London Funders

Working together to strengthen London's voluntary and community sector

SMART MONEY… MAGIC BULLETS?

A meeting of London's funders on new and different forms of investment and support for London's VCS

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Hosted by

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SOLICITORS

Whatever their response to the government's approach to reducing the deficit through public expenditure cuts, all funders are inevitably affected by it. While much attention is going into managing cuts intelligently and coping with reduced budgets, many funders are asking whether it is time to break away from the same old funding and investment processes and try something different from contracts for commissioned work, and grants.

This event aimed to help funders make sense of the social investment market, the broadening array of charitable and enterprise vehicles and increasingly blurred boundaries in delivery mechanisms. It explored the relevance and viability of different approaches - how do they work, how risky are they, will they stretch meagre budgets, is there an appetite in the voluntary and community sector (VCS) for new forms of funding?

ACKNOWLEDGEMENTS

Bates Wells & Braithwaite generously hosted this meeting: our thanks to Stephen Lloyd and his colleagues.

CCLA Investment Management Ltd donated an iPod used in a prize draw to encourage participants to complete evaluation forms.

GLOSSARY

Blended value: the mix of economic, social and environmental value components generated by organisations.

Mission-related investment/ Mission-connected investment: an investment approach that targets a market rate return and contributes to a foundation's mission by aligning investments with values and mission.

Programme related investment: investment activity funded from income or capital with the principal aim of advancing the funders' charitable purpose.

Social enterprises: businesses with primarily social objectives, reinvesting any surpluses back into the business or to the community for social purposes.

Social impact bond: the first UK example is the Peterborough Social Impact Bond offered by Social Finance, a derivative tied to the performance of an organisation supporting short-sentence male offenders leaving Peterborough prison to stay out of prison over five/six years. A financial return is offered to the bond-holders that have funded the support; the size of the return is related to the money saved by the Ministry of Justice (MoJ) through deterring reoffending. Fairly simple metrics are based on the number of court events and the MoJ are also measuring the reduction of re-offending of this cohort of 3,000 short-sentenced offenders against a control group.

Social investment: investing capital with the primary purpose of building capacity and achieving impact.

Socially responsible investment: investment with the principal aim of producing income or capital growth but with weight given to social considerations in choosing which investments to make and how to manage them.

Social return on investment (SROI): a framework for measuring social value, based on cost-benefit analysis that allows a proxy financial value to be put on the results of a charity's work.

Networking time

SERVICE TRANSFORMATION: ADAPTATION IN THE SECTOR

Stephen Lloyd

Stephen Lloyd, Senior Partner at Bates Wells & Braithwaite, is increasingly involved in the phenomenon of "charitisation" and he provided an example of this – very much the shape of things to come as the Coalition government's policies work through.

Two years ago, the British Waterways Board (BWB), a statutory corporation which manages Britain's network of canals and both a large scale employer and a significant manager of listed buildings, decided to move to the third sector. This was in advance of the current government's interest in shifting it from the government's balance sheet (where it has needed a subsidy of some 25-30% of its annual £230 million or so of income). Stephen has worked with BWB on the legal aspects of becoming a charity and is very aware of the need it will have to raise substantial funds and maintain high levels of volunteers. Part of the complexity of transferring from statutory status is to do with continuity of employment and current terms and conditions based on public sector provision.

He noted that this process of moving from the public sector either to privatised or voluntary structures is very much what the Coalition has in mind for many future services. For example, the NHS White Paper has little detail but a strong vision for different delivery vehicles, and the Secretary of State has expressed his hope that this will include "a vibrant social enterprise sector".

While this is an interesting legal issue, Stephen noted his concern that people in medical/clinical jobs in health services will have many new skills to learn if they are to run free-standing enterprises: he drew a comparison with the big shifts in knowledge, skill and attitude that had been needed in post-Communist countries – and which took time to develop.

One of the concerns amongst funders and the VCS is whether such enterprises, especially if they are private sector operations, will be able to maintain community "buy-in" and involvement, including volunteers. Stephen emphasised how much this had figured in the Waterways Board's planning for change especially in relation to governance and operations.

