

ENTERPRISING COMMUNITIES: WEALTH BEYOND WELFARE

A REPORT TO THE
CHANCELLOR OF THE EXCHEQUER
FROM THE
SOCIAL INVESTMENT TASK FORCE

18th October, 2000

The Rt Hon Gordon Brown
Chancellor of the Exchequer
The Treasury
Parliament Street
London
SW1P 3AG

Dear Chancellor

It is my great pleasure to submit to you this report from the Social Investment Task Force.

The Task Force has been hard at work since April, responding to your request for an urgent but considered assessment of the ways in which the UK can achieve a radical improvement in its capacity to create wealth, economic growth, employment and an improved social fabric in its most under-invested, that is to say its poorest, communities.

We have considered numerous ways of building upon recent initiatives, notably the important new incentives for charitable giving, the tripling in the size of the Phoenix Fund, the announcement of matching funds for a social venturing initiative and the launch in Scotland of the Social Investment Fund.

Our central conclusion is that the potential now exists to achieve a transformation of investment flows to support entrepreneurial value creation in those communities which have been most deprived of capital and management expertise.

Our report makes five specific proposals, which together would create the conditions for a vibrant, entrepreneurial community development sector to emerge, namely:

- **A Community Investment Tax Credit** to encourage private investment in community development. The resulting investment of £1 billion over the programme duration would be invested in both profit-seeking and not-for-profit enterprises in under-invested communities.
- **Community Development Venture Funds.** We suggest a matched funding partnership between Government on the one hand and the venture capital industry, entrepreneurs, institutional investors and banks on the other. Initially, we suggest that £100 million be made available by the Government on attractive terms in matching funding over the programme's duration.
- **Disclosure of individual bank lending activities** in under-invested communities. This should if possible be done on a voluntary basis, but if voluntary disclosure is not made, legislation should require disclosure.
- **Greater latitude and encouragement for charitable trusts and foundations** to invest in community development initiatives, even where these include a significant for-profit element.
- **Support for Community Development Financial Institutions**, including Community Development Banks, Community Loan Funds, Micro-loan Funds and Community Development Venture Funds. This requires action by the Government and its agencies (such as the Small Business Service), the private sector and the voluntary sector.

I am sure you will want to reflect on how best to achieve momentum in this important area of policy. To that end, we think it would be wise to consider the appointment within a government department of a champion for community development finance: an experienced and high ranking individual capable of conveying the message of this report and helping to refine its implications with bankers, large companies, venture capitalists, entrepreneurs and government agencies. Such a champion would help to encourage a more coherent approach among different branches and tiers of government and collaboration among social and community entrepreneurs and charities.

In the course of our work, I have been impressed with the level of skill and dedication of the large number of people I have been privileged to meet who have devoted their careers to helping communities in need. I have also much appreciated the expertise and generosity of those who have given their time to provide evidence and advice and the invaluable insight of the members of the Task Force.

I hope you will agree that, thanks to all their efforts, this report offers a new approach and a far-reaching programme to improve dramatically the prospects of under-invested communities.

With best wishes,

Yours sincerely,



Ronald Cohen
Chairman, Social Investment Task Force

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INTRODUCTION

The remit of the Social Investment Task Force was:

“To set out how entrepreneurial practices can be applied to obtain higher social and financial returns from social investment, to harness new talents and skills to address economic regeneration and to unleash new sources of private and institutional investment. In addition, the Task Force should explore innovative roles that the voluntary sector, businesses and Government could play as partners in this area.”

This Task Force was an initiative of the UK Social Investment Forum, in partnership with the New Economics Foundation and the Development Trusts Association. It was announced by the Chancellor of the Exchequer in February 2000. HM Treasury had observer status on the Task Force. It has not addressed issues that are the responsibility of devolved administrations, but its consultation has aimed to include developments across the whole of the UK, with a view to understanding best practice.

The members of the Social Investment Task Force were:

Ronald Cohen	Chairman, Apax Partners & Co. (Chair)
David Carrington	Chief Executive, PPP Healthcare Medical Trust
Ian Hargreaves	Journalist and academic
Philip Hulme	Chairman, Computacenter
Geraldine Peacock	Chief Executive, Guide Dogs for the Blind
Joan Shapiro	formerly Executive Vice President, South Shore Bank, Chicago
Tom Singh	Managing Director, New Look

All participated in the Task Force in a personal capacity. Further details about the Task Force members are given in Appendix B.

The UK Social Investment Forum, with assistance from Shorebank Advisory Services, provided the Secretariat to the Task Force. Research was supplied by the Development Trusts Association and the New Economics Foundation. Appendix C lists those who gave evidence or made other contributions to the work of the Task Force.

The UK Social Investment Forum defines “social investment” as “financial transactions intended both to achieve social objectives and to deliver financial returns to investors”. The Task Force focused on the specific issue of community development finance to meet the needs of under-invested communities.

EXECUTIVE SUMMARY

After a period of sustained growth, the UK enjoys more material wealth than ever before. Yet, at the same time, poverty has become more concentrated and inequality more marked. Some of our poorest urban and rural areas have become no-go areas for investment. In spite of this, they contain a strong core of entrepreneurs and the potential for more to emerge. What is lacking is the capital and managerial expertise to support them.

At present such communities are heavily dependent upon philanthropy and public money, whether in the form of welfare payments or grants aimed at supporting community regeneration. This money is vital for the maintenance of basic living standards, but on its own it will never be sufficient – and in some circumstances public money can discourage or crowd out private sector investment. The long-term aim of the Social Investment Task Force is to achieve a move away from this culture of philanthropy, paternalism and dependence towards one of empowerment, entrepreneurship and initiative. This cannot happen without the addition of significant private investment and management expertise.

The Task Force recommends to the Chancellor of the Exchequer a five-point programme of action for Government, business, finance and the voluntary and community sector aimed at increasing investment, enterprise and wealth creation. In particular, the report identifies mechanisms to unleash new and sustainable sources of private investment in under-invested communities¹. Business will need to work in close partnership with social and community entrepreneurs². Government, at all levels, must play an active, enabling role.

Enterprise and wealth creation are vital to building sustainable communities. But under-invested communities are too often seen as areas with little economic or business potential. Our research shows that, on the contrary, such communities can offer many profitable opportunities for companies, banks and other investors. Social investment, intended to achieve both social objectives and financial returns, can work alongside conventional commercial finance and business, to the advantage of the whole community.

The Government should frame policy with a view to encouraging the development of an effective system for stimulating enterprise and wealth creation in under-invested communities. In particular, policy

should seek to release capital from institutional, charitable and individual investors; to develop a more robust community development finance³ sector; to engage community and social entrepreneurs; and to attract new approaches from local, regional and national Government. Our recommendations are based on innovative approaches that have proved successful in stimulating community enterprise in under-invested communities in a number of countries.

It is essential that the recommendations of this report are properly situated within the context of other programmes and that the complex administrative procedures of some grant schemes are not transferred to them.

The report contains five specific recommendations aimed at building a new system of entrepreneurship.

1

RECOMMENDATION ONE

A Community Investment Tax Credit (CITC) to encourage private investment in under-invested communities, via Community Development Financial Institutions⁴ (CDFIs) which can invest in both not-for-profit and profit-seeking enterprises.

Many enterprises in under-invested communities find it difficult to access finance because their financial returns are insufficiently attractive for lenders and equity providers. There is a need, therefore, for strong incentives to be provided in order for significant finance to flow to CDFIs and enable them to guide and finance the growth of businesses as well as social and community enterprises.

After considering many alternatives, the Task Force proposes a tax credit which would provide lenders to, and equity investors in, CDFIs with a guaranteed minimum rate of return. Loans would be for a minimum five year term. This would, in our view, be the best way of generating a significant flow of capital to CDFIs.

The Tax Credit would work in the following way. If a lender provides a

¹ See Glossary: Under-invested Communities

² See Glossary: Social and Community Entrepreneurs

³ See Glossary: Community Development Finance

⁴ See Glossary: Community Development Financial Institutions

five-year loan to or invests in the equity of a CDFI, the sum of £100,000 for example, the lender would receive a 5% credit against its tax liability in each year. In this way, £50m of tax credit in each of five years would support £1 billion of capital investment. The Tax Credit would cover both equity investment and loans by companies, banks and individuals.

In principle, we think the programme could operate as follows. Legislation in a Finance Bill would set the objectives and framework for the programme, and allow the Government to specify an amount of investment that would qualify for the tax credit each year. There would then be a competitive process for allocating the tax credit to individual CDFIs based on the applications they submitted. Lenders to or equity investors in the CDFI would then receive the tax credit proportionate to their investment and the CDFI would channel the money raised into selected enterprises. A key decision will be which organisation will evaluate CDFI applications and allocate the tax credit. One option would be the Small Business Service, to parallel its responsibilities for the Phoenix Fund. Suitable arrangements will also be needed for the devolved territories.

We recognise that this programme would be innovative, and that there will be many practical issues to resolve. But we are convinced that tax credits are key to attracting more investment into community development.

2

RECOMMENDATION TWO

A Community Development Venture Fund – a matched funding partnership between Government on the one hand and the venture capital industry, entrepreneurs, institutional investors and banks on the other.

The Task Force recommends that the successful principles of venture capital, namely long term equity investment, business support to the entrepreneur and rapid growth of the company backed, should be applied to community investment through the creation of Community Development Venture Funds (CDV Funds). In the last 20 years, venture capital has made a major

contribution to the growth of wealth and employment in the UK.

CDV Funds will finance and support entrepreneurs in under-invested communities who would not otherwise have the opportunity to create and develop competitive enterprises, to the benefit not just of themselves, but of employees and others in their community. CDV Funds will be run for profit and targeted at under-invested communities.

In order to attract significant funds in early years until returns are proven, the Task Force recommends ensuring that a wide range of incentives is available to encourage investment from different classes of investor, as follows:

- The CDV Fund would be partially owned by a charitable trust to which it will pledge gains from the charitable trust's investment. Charitable donors will benefit from tax relief on their donations to the trust.
- Other equity investors such as companies, banks, charities and individuals, will benefit from:
 - matched funding from the Government
 - 5% annual tax credit on their investment for five years
 - capital gains on the CDV Fund's investments

It would be desirable for individual investors in CDVFs to be broadly in the same a position as investors in Venture Capital Trusts (VCTs). In order to achieve this, individual investors in CDV Funds should be exempted from capital gains tax.

Since property redevelopment is a vital component in the regeneration of areas suffering from under-investment, it would be helpful to consider, in due course, whether the CDV Funds should also have the ability to invest up to one third of their capital in property assets and the balance in businesses.

The Task Force welcomes the announcement by the Chancellor in June 2000 that the Government would be willing, in principle, to support this initiative by matching private sector CDV funding. The Task Force proposes that in order to achieve a significant impact, the Government should provide up to £100 million on attractive terms in matching funding, for example by scaling up the Phoenix Fund.

The Task Force hopes that the first CDV Funds will inspire the growth of a significant community development venture capital sector across the UK.

EXECUTIVE SUMMARY

3

RECOMMENDATION THREE

Disclosure by banks

Banks need to play an essential role in under-invested communities, where they are a major source of private investment. However, in the UK there is a serious shortage of information about the level of activity of individual banks – at a time when there is a general perception that banks are withdrawing from poor communities through branch closures.

Together with evidence of general physical neglect, this contributes to a pervasive impression that such communities are, in effect, enterprise “no-go” areas. More detailed information about the lending pattern of individual banks, as is available in the US, makes it possible to compare good and bad practice and encourage a cumulative “improvement in performance”.

The Task Force welcomes the Bank of England’s commitment to monitor access to business finance in deprived areas. We believe, in addition, that there is a need to request much more detailed, individual disclosure by banks of their lending activities in under-invested areas, and to sponsor the creation of a rating system to reward excellent performance.

If voluntary disclosure is not made quickly, the Task Force believes that Government should require disclosure, in the manner of the 1977 US Community Reinvestment Act.

