can be included under the levy.**