UK COMMUNITY FOUNDATIONS
GIVING FOR LOCAL GOOD

COMMUNITY FOUNDATIONS AND SOCIAL INVESTMENT

Connect Fund
Building a better social investment market

SEPTEMBER 2019

COMMUNITY FOUNDATIONS AND SOCIAL INVESTMENT

PART ONE

WHAT AND WHY:
CONSIDERING WHETHER BECOMING AN INVESTOR IS RIGHT FOR YOU

WHAT IS SOCIAL INVESTMENT? 3
WHY PROVIDE SOCIAL INVESTMENT? 4
UNDERSTANDING THE MARKET AND LOCAL AREA 7
GETTING BOARD BUY-IN 10
LEGAL REQUIREMENTS 11
UNDERSTANDING AND MANAGING RISK 12

PART TWO

HOW AND WHO:
WHEN YOU DECIDE TO SET UP A FUND

FUNDING THE LOAN POT AND OPERATING COSTS 15
STAFF SKILLS AND CAPACITY 18
BUILDING THE PIPELINE 19
APPROPRIATE PARTNERSHIP WORKING 21
EVIDENCING OUTCOMES 21
OTHER TOOLS AND RESOURCE FOR COMMUNITY FOUNDATIONS AND VCSEs 23

REFERENCES 24

COMMUNITY FOUNDATIONS

Community Foundations are local champions, connecting people and organisations that want to improve their communities. Community Foundations invest in local people and organisations tackling the biggest issues facing communities today and supporting some of society's most disadvantaged people. They provide help and advice to those who want to give at the heart of their communities, both now and in the long-term. They match donors and partners to important local causes.

UK COMMUNITY FOUNDATIONS

UK Community Foundations (UKCF) is the membership organisation for the 46 accredited Community Foundations across the UK, which collectively to date has awarded £1 billion in grants to charities, community groups and individuals. We provide advice, learning and resources to support our members to deliver the highest standards of service to communities. We promote the vital work of Community Foundations with government and other national stakeholders, championing local philanthropy at a national level. We partner with clients who want to make a difference by developing grant-making programmes involving multiple Community Foundations.

THIS RESOURCE

This resource is aimed at Community Foundations that are considering whether social investment is right for them. There is no one-size-fits all approach to delivering social investment and so this resource does not aim to provide an exhaustive checklist. Instead, it breaks down some different elements of social investment that Community Foundations may wish to consider, examples of what options are available and links to existing helpful resources.

This resource was produced as an output of the UKCF Connect Fund Learning Pilot (2018-19), funded with generous support from the Access Foundation and the Connect Fund at the Barrow Cadbury Trust. The pilot set out to develop the Network's understanding of the opportunities associated with social investment and how it could be used to support local voluntary, community and social enterprise organisations (VCSEs) and the communities they serve. In the spirit of the pilot, which had a peer network at its core, we encourage any Community Foundation considering social investment to seek advice from their peers, many of which have extensive experience in social investment that they would be happy to share.

PART ONE

WHAT AND WHY: CONSIDERING WHETHER BECOMING AN INVESTOR IS RIGHT FOR YOU

WHAT IS SOCIAL INVESTMENT?

Social investment is the use of repayable finance (usually but not always loans) to help an organisation achieve a social purpose. VCSE organisations can use repayable finance to help them increase their impact on society by, for example, purchasing the right property to support their activities, growing their business, providing working capital for contract delivery or buying assets. Charities and social enterprises may then generate a surplus through trading activities, contracts for delivering public services, grants and donations, or a combination of some or all of these. This surplus is then used to repay investors.

Common social investment models include secured loans, unsecured loans, blended funding (part-grant, part-loan), community shares, crowdfunded investment, equity and quasi-equity investments, charity bonds and social impact bonds. Each model is different and reflects different circumstances and objectives, although Community Foundations are likely to focus primarily on providing loans, bridging finance and repayable/part-repayable grants (quasi-equity). However, social investment is not just about the money; it's also about the people. Often an investor and investee will work together to support each other on a shared mission. Social investment certainly isn't appropriate for all VCSE organisations but it can be transformational for both investor and investee – and, as place-based funders, its role in the funding landscape ought to be of interest to many Community Foundations.

Key Fund has produced **a glossary** that includes the investment models mentioned above, along with other terms and language used in this resource and the investment process.

Social investment certainly isn't appropriate for all VCSE organisations but it can be transformational for both investor and investee

WHY PROVIDE SOCIAL INVESTMENT?

Many VCSE organisations want to develop trading income streams, but they haven't got the capital, capacity or capability to do so. This is where social investment can be useful to help organisations to diversify their income sources. Ultimately, VCSE groups can become more resilient by gaining greater control over a larger proportion of their income. In this context, social investment sits alongside grants, contracts and other sources of income. It's not here to replace them – it's simply another tool in the funding toolbox.

