

Response by the Social Enterprise Coalition to the Office of the Third Sector's Re-tender of the Futurebuilders Fund: discussion paper

Contact: Kieran Larkin

Telephone: 020 7793 2325

Email: kieran.larkin@socialenterprise.org.uk

Response to the Re-tender of the Futurebuilders Fund

1. The Social Enterprise Coalition (“the Coalition”) welcomes the opportunity to respond to the Office of the Third Sector’s re-tender of the Futurebuilders Fund. The Coalition has previously submitted a response to the two questions highlighted as time sensitive. This response addresses the remainder of the questions raised in the discussion paper.
2. The Coalition was established in 2002 as the national body for social enterprise. The Coalition represents a wide range of social enterprises, umbrella bodies and networks, with a combined membership reaching over 10,500 social enterprises. These include co-operatives and mutuals, development trusts, housing associations, leisure and football supporters’ trusts and Social Firms. Social enterprises are businesses with primarily social or environmental objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners. In preparing this response the Coalition has consulted with our members.
3. The Coalition recognises that the Futurebuilders Fund has already made substantial investments to social enterprises and other third sector organisations. The Coalition welcomes indications that the next phase of the Fund will place a greater emphasis on investment to social enterprise, which, given their business focus are often particularly well placed to take on the combination of grant and debt finance that Futurebuilders provides.

The OTS is interested in exploring whether other definitions of public services could be more appropriate in the future. Is the 51% rule appropriate? If not, what other definition of public services could be used in its place?

4. The Coalition believes that 51% rule is inappropriate and restrictive to many social enterprises delivering public services. Organisations that are starting up and those that have a diverse income base, using the trading of goods to cross-subsidise the provision of other services, are unlikely to receive 51% of their projects income from public service funding. The third sector is still a growing provider of public services, particularly in certain sectors such as health and it is important that the Fund embraces new approaches across the whole range of markets.
5. The Coalition recommends that a new definition of public services should be sought that encompasses the full range of organisations operating within this environment. The definition needs to be inclusive of organisations that generate income from other markets. We recommend that the definition focuses on outputs rather than sources of income.

Comments are sought on the visibility of the Fund within the Third Sector and on how the OTS would know that the Fund manager was achieving the goal of becoming a third sector champion. Comments are also invited on how the Fund manager might best work with public services commissioners.

6. The Fund has a strong reputation within parts of the third sector; however it is not as visible within the social enterprise movement. This is partly due to the way in which that Fund has operated and language that it uses, which has resonated with the more traditional voluntary and community organisations. The Fund manager should work to create a common and easier to understand language.
7. The Coalition is pleased that the Office of the Third Sector (OTS) has recognised the Fund’s limitations in this respect and is making greater social enterprise involvement one of its key commitments in the Fund’s next phase. The Fund should engage with social enterprise networks to achieve this.

8. The Coalition would recommend increasing Futurebuilders engagement beyond the third sector. The Futurebuilders brand is not widely identified within local authorities and primary care trusts (PCTs), by mainstream and specialist financial lenders and within business support organisations. The Coalition considers these areas, particularly local authorities and PCTs, as an important place for the Fund manager to improve Futurebuilders' visibility in the next phase.
9. In the future the Fund manager should look to exercise its influence in demanding change in the local authority commissioning agenda. Given that in many areas it is supplying a source of finance which is aiding the delivery of services, it should be able to apply pressure to shape markets for the benefit of the third sector.
10. As the Futurebuilders England's '*Second Learning Report*'¹ identified, the commissioning environment remains the greatest challenge to the success of the Fund. The 'engaged investment' model often provides commissioners with an assurance of an organisations reliable business approach. This may aid the contracting relationship, and increase an organisations prospect of success in the tendering process. We propose the Fund manager engage with commissioners to provide them with guidance and improve their understanding of social enterprise. Additionally greater effort should be made to capture learning from social enterprises who work with the public sector and to develop learning tools for commissioners. The Fund manager should seek to be involved in the Office of the Third Sector's programme to train 2000 commissioners. However, this should not duplicate existing activity and resources. It is essential that an integrated approach is adopted.

The OTS seeks views on key factors or indicators that would show that the Fund manager was both reaching previously excluded organisations and to enable them to move as quickly as possible to a stage where they can accept money from the Fund.