4

RECOMMENDATION FOUR

Greater latitude and encouragement for charitable trusts and foundations to invest in community development initiatives

Support from charitable foundations and major charities has an important role to play in expanding community development finance, through grant-funding, guarantees, programme-related investment⁵ and investment in CDV funds. However, confusion about when community development finance is charitable and when programme-related investment is acceptable to the Charity Commission has inhibited the degree to which foundations and charities have supported community development finance.

The Task Force welcomes the clarification it has received from the Charity Commission that charities with appropriate objects can work through CDFIs to assist a wide range of entrepreneurs in under-invested communities and can undertake programme-related investment. However, the Task Force urges the Charity Commission to publish formal guidance on Community Development Finance and the charitable status of CDFIs, taking into account the significant public benefits of their role in under-invested communities.

5

RECOMMENDATION FIVE

Support for Community Development Financial Institutions

A thriving community development finance sector comprising Community Development Banks, Community Loan Funds, Micro-loan Funds and Community Development Venture Funds

⁵ See Glossary: Programme-Related Investment

⁶ See Glossary: Charitable Foundation

– standing between Government, banks and other investors on the one side, and businesses and social and community enterprises on the other, is vital to boosting enterprise and wealth creation in under-invested communities. Compared to the US, the UK CDFI sector is relatively small, but capable of dramatic development.

In order to build on the pioneering work done so far, the aim should be to engage business leaders and CDFIs in the development of:

- new mechanisms to collect funds at the wholesale level which can be channelled to CDFIs
- an effective trade association, capable of assembling reliable information and representing the needs of CDFIs.

For example, the American Local Initiatives Support Corporation (LISC) is a wholesale deliverer of community development finance and the National Community Capital Association (NCCA) is the USA's biggest community development finance trade association. These institutions, with suitable adaptation, should be replicated in the UK. The principles involved are strong private sector involvement and a mix of funding from Government, financial institutions and charitable foundations⁶.

The Community Investment Tax Credit (CITC) will itself help increase the scale and capacity of CDFIs by increasing private investment flows. But other actions are also needed to bolster this process. We recommend that:

- organisations that wish to become national intermediaries should equip themselves with the business expertise and skills evident in the leading USA intermediaries such as NCCA and LISC
- CDFIs should work closely with Regional Development Agencies and Local Strategic Partnerships
- Government should help by supporting CDFI development through the Phoenix Fund; and banks and large corporates and entrepreneurs should be encouraged to help, for example by loaning expert personnel and providing "in kind" practical support and facilities

The Task Force suggests the appointment within a Government department of a high ranking "champion" for community

development finance with strong lines both to the Treasury and (if selected as the key Government agency) the Small Business Service. He or she would help to spread the message to those whose collaboration is needed: banks, large companies, venture capitalists, entrepreneurs, institutional investors, the voluntary and community sector and Government agencies.

The Task Force believes that these five recommendations, if adopted, will result in a dramatic increase in the quality and level of enterprise in under-invested communities and reverse the downward spiral of declining investment, jobs, wealth and asset values. As enterprising communities develop, asset values will appreciate and the local economy will improve. What we seek is an upward spiral where enterprising communities create the wealth that lies beyond welfare.

FIGURE 1:
REVERSING THE SPIRAL OF UNDER-INVESTMENT

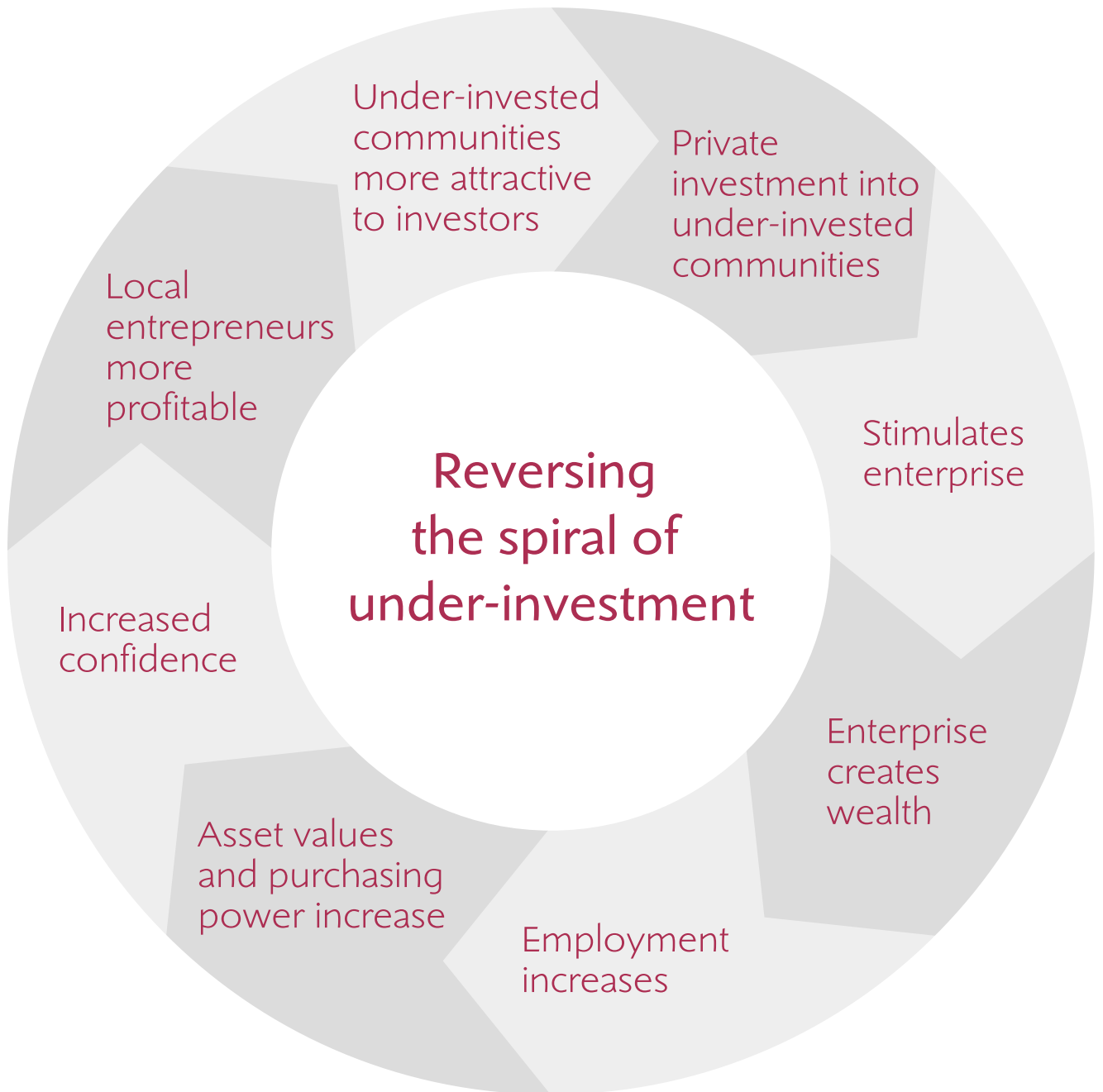
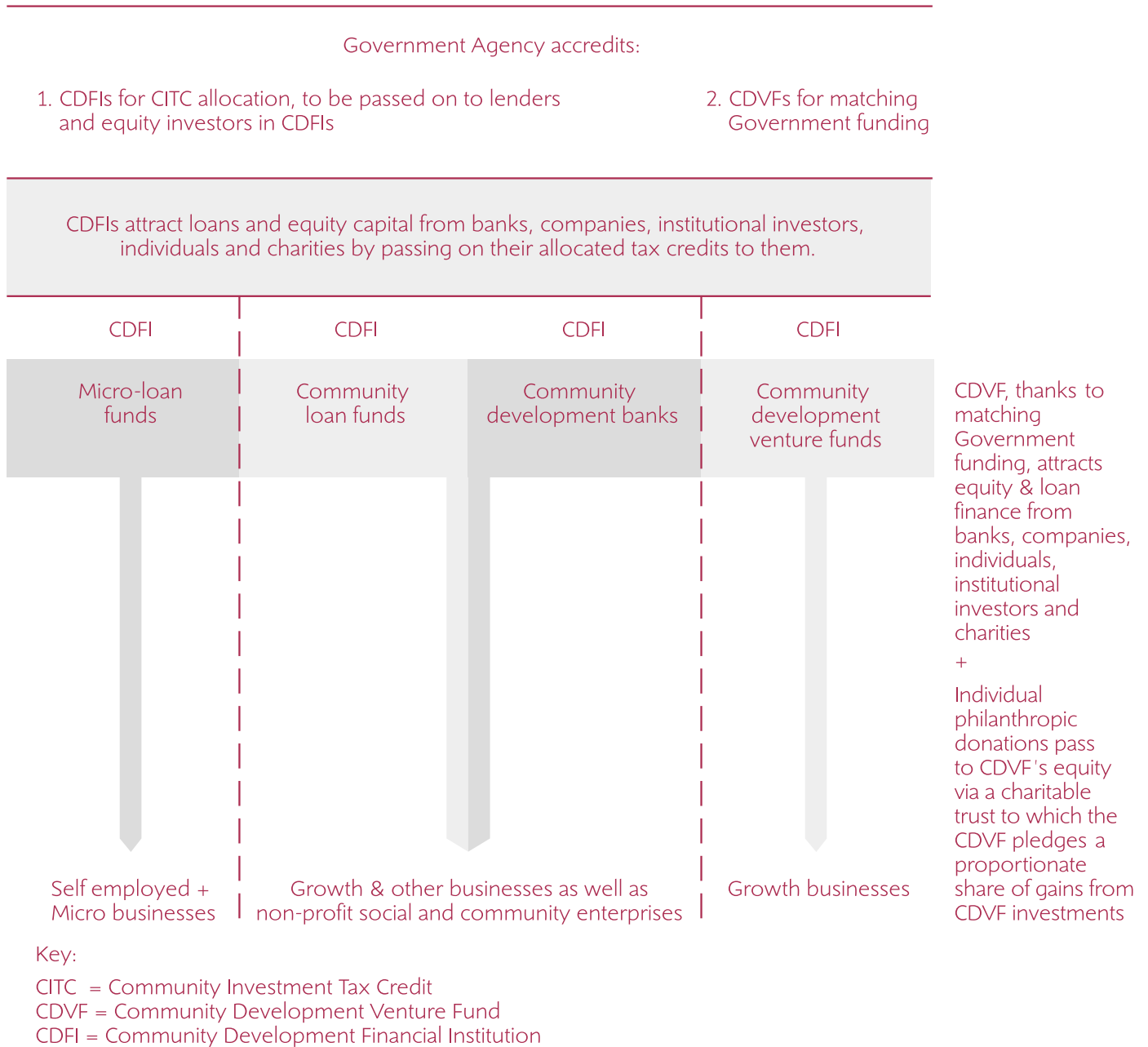


FIGURE 2:
USING THE CITC AND MATCHING FUNDING TO CDVFS TO ENCOURAGE PRIVATE INVESTMENT IN UNDER-INVESTED COMMUNITIES



THE CHALLENGE OF THE UK'S UNDER-INVESTED COMMUNITIES

1.1 NEW MARKETS

After a period of sustained growth, the UK is wealthier than ever before. Yet, poverty has become more concentrated and inequality more marked. With rates of unemployment more than six times the national average, some parts of our cities and countryside have become no-go areas for investment.

Under-invested communities suffer from a spiral of multiple disadvantage. Industries that were previously major employers have collapsed, leading to loss of employment, incomes, wealth and purchasing power. In such circumstances, it is often the case that private sector investment dries up and that even those financial resources available within a community are spent outside it. Confidence collapses and, with it, the climate for enterprise. In some poor communities, research has shown that as much as 75 per cent of the cash in circulation may come from central and local Government⁷. The result can be an intransigent form of welfare dependence, where the state confines its contribution to providing a minimum level of income and social services, but ignores wealth creation.

For a community to thrive, it needs individuals seeking to create wealth for themselves and their families and investors seeking a financial as well as a social return. Poor communities do not have enough of either, which is why they are better described as under-invested communities.