Community Foundations may therefore wish to consider offering social investment alongside grant-making and other related activities because it can open up new opportunities and has the potential to:

- 'Recycle' funding to achieve greater social impact over time[1]
- Attract new investors and leverage additional finance into the local area
- Help local organisations who struggle to access mainstream sources of investment finance
- Strengthen local VCSE organisations and help them to become more financially sustainable
- Offer smaller scale 'repayable grants' than are currently available

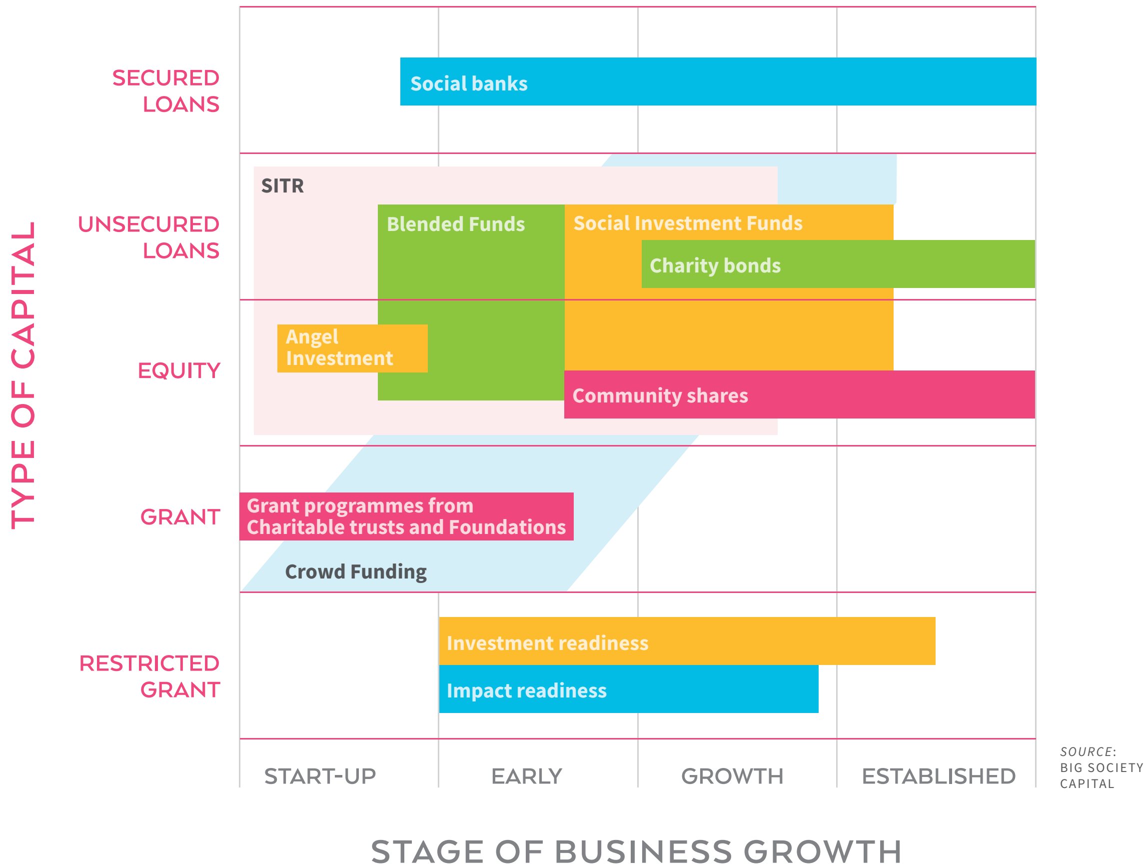
A diverse group of investors now offer social investment, from government to foundations, pension funds, high-net-worth individuals and mass retail.

Many of the financial products on the mainstream financial market are seen as unsuitable for local VCSE organisations.[2,3] Getting involved in social investment would enable Community Foundations to develop offers better-suited to smaller organisations who might otherwise see social investment as too risky or who want a smaller level of support.

The NCVO UK Civil Society Almanac 2018 is a reminder that most of the 160K voluntary organisations that exist in the UK are small and operate locally, with 82% having an annual income of under £100K or less. However, there is a clear gap in the market for small (and/or short-term) investments. Community Foundations have the potential to play a key strategic role in this space e.g. for loans of £20–50K or loans for less than 12 months.[4,5]

Moreover, local VCSE organisations often need to borrow amounts that are not cost-effective for larger lenders (due to higher transaction costs which drive up interest rates) and could strongly benefit from the level of local insight and support that Community Foundations are uniquely positioned to provide. What Community Foundations can offer could be vital in boosting the confidence of local organisations to use loan finance, many for the first time. Potential benefits of Community Foundations offering social investment therefore include:

- The ability to lend amounts that are not cost-effective for larger lenders
- The ability to be more flexible in approach e.g. by providing highly-subsidised quasi-grants, unsecured, bridging or short-term loans
- The ability to bring new funds to the market via their donors or crowdfunding
- The ability to offer blended finance e.g. offering grants alongside loans
- The ability to offer repayable grants
- Their rich understanding of their local areas, as well as the financial barriers that VCSEs face
- Their existing networks and relationships which may help them spot organisations that are suited to social investment but haven't yet considered it



However, just as loan finance is not appropriate for every VCSE organisation, not every Community Foundation will want to offer social investment. Community Foundations should be clear about what delivering social investment will involve and require of them – including but not limited to:

- **Additional governance, administrative responsibility** and other associated costs; or a partner with these capacities
- **A specific set of skills for both staff and trustees** that is qualitatively different from grant-making, including skills related to conducting deal due-diligence, investment decision-making, active portfolio management and risk mitigation
- **Getting comfortable with dealing with loss** and balancing financial risk with social gain
- **Being clear on how their offer compares** to other lenders operating in their area
- **The potential reputational risk associated** with being seen as a grant-maker moving into social investment or when an investment goes wrong
- **Confidence and perseverance when attracting investors** or providing business support to local organisations (or signposting/funding them to independently purchase support) in order to help them to become investment ready