INVESTING ASSETS: SOCIALLY RESPONSIBLE INVESTMENT
Helen Wildsmith, Head of Ethical & Responsible Investment, CCLA

Helen was unwell and unable to join us but she provided a few key messages to summarise her perspective:

High impact investments aim to deliver the direct mission-related outcomes that increasingly trustees are seeking and these can be integrated into portfolios for two reasons:

- sometimes they have risk/return characteristics that mean they can hold their own in a portfolio on financial grounds alone ("financially-led" investment)
- sometimes they gain a place in the portfolio because the alignment with mission is so strong that poorer financial prospects are seen as a small price to pay for the benefits ("mission-led" or sometimes "impact-led" investment).

Helen's article which explains these in more detail can be found in The Bulletin of The Ecumenical Council for Corporate Responsibility (www.eccr.org.uk), June 2010 edition on Positive Impact Investment.

For the most part this meeting addressed the latter – the mission-led use of money.

FUNDING AND GROWING THE SECTOR
Peter Kilgarriff, Chief Executive, LankellyChase Foundation

LankellyChase Foundation is the result of a merger between two grantmaking foundations that had operated in tandem since they were formed in the 1960s. It makes grants of about £5 million a year with priorities of empowering local communities, supporting mental health, tackling abusive relationships and criminal justice issues. It has a growing social investment programme and Peter described the last few years as a "journey" towards a more effective use of the Foundation's assets.

"The journey continues" said Peter. Investment policy used to rely on the expertise of senior trustees or the Chairman but in recent years the trustees have decided to see how the Foundation's endowment could be used to reinforce their grant programmes.

The Foundation's investment policy is based on the aim of maintaining the real value of assets (£100 million+) and maximising income. Their first venture into social investment was to set up a loan fund with 5% of their capital (after hearing a presentation from the Community Development Finance Association at an AGM). They invested £200,000 in Charity Bank preference shares in return for Charity Bank undertaking the necessary due diligence for them in deciding on loans. This was not a great success. In five years, they only made one loan, perhaps in large part because their field of interest was too narrow (i.e. aligned with their grantmaking).

Peter Kilgarriff (left) and Geoff Burnand (right)

Trustees then chose to explore the possibilities in more depth and signed up to the UN Principles of Responsible Investment (http://www.unpri.org) and developed a code of practice which informs investment decisions and helps in relations with fund managers. They renamed their loan fund a "social investment fund", intended to fund a portfolio of social investments that, in turn, are expected to produce a financial return. They have invested so far in:

- East Lancs Moneyline (www.elmline.co.uk), supporting work in five towns in South Wales to combat doorstep lending (£200,000 over eight years; capital is returned with interest in the last three years), and
- Peterborough Social Impact Bond (£500,000); see Glossary, page 2. Peter noted that most of the investors in this Bond are grantmakers working in the criminal justice system and see this investment as deepening and widening their work.

They are also looking at Big Issue Invest, a £10 million fund for developing social enterprise. They are considering an investment of £250,000 over five years at 5-10% return. Other investment scope might be with the Ethical Property Company which is exploring (with Trust for London) establishing a building which could house a range of human rights and social justice organisations.

The first Social Impact Bond has started well, reaching (or exceeding) its £4.9 million investment target. It has selected an area where highly measurable and relatively short term goals can be set. Participants queried how easily this might be transferred to other areas. Peter felt that there were many areas of social care provision as well as other parts of the criminal justice system where similar projects could be devised that would represent scope for investment with returns based on savings made. Addiction was one obvious field that seemed ripe for such support; preventing children going into public care by supporting families is another. Peter stressed, however, that this is not an easy answer. Contracts between Government and Social Finance were detailed and time consuming and attracting investors is a big challenge whilst the model is in its infancy.

The Foundation's staff and Board feel more comfortable working through these social investment vehicles at the same time as grantmaking, rather than directly offering loans themselves: this plays to the different organisations' strengths.

Joe Dumont, Head of Communications, Community Development Finance Association (cdfa)

cdfa is the trade association for community development finance institutions (CDFIs), lenders to business, including social enterprise, where commercial lenders will not help. Grameen Bank, with its micro-lending in Bangladesh, was one of the key instigators of this "new way of doing business" and much impetus came from the U.S. where the Community Reinvestment Act (1977) prohibited banks from "red-lining" whole neighbourhoods as places where they would not lend to businesses or individuals and required banks to support investment in these places either directly or through CDFIs.

A major stimulus to progress in the UK was the Department of Trade & Industry's Phoenix Fund which helped several CDFIs to start. Some of cdfa's members specialise in supporting social enterprise. Others occupy different niches, only supporting start-ups or microfinance or having a regional focus.