This is not to say that there are no entrepreneurs within these communities, rather that their efforts and potential are undermined by lack of capital, skills or business mentoring. In the Gorbals area of Glasgow, local residents Louise Brown and Russell McEwan started their video production company, Left and Right Video Productions. In North Belfast, May Mulholland's Quickprint business recently doubled its turnover. Neither could have succeeded without a local Community Development Financial Institution (CDFI) which provided debt or equity finance which was not available from mainstream sources.

There is also another kind of entrepreneur who plays an important role. These are social and community entrepreneurs, who apply creativity, skills, energy and vision to achieve community benefit, often mixing commercial and non-commercial activities within an overall objective of serving the community.

The Leicester Social Economy Consortium has redeveloped three derelict former textile mills using a mix of community development finance and public funds. For twenty years, the Environment Trust in East London has been building low cost green homes for local people, primarily using private investment but also benefiting from grants from English Partnerships and land transfers from the local authority. Dean Clough Mills in Halifax generates cash from business activities to support a hugely ambitious set of arts activities. In Birmingham, the Employment Needs Training Agency (ENTA) recently used a loan from a CDFI to upgrade its community café and workshop training facilities.

In various ways, projects like these demonstrate the effectiveness of an entrepreneurial approach, but across the UK such activities are not yet effective on a sufficient scale to make the necessary impact on the spiral of poverty and joblessness.

At the same time, around £3 billion a year of public regeneration funding⁸ has been poured into the UK's poorest areas. But the effect has often been confined to improvements in the physical appearance of places that, year after year, remain stuck on the UK's list of poorest neighbourhoods. Public expenditure programmes have done little to increase the incomes or personal assets of the people living in these areas. Public funding has too often "compensated people for being poor" rather than helping them find ways of creating wealth. Public money comes in, through welfare, housing, public services and regeneration projects, but it leaks straight out of the area rather than fostering local markets and enterprise.

A new approach to addressing the needs of under-invested communities would help to rebuild their economic base. In turn, that can lead to rising property values, wealth and an upward spiral in which more enterprise and employment create more purchasing power, which in turn generates further opportunities for entrepreneurship and investment.

Such a new approach requires greater co-ordination between Government tiers and departments and among funders of regeneration. It needs a major cultural shift from the public, charitable, voluntary and community sectors towards a more entrepreneurial approach. And it needs finance through a range of appropriate CDFIs.

⁷ "Where does public spending go? Pilot study to analyse the flows of public expenditure to local areas", DETR 1998.

⁸ Average annual public regeneration funding, 1994-2006 New Economics Foundation research, October 2000

1.2 COMMUNITY DEVELOPMENT FINANCE AND ENTREPRENEURS

While banks have been consolidating and moving away from a local branch presence, a new set of specialist financial organisations has begun to emerge to address the needs of entrepreneurs in under-invested communities. These CDFIs see their primary purpose as the provision of finance to self employed individuals and businesses just outside the margin of conventional finance. They bring specialist knowledge and methods.

The origins of today's community development finance sector date back to the 1970s. Early loan funds in the UK included Mercury Provident (now Triodos Bank), Industrial Common Ownership Finance, Hackney Business Venture and the Prince's Trust. Other CDFIs, such as the Local Investment Fund and the Aston Reinvestment Trust, have started more recently.

Experience with these CDFIs has illustrated the potential that social entrepreneurs can bring to regeneration. A wave of experimental civic initiatives has swept across the UK in the last two decades. In Scotland, for example, reflecting the contracting out of public services, 38 per cent of the charitable sector's income now comes from trading revenues – almost as much as comes from grants⁹. Members of the Development Trusts Association, the community-based regeneration network, have a combined income generated from community-owned assets and enterprise of over £20 million a year. In the last three years, a new organisation created by social entrepreneurs, the UK Community Action Network, has forged links between 380 social entrepreneurs running initiatives valued at around £1 billion.

Yet the evidence of these social entrepreneurs, which the Task Force has heard in some detail, is that most of the potential remains untapped – frustrated by lack of experience in using private capital, lack of skills and an appropriate enabling framework from Government. There is a need to create a system that makes it easier to exploit this potential, to make significant investments in entrepreneurial talent rather than put money into projects with a limited life.

CDFIs serve a wide range of entrepreneurs in under-invested communities. Some like the Prince's Trust provide young entrepreneurs with micro-finance. Others like the Merseyside Special Investment Fund concentrate on substantial equity investments.

One example, which serves to illustrate more general problems is the area of credit for micro-enterprises, ie. businesses with fewer

than ten employees. Such enterprises are the fastest growing sector of business in inner-city areas such as Tower Hamlets, London¹⁰. The UK has a higher failure rate for micro-enterprise than other OECD countries and one commonly cited cause is inappropriate finance.

CDFIs also serve larger for-profit entrepreneurial business, often in partnership with the banking industry. For example, Aston Reinvestment Trust provided a loan to Questions Publishing in Birmingham to enable it to expand into providing web sites for schools and interactive educational information via the internet, so employing more staff.

Some CDFIs focus on more strictly defined social and community enterprises (businesses which trade chiefly for a social purpose) and charities. For example, the Local Investment Fund made a £100,000 loan over four years to Community Links, a major East London charity, to ease its cash flow and to help develop a sustainable asset base. Charities Aid Foundation's Investors in Society lent money to Hastings Trust to enable it to buy a property, both as a shop front for its work and to provide an independent income stream.

Property assets and property-based lending are generally a crucial feature of social and community enterprise, as they have been in the much larger American CDFI scene. The UK's housing association movement shows what can be achieved when a system is put in place which brings together vision, capital, social need and an enabling Government framework. The highly successful Coin Street Community Builders is one example of the growing number of asset-based Development Trusts. It blends private enterprise, social housing and privately and publicly funded festival, arts and design activities on London's South Bank.

Business sectors with high potential for social and community entrepreneurs range from the provision of basic, everyday services, such as laundry, cleaning, gardening and child-care, to the exploitation of a growing range of opportunities to advance social inclusion by providing internet-based commerce, "distance" services of all kinds, and cultural services, such as arts projects, video/DVD rental and the provision of internet-based community information services.

There are many examples of social and community entrepreneurs in the UK developing a product or service within their local market and then expanding it to neighbouring and even more distant markets. Greenwich Leisure, for example, which began as a co-operative to run one leisure centre now runs a contracted-out network of leisure services across South London employing 1,000 people and contributing to both the local economy and quality of life.

⁹ Scottish Council of Voluntary Organisations, 1998.

¹⁰ Research on enterprise and regeneration by the Institute for Public Policy Research and the New Economics Foundation, forthcoming.

CHAPTER 1

1.3 HOW THE UK COMPARES

Community development finance is a world-wide phenomenon, from Bangladesh to the Basque region of Spain. It is therefore becoming possible to benchmark it in the UK against international best practice.

In the UK, community loan funds and micro-loan funds currently have a total capital of £80 million of which £65.6 million is private sector investment. Of this private investment, £60.9 million comes from companies, including banks, while £4.7 million comes from individuals.

There is a further £122 million of private investment in “social banks” such as Triodos Bank and the Ecology Building Society, with about £20 million coming from corporate sources and the rest from individuals¹¹. However, the primary focus of these banks is not the economic regeneration of under-invested communities. Then there are some Community Development Venture Capital Funds with about £45m. This suggests a total community development sector of about £250 million. (see Table A)

In the USA, the sector is more highly developed. By 1999, assets held and invested locally by CDFIs totalled \$5.4 billion, up from \$4 billion in 1997, a 35 percent growth over just these two years. And mainstream bank lending to small businesses located in low-and moderate-income communities and for other community development averaged a total of \$50 billion annually from 1996-8.

Table A. How UK and USA CDFIs compare 1999/2000

TYPE	£ - UK	£ - US
Social / Community Development Banks ¹²	£122m	£2,000m
Community Loan and Micro-loan Funds ¹³	£80m	£1,195m
Community Development Venture Capital ¹⁴	£45m	£207m
Total community development financial institutions (excluding community development credit unions)	£247 m	£3,402m

The strength of the USA community development finance sector owes much to a series of fair lending laws, in particular the 1977 Community Reinvestment Act, which created an affirmative obligation for banks to address under-served markets. The efforts of banks are supported by incentives, in the form of loan guarantees, tax credits and funding for CDFIs that act as partners for banks. (see Appendix A)

Even adjusted for lower population, the UK has a community development finance sector no more than forty per cent or so of its American counterpart.

Continental Europe also has extensive experience in social investment, much of which also falls under the umbrella of evolving European Union law and practice. For example, ADIE in France has a proven track record from the 1990s of lending to over 5000 micro-entrepreneurs. The CIGALES, again in France, provided some of the earliest micro-venture capital targeted at small companies with some social, cultural or ecological purpose. New markets, such as wind energy, were pioneered by the Danish social bank, Merkur Bank.

A snapshot survey by the International Association of Investors in the Social Economy¹⁵ of 86 social investment organisations in the 15 European Union member states showed capital of EUR 1.6 billion and a total loan portfolio of EUR 640 million. The survey focused solely on those organisations offering loans for small enterprise and the voluntary and co-operative sectors and thus by no means covers all social investment organisations in the EU.

The emerging economies of Eastern Europe have also shown remarkable success in developing micro-finance initiatives – Fundusz Mikro in Poland is a well-known example.

In the southern hemisphere, micro-finance institutions have at least US\$7 billion in loans outstanding to more than 13 million individuals. Many, particularly in Asia, focus exclusively on women. Such initiatives have proved that poor and socially excluded people can be profitable customers. The most celebrated micro-finance institution is Grameen Bank in Bangladesh, but diverse examples range from South and South-East Asia to Africa and Latin America.

The Task Force felt that whilst the UK can build on its own experience by learning from all these examples, the most effective practical step would be to study American experience in detail, since this appears to offer clear lessons in how an advanced and prosperous economy can make the transition from patchy provision of community development finance to a successful system capable of financing entrepreneurship

¹¹ New Economics Foundation research, October 2000.

¹² UK data, New Economics Foundation report (forthcoming). US data, “1999 Report on Socially Responsible Investing Trends in the United States”, Social Investment Forum, November 1999.

¹³ UK data, New Economics Foundation report (forthcoming). US data, “1999 Report on Socially Responsible Investing Trends in the United States”, Social Investment Forum, November 1999.

¹⁴ UK data, Source: New Economics Foundation, conservative estimate of targeted venture capital, including pioneering initiatives in the field such as the Merseyside Special Investment Fund. US data, Capitalisation of the US CDVC industry at 5/31/2000. Source: Research by Julia Sass Rubin of Harvard University for Community Development Venture Capital Alliance (forthcoming).

in under-invested communities on a sustained basis. In what follows, therefore, the Task Force has concentrated its international comparisons on the American experience.

The Task Force recognises that the USA record in tackling poverty is in many other ways less impressive than the UK's. Indeed, it is the sheer scale of income inequality in the USA and the comparative weakness of its welfare system that have helped to drive innovation in community development finance.

1.4 THE PUBLIC POLICY CONTEXT

The Task Force is aware of other Government initiatives, not least the forthcoming Urban and Rural White Papers, the National Strategy for Neighborhood Renewal and the New Deal for Communities. It seems likely that the emphasis in important aspects of policy will shift from the national to the regional level in England, as it has already shifted to Scotland, Wales and Northern Ireland.

The Task Force is hopeful that its recommendations will represent a good fit with Government policies for the regions, enterprise and regeneration. The Task Force's recommendation of a champion for community development finance (see Chapter 3) is particularly aimed at achieving coherence. The Task Force also hopes that the report of the Co-operative Commission, which is investigating the future of co-operative enterprise, will dovetail with its recommendations. Co-operatives have an important part to play in the ecology of social and community enterprise and could be a significant source of investment in CDFIs.

It is not for the Task Force to make detailed comments on policy shift to the regional level, but it is important to make the following points:

- The Task Force's analysis of the shortfall in community development finance requires enabling actions by Government at all levels. If, for example, local Government pursues community development strategies that ignore the role of the private sector or the importance of wealth creation, they will undermine the effectiveness of what is proposed here.
- From the EU to the local level, the Task Force would hope that community regeneration strategies would recognise the importance of the finance mechanisms outlined in this report. American experience demonstrates that a devolved political structure sits comfortably with the initiatives proposed by the Task Force. The devolved administrations, the Regional

Development Agencies and Local Strategic Partnerships responsible for economic development and regeneration at regional and local level will be especially important in implementing the Task Force's recommendations.