CASE STUDY

KENT COMMUNITY FOUNDATION
WOOD N WARE

Wood N Ware CIC are a not-for-profit organisation providing opportunities for vulnerable adults to learn woodwork skills, build confidence and build social networks. Their members make a wide variety of products from planters to bird boxes and are also commissioned to carry out projects. Items are sold online and at farmers' markets, local craft fairs, events and at visitor attractions – giving members the added experience of selling. Wood N Ware only use repurposed, reclaimed and donated materials that are provided by local businesses or restore shabby chic old furniture. In this way, they teach the basic woodwork skills while also teaching the importance of recycling and being environmentally sound.

KENT COMMUNITY FOUNDATION

Wood N Ware CIC received a £28K loan from Kent Community Foundation (KCF) alongside a £7K grant to assist with cash flow and increase the number of daily attendees.

In four years, the company have increased members accessing their service from six to 40, with a maximum of 15 per day. They have taken on volunteers, increased their community involvement and partnerships, worked with local schools, set up local business links and run an open day service for members of the public to pop in.

Louisa Fry, Director: "Our experience of KCF and the loan fund service was very positive and we have actually recommended KCF to others. I had never run a business and my weakness was book keeping. KCF were aware of this from the start and focussed on support in this area. KCF were incredibly supportive and met us at times that were convenient to us. They gave us a wealth of knowledge and information, emailing links to websites that they thought would be helpful to us. They talked us through other services and gave us lots of general information about how things could be done or what was working or even things that didn't work, which was equally important at the time. They looked over our business plan and sent back constructive critique. They supported us a lot and in the first year stayed in regular contact, giving us feedback and helping us stay on track."

UNDERSTANDING THE MARKET AND LOCAL AREA

VCSE organisations primarily need money for:

- Revenue costs (rent, staff etc)
- Working capital (to manage cash flow fluctuations especially when delivering projects that pay in arrears)
- Capital investment to purchase buildings and other fixed assets

The primary focus of social investment is on working capital and capital investment to enable VCSEs to set up new income streams, expand existing income streams or simply to better manage existing income streams. Depending on the capital needs and the planned activities of the organisation different types of financial support may be required, e.g. secured loan, unsecured loan, standby facility, overdraft, quasi-equity, equity (for CIC's limited by shares and community benefit societies) or, of course, simply a grant.[6]

To understand your market, potential gaps and how your Foundation is best placed to operate, you might first want to review the following:

- **Who is already active in your area?** E.g. national, regional and local investors, social investment finance intermediaries etc.
- **Where are they positioned in the marketplace?** What is their income and what is the size of the average loan they make?

The grid on page 9 can be used to plot where investors are positioned in the marketplace.

- **Where would you position your Community Foundation?** What gap could your Community Foundation fill?
- **How would your offer differ** from those of other lenders operating in your area?
- **How would a highly-subsidised quasi-grant offer be received** in your area?

There are several lists of investors available online that can be used to map the marketplace, including **The Access Foundation's Growth Fund**, **Good Finance** and **Big Society Capital's list of social investors, funds and advisors.**

Understanding what finance is available at the right time can be a major barrier for many organisations

Understanding what finance is available at the right time can be a major barrier for many organisations. Community Foundations usually have in-depth knowledge of their communities and the socio-economic landscape that shape them. They are thus able to identify local organisations who might benefit from social investment and help them to build their confidence and capacity in taking on investment. In doing so, Community Foundations can act as a steppingstone, preparing VCSE organisations to take on larger investments in the future by supporting them with their first steps in social investment. Alternatively, some Community Foundations might be interested in setting up or providing match-funding for local crowdfunding campaigns, which local organisations could use to test out their business model before taking on larger investment.

However, Community Foundations may need to actively scan their local area to find out what organisations exist and who could benefit. When researching potential clients/beneficiaries in the local area, some questions that could be considered include:

- What type of organisation is it? E.g. registered charities, companies limited by guarantee, Community Interest Companies, registered societies/community benefit societies etc.
- What is the business model?
- Is the right governance, management structure and other skills required to deliver the organisational mission or to expand delivery through investment in place?
- Has the intended target market been properly researched and understood?
- What is the financial situation? E.g. fixed assets, turnover, free reserves, profits/surplus, historic performance, sources of income etc.
- What partnerships/networks are there in place?
- Has the organisation successfully used crowdfunding to support capital raises or develop new income streams in the past?
- What additional support is needed?

		LOANS					
		< £50K	£50K–100K	£100K–250K	£250K–1m	£1–5m	> £5m
INCOME	> £500K						
	< £500K						
	< £250K						
	< £100K						
	< £50K						
	Startup / Charity / Soc Ent						

Community Foundation staff and the Board should be ready to learn from their experiences and to go on the social investment journey together

GETTING BOARD BUY-IN

Trustees can be risk-averse. As with all new propositions, education and familiarisation with social investment is required before trustees will be confident making decisions about what investments their Foundation should make.

Most anxiety from trustees is related to the risk of things going wrong. However, this can be re-framed as the risk of not doing something that has the potential for social impact, coined by **CAF Venturesome** as 'beta risk'.

