Grant Designs

Mapping the use of subsidy in the UK social investment market

A Flip Finance report for the Access Foundation – September 2017

FLIP FINANCE

ACCESS
The Foundation for Social Investment

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Research

Chapter 1
About the project

Who we are

- A social enterprise-led approach to designing and developing practical social investment solutions.
- A group of researchers, designers and social entrepreneurs.
- An initiative built off the back of the Alternative Commission on Social Investment and Social Invest Fest.

What we do

- **Research** – into the development of the social investment market and access to finance for social enterprises and charities.
- **Engagement** – with providers and potential users of social investment products.
- **Action** – working with stakeholders to develop products and support services the meet demand and promote positive social change.

The project - why we've done it

- Since 2003, many initiatives have sought to use subsidy to develop the social investment market
- Initiatives have been evaluated individually but evidence has not been brought together to provide an overall picture
- Access as a time limited provider of subsidy is keen to both learn from the past and shape discussions about the future

This initial overview considers:

- Mapping of commonly used structures for subsidy
- Sources of subsidy and their stated motivations
- How much subsidy has been provided
- Evidence of direct impact & on the broader market
- Assessing value for money

The questions we address are:

What subsidies have been provided?

What has happened as a result?

What are the big questions for the future?

What should happen next?

How we've done it

Desk-based research

Three blog posts

A roundtable event with social investors and sector leaders

Chapter 2

A short history of subsidy in the UK social investment market

The role of subsidy

"Most social investment requires subsidy, and subsidy should not be a dirty word. The enterprises we invest in typically lack scale, carry levels of risk that are disproportionate to the financial return, provide goods or services in markets or to clients where the margins are too thin, rarely provide any visibility on exits and often have capped returns to shareholders."

Nick O'Donohoe, (then) CEO, Big Society Capital (2013)

Tools for subsidy

While investing money with both commercial and social aims is not a new idea, UK government-backed efforts to support social investment began in the early 2000s. The practical tools that have been used to support the market have included:

- Grant funding (and other 'free capital')
- Tax breaks for investors
- Guarantees for investors
- Subordinate investment

Functions of subsidy

Five of the most important functions of (mostly) government subsidies for UK social investment since then have been:

- **Providing investment:** funds (including match funds) made available to be invested into charities and social enterprises
- **Funding market infrastructure:** grants and investments into organisations and resources that enable the market to function effectively
- **De-risking investment:** tax breaks and 'blended capital' – grants and subordinate investment used to 'crowd in' other investment and/or make investments viable
- **Promoting 'investment readiness'**: funding and support to enable charities and social enterprises to become better able to take on repayable finance
- **Supporting specific products:** funding for the development of new social financial instruments such as Social Impact Bonds

Short history of Subsidy - Prelude

Enterprising Communities: Wealth Beyond Welfare - Social Investment Task Force (2000)

Three out of five recommendations from Sir Ronald Cohen's task force were calls for government to subsidise social investment by:

- Creating Community Development Venture Funds (CDVF) with government match funding for investment from venture capital and institutional investors
- Supporting Community Development Finance Institutions (CDFIs), including via the creation of a trade association
- Offering a Community Investment Tax Credit (CITC) for investment into CDFIs

Phase One - 2000-2004: What's the big idea?

Problem: There was limited awareness of social investment as a concept. There was not much money available and no examples of social investment working in practice.

Solutions:

Bridges Ventures (2002) – example of CDVF's proposed by the SITF. UK govt provided a £20m matching investment to 'crowd in' funding from private sector

Adventure Capital Fund (2002) – 1st blended capital fund, offering mix of grants and loans, launched as a £2m fund to create sustainable community enterprises

Community Investment Tax Relief (2003) – tax break for investment into CDFIs worth up to 25% over 5 years, aimed to encourage investment in 'deprived areas'

Phase Two - 2004-2010: Making something happen (in public services)

Problem: Social investment popular as an idea but not much happening. Govt wanted charities to become more businesslike and develop innovative public service models backed by private finance.