Normally, to achieve a loan from a CDFI, an applicant needs to demonstrate that a bank will not lend it all the finance it needs; and it will have to show the CDFI a business plan or at least a viable proposal. Typically CDFIs fund one in six applicants: they are known for being rigorous in their review of proposals, but they are also still underfunded compared with demand.

cdfa members based in London	cdfa members lending in London
• Croydon Enterprise • Faith in Business • East London Small Business Centre • London Rebuilding Society • GLE oneLondon • HBV Enterprise • North London Community Finance	• Big Issue Invest • Bridges Ventures • Charity Bank • Cooperative and Community Finance • Rootstock • The Social Enterprise Loan Fund • Triodos

Joe looked at the reasons why different funders supporting the VCS might consider investing in a CDFI:

- For corporate/private investors it is a way of giving something back, or raising skills and improving the commercial environment in disadvantaged communities
- local authorities might want to create a legacy to support the local economy. Doing this through a CDFI means they do not need to create a lending vehicle from scratch but use existing infrastructure and expertise; their investment can be closely targeted, e.g. create X number of jobs in Y number of SMEs (perhaps in specific postcodes).

Joe Dumont

For both sorts of investors (including charitable foundations) a vital part of the equation is the ability to recycle finance again and again into the communities they serve. For the borrower, there can be more than cash flow involved: e.g. East London Small Business Centre also offers coaching and support for small businesses and all are aware that their lending can also help lever bank loans.

In the question session, Joe was asked how many loans are successfully paid back: cdfa's figures show that defaulters account for 11% overall but in the social enterprise sector it is only 2%.

WHY LOANS?

Clare Thomas and Kristina Glenn asked a question in many funders' minds - why would a voluntary organisation opt to borrow money rather than apply for a grant? The answer lies in part in the scarcity of resources: where an organisation has a reliable stream of income, borrowing against that for growth, development or cash flow needs may be a much more realistic option than grant support. Joe suggested the Key Fund Yorkshire as a good example of an organisation that mixed loans and grants and understands the different roles of each (www.keyfundyorks.org.uk). LankellyChase had been willing to offer very much bigger sums on loans than they could in grants, and this was one factor for groups seeking ambitious development or growth plans.

Some of the experienced grantmakers in the room were concerned that loans might seem an easy route for groups unable to get grant support, but would be in danger if they have no guaranteed stream of income to ensure repayment. Iona Joy cautioned that borrowers needed to be very rigorous about identifying robust income sources and deducting their operating costs before making any promises about repayment. Geoff Burnand also noted how important it is for groups seeking support not to oversell their impact. Noted were strong examples of good loan arrangements, as in the way hospice building development has been managed.

Alastair Wilson believes that funders could and should encourage loans where groups have a "tradable" element of income to foster independence from grants, e.g. by a mix of 70% grant and 30% loan. It would foster enterprise and make money stretch further but it would be a more complicated exercise for funders. Experience in reading business plans is vital too – a laudable community café in a disadvantaged area would have no certainty of being profitable.

Roger Ong of Charity Bank gave some real examples of support where lending made entire sense:

- help with cash flow support: a £500,000 loan against committed but late UN financing
- a £100,000 loan for voluntary sector tenants to repair a local authority building where the borough itself could not afford the cost. The deal was to give the tenant a 15-year lease, rent free for the first ten years
- a bus-based project where the garage costs were very high: a loan allowed the purchase and upgrading of suitable accommodation for the vehicle and eliminated high parking fees.

DEVELOPING THE SOCIAL INVESTMENT MARKET
Geoff Burnand, Chief Investment Officer, Charity Bank

Geoff's background is in wealth management, advising private and foundation investors but over time he became aware of the gap between money and good uses of money, so through Investing for Good and now Charity Bank he has set about persuading the financial advisory community to invest in the VCS and social enterprise.

He explained Charity Bank's structure and purpose briefly. It pioneered the dual roles of being both a charity and a bank and is the only UK bank that functions exclusively for social purpose. It has over £50 million in deposits and over £111 million out on loan, with a track record of 99.6% of loans repaid and a further £170 million unlocked from other lenders and funders. He noted that many clients seem "unbankable" when they first approach Charity Bank: they hold open days to inform and advise borrowers about the preparation needed to be investment ready.