Both Community Foundation staff and the Board should be ready to learn from their experiences and to go on the social investment journey together. When it comes to pitching social investment to Community Foundation boards, Community Foundation staff should:

- Help them to connect with the **philosophy behind the money**. If the philosophy is about building the capacity of local organisations to do good work, then loans and grants can be seen as parts of the same toolkit
- **Have ongoing conversations about risk.** Set up systems to help understand and navigate appetite for risk. In doing this, management and board can negotiate what level of risk/loss they are comfortable with
- **Take measures to reduce risk and liability.** Including through introducing enhanced monitoring or more regular check-ins when a loan you are providing to a VCSE is seen as higher risk; ensuring the Board is comfortable with the terms written into any agreements with investees, partners or investors; and ensuring clarity around the Community Foundation's responsibilities

- **Help them to understand the unique role Community Foundations could play in the market.** Including in relation to:
  - the size and nature of the investments Community Foundations are best placed to provide
  - the importance of the local insights your team has about local VCSE organisations
  - the potential to leverage more capital and a flow of finance into the area
  - the potential to recycle money and extend the longevity of impact, in the form of repayable grants over standard grants
- **Learn from peers.** Hearing from other Community Foundations who deliver social investment about why they started out and what the benefits have been will help the Board become more comfortable about getting started themselves
  - Ask a board member or other staff member from another Community Foundation to come and talk to your board about why they started making social investments
  - Use case studies of VCSEs that have taken on social investment and what this changed for them[7,8]
  - Ask other Community Foundations with more experience of social investment for input on documentation being developed e.g. on due diligence or investment manuals

LEGAL REQUIREMENTS

The Charities (Protection and Social Investment) Act 2016 gives all charities, except statutory charities and Royal Charter bodies, the power to make social investments. However, there are legal implications to consider when making loans. Having staff members or representatives with a legal background on your board will be helpful. If there are gaps on the Board or management team, external legal or financial advice may be necessary to develop appropriate systems and procedures.

Just as it should be in a Community Foundation's memorandum that they can lend as well as provide grants, it is important to ensure that any VCSE that you consider lending to also has legal powers to borrow.

The Access Foundation has teamed up with Bates Wells Braithwaite to develop a set of freely available **model legal agreements** that can be used as a starting point for charities, social enterprises and social investors, and adapted as appropriate for Community Foundations' clients.

The Financial Conduct Authority (FCA) has complex regulations in place to control financial firms providing services to consumers and to maintain the integrity of the financial markets. However, these regulations do not apply if you are providing business loans to corporate entities or are not investing on behalf of other investors i.e. are investing your 'own money' and not utilising 'client assets' to generate a financial return. FCA regulations are unlikely to impact on Community Foundations but, in some cases, Community Foundations may choose to look further into this.

Big Society Capital launched its Get Informed campaign to educate boards about social investment. Their Get Informed Guide contains lots of information that your board might find helpful. The Social Impact Investment Group (SIG) peer network also exists for Foundations starting or undertaking social investment.

Discussions with the Board about their appetite for risk should be ongoing

UNDERSTANDING AND MANAGING RISK

When looking to address the financial needs of VCSEs, it is important to understand how these needs correspond with the activities that the organisation offers and the different levels of risk these bring in terms of the estimated level of income generated through each activity.

Discussions with the Board about their appetite for risk – what balance of potential social and financial returns or losses they are comfortable with – should be ongoing. This relates to both the financial risk of losing money and reputational risk[9] related to how the Foundation might be viewed by the sector or its own staff when it begins making social investments.

Reputational risk may be underpinned by misconceptions about social investment[10] e.g. – "a loan is an expensive financing option for charities", "a loan is a poor substitute for a grant" or "a loan will lead to irreversible debt" – none of which are supported by available evidence.

Reputational risk may be mitigated in the following ways:[11]

- Designing financial products flexibly to meet the specific needs of VCSEs
- Taking time to understand the needs and selecting the right tool for the right problem
- Ensuring investments are linked to the Foundation's charitable mission
- Putting in place systems for demonstrating social outcomes from investments
- Managing investors' expectations regarding returns with proof that the money is working harder by being recycled and using the evidence of positive social outcomes
- Sharing positive case stories of when Foundations have lent to local VCSE organisations and how this benefited those organisations
- Taking a gradual approach to give social investment recipients plenty of time to get used to the new relationship

Assessing risk on an applicant-by-applicant basis will form part of your due diligence process. A risk register should be maintained to document risks across the portfolio and record approaches to mitigation.

Robust assessment and due diligence at the start will give Community Foundations a full picture of the organisations in which they are investing and enable them to build in conditions to mitigate risk.

For example:

- In-depth financial analysis of accounts and projections before investment
- Enhanced monitoring of accounts and financial performance over the course of the loan as a condition of investment, including monitoring key financial ratios to measure their progress against predetermined goals set in the loan agreement or aspects of their financial health flagged up in the due diligence process as in need of monitoring
- Regular conversations with the VCSE, particularly in the early stages of the relationship

Alongside the due diligence process, scoring systems could be developed to rate an application by its level of risk and support discussions during decision-making panels.

As well as deciding on your risk tolerance – the degree of variability in returns that you are willing to accept – a policy will also need to be in place for when payments are not made. Your plan for delinquencies should form part of a wider risk and loss policy.