Solutions:

Futurebuilders (2004-) – a £145m fund offering a mix of grants and loans to support voluntary sector organisations to bid for public contracts

Department of Health Social Enterprise Investment Fund (2007) – initial £119m grant/loan fund to support social enterprises in health & social care.

Development of the Social Impact Bond (2010) – new approach to Payment by Results contracting - charity service delivery supported by private finance. £11.25m grant from Big Lottery Fund to Social Finance to pay for outcomes from first SIB at Peterborough Prison (£6.25m) & development of the model (£5m).

Phase Three (part one) - 2011-2016: Building the market

Problem: The social investment market was heavily dependent on government and not big enough – in terms of size or volume of investments – to support a viable market of intermediaries...

Solutions:

Big Society Capital (2012) – a £600 million wholesale finance institution, supported by £400 million of public money – 'unclaimed assets' from dormant bank accounts. The aim was turn social investment into a 'self-sustaining independent market'.

Social Investment Tax Relief (2014) – a 30% tax break for individuals investing into charities and social enterprises.

Phase Three (part two) - 2011-2016: Building the market

Problem: ... while more private money was needed to grow the market, equally not enough charities and social enterprises were willing/able to take repayable investment

Solutions:

Investment and Contract Readiness Fund (2012) – a £13.2m grant fund supporting organisations seeking to bid for contracts or raise over £500k in social investment to work with approved consultants to become 'investment ready'.

Big Potential (2014) – an initial £10m grant fund with similar model to ICRF but initially for organisations aiming to raise less than £500k

Access (2015) – A £100m+ foundation with a £45m Growth Fund, offering grant/loan mix to charities and social enterprises seeking investments of £150k or less, and £60m to support investment readiness and market infrastructure.

Role of philanthropy

Alongside government-backed support for social investment, there is a long history of support from charitable sources. While repayable, philanthropic social investment is often provided at lower interest or on more patients terms than more commercial social investment. As these examples demonstrate, foundations have also played a significant role in the development of the market itself.

CAF Venturesome - set up in 2002, CAF's social investment arm has made investments totaling over £40m into more than 500 charities and social enterprises. The capital has been provided by over 100 philanthropic funders - both institutions and individuals.

Social Impact Investors Group - this ACF co-ordinated group includes 50-60 trusts and foundations with an interest in social investment meets regularly to consider issues including the role of foundations in development of the market.

Esmee Fairbairn Foundation - the leading trust in the social investment market launched its 'Finance Fund' in 2008 and has since made 120 investments with £45 million available to invest. Investments include direct investments into charities and social enterprises and investments into other social investment funds.

List of subsidy programmes - part one

Programme/ Organisation	Tool	Function	Date	Funder	Cost
Bridges Ventures	Free Capital	Providing investment	2002	HM Treasury	£20,000,000
Adventure Capital Fund	Grant funding / free capital	Investment readiness / providing investment	2002-2009	Home Office	£2,000,000
Community Investment Tax Relief	Tax break	De-risking investment	2003-ongoing	HM Treasury	£23,750,000
Futurebuilders	Grants / free capital	Investment readiness / providing investment	2004-2010	HM Treasury / Cabinet Office	£145,000,000
Department of Health Social Enterprise Investment Fund	Grant funding / free capital	Investment readiness / providing investment	2007-2013	Department of Health	£119,000,000
Communitybuilders -	Grant funding / free capital	Investment readiness / providing investment	2009-2012	Department of Communities and Local Govt / Cabinet Office	£70,000,000
Development of Social Impact Bonds	Grant funding	Supporting specific products	2010-2017	Big Lottery Fund	£11,250,000
Next Steps	Grant funding	Supporting specific products / Market infrastructure	2012-2013	Big Lottery Fund	£6,000,000

