Enterprise Growth for Communities

Investment Policy

(V1.1 April 2022)

In February 2022 DCMS announced an additional £20m blended finance facility to Access, funded through Dormant Accounts.

This investment policy sets out how that funding will be committed.

Part 1: Overall Investment Objectives

Through the provision of subsidy into fund structures, the programme aims to enable intermediaries to support charities and social enterprises which they would otherwise be unable to invest in due to barriers including risk and cost. At an ecosystem level the programme will build upon the Growth Fund's legacy and further demonstrate the efficiency of subsidy in small-scale investment.

The programme aims to hone the delivery models for this type of finance, building on the elements of the Growth Fund which worked well whilst also adapting in response to: a) the learnings from the Growth Fund (and Access's other programmes); b) the context of a pandemic and post-pandemic environment; c) our desire to ensure that EDI is more closely considered in everything that we do; and d) the different grant source for this programme.

Access to appropriate finance should increase the financial resilience of charities and social enterprises in order to enable them to better serve their communities by sustaining or increasing their social impact. The programme should serve those organisations which require small-scale, simple, subsidised finance products and for whom the larger, less subsidised or more complex products in the wider market are unsuitable. The programme also aims to strengthen the social investors who will deliver the programme.

Part 2: Aims & Objectives

- **Overall Ecosystem goals**
  - The programme should maintain and increase the supply of small-scale blended finance. The use of grant by intermediaries should enable charities and social enterprises to access suitable small-scale capital where they would not otherwise be able to do so.
  - The programme will focus on supporting the capital needs of small and medium sized trading charities and social enterprises. These organisations will typically turnover less than £500k with fewer than 20 staff.

- The programme aims to make up to 1,000 investments into charities and social enterprises
- At a programme level finance should be available to charities and social enterprises located anywhere in England, but with a particular focus on reaching those in (or serving) areas of higher deprivation. We will aim for at least 50% of the fund to be invested in the most deprived 30% of neighbourhoods and at least 25% of the fund in the most deprived 10% of neighbourhoods.
- This programme does not have a focus on any specific outcome areas or beneficiary types. Individual funds may choose to specialise/ target their reach towards certain places or outcome areas, but funds should not be overly niche.
- The overall programme should make finance available to the sector from January 2023 (or earlier) to at least the end of 2025.
- Building on the knowledge base from previous programmes, this programme should seek to hone (rather than prove) the delivery model(s) for small-scale social investment.

- **Co-investment and leverage goals**
    - With £20m of grant the programme aims to enable £60m+ of investment to flow to charities and social enterprises. This can be achieved through a combination of capital leverage and recycling.
    - It is expected that social investors will apply for co-investment separately to the Access grant rather than as a package. Co-investment fundraising will be led by social investors, but Access will endeavour to support with this where requested/ possible.
    - The sources of co-investment and, therefore, the interest/ fees that fund managers are charged on that co-investment will likely vary. Levels of subsidy provided into individual funds should be appropriate to the need and should be mindful of the potential for competition and the risk of market distortion.
    - The Access investment is anticipated to be provided to intermediaries as a grant and therefore is not expected to be repaid. It is however possible that some of this grant is made on the basis that it may be repayable. Where this occurs, the guiding principle will be to align incentives between Access, co-investors and social investors.
    - The investment from Access is expected to offset risks sufficient to leverage repayable capital from external capital sources where capital could not otherwise be made available in this way.
    - It is assumed that most external capital that is leveraged will be repayable back to co- investors, although this may not always be the case. It is possible that match may be in the form of other grant but only in so far as this achieves the overall objectives of the programme by using subsidy in the most efficient and effective ways. As such, subsidy –

both Access's and that from any other sources – should be used where it is needed and not where it is not.
    - Repayable co-investment capital may generate a modest return for the co-investors, which we would not usually expect to exceed c. 6% (and in many cases will be much lower), although the appropriateness of the return rate should be considered in the context of the loss coverage, risk and other relevant factors.
    - It is the aim that this programme plays a role in maturing the overall market and as such there is an expectation that sources of co-investment will vary to a greater extent than on the Growth Fund, with less overall reliance on BSC capital at a programme level (an ambition which BSC share). However, leveraging new and innovative sources of capital is not an explicit objective as it was on Flexible Finance, so there is no particular expectation that one source of capital will be deemed preferable to another. As such, our assessments will focus on the overall suitability of the capital to a greater extent than the source.

