



Select Committee on Charities

Corrected oral evidence: Charities

Tuesday 25 October 2016

5.35 pm

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Members present: Baroness Pitkeathley; Lord Bichard; Lord Chadlington; Lord Foulkes of Cumnock; Baroness Gale; Lord Harries of Pentregarth; Baroness Jenkin of Kennington; Lord Lupton; Lord Rooker; Baroness Scott of Needham Market; Baroness Stedman-Scott.

Evidence Session No. 8

Heard in Public

Questions 81 - 88

Witnesses

I: Jonathan Jenkins, Chief Executive Officer, Social Investment Business; Ben Jupp, Director, Social Finance Ltd; Caroline Mason, Chief Executive, Esmée Fairbairn Foundation.

Examination of witnesses

Jonathan Jenkins, Ben Jupp and Caroline Mason.

- Q81 **The Chairman:** Good afternoon, gentlemen and lady. We are delighted to see you. Thank you very much for coming to give evidence to this ad hoc Committee today. We apologise that the session is slightly curtailed because of various parliamentary procedures that we had to deal with.

I must remind you of some specific things. The session is open to the public, as you know. A webcast of the session goes out live and is subsequently accessible via the parliamentary website. A verbatim transcript will be taken of your evidence and this will be put on the parliamentary website. A few days after the evidence session you will be sent a copy of the transcript to check for accuracy, and we would be grateful if you could advise us of any corrections as quickly as possible. If after this session you want to clarify anything you have said or add anything you feel you have not had the opportunity to say, please feel free to submit more written evidence to us.

Perhaps you would like to introduce yourselves for the record, and then we will go straight into our questions.

Jonathan Jenkins: I am Jonathan Jenkins, Chief Executive Officer of Social Investment Business.

Ben Jupp: I am Ben Jupp. I work for Social Finance.

Caroline Mason: I am Caroline Mason. I am the chief executive of the Esmée Fairbairn Foundation.

The Chairman: The Committee of course has had your background, biographies and so on. We will start with Lady Jenkin's question.

- Q82 **Baroness Jenkin of Kennington:** What opportunities and challenges do social investment and social enterprises present for investors?

Caroline Mason: I will start with that.

The Chairman: Just a minute, Caroline. I should have said that you do not all have to answer every question. We leave it to you to decide who is going to speak on what, and you do not necessarily have to answer every question. Please carry on.

Caroline Mason: We see three areas of opportunity. One is in the local real economy, as an engine for a more inclusive economy. We invest in things such as community renewables, community transport, food, leisure, sport, conservation, the environment, and the arts, so generally that idea of an engine for community economy. The second thing is buying power of the state through commissioning; with corporates it is how they use their supply chains, buying from social enterprises and charities—we see a growth in that, in trading models, co-operative and social enterprise models. The third is the retail and consumer side, so simple retail products such as social ISAs, crowdfunding platforms, and

charity bonds. These are very simple, well-known, effective and efficient financial constructs that people understand and are already gaining traction. People connect directly with these types of products and what they are trying to achieve.

Ben Jupp: I know there will be some questions on other topics, having listened to the previous session, so I will keep my answer as an introduction really. This is really important for me and, I am sure, for Jonathan and Caroline. The reason I am interested in this is that I see a set of social challenges, whether these are around ageing, vulnerable people with needs, or the environment, where to get the responses right requires capacity, time, effort and diligence. The opportunity of social investment is to try to support that capacity, that time and that diligence, and the challenge is that that is difficult. Anybody who has not tried to tackle those things will know that.

Jonathan Jenkins: Very quickly, the attraction for me of social investment is social investment going into areas where mainstream money will not go, because we are capable. I think we understand the risks better, and we see ourselves as responsible for educating other investors, particularly mainstream investors. The risks are not maybe as dramatic as they think, and there are opportunities for mainstream money to follow us into areas that we have gone into already. We see refinancing of a lot of our loans by mainstream investors as a success—that they would then take organisations to a further stage of growth. The one thing Caroline mentioned that has developed with very little input from the social investment market, a natural state of business, is the rise in the interest of retail investors. We were probably all structured to try to engage institutional money coming in, but over the last 18 months or two years, the dramatic increase in community share offers, in retail bonds coming through, has probably equalled, if not surpassed, the money that has been put into the market by the traditional social investment market.

Q83 Lord Chadlington: The point I would like to go on to has to do with what the social investor is looking for in the way of return, the social or financial return. Often in the cases that you look at, the return is quite long-term; sometimes exactly what one is looking for is quite diffuse. How does the social investor look at that step in what they do?