List of subsidy programmes - part two

Programme/ Organisation	Tool	Function	Date	Funder	Cost
Big Society Capital	Free Capital / Subordinate investment	Providing investment, De-risking investment, Funding market infrastructure	2012-ongoing	HM Treasury	£400,000,000
Social Incubator Fund	Grant funding / free capital	Providing investment	2012-2015	Cabinet Office	£10,000,000
Social Outcomes Fund	Grant funding	Supporting specific products	2012-2016	Cabinet Office	£20,000,000
Commissioning Better Outcomes	Grant funding	Supporting specific products	2012-2017	Big Lottery Fund	£40,000,000
Social Investment Tax Relief	Tax break	De-risking investment	2014-ongoing	HM Treasury	£1,020,000
Life Chances Fund	Grant funding	Support specific products	2016-ongoing	Cabinet Office	£80,000,000
Investment & Contract Readiness Fund	Grant funding	Investment readiness,	2012-2015	Cabinet Office	£13,200,000
Big Potential/Big Potential Advanced	Grant funding	Investment readiness	2014-2017	Big Lottery Fund	£20,000,000
Access	Grant funding	Providing Investment / Market Infrastructure	2015-ongoing	BLF /Cabinet Office	£82,500,000

Overall Totals

Activity	Funder	Dates	Amount
All Social Investment Subsidy	Government & Big Lottery	2002 - ongoing	£1,062,720,000

Chapter 3

What's happened as result of subsidy programmes

Subsidy so far...

This section looks at the apparent results of some of the subsidised activities based on publically available reports and evaluation.

It presents a series of examples covering a range of different tools and functions rather than a comprehensive overview.

There is no example of use of the tool 'guarantees for investors' as this tool has not been used in the UK market.

Community Investment Tax Relief (CITR) - (2003-ongoing)

Tool: Tax break for investors
Function: De-risking investment

What is it? A tax break of 25% over 5 years on investments by both companies and individuals into Community Development Finance Institutions (CDFIs) operating in 'deprived areas'.

What has it achieved? CITR has not been as successful as anticipated. In a government consultation response in 2013, the umbrella body for CDFIs, the CDFA (now Responsible Finance) explained that: "Since 2002, £95m has been raised mainly through bank loans to CDFIs and deposits into CDFI banks" with only 7 CDFIs raising money via using the scheme in 2012.

Key questions: To what extent has the de-risking of investment available via CITR generated investment for CDFIs that would not otherwise have been available? Is the limited uptake of CITR primarily due to the complicated specifications of the relief or to lack interest from investors?

Futurebuilders - (2004-2010)

Tool: Grant funding/subordinate investment
Function: Promoting 'investment readiness'/providing investment

What was it A fund providing grant/loan finance to charities and social enterprises to help them bid for public service contracts.

What did it achieve? By some distance the single biggest loan fund investing into charities and social enterprises in the UK. Invested £145m into 369 organisations including £117m in loans at a fixed rate of 6%. Evaluators describe the take up of investment by 'a sector unused to repayable finance' as 'a significant achievement' and notes the fund's Internal Rate of Return of -3% per annum as 'unarguably more positive than might otherwise have been expected'. Some critics challenged the costs of the programme while others worried that the fund became 'too dominant' within the wider social investment market.

Key question: Does the provision of government-subsidised, low interest loans, inhabit the development of a sustainable market for social investment?

Department of Health Social Enterprise Investment Fund (SEIF)- (2007-2013)

Tool: Grant funding/subordinate investment
Function: Promoting 'investment readiness'/providing investment

What was it? SEIF was a £100 million fund set up to stimulate the role of social enterprise in health and social care by offering applicants a mixture of grants and loans. A further £19 million was made available in 2012.

What did it achieve? By March 2011 the fund had invested £80,712,510 into a total 531 organisations. £11,372,637 (14%) was invested as loans. £3,086,430 was invested as 'repayable grants'. The remaining £66,253,443 (82%) had provided as grants.

Key question: Does the breakdown of spending suggest that SEIF should be regarded as: (a) an unsuccessful investment fund (b) a successful grant fund (c) both (d) neither (e) it doesn't matter if it supported more social enterprise involvement in health and social care?