Charity Bank is a response to demand for social finance and several elements of current government policy indicate that this will grow significantly: these include the Big Society agenda, increased outsourcing of public services, the impact of economic policy with the withdrawal of government grants.

Geoff introduced a note of both realism and challenge when he turned his focus to overall problems in developing a social investment market. To attract personal and corporate wealth into social investment requires considerably bigger opportunities than there are at present, so that investment of £50 million and more can come from new sources. He believes that there would be a move to such investment, not based fully on profit maximisation, but rather "blended value" if only it could be scaled up and externally accredited.

Investors tend to be interested in specific areas too, e.g. social care or housing. He has a vision of an alternative investment class, which is illiquid, whose data are not correlated to the market and which has added value. Geoff's vision is of bond issues that can raise money from donors based on a prospectus explaining and showing impact and starting with some "cornerstone" investors underwriting the effort. Such bonds would not be credit-rated but would rely on investors committed to the bonds' mission. Charity Bank is a conservative lender but would welcome the opportunity to develop funds with external investors big enough to take more risks. Without developments like this there cannot be an expectation of private investment beyond the cautious involvement of relatively small institutions already in the field.

SUSTAINABLE (ISH!) FUNDING: MOVING FROM GRANT DEPENDENCE TO A BUSINESS MODEL
Alastair Wilson, Chief Executive, School for Social Entrepreneurs (SSE)

Alastair generously shared SSE's journey from single-site activity with relatively small scale and grant-dependent operations, to growth and diversification, especially in supporting SSEs in many new places. This represents a cultural shift as much as a financial or operational one. When he joined SSE it was not financially strong. While it had excellent services, as long as its students were primarily from disadvantaged areas they needed subsidy. He pursued two primary strategies, both based on maximising the value of outputs, rather than the traditional funding of inputs:

- shifting the way students were funded so that relevant organisations are involved: housing associations, for example, sponsor a number of students who will go on to work in fields of value to their tenants
- franchising the model of the school itself – charging a licence to operate in exchange for quality assurance, branding, etc.

Alastair Wilson

These had both been pursued to great effect: the London operation is much bigger and there are now 11 schools, including three overseas. Funding is diversified and the School is much less dependent on grant support for its general running costs. These strategies need very different approaches from the usual voluntary sector mindset and they require some very specific new skills as well as the confidence to experiment and take risks. Timing is important – and not giving up on new approaches too early (or too late!). Expectations need to combine realism and pragmatism with some ambitious leadership. The new ideas remain faithful to the core purpose of the School – "stick to the knitting", says Alastair, "but think afresh about how to support it". He advocates trying out selling services, learning about marketing and trading and always staying at the clever end of the spectrum, ie keeping activity close to mission, and going for optimal financial returns (being wary of new approaches which bring in little new money).

Alastair also urged funders to help organisations make this change – understand the issues, perhaps underwrite some experiments, and pay for capacity-building for the new skills needed – negotiating skills, creative thinking, understanding different legal and governance structures, partnership building, measuring and communicating added value, and sustainability training.

TOUGH TIMES: CHANGING TIMES

Mathew Pelling of London Borough of Haringey voiced some of the dilemmas and questions facing local authorities in particular. One is simply the levels that they anticipate cutting from budgets and the tough choices that will need to be made. An aspect of this is the near certainty that commissioning and procurement will become much more a case of block contracts and framework arrangements in which smaller voluntary and community organisations cannot expect to figure, despite the value they may be offering.

The personalisation of services, with its focus on individual needs and wishes and on prevention, offers positive change that all should welcome, but in this current climate there are challenges as much as opportunity.

Intriguing too are the new structures and hybrid forms that should emerge from service transformation – bodies which may not be quite public or social enterprise models or voluntary organisations but different combinations: local authorities will need to keep up to speed on these.

Alastair's final comments about the role of funders apply very strongly in this context, if service provision is to survive in new forms. Smaller providers need help in understanding how to band together to maximise the value of their specialist knowledge and role; and structures like 3SC, a limited liability partnership made up of multiple service providers forming different clusters to pursue major contracts, could be widely promoted.

CASE STUDY: SCOPE'S GRANGEWOOD PROJECT
Iona Joy, Head of Charity Analysis at New Philanthropy Capital

Iona contributed a vivid real life example which NPC (a think tank and consultancy) has reviewed and assessed. Scope aims to replace old facilities and break down residential units into homes for five people. To exchange one old facility for three new homes required investment which Scope decided to tackle in a fresh way, partly wanting to work rapidly, and partly because they have a limited donor base and need new sources of funding.