Ultimately, final decisions on loans will be made by the Board or the delegated credit committee. But setting up systems like this will help you to navigate risk together with the Board and make sure decisions about risk are fully transparent.

Some Foundations may choose to develop a Credit or Investment Committee to make the decision on whether to approve a loan, following assessment by staff, or to source these capacities from other local/regional/national partners. Ideally, the Committee should have a greater level of investment experience than a standard Grants Committee so that they can assess the ability to repay and the risk involved.

EXAMPLE

CAF Venturesome developed three categories of risk: green, orange and red. Red was the highest level of risk and represented a predicted 50–50 chance of them getting their money back from the investment. In the end, CAF Venturesome did not lose any money from the 'high-risk' investments they made. However, the simple exercise of coming up with these categories meant that as an organisation they became comfortable with the idea of loss and taking on higher-risk investments, in pursuit of a certain level of social impact.

CASE STUDY

RESILIENT SCOTLAND
ASSESSING RISK AND EVALUATING OUTCOMES

Since 2013, Resilient Scotland Limited has invested over £8.8M in social enterprises, community organisations and charities across Scotland. In 2016, their busiest year, they made 30 loans. Resilient Scotland Limited is the corporate trustee of the JESSICA (Scotland) Trust. The JESSICA (Scotland) Trust was established with a £15 million endowment from the Big Lottery Fund.

Resilient Scotland developed templates to help them be consistent and objective when assessing applicants. These tools help the investment team and panel to decide whether the perceived level of risk involved in investing in an organisation is justified by the social impact that could be achieved through the investment. Their assessment package consists of:

- **A business risk template**. Applicants are scored in eight risk areas: age of business, business structure, experience of the management team, sector/market, base case forecast, sensitised forecasts, financial gearing and operational gearing.
- **A social outcome template**. Applicants are scored on two outcomes areas that map on the intended impact of their activities. These outcome areas are based on Big Society Capital's outcomes matrix.
- **A social activities and outcome framework**. Each outcome the organisation chooses is then put into a social outcome framework during a visit with one of Resilient Scotland's Investment Executives. This framework helps to articulate how the activity will lead to the intended social impact, and how the loan will help this to happen. For each outcome the Investment Executive works with the investee to record:
  - The activity – what will it do?
  - The beneficiary group – who will benefit?
  - Evidence of need – what existing research or national/local figures demonstrate the need?
  - Impact – How will activity X meet this need?
  - Return on RSL investment – how will this impact be facilitated by the funding?
  - Impact reporting – what indicator will be used to track impact and will the target be?
- **Loan assessment paper**. This is a written assessment, containing recommendations from the Investment Executive, which goes to the investment panel along with the business risk assessment, social outcome template, social outcomes framework and base case and sensitised financials.

As a general rule, a relatively weak business risk rating would need to be offset by a strong social outcomes rating in order for the investment to be recommended to the panel by the investment team. Four team members assess applications and each one is peer reviewed by another team member before it goes to the investment panel. The panel meets every two months to discuss the assessments that have been made by the team and may challenge the ratings they have given to different components of the applications.

If you would like to know more about the templates that Resilient Scotland use please get in touch with their team.

PART TWO

HOW AND WHO:
WHEN YOU DECIDE TO SET UP A FUND

FUNDING THE LOAN POT AND OPERATING COSTS

A social investment loan 'pot' may come from a variety of sources, such as:

- Funding from the local council, either as a loan, grant or a gift
- A grant or investment from a national funder for the purposes of social investment
- Local philanthropic donors/benefactors
- Endowment
- Crowdfunding[12]
- Through a partnership with local or national investors

The funding requirements for a programme will differ depending on the target market e.g. social enterprises may require larger, longer-term loans whereas other local organisations may require low value and short-term loans.

Operating costs should also be factored in on top of the cost of the actual investment. Operating costs include all the costs associated with lending, including staff time, administration, costs for outsourced services or management systems and the range of activities required to support applicants through the pipeline, from promotion of the offer to the completion of the deal.

> Another misconception relating to social investment is that loan funding will generate profits for the lender

Once the cost of the programme has been estimated, a strategy for covering these costs should be agreed upon. Another misconception relating to social investment is that loan funding will generate profits for the lender. In fact, it is difficult to cover operating costs from social investment revenue, particularly when focusing on small and medium-sized charities and social enterprises. Community Foundations may choose to use different approaches to cover these costs. Some examples from the Network include:

CHARGING A FEE Charging a fee may provide additional income to cover the costs of making the loan.

EXAMPLE

Heart of Bucks generates a yearly average income of £24K based on an Associate Fee they charge to investees. This is used to cover their operational costs. The first fee payable is equal to 4% of the total loan amount and is deducted from the loan amount. The remaining fees are 3% in the second year, 2% in the third year and then 1% in the fourth year. The Associate Fee is therefore calculated on the initial sum lent (not diminishing balance).

SHARING BACK OFFICE SERVICES A number of social investment intermediaries (e.g. Key Fund) offer back-office services that can be used by Community Foundations. **Singlify** and other software packages are also available to facilitate loan management and provide an alternative back-office platform for social investors.