- The enabling framework described in this report requires attention to points of detail – for example local authority rules about the use of council property for business start-ups – as well as the deployment of new funding streams for community development.

1.5 THE EVIDENCE CONSIDERED

The Task Force heard evidence from a wide range of practitioners in the UK and the USA¹⁶.

From this evidence, the Task Force has identified what it sees as the main barriers to enterprise and wealth creation in under-invested communities. These are the key difficulties:

- **Systemic failure.** It is clear that in comparison with the US, the linkages between Government policy, banks, venture capital, institutional investors, foundations, business and social and community entrepreneurs fall short of what is necessary. There are major gaps in sources of funds, in the Governmental framework surrounding community development finance and in the current capacity and skills of many community-level organisations to respond to these new challenges.
- **Public sector grants and charitable funding.** Grants from local authorities and other public sector bodies and from charitable sources play an essential role in providing the start-up funds and "social equity" needed to build organisations and support activities that cannot otherwise be funded. However, when they are the sole or primary source of funds they have encouraged a culture of over-dependence, which can stifle enterprise and even crowd out other finance options. At the same time, grants have not focused on building sustainable organisations. There is no consensus among grant-makers on what activities should be grant funded and where debt or equity should be used to fund income generation.
- **Weak incentives for private investment in communities.** At present, CDFIs are unable to offer the rates of return needed to attract large-scale private sector investment and managerial talent. Some under-invested communities are, in effect, no-go areas for private capital.

¹⁵ Unpublished research by INAISE, 1999. The data for this survey was mainly from 1998, but some data also came from earlier years, making these figures indicative rather than precisely comparable. Data on a number of organisations was from between 1995 and 1998.

¹⁶ Details are given in Appendix C and on the Enterprising Communities web site at www.enterprising-communities.org.uk

CHAPTER 1

- **Low levels of entrepreneurship, indicated by low rate of small business creation.** The Task Force heard evidence about the UK's risk averse culture, deterring entrepreneurs and discouraging voluntary and community organisations from branching out in new directions such as income-generating activities.
- **Lack of information about bank lending activities and the potential markets in under-invested communities.** Small business lending by the banking industry is the major form of private sector investment in under-invested communities. The Task Force expects this to continue to be the case, even as the community development finance industry grows. USA experience suggests that the active engagement of the banking industry in lending to entrepreneurs is critical to wealth creation in those communities. But in the UK there is no public knowledge of the lending patterns of individual banks in specific communities. This makes it harder to ensure that competitive pressures are properly at work and harder to decide what other action should be taken. Lack of information also makes it impossible to measure progress in funding community regeneration and to benchmark one area against another.
- **The UK has an underdeveloped community development finance sector, compared with the US.** It is clear to the Task Force that this is a critical and reversible disadvantage for the UK. The creation of a vibrant range of community development financial institutions including lenders, venture capital funds and the organisations which serve them needs to be a key objective.
- **Interpretation of UK charity law as it relates to community development finance lacks clarity.** Confusion about when community development finance is charitable and when programme-related investment is acceptable for a charity has inhibited the degree to which foundations and charities have supported community development finance. Trustees of many charities take an excessively cautious view in these matters.
- **Lack of a coherent approach by different tiers and departments of Government.** Social and community entrepreneurs have much experience of dealing with Government. They report that demands from different Government departments frequently contradict each other and they complain about the complexity of paperwork, delays and bureaucracy that goes with many existing funding streams. These entrepreneurs also often find that something which is encouraged by, say, a central Government department is resisted at the local Government level. It is still not clear that all tiers of Government recognise

the importance of setting an enabling framework and providing incentives, rather than seeking to deliver services directly.

- **Entrepreneurial behaviour in the voluntary sector tends to be fettered by its traditions, laws and established practices.** Social and community entrepreneurs recognise that they need to take well-judged risks, develop commercial competencies, attract business and management skills and increase management capacity. Risk averse trustees and a culture of "begging and benevolence" are raised as just two factors which work against the voluntary sector promoting and practising entrepreneurship.
- **Public policy obstacles to entrepreneurship exist.** For example, the benefits system must encourage rather than discourage claimants wishing to take the first steps out of poverty into self-employment or micro-enterprise.

ENTERPRISING COMMUNITIES: WEALTH BEYOND WELFARE

2.1 A NEW SYSTEM TO SUPPORT ENTREPRENEURSHIP

New thinking is required if society is to tap into the abilities of entrepreneurs to improve their own situation and to rebuild the economic base of under-invested communities. It requires approaching them as an economic opportunity and recognising that their financial needs involve multiple elements, public, charitable and private. The challenge of neighbourhood renewal should also be seen as a challenge of restoring local market forces. What is needed is a market-driven system that harnesses entrepreneurial drive.

Perhaps the best example in the UK of how the creation of an enabling framework has acted as a driver for success and wealth creation is the UK venture capital industry. There, the establishment over 20 years ago of a “system” by introducing stock markets for small companies, legal vehicles for venture capital funds, lower tax rates and Government support of entrepreneurs stimulated a process which has led to today’s thriving venture capital industry.

The system proposed consists of financial incentives and market-driven institutions and it requires long-term sources of finance. It depends on entrepreneurial action within a supportive culture and infrastructure over a significant time period.

The Task Force believes that the following five recommendations will lead to a dynamic community development system in the UK. Its full development will take many years, but all of the proposals outlined here invite action within the next year.

2.2 RECOMMENDATIONS

1

RECOMMENDATION ONE: A COMMUNITY INVESTMENT TAX CREDIT

Tax incentives for under-invested communities are a necessary intervention to reverse a spiral of multiple deprivation. Without incentives, these communities will fall further behind the rest of the economy.

By stimulating new private investment into under-invested communities, the Task Force believes the Government can reverse the downward spiral, so that investment stimulates enterprise growth, which in turn provides employment and builds assets and wealth, resulting in increased purchasing power, bringing more jobs, more asset creation, more spending and eventually a higher tax yield. This process opens up new markets for more conventional investments, creating a bridge between investors (both corporate and individual), investment intermediaries and the customers they serve.

Community Development Financial Institutions (CDFIs) are best-placed to provide the initial pump-priming investment. They are able to match a business-like approach to lending with social motivations. Typically, CDFIs look for higher social returns than traditional private investment and higher financial returns than traditional public expenditure and grants. These organisations are able to direct finance effectively because they know their markets and can deliver services to them cost-effectively.

However, evidence to the Task Force showed that, while the CDFI market is beginning to demonstrate resourcefulness and skill in leveraging in new money, unmet needs continue to outstrip available resources. Access to funding is limited because, to date, CDFIs have only been able to seek grants and low or zero-return capital. This means that private sector companies and individuals take investment in CDFIs out of their “charitable-giving” or “public relations” budgets. This is a very limited pool. To expand the pool of investors willing to invest in the sector, there is a need for Government incentives to bring returns closer to market rates. The clearest way to do this is through tax credits.

CHAPTER 2

Investment in all UK CDFIs currently totals about £250 million¹⁷. Tax incentives could multiply this source of funding enormously, at relatively little cost to the Government, allowing existing CDFIs to expand and stimulating the creation of new institutions.

Using tax incentives to attract private investment also brings other advantages:

- **Linkages:** Fostering business-like links between private investors and CDFIs can promote investment from the initial investor's networks. In addition, this relationship-building brings with it expertise such as financial skills, technical support and marketing expertise for the CDFI and its clients.
- **Financial prudence:** In general, loan or equity finance promotes financial discipline and prudent policies, increasing pressure on the CDFI to work efficiently and maintain portfolio quality.

WHO WOULD USE THE TAX CREDIT?

The Task Force believes that this tax credit should be available to all investors, including individuals, banks and corporate investors – reducing their tax liability. It should cover both equity and debt investments in CDFIs, including CDV Funds. (See Figure 2, page 9)

A correctly administered tax credit programme would attract banks, insurance and other companies into partnerships with CDFIs, along with other community organisations. It is also anticipated that high net worth individuals and other individuals will invest in new and existing initiatives. By way of comparison, in 1999, CDFIs that belonged to the National Community Capital Association in the USA reported that 23% of their loan capital came from individuals.¹⁸:

Table B. American CDFIs in the National Community Capital Association – Sources of loan capital 1999

SOURCES	% OF BORROWED CAPITAL
Individuals	23%
Foundations	22%
Banks and Thrifts	15%
Religious Institutions	14%
Federal Government	11%
Other	10%
Non-Bank Financial Institutions	4%
State Government	1%
Total	100%

PRINCIPLES OF A SUCCESSFUL TAX CREDIT PROGRAMME

Details of the tax credit programme are a matter for the Government. We recognise that a wide range of practical issues will need to be resolved. However, the Task Force strongly recommends that tax credit allocations should be awarded to CDFIs that possess sufficient knowledge of investment conditions and opportunities within communities. Tax credit allocations awarded to accredited CDFIs would be distributed by them to lenders and equity investors.

In principle, we think the recommendation could operate as follows. Legislation in a Finance Bill would set the objectives and framework for the programme, and allow the Government to specify an amount of investment that would qualify for the tax incentive each year. There would then be a competitive process for allocating the tax incentive to individual community development financial institutions (CDFIs) based on the plans that they submitted. CDFIs would use their tax incentive allocation to attract finance from investors, and channel the money raised into selected enterprises. A key decision will be which organisation should carry out the evaluation of CDFIs' applications and allocate the tax incentive. One option would be the Small Business Service, to parallel its responsibilities for the Phoenix Fund. Suitable arrangements will also be needed for the devolved territories.

RATE OF RETURN

The Task Force recommends that the tax credit should offer a level of return that will help bridge the gap between the return available from a CDFI today and a market return, in order to attract investment from individual, bank and corporate investors of a business-like, and not just a philanthropic nature. It recommends a 5% Tax Credit.

If the return is too far below market, the tax relief will not succeed in attracting adequate volumes of investment because investors will continue to invest based only upon social goals – i.e. from their philanthropic or public relations budgets. Tax incentives have a higher chance of success if there is a "win" for each party at the table – investor, CDFI and the target community. This approach will create commercial motivation for banks and other private investors to become involved in community development projects. And it will lead to healthier, more productive and more efficient CDFIs.

¹⁸ Figures from the National Community Capital Association, referring to its own members, 1999.

Based on evidence gathered from UK community loan funds, the average rate of return they currently offer is no more than 1% p.a. This rate of return should increase as CDFIs become larger and achieve economies of scale. In the more mature USA community development finance industry, the National Community Capital Association, a leading association for CDFIs, provides its loans to members at 3.5 - 4.75% p.a.

In considering an appropriate level of tax incentive for the UK, the Government might consider the tax credit programme included in the New Markets Initiatives presently before the US Congress. This would provide a 5 percent credit per year for the first 3 years of investment, and 6 percent for the next 4 years with a net present value of more than 30% of the amount invested over the total period. It is expected that this will equate to 10-12% per year when combined with the returns generated by the CDFIs.

TYPE AND TERM OF INVESTMENT

To qualify for the tax credit, investors must make a long term investment because CDFIs need patient capital, in the form of both debt and equity.

At present, most CDFIs dedicate an inefficient proportion of their resources to raising capital. This greatly reduces their ability to focus on their core business of community development finance. It also makes it extremely difficult to plan for a medium term strategy of expansion. We recommend a minimum qualifying investment commitment of five years.

EVALUATION PROCESS

The organisation selecting CDFIs to receive tax credits will need to devise appropriate eligibility criteria. It could draw on US experience.

For example, the following criteria are used by the US CDFI Fund¹⁹:

- ✓ **Primary mission.** An applicant must have a primary mission of promoting community development.
- ✓ **Target market.** An applicant, collectively or with its Affiliates, must serve an Investment Area(s) or Targeted Population(s). Generally, at least 60% of the applicant's activities must serve its Target Market.
- ✓ **Financing entity.** An applicant must be an entity whose predominant business activity is the provision of loans or equity

investments. Generally, at least 50% of the applicant's activities must be lending or investing.