Scope broke down the funding need (£1.8 million overall) into three elements:

- a commercial loan of £750,000 over 15 years, repayable from local authority fees supporting residents
- a new structure to let them borrow £700,000 for three years at zero interest, with repayment possible once the old building has been sold
- £350,000 in donations and Gift Aid claims.

Iona Joy

While there may be some challenges in the first and third of these (Will local authority fees hold up? Was the Gift Aid calculation a little optimistic?) it is the middle point which is the experimental one, being based on the idea that donors offer a sum that is part donation (£2,800 gross, with gift aid benefits if applicable) and part zero interest loan of £7,000 (for three years). At the end of three years, the loan element is returned to donors (perhaps for use in other projects?). This assumes that some donors may have capital they can manage without for a period but it also ignores the erosion of value by inflation.

There are many advantages for Scope in this combination of vehicles. It avoids a lengthy capital appeal (which would also risk taking money from donors on whom Scope relies for regular revenue support). Getting a commercial loan is a relatively fast process. The new loan/donation package aimed to attract new donors: this is proving to be the case and two thirds of the units were sold between May and September though it seems that many potential donors do not really understand the model. Scope hopes that other charities will experiment with this structure as well and learn lessons from it.

Iona noted that there are many other relatively small scale offers which aim to try out different ways of raising capital: one which was discussed in some detail is Citylife Bonds in which The City Bridge Trust has recently invested. Clare Thomas explained that the return her Trust sees from this investment is threefold: the capital is returned in full after five years; in the meantime it has been lent for affordable housing development; and the repayment of those loans to Citylife includes a surplus that is given to community-based projects. Several charitable foundations have begun to invest in bonds of this kind as have charitably minded companies.

THE NEW WORLD WE ARE IN

Some of the key questions and areas for discussion went back to Stephen Lloyd's opening remarks about service transformation and blurred sectoral boundaries. There are plenty of people interested in forming enterprises out of areas of public service provision, but how many have the knowledge to make them thrive? Stephen quoted experience of the NHS "right to request" process where it is possible to create a social enterprise in place of a primary care trust service: but "clinicians want to be clinicians, not deal with payroll and premises". There may be room for "plug in" organisations to provide back office services: SSE is certainly looking at training in some of the essential softer skills of leadership, confidence, legitimacy, attitude, networking and partnership-building.

There were some final comments on funder motivation. Iona Joy believes that most, focused on social impact, will assess any different use of their resources in the same way that they assess grant applications. On the other hand, she would expect Charity Bank to be quite properly more concerned with the creditworthiness of a proposal. There is room for both and perhaps a gradual blending will come from experience. At least one question remains in this context of hugely varied funders and funding mechanisms: funders are always interested to see which other funders are supporting organisations they are considering, not least as a way of checking organisational robustness. Will the presence of loans on balance sheets be over-interpreted as liabilities/risks by the more traditional funders?

In summarising the outcomes of an interesting series of presentations and discussion, Lisa Greensill, meeting Chair, noted the changes facing both funders and fund-seekers – never was it more important that contracts and arrangements are well thought through and carefully expressed, that new skills are recognised and developed, that culture change is analysed and understood – and that minds remain open to the full spectrum of funding possibilities.

Working together to strengthen London's voluntary and community sector

London Funders exists to strengthen and support London's funders to better meet the needs of Londoners. It is the membership organisation which works with funders and investors supporting London's voluntary and community organisations. It links all the sectors, providing foundations, funders from the public sector and corporate givers with opportunities to share their experience and learn from each other. It helps to forge productive relationships which contribute to the wider benefit and overall sustainability of London's voluntary and community organisations. It aims to contribute to a vibrant, varied, fit for purpose third sector which is appropriately and fairly funded.

PARTICIPANTS

Sue	Bowers	Heritage Lottery Fund
Phillippa	Brown	Media Trust
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Frances	Connelly	London Borough of Camden
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Alex	Czerniewska	Capital Community Foundation
Marina	David	Barrow Cadbury Trust
Joe	Dumont	Community Development Finance Association (speaker)
Sarah	Elliott	In Kind Direct
David	Farnsworth	Diana, Princess Of Wales Memorial Fund
John	Gahan	Girdlers' Company
Kristina	Glenn	Cripplegate Foundation
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