Examples of back-office services that organisations or software package could help to provide:

- Accounting or bookkeeping
- Processing Agreements and Disbursements
- Invoicing and collection of payments and fees
- Client database maintenance

ENDOWMENT MODEL Resilient Scotland Limited is the corporate trustee of the JESSICA (Scotland) Trust. the JESSICA (Scotland) Trust fund was set up with £15m that was to be invested as a ten-year expendable endowment. All relative returns from investments made by Resilient Scotland are used to cover the operating costs. The endowment was invested based on low risk, with the aim good returns. However, it is important to note that returns from deals are often not as good as expected and therefore operating costs need to be covered elsewhere.

EXAMPLES FROM THE NETWORK

Cornwall Community Foundation has been lending for six years and has given out a total of 30 loans. Their average loan size is £7K and their maximum loan size is £15K. Their programme was set up with £30K received from the Fredericks Foundation, £32.5K from charitable trust funds, £50K from Cornwall Council and £60K from private individuals.

Heart of Bucks has been lending for eight years and has given out a total of 32 loans. On average they lend £62,000 a year, with average loan size of £16K. £25K is their maximum loan size. They received £215K in funding from their county council, one of their four district councils and a small number of private and corporate donors.

Kent Community Foundation has been lending for seven years and has given out a total of 40 loans. On average they lend seven loans a year, with an average loan size of £50K. They set up the programme with £3M from Kent County Council; more recently they received a grant of £508K from The National Lottery Community Fund.

STAFF SKILLS AND CAPACITY

Social investment requires a different set of skills to grant-making. But what works in the team will differ for each Community Foundation.

There will be benefits to having a balanced team working on lending, including those with experience of social or commercial lending and those with the local knowledge and understanding of VCSEs that is necessary when working with local community organisations taking on investment for the first time.

CAPACITIES TO LOOK FOR INCLUDE

- Understanding of the local context and the needs of stakeholders
- Understanding of VCSEs and how the current political and economic context has impacted on them
- Understanding of different forms of finance and what they are appropriate to use
- Ability to spot investment opportunities
- Ability to assess business models and financial performance
- Ability to analyse risk, with the help of organisational processes and templates
- Ability to maintain ongoing supportive relationships with investees beyond an initial face-to-face discussion with all new applicants

As grant-making has become less project-focused and more concerned with building the capacity of local organisations to have an impact in their communities, more Community Foundations' staff have the capacity and mentality that is required of social investors. Upskilling current staff members may therefore also be an option.

OUTSOURCING CAPACITY

There is also the possibility of outsourcing some back-end services and processes, including:

- Investment/appraisal documentation and associated back-office support e.g. another more experienced Community Foundations or Key Fund
- Front end training e.g. Big Society Capital and Responsible Finance
- Second stage assessment – buying in support from other funders will enable you to benefit from the expertise others have built up about which deals work
- Compliant legal offer documentation
- Payments and returns. Several large lenders will do this for small lenders (for a fee)
- Investment recovery. Some national organisations will also offer this as a service (for a fee)

When considering outsourcing or buying in documentation, it is important to look for organisations that have a similar investment model to your own. Outsourcing can be helpful when you are first starting out. But over time, the aim should be to internalise these capabilities and to rely less on external expertise.

INVESTMENT IN THE RIGHT STAFF IS CRUCIAL

There is a tendency to over-rely on back-end processes and systems. To make the right investments and avoid issues like recovery, you need to get the due diligence right, understand the applicant organisations and have the right staff in place to support decision-making.

RELATIONSHIPS ARE KEY!

No single tool or calculation will make the assessment of applicants into an algorithm. The team assessing the application will need to spend time understanding the organisation's context, motivations and capacities, just as the grants teams do for current applications.

BUILDING THE PIPELINE

The pipeline refers to the flow of organisations interested in accessing social investment, from the expression of interest, through formal inquiry, application and approval (or not) to the allocation of a loan or other appropriate investment.

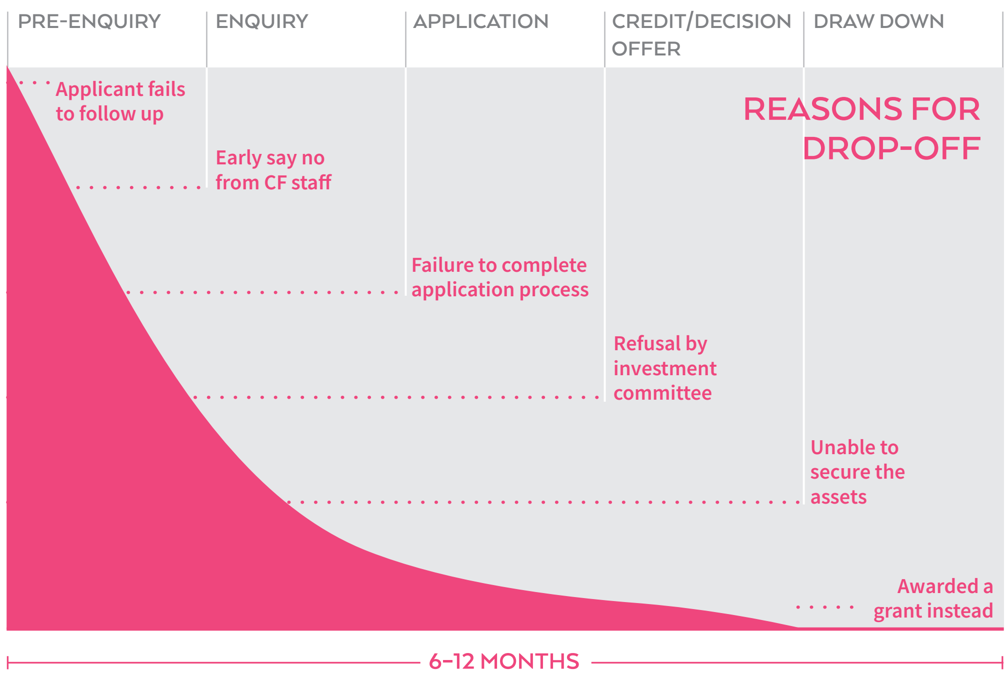
Building the pipeline requires proactivity and forward-thinking. It will often involve working with and identifying VCSEs at the early stage of their social investment journey. Some strategies that could be used include:

- **Using existing networks** and personal relationships to scout for suitable organisations locally
- After doing an initial scan of which organisations are in the local market, **developing a watch list of organisations** to approach
- Considering whether some organisations that apply for grants are in fact **suited to taking on investment**
- Actively **promoting social investment locally**, through putting on and attending local events to talk about your offer and promoting the offer via your website and social media channels
- Spending time with organisations to discuss and **work through their anxieties** with taking on loan-funding
- **Being clear about your proposition** and what you are offering – using clear language and being consistent in your message

It is not possible to set a threshold for when an organisation is 'ready' for social investment. Whether an organisation is 'ready' depends on the investors' appetite for risk

Drop-off is to be expected throughout the pipeline, as demonstrated in the diagram below. Only a small amount, roughly 20–30%, of pre-enquiries and early-stage conversations will convert into formal enquiries or applications. Another tranche of organisations is often lost at the application stage as they struggle to provide the information required in application forms.

However, it is not possible to set a threshold for when an organisation is 'ready' for social investment. Whether an organisation is 'ready' depends on the investors' appetite for risk – individual Community Foundations may be comfortable working with organisations at different stages of readiness.



Once established, you could learn from your pipeline by recording data and analysing the deals that converted after initial enquiry. How did that deal come about and how did they hear about you? Use what was learned from those deals to refine your approach.

APPROPRIATE PARTNERSHIP WORKING

Working in partnership with other local, regional or national organisations might help you to boost your offer. In some cases, getting involved in social investment may be an opportunity to deepen and strengthen existing partnerships that the Community Foundation has. However, it is more likely that moving into social investment will bring in a new set of relationships. This might include developing reciprocal relationships with social investors that can refer local organisations to the Community Foundation for investment or grants where appropriate, or where Community Foundations serve as a pipeline of referrals to existing investors when a different set of skills or level of investment is required.

When considering entering into a new partnership, consider:

1. What are the objectives of the partnership? E.g. access to additional funding, networks, technical support or learning.
2. How will this partnership help you to strengthen your offer and better serve your community?
3. Are your values and organisational cultures aligned?
4. For what would each organisation in the partnership be responsible?
5. What are you good at and could a partner free you up to focus more on these elements?
6. Will you develop a joint approach or offer complimentary products?
7. Are there additional legal or regulatory compliances that the organisation is subject to that need to be considered?
8. What will you do if things go wrong or need to change? Clear agreements and plans for the management of the partnership for its entire lifetime need to be put in place at the beginning to protect both parties and the beneficiaries.

EVIDENCING OUTCOMES

Measuring the outcomes of social investment is an important part of the overall picture. It will help Community Foundations to understand how their investments are making a difference locally and to gather evidence that can be used to demonstrate the power of social investment to potential applicants, partners and donors/investors.

For Community Foundations, the priority will be understanding their impact, as social investors, on two main levels:

- VCSE business resilience and sustainability
- Social outcomes for the end beneficiary or community

It is important to note that, for Community Foundations, understanding the impact of a loan on the investee's organisational **sustainability** will be just as important as understanding impact on **growth**. This is because growth is not always a priority for VCSEs and what they often need is the stability to continue doing what they are doing, reinvesting their profits so they can continue to deliver impact in the communities they serve.

Community Foundations will choose to measure outcomes in different ways depending on their charitable objectives and internal capacity. But it is important to strike a balance by evaluating both social outcomes and business sustainability and by ensuring that the data that is collected is **proportionate, meaningful** and **useful.**

Good evidence will help Community Foundations and the organisations they invest in to tell the story of social investment and how it can be harnessed to support activities that make a difference to communities.

> There are a lot of existing outcome frameworks that are being used by the sector

One way to help make evidence requirements manageable is to use information that has already been collected from the organisation to evaluate their impact e.g. management accounts, annual accounts or notes from meetings or telephone calls with investees. Using data that is already part of the application process or the organisation's usual business will help to ease the burden of evaluation for both Community Foundations and investees.

Another way to make data manageable is to collect quantifiable outcomes evidence. For example:[13]

SOCIAL OUTCOMES

- Number of people reached by the project or investee organisation each year
- Footfall
- Number of children on free school meals accessing the service

BUSINESS OUTCOMES

- The proportion of staff that have stayed in the organisation over the past year
- Whether the organisation retained key contracts/customers/grants/income streams in the last year
- Whether the organisation made all their payments on time over the past year

Where possible, metrics and indicators should be chosen in collaboration with the investee organisation based on the outcomes they intend to achieve using the loan. If recorded from the start of the loan (baseline), evidence can then be collected and compared at regular intervals, creating a picture of what impact the investment is having over time. There are a lot of existing outcome frameworks that are being used by the sector and so Community Foundations can easily draw on existing models or develop an evaluation framework based on their own charitable objectives.