- ✓ **Development Services.** An applicant, directly or through an affiliate, must provide development services in conjunction with loans or equity investments. Common examples of development services are homebuyer counselling, budgeting, resolving credit history issues and educational workshops.
- ✓ **Accountability.** An applicant must maintain accountability to residents of its investment area(s) or targeted population(s) through representation on its governing board or otherwise.
- ✓ **Non-Government entity.** An applicant must not be an agency or instrumentality of the Government.

The Task Force recommends that the criteria apply to a variety of legal forms, to include bodies regulated by the Financial Services Authority, other private sector businesses and non-profit organisations.

TAKE-UP

The Task Force believes that the Government should be ambitious in setting the maximum value for tax credits, but rigorous in its quality criteria for awarding them.

If the Government allocated tax credits worth £50m per annum to five year finance, this could attract over the next few years £1 billion in capital which would remain outstanding for five years or more.

As described in Chapter 1, total investment in CDFIs totals about £250m. Such a tax credit could therefore increase such investment five-fold.

£1 billion of additional investment is no more than one third of public-led programmes such as New Deal for Communities directed at under-invested communities.

The growth rate for the CDFI sector in the UK that this would imply is in line with the successful development of sectors such as Community Development Venture Capital and Community Loan Funds in the USA and credit unions and Micro-loan Funds in European countries such as Poland. The Task Force believes that it is important to set bold incentives in order to attract talented individuals into entrepreneurial businesses and CDFIs.

¹⁹ from CDFI Fund certification criteria, US Treasury Department.

2

RECOMMENDATION TWO: A COMMUNITY DEVELOPMENT VENTURE FUND

VENTURE CAPITAL IN THE UK

Venture capitalists invest in shares of private companies, often at a very early stage, providing the equity finance necessary to enable the business to grow rapidly. The venture capitalist has the long-term success of the company of which it becomes part owner as its key objective. The venture capitalist will also bring to the entrepreneur skills, experience and a network of contacts to enhance the development of the business. Once the business's success is established, the venture capitalist will exit from the investment through the sale of its shares either through a trade sale, a sale to management or through flotation on a stock market.

The UK venture capital industry proper is generally considered to have started in the 1980's. Over the past 20 years, its investment has increased from £111 million (1984) to £1.4 billion (1990) to £8 billion (1999), and it is now the second largest in the world after that of the USA.

Venture capital has proved a highly effective means of building companies. In the UK, over two million people are estimated to be employed by companies backed by venture capitalists. The number of people employed in venture-backed companies has increased faster than in the economy as a whole and faster than in large companies. Between 1994 and 1998, UK venture-backed companies' employment has increased by 24% p.a., against a national growth rate of 1.3% p.a.²⁰

In the latest BVCA survey on "The Economic Impact of Venture Capital in the UK" (1998), all venture backed companies in the survey felt that venture capital firms had made a major contribution beside the provision of money.

This contribution included acting as a sounding board for ideas, giving guidance on strategic matters and providing contacts and market information.

COMMUNITY DEVELOPMENT VENTURE CAPITAL IN THE UK

The term "community development venture capital" encompasses venture capital investment for both economic and social gain in businesses in under-invested communities. But it is different from investment in social and community enterprises that do not aim to generate sufficient revenue or profit.

There is a limited range of community development venture capital in the UK. What there is tends to focus on very small, local businesses, and is seldom focused around economic development and regeneration. Recent policy initiatives around regional venture capital funds are not focused on investment shortfalls in under-invested neighbourhoods. There is also a knowledge gap, with little research carried out on enterprise formation and capital requirements in under-invested communities.

Access to equity investment by businesses in under-invested communities can meet an important need, particularly if the business has significant expansion potential. If, in order to finance expansion, the business does not generate sufficient cash flow to service debt capital repayments and interest, then patient equity finance is critical.

It would seem feasible, in principle, to satisfy this need through the creation of a new community development venture capital sector.

COMMUNITY DEVELOPMENT VENTURE FUNDS

It is the recommendation of the Task Force that the successful principles of venture capital, namely: long term equity investment; business support to the entrepreneur and rapid growth potential of the company backed, should be applied to community investment through the creation of Community Development Venture Funds (CDV Funds).

CDV Funds will finance and support entrepreneurs in under-invested communities in the UK who would not otherwise have the opportunity to create and develop competitive enterprises, to the benefit not just of themselves, but of their employees and others in their community. Like limited partnerships used by the mainstream venture capital community they need to be transparent for tax purposes.

While the Task Force envisages significant commercial parallels in the structure of traditional venture capital funds and CDV Funds, the CDV Funds will have special requirements given the high risk nature of the

investments and lower anticipated returns relative to mainstream venture capital. The CDV Funds will need to form part of a system of community development finance, if they are to develop into a meaningful engine for development of under-invested communities. In order to attract significant funds in early years until returns are proven, the Task Force recommends ensuring that a range of incentives is available to encourage investment from different classes of investor, as follows:

- The CDV Fund would be partially owned by a charitable trust to which it will pledge gains achieved on the charitable trust's interest. Charitable donors will benefit from tax relief on their donations to the trust.

While this has been discussed in outline with the Charity Commission, we anticipate that more detailed discussions will be needed as this recommendation is taken forward.

- Other equity investors such as companies, banks, charities and individuals, will benefit from:
 - matched funding from the Government
 - a tax credit for each of five years, equal to 5% of the sum lent or invested, so long as it is outstanding for five years or more
 - capital gains on the CDV Fund's investments
- It would be desirable for individual investors in CDVFs to be in the same position as investors in a Venture Capital Trust. In order to achieve this, investors in CDV Funds should be exempted from capital gains tax.
- Lenders to the CDV Funds will benefit from the 5% tax relief and a senior position as regards security.

Since property redevelopment is a vital component in the regeneration of areas suffering from under-investment, it would be helpful to consider, in due course, whether the CDV Funds should also have the ability to invest up to one third of their capital in property assets and the balance in commercial businesses.

The Task Force welcomes the announcement by the Chancellor in June 2000 that the Government would be willing, in principle, to support this initiative by matching private sector funding. As a first step, the Task Force proposes that the Government should make available £100 million over the next few years to match £100 million from the private sector, for example by scaling up the Phoenix Fund.

The total sum of £200 million to be invested over a few years, compares with a total UK venture capital pool of more than £29 billion, with total annual UK venture capital investment of £6.2 billion and with £1.5 billion of annual investment in start-up, early stage and expansion capital.²¹

It is anticipated that the ongoing sources of capital for CDV funds will be:

- **philanthropic donations** from successful entrepreneurs, venture capitalists and others,
- **direct equity investment** by corporate investors, banks, insurance companies, local authority and other pension funds, major foundations and charities, successful entrepreneurs and venture capitalists,
- **loan capital** from banks and insurance companies.

The Task Force hopes that the first CDV Funds will stimulate and inspire the growth of a community development venture sector across the UK, covering a range of needs and focusing on all investment sizes.

As in the traditional venture capital model of equity investment, it is expected that the managers of the CDV Fund will be experienced business people and venture capitalists, able to select entrepreneurs with the potential to succeed, and to provide them with business support.

Thanks to the CITC and matching funding, we anticipate that the CDV Funds, as dedicated funds with a clear economic objective in under-invested communities, will be successful by investing in enterprises which mainstream venture capital funds would not normally regard as offering a sufficiently high return. By making significantly sized investments, these funds will be able to make a significant contribution in under-invested communities. It is important to recognise however, that as in mainstream venture capital, some of the companies backed will fail.

The British Venture Capital Association (BVCA) welcomes this initiative because it recognises that many of its successful members want to contribute to the community. It foresees contributions in terms of expertise as well as investment, particularly because the CDV Funds will need to be staffed by talented executives experienced in business and venture capital. The BVCA will facilitate

²¹ BVCA Report on Investment Activity 1999.

communication about the initiative and its potential benefits to BVCA members and will keep them informed following publication of this report, as the proposals are developed. The Task Force recognises that a range of practical issues will need to be addressed in order to implement the proposals set out above.

3

RECOMMENDATION THREE: DISCLOSURE BY BANKS

Banks need to play an essential role in under-invested communities, not only in providing finance for bankable businesses, but also in ensuring that viable businesses operating below market levels of financial acceptability can grow and become bankable. Using incentives such as the Community Investment Tax Credit described in this report, there is scope for a step change in the role of banks in under-invested communities – both directly, via subsidiaries with an explicit social mission to be CDFIs and also in partnership with independent CDFIs.

In order to enable this step change, a set of incentives is needed, but such incentives can only be monitored for effectiveness if satisfactory information is available about individual bank lending in under-invested communities. Information is also needed at the community level, in order to inform entrepreneurs and others. The Task Force believes that the provision of detailed information about individual bank lending in under-invested communities is essential to its vision of an effective community development finance system. It hopes that such disclosure will be made on a voluntary basis.

Figures from the USA support the view that the determined involvement of the banking industry is crucial to the process of turning around the UK's under-invested communities. There, mainstream banks' lending by Community Reinvestment Act-covered institutions to small businesses located in low-and moderate-income communities and for other community development averaged a total of \$50 billion annually from 1996-8²². Since the total capital of US CDFIs stood at only \$5.4 billion²³, including community development credit unions, it is clear that

banks continue to dwarf other players in community development finance.

This in no way undermines the importance of CDFIs, which are working below the level of acceptability of the banks. They have a crucial market-priming effect and often generate investment opportunities that allow banks to make loans that they would not otherwise consider.

However, these statistics do indicate that the community development finance sector alone cannot bring the volume of financing needed.

The Task Force was told that UK Banks are taking initiatives in under-invested communities – mainly through CDFIs. According to the British Bankers Association, banks have supported at least 70 local loan funds of various types. These are welcome moves. However, they are mostly inspired by philanthropy, public relations or marketing. Banks should seek not only to fulfil their philanthropic aims through grants and low or no-interest loans, but also to find profitable lines of business in these communities and so boost these communities' market-driven revival.

In the US, a series of fair lending laws, in particular the Community Reinvestment Act (CRA), has encouraged banks to find ways to address under-served markets on a profitable basis. The CRA operates at three levels: **disclosure** (allowing banks and local parties to identify market gaps); **ratings** (affecting the reputation of banks positively or negatively); and **sanctions** against worst performers.

Time and again, the Task Force has heard evidence that this legislation has been more responsible than any other factor for the increased flow of capital into under-invested communities.

In addition to the CRA, bank investment has been supported by public funds in the form of loan guarantees and tax credits and by funding for CDFIs, which act as partners for banks. National banks' investment in community development has increased eight-fold over the past six years.

In a survey of banks presented in a recent report on CRA by the Federal Reserve System²⁴, banks reported that their small business lending in CRA areas and community development is either profitable or marginally profitable. More than two-thirds of the banks that responded to the survey also reported that their CRA-related lending had led to new profitable opportunities.

²² "The Community Reinvestment Act After Financial Modernization: a Baseline Report", Department of the Treasury, 2000.

²³ "1999 Report on Socially Responsible Investing Trends in the United States", Social Investment Forum, November 1999.

²⁴ "The Performance and Profitability of CRA-Related Lending", Report by the Board of Governors of the Federal Reserve System, submitted to the Congress pursuant to section 713 of the Graham-Leach-Bliley Act of 1999, July 17, 2000.

²⁵ The Inner City 25 survey is being led by the New Economics Foundation, email: info@neweconomics.org or tel: 020 7404 7447.

The Task Force welcomes the Bank of England's commitment to monitor access to business finance in deprived areas. It believes, in addition, that there is a need to request much more detailed, individual disclosure by banks of their lending activities in these areas, to sponsor the creation of a rating system to reward excellent performance and to take a close and active role in illuminating each bank's performance in under-invested communities.

If voluntary disclosure is not made quickly, the Task Force believes that Government should require disclosure, in the manner of the 1977 US Community Reinvestment Act.

Such legislation should not be limited to banks, but should address other financial institutions providing services to individuals and small businesses, such as leasing, factoring and insurance companies.