- **Intermediary market goals**
    - This programme aims to build on existing and experienced infrastructure by strengthening the fund managers who will deliver it. Therefore, consideration of how a fund will leave the fund manager stronger and more resilient will form part of the primary assessment.
    - The programme will enable fund managers to offer small-scale loans by mitigating transaction costs to make this affordable
    - The programme will enable fund managers to widen their reach and to support (although not exclusively) organisations which have been unable to access social investment before.
    - This programme should be inclusive by design: borrowers and intermediaries will be expected to embed equality and diversity into their governance structures and to monitor/ report these areas.

- **Product goals**
    - The programme is designed to meet the demand for small-scale investments. Fund managers will be asked to propose an upper investment threshold for their fund which should not exceed £200k (which is the programme's maximum investment size) but in many cases will be lower. The programme will target an average investment size in the region of £60k - £80k. Fund managers will be asked to propose a target average investment size for their fund in their application which will then form part of their mandate.
    - The vast majority of investments made through this programme should be unsecured. Fund managers may opt to take security in occasional and limited circumstances by exception. This should only be considered if there is a particular concern about an asset falling into private hands/ not being retained for the community in the event that an investee

ceases trading. Security should not be taken for the purpose of de-risking an investment as subsidy is being provided to offset the risk of making small unsecured investments.
  - Loans will typically be repaid over a maximum of 3-6 years although some, particularly for cash flow needs, may be for a shorter period
  - The programme will offer appropriately priced, affordable loans, with <u>average</u> effective interest rates on the loan element expected to be in the region of 4-8%. Whilst Access agrees that there is a need for very low or nil interest products in the market, this is not the need/ gap that this particular programme is designed to fill. As such, funds established under this programme will be expected to offer average rates which are affordable, but which do not significantly distort the market or undercut other funds' offers within the programme.
  - It is expected that loans will include a degree of flexibility (for example initial 12-month capital repayment holidays) as well as post-investment flexibility when required without incurring significant additional fees.
  - Some borrowers will receive direct grant alongside their loans where doing so makes the overall package most suitable and affordable. Fund managers may also opt to provide a limited portion of the direct grant to investees post-investment.
  - Fund structures/ operating costs will enable social investors to support their applicants and investees both pre and post investment. However the Reach Fund will be available for more formal or substantial pre-investment support so the grant should not be used for purposes which that programme can serve.

- **Impact on charities and social enterprises**
  - The programme will seek to remove barriers to social investment that are often faced by smaller and/ or younger organisations
  - Access to appropriate finance should increase borrowers' financial resilience to bring stability and growth (of earned income/ element being invested in) over the medium term, with the view to protect and where relevant augment the social impact of each organisation so that they can continue to serve the communities they serve both now and in the future.
  - This programme should be inclusive by design: borrowers and intermediaries will be expected to embed equality and diversity into their governance structures and to monitor/ report these areas.

- **Impact on people and communities**
  - We believe that more resilient organisations are better placed to deliver social impact and meet the needs of the communities that they exist to serve. Social investors will have good systems in place to assess and ensure that they are investing in socially impactful organisations,

although we recognise that it is not always possible to draw a direct line of attribution from investment to specific impact outcomes.

Part 3: How will we achieve those aims?

a) at a wholesale level

Fund sizes, length & composition

It is anticipated that the Investment Committee will make in the region of 5-8 individual grant awards, to use up to a maximum of £20m of Access funding.