Alongside an outcome framework, Community Foundations could also write up or produce video case studies to bring the story of investments to life. This could focus on how the investment changed things for a local organisation and helped them to make an impact in the community, including who and how they helped locally. Case studies can be shared via Community Foundation websites, publications and social media channels and used in meetings with potential applicants, partners, investors or their own board. There are banks of case studies available through organisations like **Resilient Scotland**, **Big Society Capital**, **Good Finance**, **Responsible Finance**, **Crowdfunder** and **The National Lottery Community Fund**.

> **Collecting evidence may be time-consuming, but clear and easy-to-understand outcomes evidence is needed to make the case for increased funding for the lower end of the social investment market and to increase demand among local organisations.**

OTHER TOOLS AND RESOURCE FOR COMMUNITY FOUNDATIONS AND VCSEs

Social Enterprise UK's *Social Investment Explained.*

Investment readiness tool:
https://www.vcsestrengthchecker.org.uk/

A beginner's guide:
https://www.bigsocietycapital.com/sites/default/files/BeginnersGuidetoSocialInvestment.pdf

Research on the market for social investment:
https://blogs.ncvo.org.uk/2016/04/27/social-investment-whos-got-it-who-wants-it-and-whats-next/

Foundations and Social Investment in Europe, Social Investment Group Survey Report
http://efc.issuelab.org/resources/16021/16021.pdf

Research on social enterprises in the UK:
https://www.socialenterprise.org.uk/the-future-of-business-state-of-social-enterprise-survey-2017

An investor and advisor directory:
https://www.goodfinance.org.uk/investors-advisors

Guidance on responsible finance:
https://responsiblefinance.org.uk/responsible-finance-providers/

Guidance on Social Investment Tax Relief (SITR):
https://www.bigsocietycapital.com/sites/default/files/GET%20IT%20leaflet%20NEW%20May%202017.pdf

Interim Guidance on social investment powers:
https://www.gov.uk/government/publications/charities-and-investment-matters-a-guide-for-trustees-cc14/charities-and-investment-matters-a-guide-for-trustees

Guidance and information on setting up a Donor Advised Fund (DAF):
https://www.bigsocietycapital.com/sites/default/files/BSC_DAF_PRACTIONERS_GUIDE_NOV17_LO.pdf

Information on investing endowment:
https://snowball.im/ https://www.friendsprovidentfoundation.org/investment/social-impact-investing/

For help facilitating events to build awareness of SI locally:
https://www.bigsocietycapital.com/lets-talk-good-finance

Information and research on matched crowdfunding from Nesta:
https://www.nesta.org.uk/report/matching-the-crowd-combining-crowdfunding-and-institutional-funding-to-get-great-ideas-off-the-ground/

REFERENCES

1. Bolton (2005), Foundations and Social Investment: Making Money Work Harder in Order to Achieve More. https://www.issuelab.org/resources/16022/16022.pdf

2. Davison & Heap (2013), Can Social Finance Meet Social Need? http://www.huckfield.com/wp-content/uploads/2013/06/13-Heap-Davison-Soc-Fin-Soc-Need-U26.pdf

3. Sortified & Lincolnshire Community Foundation (2019), On An Equal Footing: Identifying and Removing Gender Barriers to Social Investment within the Community Sector in the East Midlands. https://static1.squarespace.com/static/5b167637ec4eb741d86e3130/t/5d0ce7dc3619d10001f484e5/1561126887325/OAEF+report+FINAL.pdf

4. Social Enterprise UK (2017), The Future of Business: State of Social Enterprise Survey 2017. https://www.socialenterprise.org.uk/the-future-of-business-state-of-social-enterprise-survey-2017

5. James, Kane & Ravenscroft April (2016), Understanding The Capacity and Need to Take on Investment Within The Social Sector. https://blogs.ncvo.org.uk/2016/04/27/social-investment-whos-got-it-who-wants-it-and-whats-next/

6. European Foundation Centre (2014), Making Your Money Work Harder: Social Investment Practices: An Introduction for Foundations https://www.issuelab.org/resource/making-your-money-work-harder-social-investment-practices-an-introduction-for-foundations.html

7. https://www.bigsocietycapital.com/what-we-do/investor/case-studies

8. https://responsiblefinanceforum.org/map-case-study/

9. Ibid.

10. CAF Venturesome, Nine Misconceptions About Social Investment [online webinar] https://www.cafonline.org/charities/borrowing/social-investment/misconceptions-social-investment

11. Ibid.

12. https://www.crowdfunder.co.uk/womensloanfund

13. https://www.resilientscotland.org.uk/impact/

ACKNOWLEDGEMENTS

This resource was produced as an output of the UKCF Connect Fund Pilot, with generous support from the Access Foundation and the Connect Fund at the Barrow Cadbury Trust:

Report Author:
Esther Goodwin Brown
Voluntary Sector Consultant

CONTACT DETAILS

Registered office
Unit 1.04 Piano House
9 Brighton Terrace
London SW9 8DJ

020 7713 9326
info@ukcommunityfoundations.org
www.ukcommunityfoundations.org
@UKCF_tweets

Registered charity number 1004630
Company registration number 2651777