11. The discussion paper identifies excluded organisations as those that are 'unable or unwilling to seek outside funding'. The Coalition questions this limited definition given the changing nature of the Fund. Following the removal of the restriction on areas of service delivery and potential redefinition of the public service rule, we would propose that the definition of excluded organisations includes those organisations previously ineligible.
12. Many social enterprises have the capacity to take on loan finance but have been previously excluded by the Fund because of the factors outlined above. Social enterprises that were seen as being successful businesses have been ineligible for support, which has been counter productive to the sustainable goals of the Fund. Reaching these organisations requires the use of infrastructure support organisations, and the appropriate social enterprise networks. More work needs to be done to ensure that specialist social enterprise support agencies and Business Links are aware and refer social enterprises to the Fund. The Coalition would also recommend that the Fund manager works with high street banks, to ensure that if social enterprises are rejected when trying to access finance at these sources, they can be referred to Futurebuilders.
13. For those organisations that have been excluded due to cultural aversions to debt, it is important that support agencies are used that help develop their investment readiness. The Fund should also look to confront their doubts by profiling the success stories of the previous phase.
14. The Coalition commends the Fund manager's success in reducing the current application time to an average of five months, but suggests that this should be improved this further. A number of the social enterprises we consulted reported application periods of 12-18 months. Social

¹ Is Futurebuilders Working? Futurebuilders England's second learning report, Futurebuilders England, July 2007

enterprises often need to be more responsive to take advantage of market opportunities much like mainstream business, and need to access finance quickly and efficiently. The length and complexity of the application process also excludes organisations that are unwilling to engage in such a bureaucratic procedure.

15. It has been recommended that the Fund manager implements a more realistic early assessment procedure, to exclude organisations that are unlikely to be successful. Many organisations are taking part in the extended application process that we believe could be rejected at an earlier stage. This would save the both the organisations and the Fund manager time and resources.

The OTS wishes to ensure that applications are assessed fairly and transparently so that Funding is awarded to areas where it will have the greatest impact. Comments are requested on what the OTS should be looking for in a potential Fund manager to ensure that this occurs. In addition, it seeks views on the key indicators it should look at to encourage the Fund manager to achieve the government's policy requirements in this area.

16. The management of the Fund requires skills, combining knowledge of public services and the third sector, with experience in evaluating investments and offering business support services. It is important that the specification requires the Fund manager to have these skills.
17. The Coalition is wary of stipulating targets if these detract from focussing on making good investments. However, we would recommend that the fund should reduce its investment in assets. Whilst the Coalition recognises the benefit of transferring an asset to a community's control, asset ownership is not, in isolation a solution to creating innovative community led services. The Fund should focus on building the capacity of organisations to deliver public services, and their willingness and investment readiness to take on other forms of finance such as commercial loans.

How can the OTS encourage the new Fund manager to engage appropriately with investees following the decision to invest?

18. The current 'engaged investor' model has been a successful and worthwhile strategy. It is important that the Fund manager continues to fulfil this role. The selected candidate should have a strong track record of working with organisations in the third sector.
19. In some cases there is a need for the Fund manager to provide ongoing support after an investment is made. The Fund manager could also provide guidance and support for organisations, helping to implement a framework to measure and evaluate their success. Implementation of a standard form of social accounting or social return on investment would also provide the Fund manager with data by which to evaluate investments. The OTS should, however, consider that the engaged investor approach requires significant administration costs.

The OTS considers it is essential that there are simple, strong measures and systems in place to evaluate the success of individual funding awards. Comments are sought on the key factors that should underlie any such measures and how information surrounding this is best gathered.

20. The purpose of the Fund is to bring about an improvement in the quality of public services. Therefore the primary measure should be the ability of the Fund to deliver on this social output. Whilst it is vital that the Fund manager carries out a fair and transparent evaluation process, an excessive number of targets are likely to distort the funding picture, or encourage perverse investments.

21. A simple measurement for awards would be the number and value of contracts won by organisations. However this does not measure the success of the service. To achieve this aim the Coalition suggests that the Fund manager should look to incorporate and support organisations to introduce a standard form of social accounting, to assist in measuring their social impact.

How will the OTS know that the 'hard to reach' organisations are aware of the Fund and are participating in the funding process? How can those organisations be encouraged to overcome any reservations they may have about borrowing money and managing risk?

22. The Fund should look to link with existing support networks that target 'hard to reach' communities. The Fund manager may look at providing a set of workshops focusing on the benefits of risk, aimed at assisting these organisations in the process of deciding whether taking on a loan would be beneficial. These workshops should be regional and use the appropriate support networks to provide access and visibility to 'hard to reach' communities.

What information should be sought and what factors should be considered to ensure that service users see improvements in the public services they receive as a result of the Fund? How can these improvements be measured?

23. The Fund is designed to improve the delivery of public services by expanding the number of third sector providers. Measuring improvements in services, which could use mechanisms such as user satisfaction ratings, should be carried out by the third sector organisations as they often already have a direct relationship with the service users and have a better history of representing their user's needs. The Fund manager's role should be in assisting organisations with the implementation of a framework to collect and monitor this information.

How will the Fund manager and OTS know that it is assisting in matching the capabilities of third sector organisations with the needs of public service commissioners and in helping drive change within the commissioning environment?