Fund sizes should ensure value for money and sustainability during the course of the programme. Therefore it is not envisaged that there will be very small funds (e.g. <£2m total fund size) under this programme. However, there is no explicit minimum fund size so the IC may decide to approve smaller funds if there is a compelling reason to do so. Similarly, there is no maximum fund size, although with any larger funds (e.g. >£12m total fund size) the IC should be comfortable that any risks relating to over-reliance on individual partners are appropriate.

It is envisaged that a minimum ratio of 50:50 grant to co-investment should apply to individual funds. However this ratio may be exceeded where there is a compelling reason to do so. The amount of capital being made available to the frontline will be a greater consideration than the amount of capital leveraged into the fund, recognising that fund structures which enable large volumes of recycling can be more cost effective than their leverage ratio alone might suggest. The programme aims to make at least £60m of investment available to charities and social enterprises by the end of 2026.

This grant cannot be blended into existing Growth Fund funds alongside TNLCF grant. It is envisaged that this grant will be used purely to establish new funds, however we can consider requests to blend the grant into an existing (non-Growth Fund) fund structure if appropriate. The subsidy should be used to grow the small end of the market but not to the detriment of other areas of the market, so this should be an area of consideration if existing fund structures are proposed.

Individual funds' deployment periods may vary but should not initially be shorter than two years. Funds should be structured to initially utilise all of the Access grant by the end of December 2026 (or earlier) and will be assessed primarily on the volume of deployment that they expect to do during this period. However, if fund managers wish to structure funds to continue recycling/ utilising residual grant beyond this period, and/ or create structures into which they would plan to bring in additional investment in a few years' time, then this would be welcome.

Access is open to different legal structures for funds and will not require the use of wholly owned subsidiaries, although some co-investors may require this.

Fund Manager experience

It is envisaged that the majority of proposals will come from experienced fund managers with proven track records of undertaking similar types of activity and who can demonstrate strong levels of customer satisfaction of the investment and support offered. Applicants who have managed a Growth Fund fund should be able to demonstrate how their proposal factors in the learnings which that generated. It is not a requirement that applicants have managed a Growth Fund, however any who have not should be able to demonstrate suitable alternative experience as well as an understanding of how the aims of this programme relate to the continuation of Growth-Fund style activity. This is in order to ensure that the programme builds upon the Growth Fund's tried and tested approach rather than seeking to re-invent the wheel.

Unlike when the Growth Fund was launched, bringing new entrants into the social investor market is not an explicit aim of this programme. New entrants may be considered by exception but would need to clearly articulate the gap/ need that they would be serving and why this would be unlikely to be met by other providers, and evidence their ability to deliver a social investment programme. Partnerships are welcome but should identify a Lead Partner, usually an experienced social investor, to take overall responsibility for the application and the management of the fund and to act as Access's primary contact throughout.

Use of the grant in the blend

The grant can be used in a number of different ways but these will broadly fall into three purposes: operating cost subsidy (which can include set-up costs and costs relating to supporting the expansion of reach and enhancing EDI practice) ("Grant A"), fund level loss layer ("Grant B") and/or direct grant to investees ("Grant C") . We will not necessarily require Grants A and B to be ringfenced as two separate pots, so fund managers may propose flexibility there. However we will generally expect any Grant C pots to be ringfenced. Fund managers will not be penalised for proposing similar or identical structures to Growth Fund funds if they consider those to be optimal already. However, fund managers are encouraged to build on Growth Fund learnings and propose improved structures where they believe these will better serve the needs of their investees and support their own resilience.

It is presumed that loss protection will be a major use of grant and we are open to social investors proposing the most suitable structures in this regard. This need not necessarily rely on a single subsidy:capital ratio across a fund's entire portfolio, however the principle should be around efficient use of the grant. On this basis we will discourage ringfenced mechanisms where first loss grant is set aside for individual deals.