AN INTEGRATED DATABASE ON MARKETS IN UNDER-INVESTED COMMUNITIES

Detailed information is needed on a regular basis on business activity and opportunities in under-invested communities. For example, in the US, the Housing and Urban Development Department (HUD) publishes annual reports on the state of America's cities and regions.

The Task Force welcomes the Chancellor's announcement in June that the Government would sponsor the Inner City 25²⁶, a survey of the fastest growing firms in deprived areas, and fund Regional Development Agencies to map the economic asset base and develop growth strategies in certain low-income, inner-city areas.

The Task Force recommends starting to build an integrated database. For example, it might make sense to focus the RDAs' City Growth Strategies and the IC25 on some of the same inner-city areas being monitored by the Bank of England. This would help to place the banks' business lending activities in the wider economic context of the communities in which they operate and highlight growing businesses in these areas. A similar focus is required on under-invested rural areas.



RECOMMENDATION FOUR: CHARITIES AND COMMUNITY DEVELOPMENT FINANCE

In the UK, some charitable foundations have done important, pioneering work in the area of social and community enterprise. In the USA, leading charitable foundations have played a key role as investors in community development finance. For example, in 1999, members of the National Community Capital Association reported that 22% of their loan capital came from foundations.²⁶

However, as Alex MacGillivray, Deputy Director of the New Economics Foundation, has said: *"Currently, it is charitable to help people who are poor. However, if you want to help them out of poverty through enterprise, the odds are stacked against you. So, charity ends up as helping the poor, so long as they stay poor. It is time to change the rules."*

Support for community development finance is a significant way in which many grant-making charitable foundations and major charities can advance their charitable objects.

The Task Force suggests three ways in which they can do this:

- programme-related investments via CDFIs
- grants and loan guarantees to CDFIs to enable them to build their organisational capacity and to meet running costs until they achieve sustainability
- investment in Community Development Venture Funds

CHARITY LAW

The Task Force believes that one obstacle to the development of charitable support for community development has been uncertainty as to when community development finance is charitable and when it is not. We have had helpful discussions with the Charity Commission on this issue.

The Charity Commission has told the Task Force that their recent

²⁶ Figure from the National Community Capital Association, 1999.

²⁷ Promotion of Urban and Rural Regeneration (RR2) and Charities for the Relief of Unemployment (RR3). Available from the Charity Commission at www.charity-commission.gov.uk or 01823 345427.

CHAPTER 2

guidance on regeneration and on unemployment²⁷ do not limit the pre-existing ability of charities to offer help to those who need it – which could include people in casual, insecure or low paid employment as well as the unemployed. Such charities include those with purposes of general community benefit or the relief of poverty.

Almost any charity can help other organisations, including smaller organisations, if that is a way of achieving its charitable purposes. This could include helping small businesses in regeneration areas to access financial support. Help could take the form of vocational training or retraining, or could involve the provision of grants, loans or equipment. This does not mean that all regeneration is charitable. A key consideration is the balance between the public and the private benefits flowing from the regeneration initiative. For the initiative to be charitable, any private benefits it generates must be outweighed by the wider public benefit.

Similarly, charities with more restrictive purposes, such as disability charities, can provide such support when this assists their beneficiaries.

The Charity Commission has told The Task Force that they would welcome more inquiries about charitable status from CDFIs concerned with local regeneration.

The Task Force urges the Charity Commission to publish formal guidance on Community Development Finance and the charitable status of CDFIs, taking into account the significant public benefits of their role in under-invested communities.

PROGRAMME-RELATED INVESTMENT

A programme-related investment is an activity that has the primary purpose of accomplishing charitable objectives.

The Charity Commission has confirmed to us that there are two ways in which charities can undertake programme-related investment as a way of achieving their objects. The first is simply for a charity to use some of its distributable income, or reserves, to make grants or loans as programme related investment.

The second is where a charity, whose objects are wide enough to allow this, uses some of its expendable endowment to make programme related investments. By definition this is not a decision that has been made on purely financial grounds: the charity is accepting that the financial returns are likely to be below market rates. The returns thus foregone are effectively an

amount spent on current beneficiaries. The trustees need to take this into account when considering how to allocate their resources between present and future beneficiaries.

In some cases, charities with similar objects may want to work together or through a suitable CDFI by pooling available funds so as to be able to support a wider range of programme-related investments than they could on their own. This could increase the total amount of money available while also helping charities develop a diversified portfolio of projects.

In future, the ability of charities to support programme-related investment will be encouraged further if the Charity Commission adopts the “total return” approach to charity investment on which it is currently consulting, as this would increase the scope for charities with a permanent endowment to have programme-related investments as a component of their investment strategy.

The Task Force recognises the concern of charitable trustees to be prudent in the way that they manage their assets and to avoid inappropriate risk. Positive and informed professional advice is essential to successful programme-related investment.

The Task Force strongly recommends that charitable foundations and major charities should undertake programme-related investment via an appropriate CDFI rather than by making such investments directly. This is because selecting and managing such investments requires specialist expertise. It is also wise to separate clearly the culture and expectations associated with grants from those of an investment relationship. We encourage charitable foundations and charities to press their professional investment consultants to provide the expertise needed to advise on the selection of appropriate CDFIs for programme-related investment and asset allocation to under-invested communities. The UK Social Investment Forum could provide a network for these specialists.

As with other investors, it is likely that programme related investment by charities and charitable foundations would increase significantly if suitable incentives existed. We believe that the most appropriate incentive would be to provide matching Government funding in CDFIs. If the Government funding took the form of a contribution to the equity of the CDFI, this would assist with the capitalisation of CDFIs. Such matched funding might be part of a central Government programme, but there are also opportunities for matched funding at the devolved administration, regional or local level. For example, their regeneration funding programmes might provide programme-related investment with matched funding on favourable terms.

5

RECOMMENDATION FIVE: A STRENGTHENED COMMUNITY DEVELOPMENT FINANCE INDUSTRY

A thriving community development finance industry – standing between finance providers and enterprises in under-invested communities is crucial to boosting enterprise and wealth creation. Banks and other mainstream players cannot reach these enterprises because of:

- lack of contacts within the community,
- perceived risk of enterprises in under-invested communities and social and community enterprises in general,
- the need for support and advice or training to help these enterprises survive and become creditworthy,
- transaction costs, which are often too high for a profit-maximising institution.

CDFIs are therefore important “pump-primers”, seeking out and supporting success, graduating enterprises to the mainstream financial sector and, in doing so, drawing communities out of exclusion.

The Community Investment Tax Credit proposed in this report will have a dramatic effect on the sector by considerably increasing private investment flows. If it is to make best use of these flows, the sector must improve its expertise and organisational capacity. This involves:

- bringing in new talent,
- organisational capacity building for the existing CDFI industry,
- building organisational capacity in support institutions like Government, banks and foundations.

Compared to the USA, the UK CDFI sector is relatively small, but ready for development. The UK has benefited from a number of impressive social entrepreneurs and entrepreneurial CDFIs. Now is the time to build on the achievements of these pioneers.

Today, there are few linkages between different types of CDFIs and, as a result, there is frequent reinvention of the wheel. In the USA,

likewise, initiatives sprang up separately over a period of many years since the 1960s.

Not until the 1980s and 1990s did people working in different kinds of US community-based financial institutions develop a sense of a movement or an industry. Among the factors that have assisted this process in the USA have been the following:

- strong trade associations
- effective wholesaling institutions
- championing by senior politicians, business people and others
- a fund for CDFIs at the national level to help them to scale up
- linkages with sources of research
- attraction of new talent to the sector

The Task Force has recommendations about each of these in the UK context.

TRADE ASSOCIATIONS

In the USA, after 25 years of development, each part of the community development finance sector now has at least one dedicated trade association. In the UK, there are no trade associations for the CDFIs described in this report although work is in progress to create one.

The Task Force recommends that CDFIs should move rapidly to ensure they establish one or more trade associations. The Government should support capacity-building, possibly by way of the Phoenix Fund.

The main roles of a trade association would be:

- networking for CDFIs
- strengthening and expanding a national industry of performance-driven CDFIs
- capacity building, through training, consulting, promotion of best-practice and benchmarking
- provision of information such as model CDFI business plans, lending guidelines and CDFI news
- representing the sector to Government, RDAs and others.

Existing CDFIs address a wide range of finance needs in relation to community development, but there are significant new opportunities as well, such as finance for housing repair and developing new forms of equity or quasi-equity for the fast

²⁸ Since NCCA is a selective membership association, it has loan quality requirements. The delinquency figures for NCCA membership are therefore better than for the overall Community development finance Industry in the USA.

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growing sector of social and community enterprise. The trade association could publicise these.

Over time, a trade association might choose to raise capital for on-lending to its members, but this should be the choice of the association not a move promoted by Government.

In the USA, perhaps the most directly comparable organisation is the National Community Capital Association. NCCA offers the following services: networking, conferences, a job bank, a CDFI locator that helps people find their nearest CDFI, sample loan applications, operations manuals, web-based training, and consultancy both to CDFIs and to potential investors in CDFIs.

NCCA also has a fund it uses to provide affordable loans to its members. Since 1990, the capital of its members has grown from \$72.5 million to \$1.16 billion. The average delinquency rate (over 90 days) of members of NCCA is 1.7% and their cumulative loss rate was 1.35% at the end of 1999.

In the UK CDFI sector, delinquency rates and loss rates are much higher than those achieved by NCCA's members²⁸. There is sometimes a tendency in the UK to make a direct link between delinquency and loss rates and social impact. A community development finance association would have a crucial role in promoting new techniques in social impact evaluation models.

WHOLESALE INTERMEDIARIES

As the UK community development finance industry expands, the Task Force believes there will be an important role for independent, non-Government wholesale intermediaries. The potential power of intermediaries is shown by the work of wholesale intermediaries in the USA such as the Local Initiatives Support Corporation (LISC), which has two main functions: to attract private capital to local regeneration activities and to develop the local capacity to use this money effectively. It acts as an intermediary between regeneration activists and the business sector and receives considerable direct grant support from the US Government as well as raising substantial loan finance. LISC now operates through 43 offices across the USA.

In the UK, the wholesale intermediary for the social housing sector, the Housing Finance Corporation has raised £1.15 billion in the banking and capital markets for investment in that sector. There are already a number of other wholesale intermediaries operating in

areas close to community development, but none focuses directly on the community development finance market.

Among UK CDFIs, none currently acts as a wholesaler, though some are taking steps in this direction. For example, as well as providing a wide range of investment services to charities, the Charities Aid Foundation runs Investors in Society, a CDFI which raises capital from a variety of sources and makes loans not only directly, but also in partnership with other CDFIs. The Local Investment Fund started as a national initiative, but is now developing into a network of regional funds, aiming to end up as a small central office providing many of the development, finance and information functions of an intermediary. In London and Scotland, new partnerships are being set up which combine direct financing with a deal brokering service to larger-scale funding sources, including banks.

Appropriate intermediaries would need to have the capacity:

- to raise private sector finance – this requires contacts and a reputation that private investors will trust
- to contribute to quality control among CDFIs – intermediaries would need clear principles for accrediting CDFIs and structuring loans or equity investments, as well as the capacity to monitor the success of the CDFIs financed
- to achieve management efficiency, in order to become self-sustaining.

The funding that intermediaries could facilitate might include the following:

- programme-related investment from charities and foundations
- private sector investments
- local and national Government funding

Wholesalers can be a powerful force in stimulating the growth of a sector. However, like a secondary market, the function of which is to make the primary market work better, intermediaries emerge when there is sufficient demand for their services. If the opportunity is there, then stronger intermediaries are likely to emerge. The tax credit, in combination with a fortified Phoenix Fund and strengthened involvement of charities, should provide the opportunity for wholesalers to emerge.

The Task Force believes that one or more wholesale intermediaries need to emerge in the next three years. The onus is upon the community development finance sector to drive this, but

Government should follow developments closely and, if appropriate, be prepared to play a supportive role. A specialist intermediary would enable the CDFI sector to access larger scale capital, including capital from quasi-public sources such as the European Investment Bank.