Development of the Social Impact Bond (SIB) - (2010-2017)

Tool: Grant funding
Function: Supporting specific products

What is it? The SIB is a new approach to Payment by Results contracting which deploys socially motivated private finance to support voluntary sector delivery of outsourced public services. The £11.25m grant from Big Lottery Fund to Social Finance in 2010 was a grant specifically designed to support the development of SIBs as product. £6.25m of that money was allocated to cover some of the outcomes costs of the first SIB with £5m supporting development of further SIBs.

What did it achieve? The first SIB was halted early due to policy changes but the completed parts successfully achieived outcomes and delivered investor returns. It is too soon to form a clear view on the wider effectiveness of 'the SIB' as a model.

Key questions: How important was grant funding in enabling the first SIB to be developed and launched? To what extent have lessons learned from the first SIB been helpful in developing the wider market for the product?

Investment & Contract Readiness Fund(ICRF) - (2012-2015)

Tool: Grant Funding
Function: 'investment readiness'; Funding market infrastructure

What is it? ICRF was a a £13.2m grant fund supporting organisations seeking to bid for contracts or raise over £500k in social investment to work with approved consultants to become 'investment ready'.

What did it achieve? The evaluation reported that: Every £1 spent unlocked £18; £233m unlocked – £154m in contract / £79m investments; 78 (50.3%) out of 155 'successfully secured at least one contract or investment as a consequence of the support they received'. The report noted that amongst organisations who raised investment or secured contracts: "Around one in three ventures interviewed reported they would not have secured the deals without the support they received."

Key questions: To what extent did ICRF 'unlock' investment that would not have been raised otherwise?

Big Society Capital (BSC)- (2012-ongoing)

Tool: Free capital/Subordinate investment
Function: Providing investment; De-risking investment; Funding market infrastructure

What is it? BSC is a £600m wholesale finance institution, supported by £400m of public money – 'unclaimed assets' from dormant bank accounts, launched in 2012 aiming to turn social investment into a 'self-sustaining independent market'.

What has it achieved? BSC's Impact Report (2017) notes that since their launch '£467m of our capital has reached charities and social enterprises, of which £325m came from our co-investors.' In terms of the overall size of the social investment market: 'Overall £2B outstanding by the end of 2016, versus an estimated £800m in 2012'

Key questions: How big a factor has BSC investment been in 'crowding in' matching wholesale investment that would not otherwise have been available? How much closer is the social investment market to being 'self-sustaining and independent' as a result of BSC's activities?

Chapter 4
The big questions

Broad vs specific

This section considers some of the key questions about the role of subsidy for social investment and the social investment market in the future.

We initially planned to break these down into **practical questions** (about how particular outcomes are achieved) and **ethical questions** (about which outcomes and approaches are socially positive) however many of the biggest questions ultimately involve significant overlaps between the two.

What we have done is to highlight some **broad questions** (variations on questions that would be relevant to most attempts to fund social change), some specific questions particularly relevant to subsidising social investment and **a philosophical question** about when funding becomes subsidy..

What are we trying to make happen with subsidy?

As Allia's Phil Caroe highlighted last year, there are a wide range of perspectives on what 'social investment' is and what it's for.

Broad goals - from promoting the idea, to testing it out in practice through to building a market - are based on the assumption that support for 'a social investment market' as a distinct branch of the overall market for finance is either useful to have or possible to create. Others may like the idea in principle but not believe that it is important enough to be (partially) paid for with public or philanthropic money.

Even amongst those supporting subsidy for 'a social investment market' is the aim:

- ➔ to ensure the largest possible amount of money is made available to do social good?
- ➔ to ensure as many organisations as possible receive investment?
- ➔ to support organisations to help the largest possible number of people?
- ➔ to generate the maximum possible amount of 'social value' using an approach such as SROI?

Why subsidise social investment & not something else?