It is expected that there will be a level of default (by charity and social enterprise borrowers) within the programme. The existence of grant enables social investors to invest with a higher level of risk, so if no defaults were to occur it would be a sign that the programme had not succeeded in reaching the smaller, higher-risk borrowers that it aims to serve. Individual funds' projected default levels should be evidence-based and might be expected to be within the 10-40% range depending on their target market and other relevant factors.

Some grant may be passed onto charity and social enterprise investees directly as grant. This need not necessarily be limited to grants at the point of investment – fund managers may make a case for providing an element of grant post-investment instead if this would best serve their investees' needs. However programme grant should not be used for purposes which Reach Fund grant can serve, as the programme will be supported by the Reach Fund and fund managers will have the opportunity to become an Access Point if they are not one already. Any direct grants to an investee (excluding any separate Reach Fund support) should be capped at the value of their repayable investment.

Fund managers' operating costs

This programme seeks to improve upon the Growth Fund structure when it comes to operating costs, potentially by exploring ways to decouple operating costs from short-term deployment in order to avoid fee drag and difficulties for social investors by seeking to strengthen the sustainability of the model.

This programme aims to strengthen the fund managers delivering it, with a focus on "build not buy". It will be necessary to balance this objective – and operating cost mechanisms – with the need to ensure value for money and the continual flow of capital to charities and social enterprises. We are open to investing directly into intermediaries (as opposed to SPVs) should this help to achieve these goals.

b) at a retail level

Capital need

The programme is designed to serve charities and social enterprises who require small-scale, simple, subsidised finance products and for whom the larger, less-subsidised or more-complex products in the wider market are currently unsuitable.

Organisation eligibility

Eligibility criteria for charities and social enterprises will match those of the Growth Fund and the Reach Fund (see Appendix for full criteria).

Investees must be based in England and primarily serve beneficiaries in England.

This programme does not have a focus on any specific outcome areas of beneficiary types. Individual funds may choose to specialise/ target their reach towards certain outcome areas but should not be overly niche. Charities and social enterprises working in any eligible outcome area should be able to access finance at a programme level. Organisations which seek investment specifically for political campaigning or the advancement of religion are ineligible.

Deal Size

The primary objective of this programme is to ensure the continued supply of small-scale blended finance which the Growth Fund provided before it. The programme level maximum deal size will be £200k, which is £50k higher than it was on the Growth Fund. This is partly in recognition of inflation that has occurred since the Growth Fund launched in 2015 and will continue to occur throughout this programme. It is also in order to enable flexibility in responding to the needs of the sector and to enable fund managers to offer occasional larger loan and grant blended deals where there is an opportunity to support the scaling of a proven intervention. However social investor applicants will be encouraged to propose their own maximum thresholds (which in many cases will be lower) and targets for average deal size in-keeping with the aims of the programme. The majority of funds will be expected to target a median investment size of between £60-80k in line with the aims of the overall programme. Fund managers should provide clear justification for their proposed average and maximum deal sizes (including in the context of the level of subsidy required).

If an investee is also receiving other repayable investment at the same time/ towards the same project – either from another fund operating under this programme or from another investor outside of this programme – then the £200k upper investment limit applies to the **total** amount received by the charity/ social enterprise. The £200k cap is inclusive of any EGC grant. However if the investee is also receiving other sources of grant towards the project this would not count towards the £200k limit.

Fund managers should ensure that investments made through the programme necessitate the use of subsidised finance and that subsidy is not being duplicated elsewhere. Fund managers are welcome to invest in a charity or social enterprise alongside another investor as part of a co-investment, this should not be done for the purpose of making a larger investment than could otherwise be made through this programme alone. Where co-investments occur, the total investment size will need to be within any maximum investment cap that has been set at either a programme or fund level. Such caps include grant provided through this programme but exclude any external grant that the investee receives towards the same project.

Product & purpose

We imagine that in most cases investments will be comprised of small-scale term loans with relatively simple repayment profiles. An element of grant may also be passed onto the charity or social enterprise akin to "Grant C". It is anticipated that investments will be used by VCSEs to support with general enterprise or growth and/ or to strengthen their medium-long term resilience.