A CHAMPION FOR COMMUNITY DEVELOPMENT FINANCE

There is no easy, short term solution to building a thriving community development finance sector, given the range of cultural and other issues identified in evidence to the Task Force and outlined in Section 1.6 above. The Task Force believes that a high-level “champion” for community development finance could play an important role in facilitating this process.

The Task Force suggests the appointment within a Government department of a high ranking “champion” for community development finance with strong lines both to the Treasury and (if selected as the key Government agency) the Small Business Service. He or she would help to spread the message to those whose collaboration is needed: banks, large companies, venture capitalists, entrepreneurs, the voluntary and community sector and Government agencies.

GOVERNMENT FUNDING

We welcome the creation of the Phoenix Challenge Fund at the DTI and its recently announced funding increase. Like the CDFI Fund in the USA, this can play a crucial role in stimulating the growth of a robust community development finance sector. There will be a continued need for matching funding in order to scale up initiatives, experiment and achieve effective social returns.

We also think that Government should continue to review the US New Markets Initiative and consider holding an independent social audit of the Phoenix Fund after its second year of disbursements.

The Task Force believes that it would be helpful to provide greater clarity regarding the possibility of funding from the Phoenix Fund for CDFIs over the next three years. In addition, we suggest that the Phoenix Fund should:

- support initiatives that help build the CDFI industry, including wholesalers, associations and research initiatives
- provide financial assistance to CDFIs to enable them to give technical assistance to the enterprises in which they invest

NEW TALENT AND SKILLS

If the CDFI sector is going to grow in size, capacity and efficiency, it will need to draw on as many sources of talent as possible. In general terms, this means paying market or near-market rates for key staff, a point which needs to be kept in mind as CDFIs emerge and bid for accreditation.

Another way to build expertise is through the development of research institutes or departments of universities dedicated to community development. Harvard already runs a summer school on the financing of micro, small and medium enterprises (MSMEs).

We recommend that the emerging CDFI trade association(s) focus, as a priority, on the following initiatives to build CDFI organisational capacity:

- **Practical training for CDFIs.** The Small Business Service is currently sponsoring development of a training programme which, at a suitable point, could be taken on by the association(s).
- **Seek appropriate champions** for the sector from private, community, voluntary and Government sectors. For example, in the US, Robert Rubin, formerly Treasury Secretary, chairs LISC, a major CDFI. This greatly raises the profile of the sector.
- **Foster partnerships** between business schools, CDFIs and banks that seek to investigate the market in under-invested communities.
- **Foster secondment relationships** between banks and venture capitalists on the one hand and CDFIs on the other and also visits and secondments for UK CDFI practitioners to learn from international experience.
- **Encourage innovative relationships** between CDFIs on the one hand and private companies and the voluntary and community sector on the other which explore new ways to link money and talent – e.g. individual investors in a fund also volunteering their own time to help social and community entrepreneurs.
- **Design modules on community development finance** for business school and economic development programmes

Similarly, Government departments, such as the SBS, should explore the opportunities for building their own organisational capacity; for example, by international visits and secondments.

REGULATION

As the sector grows, it will need to improve its financial management and make significant strides in developing common reporting benchmarks for social and financial performance. Similarly, there will

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be a need to ensure that CDFIs adhere to relevant regulation, whether of the Financial Services Authority or EU State Aid restrictions, and these in turn take the needs of CDFIs into account.

There are arguments anyway for the overhaul of the law relating to mutuals and co-operatives, which will be raised again when the Co-operative Commission reports at the turn of the year. Over time, there may be the case for a Europe-wide approach that recognises the distinct status of CDFIs in relation to wider banking regulation. There may also be scope for a new form of investment fund, aimed at attracting long-term savings into community development finance activities.

It would be fatal to over-regulate the emerging community development finance sector, but we recommend that the Financial Services Authority develops expertise in this area, with a view to opening up discussion in due course.

AN EFFECTIVE LEGAL FORM FOR COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS

Currently, the most common legal forms for CDFIs are the company limited by guarantee and the Industrial and Provident Society (I&PS).

There is some debate as to whether these legal structures are suitable for large-scale CDFIs. For example, the company limited by guarantee and the I&PS both have limitations in their ability to accept significant equity investments. The maximum share capital that a non-I&PS investor may hold in an Industrial and Provident Society is £20,000. This means that larger investments must be made as debt rather than equity. Companies limited by guarantee do not have shareholders and therefore do not allow for investments of regular equity. While there are ways to circumvent these restrictions by using quasi-equity investments that have many of the features of equity but use debt as the basic instrument, such constraints may limit the growth of community development finance in the future.

It is crucial for development of CDFIs in general and of CDVFs in particular that an appropriate legal form is quickly defined. The Task Force has repeatedly heard of difficulties in this area. They appear reminiscent of the early years of the UK venture capital industry, before the Inland Revenue introduced a helpful change in regulations which made on-shore limited partnerships the standard vehicle for venture capital funds.

The Task Force recommends, as a priority, further research into the appropriate legal form for CDFIs.

2.3 CONCLUSION

The Task Force believes that these five recommendations, if adopted, will result in a dramatic increase in the quality and level of enterprise in under-invested communities and reverse the downward spiral of declining investment, jobs, wealth and asset values. As enterprising communities develop, asset values will appreciate and the local economy will improve. What we seek is an upward spiral where enterprising communities create the wealth that lies beyond welfare.

COMMUNITY DEVELOPMENT FINANCE SECTORS - COMPARING THE USA AND THE UK

US SYSTEM - KEY ELEMENTS	UK SYSTEM
<p>NATIONAL GOVERNMENT</p> <ul style="list-style-type: none"> ● Community Reinvestment Act – banks are required to serve poor neighbourhoods while still making prudent lending decisions; information must be disclosed and banks are rated on performance; ratings are taken into account in regulators’ decisions on M&A. ● CDFI Fund – matched funding in form of debt, equity and grants. Bank Enterprise Awards – rewards banks for improvements in reaching low income neighbourhoods. ● Tax credits – for low income housing and planned for community development finance. ● Small Business Administration – guarantee programmes – for small businesses in general and for micro loans. 	<p>No direct UK equivalent, but the Bank of England now monitors bank lending in under-invested communities.</p> <p>Phoenix Fund – started in 1999 at the DTI. So far on a smaller scale although trebled in size in 2000. No scheme at present to reward banks for innovation in under-invested communities.</p> <p>No UK equivalent, although a significant and active market exists in private finance for social housing.</p> <p>Small Firms Loan Guarantee Scheme – not specially aimed at under-invested communities.</p>
<p>CHARITABLE FOUNDATIONS</p> <ul style="list-style-type: none"> ● A wide range of charitable foundations and a strong tradition of personal philanthropy and corporate giving. Major foundations such as Ford, Rockefeller and McArthur have played a leading role in community development finance through grants and programme-related investment. 	<p>Fewer large-scale foundations in the UK. Some, such as Esmee Fairbairn, have started to support community development finance. The Joseph Rowntree Foundation has funded research on the sector and has played a lead role in promoting investment in social housing.</p>
<p>RESEARCH/CAPACITY BUILDING</p> <ul style="list-style-type: none"> ● Many players: e.g. Woodstock Institute, Aspen Institute, Corporation for Enterprise Development. 	<p>Few players: e.g. New Economics Foundation, Community Finance Solutions.</p>
<p>POLICY ADVOCATES/COALITIONS</p> <ul style="list-style-type: none"> ● The Coalition of Community Development Financial Institutions, Corporation for Enterprise Development, the Microenterprise Coalition. 	<p>UK Social Investment Forum currently plays this role to some degree. The new CDFI association may become the lead advocate in future.</p>
<p>INTERMEDIARIES</p> <ul style="list-style-type: none"> ● Associations (eg. National Community Capital Association (NCCA), Association for Enterprise Opportunity (AEO), National Federation of Community Development Credit Unions, Community Development Venture Capital Alliance (CDVCA)) ● Wholesalers and support organisations (eg. Local Initiatives Support Corporation (LISC), Housing Reinvestment Corporation, Community Preservation Corporation, Neighbourhood Housing Services) 	<p>UK intermediaries include the Housing Finance Corporation (HFC) and the Association of British Credit Unions Ltd (ABCUL). A CDFI trade association, the Rebuilding Society Network, is currently being started.</p>
<p>CDFIs²⁹</p> <ul style="list-style-type: none"> ● Community Development Banks 25 exist with assets of about £2 billion. Fully licensed, for-profit commercial banks with a community development mission. ● Community Loan Funds 600 exist. Most focus on asset-based community development and housing loans or small business lending in low income neighbourhoods. ● Micro-loan Funds At least 341 microenterprise programmes and 283 microenterprise agencies (lending and/or Technical Assistance). The total capitalisation of Community Loan and Micro Loan Funds is £1.195 billion. ● Community Development Venture Capital Funds Approximately 45 exist, with assets of about £207 million. Sector growing as supply of loans to low income neighbourhoods has increased and now there is a need for patient equity. ● Community Development Credit Unions³⁰ Very large credit union movement, covering much of the population nationwide. 170 credit unions are focused specifically on community development. 	<p>Do not exist. UK has social banks but these do not have a primary focus on under-invested communities. As Community Loan Funds reach a sufficient scale, many are likely to seek the benefits of banking status.</p> <p>Many initiated by local authorities have failed or fallen into disuse. Other independent initiatives such as Aston Reinvestment Trust and Industrial Common Ownership Finance (ICOF) are succeeding and have potential to grow. Housing Associations are taking an increasing interest in community development finance.</p> <p>The Prince’s Trust has reached national scale but has strict age-restrictions. The recently launched Street UK aims to reach national scale. Small but growing number of other programmes exist.</p> <p>A number of equity gap funds have emerged at regional and national level eg. the GLE - Baring English Growth Fund. An estimated £45 million is targeted at under-invested communities.³¹</p> <p>Overall credit union movement still small but growing – total assets £240 million. A few emerging community development credit unions, such as in Birmingham. Few credit unions offer enterprise lending.</p>

²⁹ US data, Numbers of institutions from Woodstock Institute data, 2000. Assets (except CDVC Funds) from “1999 Report on Socially Responsible Investing Trends in the United States”, Social Investment Forum, November 1999. CDVC Fund assets from research by Julia Sass Rubin of Harvard University for Community Development Venture Capital Alliance (forthcoming).

³⁰ Credit Unions are not addressed further in this report due to other credit union policy initiatives in progress.

³¹ New Economics Foundation estimate, 2000.

THE SOCIAL INVESTMENT TASK FORCE

CHAIR: RONALD COHEN

Ronald Cohen jointly founded Apax Partners, one of the leading international private equity groups, in 1972. He is the Chairman of Apax Partners & Co Ltd. He is founder and past chairman of the British Venture Capital Association and a Founder Director of the European Venture Capital Association and the Quoted Companies Alliance (formerly Cisco) and a founder of EASDAQ, the European stock market of which he is Vice Chairman. He is chairman of the DTI "Tech Stars" Steering Committee and was a member of the DTI UK Competitiveness Committee. He has served as a member of the London Stock Exchange Working Party on Smaller Companies; CBI Wider Share Ownership Committee; the London Business School Foundation for Entrepreneurial Management's Advisory Council and the Executive Committee of The Centre for Economic Policy Research.

DAVID CARRINGTON

David Carrington has been Chief Executive, PPP Healthcare Medical Trust since 1998. Previously he was Director, the Baring Foundation (1992-1998); Director, Housing Associations Charitable Trust (HACT) (1988-1992); Housing Services Manager, Stonham Housing Association (1984-1988). He serves as Chair, Charities Aid Foundation Grants Council; Trustee, The Media Trust and The National Youth Orchestra of Great Britain; Governor, South Bank University; Member, Executive Committee, Association of Charitable Foundations (ACF); and Director, The Community Channel Ltd.

IAN HARGREAVES

Ian Hargreaves is a leading journalist and media academic. Since 1998, he has combined his position as Director of the Centre for Journalism Studies at Cardiff University with a wide range of writing, broadcasting and consultancy. He also chairs the board of trustees of the think tank Demos. He was Editor of the New Statesman (1996-1998); Editor of the Independent (1994-1996); Deputy Editor of the Financial Times (1990-1994); Director of News and Current Affairs at the BBC (1987-1990).