While accepting that different stakeholders may have different aims when providing subsidy, we can use Access as an example. Access's mission is to: "make it easier for charities and social enterprises in England to access the capital they need to grow and increase their impact."

Clearly the offer to organisations from 'the social investment market' is only one factor in determining whether this mission is achieved. For example, many organisations seeking to grow and increase impact might benefit more from business or impact management support that isn't specifically focused on social investment.

Access, as a social investment-focused organisation, will logically consider how best to achieve its goals via social investment but public sector agencies and philanthropic funders need to consider the usefulness of supporting social investment against other activities they might support.

Which approaches to subsidy work best in which situations?

We have looked at four tools – grant funding (and 'free capital'), tax breaks for investors, guarantees for investors and subordinate investment – that have been used to subsidise social investment.

These tools are not, in themselves, specific ways of providing subsidy – they have been provided both separately and together using a wide range of different models.

However there are a range of emerging questions such as:

- ➔ In what situations does grant funding consultancy improve 'investment readiness'?
- ➔ To what extent do tax breaks or guarantees encourage investment or different kinds of investment?
- ➔ How useful is subordinate investment in 'crowding in' more commercial investment – and what kind of investment does it crowd in?

How do we measure the commercial and social impact of subsidy?

We have considered the impact of various approaches to subsidising the UK social investment market by looking primarily at the evaluation of different initiatives on their own terms.

So far, no wider attempt has been made to consider either commercial or social impact of subsidy across a range of different programmes or initiatives. It is not clear the extent to which available data would enable the impact of previous activities to be assessed retrospectively. Either way, it may useful to consider what sort of data would need to be collected to enable useful learning about the impact of future programmes.

As discussed above, there are range of aims that might be considered – and there are also potentially complex questions about how to judge the extent to which outcomes or impact is attributable to particular subsidies or subsidised activity.

Who is being subsidised?

This is a practical question for any form of subsidy but for social investment it is also becomes a wider ethical question. As one example, a disproportionate amount of individual investment is made by middle-aged men living in the south east of England, therefore this demographic are likely to be the biggest beneficiaries of Social Investment Tax Relief (SITR).

In 2012, before the introduction of SITR, Clearly So's Rod Schwartz highlighted this danger warning that tax breaks: "would only benefit the rich, as only they have meaningful savings to benefit from fiscal incentives."

However, this is the tax breaks that such as EIS and SEIS that provide incentives for (mostly) rich investors to invest in early stage mainstream businesses, so the alternative angle is that SITR helps charities and social enterprises to compete for investment from rich people that would otherwise not be deployed for a social purpose.

When is it justifiable/useful to subsidise 'the market'?

Over the past 10 years well over £100m of public funding has gone into paying for activities that support the development of a market for social investment, as opposed to actual investment into charities and social enterprises.

This includes funding to develop the Social Impact Bond, a grant-funded market for investment readiness consultancy (primarily) through the ICRF and Big Potential programmes and funding for resources such as Good Finance, a website which helps charities and social enterprises to navigate the market.

Big Society Capital recently estimated that there may be as many as 120 intermediaries (60 'established' / 60 'emerging') operating within the UK social investment market. It is not clear how many of these are viable businesses without significant subsidy.

How should providers of subsidy prioritise their support for organisations that enable the social investment market function? Whose priorities are most important in this discussion – funders, investors, government, investees,, citizens?

Government-backed subsidy is time limited so what happens next?

There is a distinct role for philanthropic supporters in subsidising the social investment market.

While government and Big Lottery backed funders such as Access can make significant time-limited interventions, philanthropic funders have played a key role in supporting the development of social investment before government became interested and, crucially, will still be there after the government money has gone.

With this mind, it's important to consider:

1. whether subsidies are short term interventions to catalyse organisations or activities that will subsequently be viable without subsidy or
2. whether subsidies are create models for (or dependency on) subsidies that will need to paid for by somebody else in future

In situations where (b) applies, Access and other short term funders need to consider how well their approaches to subsidy are aligned with those of philanthropic organisations who may provide ongoing subsidy in the future.