The vast majority of loans offered by fund managers to charities and social enterprises will be unsecured and it is not the intention of this programme for lots of larger, secured deals to be made. However, fund managers may consider taking security in exceptional circumstances but only if there is a specific concern about an asset falling into private hands/ not being retained for the community in the event that an investee ceases trading. Security should not be taken for the purpose of de-risking an investment as subsidy is being provided to offset the risk of making small unsecured investments. Social investors' applications should specify whether they would want the option of taking security in exceptional cases and, if so, should set out how such decisions will be made.

The programme exists to serve those organisations which require small-scale, simple blended finance products and for whom the larger, less-subsidised or more complex products in the wider market are unsuitable. It is therefore the hope that the programme will reach a good proportion of first-time borrowers. However the programme is not limited to first time borrowers – those who have had social investment before are eligible, as are investees who may wish to return for a second investment under this programme, where appropriate. The subsidy should however always be used to benefit organisations which could not access suitable finance from other sources. This will be determined on a case-by-case basis at the fund managers' discretion – Access will not require that applicants have been specifically turned down by a bank/ other social investor for funding, although fund managers may choose to set this criterion themselves.

Charities and social enterprises may on occasion wish to access the programme in order to refinance existing debts. This should not, as standard, be the primary purpose for an investment, however there may be instances where this is an appropriate use of subsidy – particularly if the deal includes the refinancing of a small amount of existing debt as part of a larger deal such as where the organisation has taken on emergency investment during the pandemic and needs to consolidate. In any such cases there should be a clear rationale as to why that is an appropriate use of subsidy and does not constitute double subsidy, and the fund manager should have a process in place to make this assessment themselves. "Grant C" style grant provided through this programme should not be used (either in full or in part) to refinance deals made through any other Access programmes (including the Growth Fund).

Equality, inclusion and reach

The overall programme should achieve good coverage across the whole of England, although individual funds may target specific geographies and reaching areas of high deprivation will be a programme priority. Fund managers should be able to demonstrate and report on active participation in the sector's efforts to address challenges and practices around EDI, by understanding and actively working to remove barriers to access. Fund managers will be expected to sign up to – and act upon – the Diversity Forum's manifesto.

Fund managers will need to consider how their products, outreach, practices and partnerships are lowering barriers and achieving reach as far as possible. Monitoring of EDI reach will be required, and fund managers will be encouraged to set themselves targets in this regard. The programme is primarily intended to provide simple term loans; however this should not be seen as a barrier to fund managers adapting their product design to increase the inclusivity of the products on offer, which is something that Access would welcome.

Appendix: Investee eligibility criteria

An eligible organisation is an incorporated voluntary, community or social enterprise organisation which serves communities solely within England and which is either:

(a) a charity, Community Interest Company or Community Benefit Society, registered with the relevant registry body; or

(b) an unregulated organisation which:

- *i. has a clear social mission which, in the reasonable opinion of the Fund Administrator, is analogous to a recognised charitable purpose;*
- *i. distributes less than 50% of post-tax profits and reinvests at least 51% surpluses into pursuing its social mission;*
- *ii. has a constitutional or contractual lock on its social mission, its dividend and surplus distribution policy and "asset-lock";*
- *iii. carries out, or has ambitions to carry out, trading activities in support of and which are causally linked to its social mission;*
- *iv. offers its products and services for general public benefit without restrictions and barriers, such as affordability;*
- *v. is open to undertaking an independent social impact audit;*
- *vi. has remuneration and benefits policy which it is willing to make publicly accessible, and which is reasonable and proportionate relative to the market practice for VCSEs;*
- *vii. in the case of a sale of the organisation, the directors make best efforts to preserve the social mission under new ownership;*
- *viii. can demonstrate that no private benefit will arise from the Grant; and*
- *ix. no state aid/ subsidy control issues have been identified;*