Caroline Mason: We are a social investor. We have committed about £45 million across about 111 social investments. Nineteen of them are into funds, but we have also done 40 or 50 debt-style products, equity, quasi-equity, underwriting asset purchases, and we understand that the introduction of social and environmental considerations into an investment changes the nature of that investment. It is a bit like moving to 3D chess. You have to incorporate another consideration; you have risk and return, and now there is social and environmental impact. People keep on talking about win-win, and it is not win-win; I would describe it as a delicate balance of benefits, and there has to be a consideration of the tension between return and social and environmental impact, and the extent to which the focus on returns might dilute or skew the delivery of

that impact. For example, our gross returns are 2.5% and our net returns are 1.8% over time, and we are absolutely first and foremost an impact first investor, so we absolutely put impact first. We price in the value of the impact by reducing our return to make that happen. It is possible but it is not a science. There is a definite return that can be made; it is not an arbitrary return, and it is sometimes not a short-term return.

Baroness Jenkin of Kennington: Can you give an example?

Caroline Mason: A very simple example in the environmental space: we have a land purchase agreement where, when a piece of land comes on to the open market that is of extremely high conservation value, we have an agreement with a number of charities in the sector, we buy that land, and we lease it back to them over two years at 2%, including transaction costs, and they have two years in which to raise that money and pay us back. We have done that probably 11 or 12 times to the tune of about £15 million and we have never lost money. Money has always been repaid. That is a very simple form of finance; it is very clear what the transaction is. We have had a recycling rate of about 40% in our portfolio to date of people repaying that money, so it is possible to do this.

Jonathan Jenkins: I was going to add that with social investment there is a specific rate of return, a specific measurement of impact. There is an increasing variety of investors who find different balancing points on Caroline's balance between impact and finance, such that you will have the very commercial, the pure for-profit investment, but in an area of deprivation where the social impact is pure economic development, whereas you have on the other side an organisation which you maybe have an investment into that if you do well you will get your money back but it is an area that no other bank will touch. It is a very difficult balancing act, and the market tortured itself in its early days to try to get to a definitive metric or measure or "This is perfection", and I think we have grown past that now.

Lord Rooker: I want to ask about public service delivery but before I do, I had better make a short declaration of interest. My wife, Helen Hughes, is the pro bono chief executive of Ludlow Assembly Rooms, which have recently been on the receiving end of grant aid from Esmée Fairbairn, for which I might say they are incredibly grateful.

Caroline Mason: It is a pleasure. That is what we are here for.

Q84 **Lord Rooker:** Can I ask you about the role of social investment in public service delivery, and how you balance the needs of the private investors and institutional investors with those of the Government, and maybe distinguish between central government and local government? I would imagine there must be fairly substantial differences. To wrap it up, are there disadvantages in respect of this with the profit-maximising private firms that are involved in public service delivery? Are they a particular area?

Ben Jupp: First, every week I say to my team and I ask myself not, "How are we balancing the interests of government and of investors?" but, "Are we doing the very best we can for those who are being supported?" I do not say that flippantly; having worked in government, I know how easy it is to look upwards all the time, and one of the things that excites me about social investment is the opportunity to work with and look at how we can support vulnerable groups more. What I have found in developing social investment partnerships, of which I think social impact bonds are a type, is that it is worth putting in the time to make sure there is an aligned interest between the needs of individuals and communities, the right interests of local government and central government, and those of investors. Often that involves working with groups in the development of services who will be service users and involving the right sort of investors, who have an interest in that topic beforehand, and all the time making sure that there is an alignment of values and objectives. We can talk about that a little bit more if it is helpful, or I can give some examples.

Caroline Mason: I would like to comment on that from the perspective of a philanthropic investor, because I think this is an unspoken expectation that philanthropic capital will come in to take that risk on the outsourcing of public services, and we have been very judicious in those that we invest in—the social impact bonds and the contract base, and the risk contract based financing—because we do not feel that underwriting statutory risks and costs or private sector risks and costs is a particularly good use of philanthropic capital. We only do that very judiciously, when it really is, as Ben said, absolutely to the benefit and maximises the impact of those people that we care most about.

Q85 **Baroness Stedman-Scott:** Good afternoon. What are the main obstacles faced by charities and social enterprises in managing social finance, and how can investors support them in overcoming these obstacles? Also, what should the role of trustees be in helping develop social enterprise skills within the charities?