When does prioritising social returns become subsidy? - part one

When looking at individual investments (rather than wider subsidies for 'the market'), it is possible to argue that any investment that does not prioritise that highest possible risk adjusted return amounts to subsidy.

If, for example, a multi-millionaire investor has to choose between buying a football club or a spam factory. The investor believes the investment in the spam factory will deliver a significantly greater risk adjusted return but he/she would rather be known as the owner of a football club than a spam factory. Is this investor subsidising their ego at the expense of their bank balance, or are they buying the prestige of owning of a football club?

Your answer depends on your perspective. So it also a matter of perspective whether investing for 0-100% financial return on a social investment means that an investment is being 'subsidised'. Has the money that a public or philanthropic funder 'loses' when putting in a grant or guarantee alongside a repayable investment been lost or has it been spent on funding social good?

When does prioritising social returns become subsidy? - part two

Bob Thust advocates an approach to social investment that starts with what the investee/grantee can afford to repay rather than framing the issue as 'we need a return on investment so we need subsidy to make it work', adding that what we are talking about is getting the greatest available impact from limited grant funds.

So for example, if may be possible to provide £50,000 worth of 'repayable grant' to two organisations with each of them paying back £25,000 and becoming more socially useful and commercially viable in the process.

The commercial investor sees as two investments that have lost £50,000 each, the funder of social impact sees this as spending £50,000 on supporting two organisations to deliver commercially viable social impact.

For many, a binary distinction between investment that aspires to be a commercial activity and everything else is a misunderstanding of the 'market' for supporting positive social change.

Chapter 5

Next steps

Next steps

Building on current experience:

Move beyond 'investment readiness' to better align subsidised support to the needs of potential investees

Be clearer about how and why subsidy is being used to mitigate investment risk

Develop better data on financial and social impact of different types of subsidy within the market

Appendices

Blog posts

Much of this report is based on three blog posts published on the Access website in April, May and June 2017.

Blog One:

Tools used for subsidy & their intended functions; A short history of subsidy in the UK social investment market

Blog Two:

What happened next - the impact of some of the most important subsidised activities based on publicly available evaluation

Blog Three:

Key questions about the role of subsidy for social investment and the social investment market in the future

Roundtable attendees

Andrew Denney - National Audit Office

Seb Elsworth - Access

Marcus Hulme - Big Society Capital

John Kingston - Access

Fergus Lyon - Middlesex University

Gen Maitland Hudson - Power to Change

Anna Merryfield - Social Spider

Julia Morley - LSE

Jenny North - Impetus PEF

Debbie Pippard - Barrow Cadbury

Ben Rick - SASC

Gemma Rocyn Jones - Right to Succeed

Nicola Rusk - TSIC

Nick Temple - Social Enterprise UK

Dave Thornett - Key Fund

Nick Wyver - DCMS

Note on fund numbers

Over the course of the report a number of funds including Futurebuilders, Department of Health Social Enterprise Investment Fund and the Investment and Contract Readiness Fund are mentioned multiple times with links to relevant news report and evaluations.

There are sometimes discrepancies between the reported values of funds across the sources for a range of reasons including - some funds received additional funding part way through their existences; some reports include the running costs of funds as part of overall costs and some do not.

To ensure consistency, we have attempted to use the final published figures from fund managers on each occasion a fund is mentioned. Due to the multiplicity of conflicting data, minor errors or inconsistencies may remain.

Note on Peterborough SIB grant

An £11.25m grant from Big Lottery Fund was made available to Social Finance to pay for outcomes from first SIB at Peterborough Prison (£6.25m) & development of the model (£5m).

The Peterborough SIB was halted early due to changes in government policy. We understand that, as a result, the bulk of the £6.25m allocated for possible outcomes payments was not drawn down although information it is not currently clear how much of this money was used.

A Flip Finance report for the Access Foundation

September 2017

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