PHILIP HULME

Philip Hulme started Computacenter in 1981. Today, the company is listed on the London Stock Exchange and employs over 5000 staff. He also co-founded Computasoft and Biomni, respectively banking software and e-commerce businesses. In 1998, he set up the Hadley Trust. Previously, he worked from 1973 for the Boston Consulting Group in the United States, South Africa and the UK. He was appointed to head their London office in 1980.

GERALDINE PEACOCK

Geraldine Peacock is the Chief Executive of Guide Dogs for the Blind. She was the first paid Chief Executive of the National Autistic Society (1988-1997). Prior to that, she was Deputy Director of the London Boroughs Training Committee. She is a Trustee of the National Council of Voluntary Organisations, a member of the Council of The Industrial Society and a member of the Executive Committee of the Association of Chief Executives of Voluntary Organisations (ACEVO). She is also immediate past chair of ACEVO.

JOAN SHAPIRO

Joan Shapiro was formerly Executive Vice President, South Shore Bank, Chicago. She has 20 years experience building South Shore Bank into the leading community development bank in the USA. Her work pioneered the concept of community economic development through banking. She now consults with businesses and organisations on development strategies, community investment and corporate responsibility.

TOM SINGH

Tom Singh is founder and director of New Look plc – one of the UK's largest women's fashion retailers. He established the business in 1969, grew it to a chain of 25 shops by 1986 and successfully floated it on the London Stock Exchange in June 1998. By 2000, the company was trading from over 500 stores with a turnover of £418 million.

EVIDENCE TO THE SOCIAL INVESTMENT TASK FORCE

The Social Investment Task Force is grateful to all those who contributed to their work. These include:

Organisation	Name
Aspire	Paul Harrod
Aston Reinvestment Trust	Sir Adrian Cadbury, Bert Nicholson, Steve Walker, Stuart Egginton
Bank of Scotland	Susan Rice
Bank of England	Victoria Cleland
Barclays Bank	Rachel Barber
Birmingham Enterprise Fund	Kevin Caley, Sarabjeet Soar
Boston Community Capital	Elyse Cherry
British Bankers Association	Andy Brennon, Mike Young
British Venture Capital Association	David Thorpe, Jennifer English, John Mackie
Bromley by Bow Centre	Andrew Mawson and colleagues
Business in the Community	Paul Rowson
Charities Aid Foundation	Michael Brophy, Malcolm Hayday
Charity Commission	John Stoker, Michael Carpenter, Richard Carter
Citylife	Martin Clark
Coin Street Community Builders	Iain Tuckett and colleagues
Community Action Network	Andrew Mawson and colleagues
Community Links	David Robinson, David Wansborough and colleagues
Developing Strathclyde Ltd	David Brown
Development Trusts Association	George Nicholson
DETR	William Arnold
DfEE	Gordon Miles
ENTA	Kevin Hayes and colleagues
Eureka Inspirational Design Ltd	Chris Lee and colleagues
Greater Easterhouse Development Company	Stuart Miller
Harvard Business School, MBA Class	Liam Byrne
The Housing Finance Corporation	Barbara Ainger
Industrial Common Ownership Finance (ICOF)	Andrew Hibbert
Initiative for a Competitive Inner City	Claire Kaplan
International Association of Investors in the Social Economy (INAISE)	Danyal Sattar and colleagues

InterWork Enterprises Ltd	Terence Rosslyn Smith
KPM Turnkey	Julian Morgan and colleagues
Local Initiatives Support Corporation (LISC)	Robert E Rubin, Michael Rubinger, Rick Gentry
Local Investment Fund	Roger Brocklehurst, Bill Hulton
London Business Growth Fund	Bob Warren
Merseyside Special Investment Fund	Neil Kemsley
Music entrepreneur	Johnny Walker
National Economic Council, White House	Cliff Kellogg
National Community Capital Association	Mark Pinsky
National Housing Federation	James Tickell
NatWest / Royal Bank of Scotland Group	Andrew Robinson, Peter Hughes
NorthWest Development Agency	Baron Isherwood
Patricof & Co	Patricia Cloherty
Poptel	Malcolm Corbett and colleagues
Prime	Julia Evans
Primesite	Steve Manley and colleagues
Prince's Trust	John Attree
Public Management Foundation	Jane Steele
Questions Publishing Co Ltd	Howard Sharron and colleagues
Shorebank Advisory Services	Michele Giddens
Shorebank Corporation (formerly)	Joan Shapiro
Small Business Service	David Irwin
Social Enterprise London	Jonathan Bland
Social Investment Scotland	Anne-Michelle Ketteridge
South East England Development Agency (SEEDA)	David Shannon
Street UK	Rosalind Copisarow
TFF Study Group	Frank Thomas
Triodos Bank	Susan Jenkins
Whitehaven Youth Trust	Jim Baker
Women's Employment, Enterprise & Training Unit (WEETU)	Erika Watson
Woodstock Institute	Malcolm Bush
Wrigleys	Julia Pellow

Information about many of these organisations is given on the [Enterprising Communities](http://www.enterprising-communities.org.uk) web site at:

www.enterprising-communities.org.uk

This evidence was in addition to the research supplied by the Development Trusts Association and the New Economics Foundation, which is also accessible from the website.

GLOSSARY

Charitable Foundation

Charitable foundation is used in this report to describe charitable grant-giving trusts and foundations. These usually have a permanent or expendable endowment, and their primary purpose is to fund rather than directly undertake charitable activities.

Charitable Purpose

Charitable purposes are characterised by a desire to benefit others for the common good; this is known as public benefit. To be a charity, the purposes of an organisation must be exclusively charitable. There is no Act of Parliament which sets out all the purposes which the law recognises as charitable. Instead, the legal definitions of charitable purposes are developed by the courts and the Charity Commission. Charitable purpose comes under four broad headings which can be grouped as the relief of financial hardship, the advancement of education, the advancement of religion and other charitable purposes for the benefit of the community.

The Charity Commission keeps under review what qualifies as charitable purpose, has recently issued guidance on the promotion of urban and rural regeneration and on the relief of unemployment and is currently considering its view of community capacity building activities.

Community

A group of people sharing common characteristics. A community may be defined geographically – for example, by residence in the same neighbourhood – or by shared characteristics such as disability or ethnicity.

Community Development Corporation (CDC)

The term “Community Development Corporation” is used in the USA to refer to locally controlled non-profit organisations that focus on community development, primarily through development of housing and commercial property.

Community Development Finance

The provision of financial services, such as loans and equity, by CDFIs for enterprise in under-invested communities. Such enterprises may be purely for-profit or may be social or community enterprises.

Community Development Financial Institution (CDFI)

The term “Community Development Financial Institution” is used in this report to describe financial services providers (including community development banks, community loan funds and community development venture funds) whose mission specifically requires them

to achieve social objectives. The CDFIs (sometimes in the UK called CFIs – community finance initiatives) considered in this report focus specifically on financial services for businesses and social economy organisations rather than for personal use. They may provide equity, quasi-equity or debt services. While some UK CDFIs are regulated as banks or building societies, most CDFIs in the UK do not have deposit-taking status. The legal forms most often used are the Industrial and Provident Society (I&PS) and, in association with charitable status, the company limited by guarantee. The term “Community Development Financial Institution” is used in the USA to refer both to institutions specifically certified as CDFIs by the US Treasury and, more broadly, to non traditional lenders. To be eligible as a CDFI, the institution's mission must be focused on community development, i.e. it must serve either low- and moderate-income people and/or low- and moderate-income communities. The primary activity of a CDFI is lending or investing in community revitalisation. Unlike many other community development initiatives, CDFIs are market-driven rather than funder-driven.

Community Development Venture Capital Fund

A venture capital fund, run for profit, targeted at under-invested communities.

Community Loan Fund

A community loan fund is a CDFI that provides loans.

Community Reinvestment Act

American legislation introduced initially in 1977. One of a series of fair lending laws which created an affirmative obligation for banks to address under-served markets by a mixture of disclosure requirements, ratings and penalties for non-engagement.

Expendable Endowment

Resources held by a charitable foundation that it may, at its discretion, either spend on current beneficiaries or invest for the benefit of future beneficiaries.

Equity

A share of the ownership of a business, hence the term “shares” to describe units of equity. These ownership rights give, in particular, a right to a certain proportion of:

- the amount of money remaining after paying off debts and any other liabilities when the business is sold or wound up
- the profits of the business (delivered either via a direct payment or by an increase in the value of the business as a result of the reinvestment of profits)
- the governance of the business i.e. the ability to set and supervise its overall business strategy and direction

Holders of equity own a share of the success or failure of the business. A key issue is how their ownership rights can eventually be converted into money, i.e. their “exit route”.

Grant

A transfer of resources to a named organisation or individual to be spent to achieve an agreed purpose under agreed conditions. A grant is returnable only if these conditions are not met.

Investment

A transfer of resources under agreed terms and conditions in which the transferor retains the right either to the return of the resources or to a benefit such as ownership rights in return for the transfer.

Loan

A loan is a transfer of money in return for a promise of its return at a future time usually with an additional payment for its use.

Microenterprise

A very small business, usually defined as "a business with fewer than 10 staff". Sometimes defined as "a business with fewer than 5 staff". 89% of all UK businesses have fewer than 5 employees.

Microfinance

Small loans; savings facilities with no (or a very low) minimum deposit; and other financial services like insurance, money transfer or bill payment designed for people on low incomes.

Micro-loan Fund

A fund providing small loans, ie. a particular form of micro-finance. A micro-loan fund is a specialised form of financial service based on distinct products specially designed to service micro-enterprises and is not merely the occasional provision of a very small loan.

Permanent Endowment

Resources held by a charitable foundation that it is required to invest for the benefit of future beneficiaries. Only the income generated by the investment can be spent on current beneficiaries.

Phoenix Fund

A three year Government grant programme announced in November 1999 and run by the Department for Trade and Industry's Small Business Service. The fund is in several parts, one of which is the Community Finance Initiative Challenge Fund.

Programme Related Investment

A programme-related investment is an activity that has the primary purpose of accomplishing charitable objectives by providing equity or loans.

Quasi-equity

An investment that combines the characteristics of equity and loans. In general, a quasi-equity investment is a loan in which the final payment is linked to the financial success of the business.

Social Bank / Community Development Bank

A for-profit CDFI that operates as a regulated commercial bank, but with

a specific social mission. In the US, community development banks provide banking services specifically to low-income communities. In the UK, social banks tend to have a broader social mission, for example lending only to projects of social or environmental value.

Social and Community Enterprises

The term "social and community enterprise" is used in this report to describe a business that trades in the market in order to fulfil social aims. Social and community enterprises bring people and communities together for economic development and social gain. They have three common characteristics – (a) they seek to be viable trading concerns (b) they have explicit social aims and are accountable to their members and the wider community for their social, environmental and economic impact and (c) they are autonomous organisations, often with governance and ownership structures based on participation by stakeholder groups or by trustees and with profits distributed as profit sharing to stakeholders or used for the benefit of the community. The Task Force takes the view that not all social and community enterprises need to have social ownership. Some are structured as traditional enterprises while still serving a social purpose and placing great emphasis on their accountability to the communities they serve.

Social or Community Entrepreneur

A person who uses conventional business discipline, management tools and entrepreneurial skills to achieve a social purpose.

Social Investment

Financial transactions intended both to achieve social objectives and deliver financial returns to investors.

Venture Capital

Venture capital provides long-term, committed, risk-sharing equity capital together with experience, contacts and advice in order to help unquoted companies to grow. It seeks to increase a business's value without taking day-to-day management control. Venture capital shares risk with the other owners of the business. Its financial return is dependent on the business's growth and profitability and ultimately on the increase in its value.

Venture Capital Trust

An existing tax-advantageous financial investment vehicle for investing in unquoted and smaller companies.

Wholesale Intermediary

A financial services provider that only makes loans to or equity investments in other financial services providers. In general, a wholesale intermediary will receive large investments and use them to make smaller investments in financial services providers, which in turn directly serve enterprises in other sectors.

Under-Invested Community

A community that receives less investment than it needs in order to be economically and socially viable.

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