Jonathan Jenkins: We run quite a lot of the programmes around capacity building for people to take on social investments, and I think Geoff Burnand mentioned that the Government have been very supportive on a number of different programmes to provide grant money for intermediary support to make organisations ready for investment. We have been pretty much at the sharp end of what that intervention needs to look like.

We still constantly, particularly now, with an uncertain macroeconomic environment, come up against the very simple "We are not taking debt right now". I think it is fair to say that anecdotally I am hearing of more debt providers making offers than are being accepted at the moment, so there is a conservatism among trustees. There is quite a lot of work going on, in that organisations—a number of the large banks—are having sessions with their trustees to make them more comfortable with the concept of social investment. It is trying to talk to them about bringing basic debt or basic financial products into a charitable structure; social

impact bonds are further down the route. A good number of charities and social enterprises when they hear “social investment” hear “social impact bonds”, and that has been a failure of the market as a whole at not separating those two. There is a difficulty in understanding what the investment is about.

I work day to day in social investment. It has grown out of all recognition over the past five to eight years. Five years ago I could name you every organisation offering finance, probably every product, and probably every person making the decisions on those products. I cannot do that now, not by any stretch of the imagination. The experience of a front-line organisation in Hull, delivering very important services, how they navigate this marketplace, find out what is relevant, quickly, in a way that is not patronising, in language that they understand and is useful, is one of the big challenges the social investment market place has systematically failed to deliver on over the last few years. We need to make ourselves far more relevant, understandable and approachable to those front-line organisations that, as Ben was saying, we are simply here to serve.

The Chairman: Are you saying that the failure to understand or the failure to be aware of what is there is mainly on the part of trustees or on the part of the staff of organisations?

Jonathan Jenkins: Again, anecdotally from our experience, with the smaller organisations you have a very small exec team who are heads-down, delivering services, winning money. The financing is not number 1, 2 or 3 on their list of priorities. I would suggest the trustees should be looking at this, having the arm’s length away from operational delivery. If you look at where trustees can play a great role, it is post investment.

If we look at the failures that have happened in social investment, Venturesome has published its lessons learned, and we are publishing information about investments that we have had that have gone wrong. I suggest that the vast majority of those that have gone wrong have not gone wrong because the business model failed but because the governance was not strong enough on the chief executive. We live in difficult times; when they hit the bumps in the road, there was not the breadth and depth of support to turn the situation around. There is nothing more frustrating as an investor as coming across a situation too late in the day, when you cannot do anything about it. That is, again, one of the biggest areas we would like to see improvement in: nurturing and understanding and talking to investors when things are not going as well as they could be.

The Chairman: Ben, do you want to say anything more about the obstacles and the trustees?

Ben Jupp: No.

Caroline Mason: We keep on talking about investment-readiness; I think there is something about investor-readiness. The social investment

market I do not think really understands the absolute fabric of the social sector. We are very fortunate, because we are a grant funder as well as a social investor, so we know that organisations are on the ground; social investment is not the only type of funding they have. They are having to balance grant funding, contract funding, trading revenue, volunteering time, donations, as well as social investment, so their blend and mix is complex, and this idea that social investors are the thing, or are other to all of that, rather than being an integral part of an organisation's operational capacity to absorb different kinds of financing, is sometimes lost, and a lot of social investors do not understand the fundamental fabric of the market that they are operating in.

The Chairman: So it is the investors who do not understand?

Caroline Mason: I think it is both, but everything is focused on saying the organisations have to effectively come up to scratch. I think there is an equal amount of learning that needs to be done on the social investor side.

Lord Rooker: Is that a case of saying that people who are social investors should also have a minimal amount of grant work to get their hands dirty on the other side of it?

Caroline Mason: Investing in homelessness is very different from investing in mental health. There is not one, homogenous market here that people are operating in. If you are a social investor in these areas, you probably need to know quite a lot about the underlying context in which those charities operate, and I think many social investors do not, or they are getting better at it but I would say they probably do not.

Jonathan Jenkins: I think the Government have been incredibly supportive in creating the ecosystem that we have. We have Big Society Capital; we have social investment tax relief; the list goes on of the cross-party support we have had in building the social investment marketplace. I think somewhere along the way those of us operating in it have been focusing on products and lost sight of the need of those who we are eventually here to serve. This is a moment where we need to readjust that and anchor ourselves in providing money that perhaps has more relevance to a greater selection of front-line deliverers.

Lord Bichard: Before I come to the question, which you have answered—the second time it has happened to me today—these are really important points you are making. What Caroline was saying is, if you want to sell anything anywhere, you need to understand the market you are selling into, and there is probably still scope for a better understanding of the market by the investors.

Caroline Mason: Yes.

Q86 **Lord Bichard:** What Jonathan was saying a bit earlier was, not only do you need to understand the market, but you also need to market your product in a way that people can understand, but there needs to be a

simple communication. I think those are really quite important points in the social investment debate.

If you do not agree with me on that one, do say so, but I sense you are agreeing.

The question I was going to ask was pursuing this line about what you think the strengths and weaknesses of the Government's existing policies are, including issues like social impact bonds, which I have thrown in so that Ben can respond to some earlier comments that were made. What do you think about the Government's policy? Some people have said to us it is a bit fragmented; it is incoherent; some of the products are finance-driven to the point where they are too exotic and do not meet real demand. How would you suggest the Government do this better in the future?

Caroline Mason: I do not think the Government's strategy has been incoherent or fragmented; I think it has been really clear. The government policy to date has been very much about supporting the delivery of public services, and that is why it has hinged on three things. One is on SIBs—social impact bonds—so contract-based financing. I think the other is on volunteering; that has been a key part of the sector. It has also focused on this idea of—I have gone completely blank. It has basically been around public service delivery.

The Chairman: If you remember your third point, come back. Ben, meanwhile.

Ben Jupp: I think there have been lots of strengths in government policy as a whole. I said about having been involved on the government side as well as in social finance. I think that setting things up on a long-term basis at arm's length, such as Big Society Capital, has been generally a good thing to do, and we will come back with our recommendations for the last question.

I thought it might be worth saying a teeny bit about social impact bonds, if that is okay. There are lots of fantastic charities and social enterprises that could benefit, and do benefit, from social investment which enables them to expand what they are doing.

There is also a set of challenges which are not always being met due to a combination of the way that government is working and the response available from the social sector. The types of issues that I work on in health and social care include: employment support for people with health needs and disabilities, which, as Tomorrow's People will know, is abysmally developed at the moment; addressing loneliness and isolation among older people at scale rather than through a tokenistic befriending scheme involving a few dozen people; and a radical shift of social care so that it is drawing in the informal resources of communities and the gift of families, as well as in a better relationship with formal care.

For these issues, there needs to be not just investment but a bringing together of capacity and expertise around how to develop better solutions

on the one hand, often with changes in how services are contracted and procured, and finally with building up new forms of delivery organisations. That is essentially what we are trying to do. In the case of loneliness at scale, it has been about supporting local voluntary and community sectors to come together to form an infrastructure to which hundreds of organisations can refer people; in the case of health and employment, it is about how to build out from a health service to help achieve employment support.

What we are therefore trying to do is say to local government or central government, "What would work for you around achieving outcomes that would be valuable?" and to say to the voluntary and community sector, "How can we build up your capacity to deliver those?" That is the heart of the types of partnerships I think are important, and that is maybe why although at times there has been too much hype about them, I think those are really important service development discussions to be had. Social impact bonds are one way in which we can achieve those.

Jonathan Jenkins: As I said, I think the Government have been incredibly supportive and co-ordinated in what it has done and the themes that have been important to it. We have a structure that is constantly visited by other countries, in awe of what has been created. It is easy with hindsight to say, "Could we have done it differently?" I am very glad we have what we have. Do we have all the right pieces in all the right places so the money is flowing in the right way, and quickly and efficiently? No, I do not think so, but do we have enough resource collectively to get our heads down and change the structure, and make some tweaks to make it work? Absolutely. The danger and the frustration is that every day we collectively pontificate on the better way of getting our funding to the front line. The poor soul on the front line is having another day of delivery without foresight of where their funding is coming from. We have a lot of ingredients but we do not yet have the right mix, but it is perfectly within the gift of those within the social investment market to mix those ingredients better, and slightly change the way in which we use them.

The Chairman: Thank you very much. Did you remember your third point, Caroline?

Caroline Mason: Sadly, no¹.

Q87 Lord Lupton: I am going to focus now on the smaller and medium-sized charities. We have had quite a lot of evidence that there is demand at below £150,000 limits for social investment from smaller charities, but there is supply for numbers over £200,000, so there is a slight mismatch. First, do you think social investment should—and, if so, how—be more effectively promoted to those smaller charities and social enterprises? The second question, which Caroline has half-answered, is: should, and if so how, investors seek to engage at the smaller end?

¹Note from witness: The third area of government focus and support is in investment and contact readiness.

Caroline Mason: There are two avenues for that, which I do not think have been utilised particularly well. One is the foundation world, and to date, to be, honest the language around social investment has been incredibly sterile for the foundation world, because it talks about capital stacks and risk and market rate of return. That is what we do with our endowment; it is not what we do with our mission. This idea of engaging with the foundations to maybe create pools of money that might suit the organisations that we fund day in, day out with our grant money that sits alongside our grant money might be an area to explore. The other is to use the existing infrastructure within the sector. One of the reasons these small deals are very hard is the very high cost of due diligence, but you can put half a day or two days a week in with a community foundation, for example, within the infrastructure that already exists. A community foundation in Newcastle deals with these organisations day in, day out, so its due diligence costs of assessing as organisations is much lower—it already knows those organisations—so the idea of spreading out, not to create another intermediary in Newcastle or in Hull but use the existing infrastructure, the local CVSs, the community foundations that exist, and build up their expertise in simple lending might be another way of doing it.

Jonathan Jenkins: I think you are absolutely right. I think that is the misbalance of supply and demand. There is too much money available from £250,000 upwards and not enough sub-£150,000. I could put it differently: there are not enough equity-like products; there is not enough investment that is prepared to take equity risk, because you cannot get the equity-style returns. The sub-£150,000 marketplace needs subsidy.

Lord Lupton: Sorry to interrupt but do you think that is a function of the cost of putting these things together, where it is just not sensible or economic to do a £50,000 loan?

Jonathan Jenkins: I think it is no different from mainstream investment; the valley of death of investment is £50,000 up to £250,000 for normal commercial businesses. It is very risky, and you have to be able to charge high rates of return to make the portfolio balance. I do not think it is any different for the world we are in. Therefore money that is going into that space should have very different return expectations or risk appetite to money that is comfortable with investing at the higher levels.

The Chairman: Did you want to add anything, Ben?

Ben Jupp: I would add on contract finance, which is what we do a lot, one of the things we increasingly do is form a partnership with the commissioner first—with local government—and then we both sit on the interview panel for procurement. If the organisation which is chosen by the council—as long as we think it is a good organisation—needs £100,000 or £150,000 of up-front capital to develop that contract effectively, we provide that as part of the same process. That is what we are doing in Shared Lives, for example; my colleague was on two

interview panels— procurement panels—this week. That is a much simpler way to do it than to set up a whole lot of complicated contractual structures.

Jonathan Jenkins: I think increasingly we are seeing, funnily enough, almost a reinvention of the wheel. Ten years ago, when Futurebuilders came in, there was a lot of blended finance. It was grant and loan. The market seemed to move away from that about five years ago. We were trying to find a whole swathe of market-rate returns that did not need grant, and I think we have come back; the rhetoric seems to be about how we can blend money. So we have the Access Foundation blending money, and investors need to work much more closely with other sources of finance. We are working alongside grant givers, because they have done the due diligence already; they have sunk costs in what they are doing, and we might be able to support that. The market has come full circle and realised it is a blend of things.

Q88 **The Chairman:** Thank you very much. I am going to ask you the last question, and it is one we are putting to everybody who is coming to see us. When our report comes out next March, what is the one recommendation you would really like to see in it—I am going to say you must say one—about social enterprise and social investment? Who is going to catch my eye first for their one?

Caroline Mason: We would like to see more policy support for different forms of finance, such as community shares, charity bonds, rather than just funds and SIBs, and have more government support for those kinds of products.

The Chairman: In policy terms?

Caroline Mason: In policy terms, yes, and in narrative terms as well.

Ben Jupp: Within the world of improving public services, as I just talked about, support for both partnership structures, where investors who know a lot about an issue form a partnership with local government or the NHS, to then find a social enterprise to support with a contract and investment. I think is an exciting way forward, and would need some tweaks in some of the procurement regulations to do that most effectively.

Jonathan Jenkins: I would like to see more relevant shaped money available to front-line organisations based on their need. The biggest single opportunity for that, I would suggest, is Big Society Capital, which has a new CEO and is about to go into a strategic review. Use that opportunity to question its internal rates of return—not so much the price of money but maybe its risk appetite, and its longevity. How long do you need that wholesaler here if the whole idea is to make more mainstream capital available? It has done a good job till now but now is the point to completely review that, because that is the big £600 million powerhouse that a lot of us will take our lead from. Reviewing that could change, culturally and behaviourally, the entire marketplace.

The Chairman: Thank you very much indeed for those very succinct thoughts, and thank you very much on behalf of all the Committee for coming to see us today. We greatly appreciate your time. Do not forget: if there is anything else you want to add when you see your written evidence, we will be very glad to receive it.