24. It is important that the services third sector organisations applying to the Fund are looking to provide are likely to meet demand in the marketplace. The Fund should not invest in unrealistic proposals as this could undermine the Fund's reputation. The Fund manager should continue to consult with commissioners during its evaluation of a proposal to assess whether a service is viable.
25. Futurebuilders may also look to work within the remit of Local Area Agreements to ensure there is a necessary demand in the local priorities, for the services an organisation is looking to provide. Futurebuilders also has an important role to play in educating organisations in understanding the need to tailor their service to locally defined strategies.
26. However, it is also important that unidentified unmet need is also recognised. Social enterprises can often work with commissioners to develop new services that tackle problems that are not currently being contracted for; this can be a vital pre-requisite for winning contracts. It may be helpful for the Fund manager to produce guidance and examples where commissioners have recognised the need for such new services. The Fund manager also needs to recognise that commissioning a service can be a lengthy process and financial plans may need to be created that can support an organisation between the creation of their business plan and winning a contract.
27. To encourage innovative public services, there needs to be an acceptance that some of the organisations will fail, and as such the investments will not be returned. The Fund must look to

embrace an element of risk itself if it intends to champion a change in attitude within the third sector. A cautious investment institution is unlikely to encourage the necessary change in opinion to loan finance from third sector organisations.

What options should be open to the Fund manager in seeking to increase the available pool of funding and what avenues should be closed? How will the OTS and the Fund manager know that it has forged good relationships with other funders and that it has not had a negative effect on the nature of the funding 'marketplace'?

28. The Fund manager should seek to work with all existing funders, to offer a mixed finance package where appropriate. This not only increases value of the Fund, but as it promotes new relationships and will encourage third sector organisations to engage and build relationships with a new set of finance providers.
29. Providing a mixed finance package with for example, high street banks, social lenders and Community Development Finance Institutions (CDFIs), would allow the loan to be offered at a lower average rate of interest. The Fund's loans currently incur a higher rate of interest due to the increased risk and need for an engaged approach. A mixed finance package could be used to reduce some of this cost.
30. The Fund manager should consider all existing finance providers in the social finance market place when referring on an organisation that has been turned down for a Futurebuilders loan. Currently the Fund has limited itself to the partners involved in the Funds management. This approach limits the choice of organisations trying to access finance.
31. In forming a healthy relationship with the social lenders market it is important that the Fund manager clearly defines the role that it expects to play. Currently both borrowers and lenders are unsure of the Fund's position in the market, and whether it exists exclusively to lend to those organisations that could not access finance from other sources.
32. Consideration should be given to the possibility of the Fund manager working with other organisations to look at developing new financial products beyond its current provision. Social enterprises looking to access finance would be interested in a greater variety of financial products. The Fund's current focus takes a narrow view of investment, offering only development grants and loans. This should be expanded in the next phase.
33. The Coalition also proposes that the Fund manager should make greater use of its current powers to pass on loans to other providers, when organisations are financially ready. This would allow the Fund to reinvest its capital pool in other organisations.

Should the Fund continue to be overseen by an independent advisory panel? If so, what should be the remit of that panel? Should it be restricted to the Fund or should it have a wider brief?

34. The Coalition believes that the Fund should continue to be overseen by an advisory panel to ensure it remains representative of the best interests of the sector and that this body has the necessary authority and experience. As set out in the governments '*Future Role of the Third Sector in Economic and Social Regeneration*²', under point 2.39, the Coalition understands the Government has decided to create a single streamlined advisory body to oversee all third sector activity.

² The future role of the third sector in social and economic regeneration: final report, HM Treasury and Cabinet Office, July 2007.

What models should the government consider for the legal and financial management of the Fund? How can the government best enhance the independence of the Fund manager while ensuring that public funds are treated appropriately?

35. Given that these are public funds it is important that there is sufficient accountability and transparency in the Fund's decision making process and investment selections. A strong track record in conforming to these areas is essential to the successful delivery of the Fund.
36. The Coalition would suggest however, that the benefit for the public is in the provision of better public services. It is important that the Fund's purpose is defined by the third sectors needs and the aim of delivering better public services, rather than reacting to short term political pressures. The Coalition would like to see the OTS use a model that allows the Fund manager sufficient independence to achieve this goal.
37. It is also important that the returns on the Fund, which will increase as a number of the loans start to mature, should be recycled within the investment pool of the Fund rather than for wider OTS activities.

How can the government ensure that the Fund manager adopts an appropriately transparent approach to its operations? What reporting arrangements should the government have in place to ensure that the Fund's objectives are being met?

38. The Fund manager should continue to report to the OTS on its specified operations. All funding assessments should be accessible when requested to ensure there is a transparent process of decision making. The Fund should continue to report to the government on an annual basis to ensure that it is fulfilling its aims and objectives.

What measures and mechanisms should the government have in place to ensure that it receives value for money throughout the life of the contract with the Fund manager?

39. The government should work closely with the Fund manager to monitor the value for money of the contract. It is important that the Fund continues to strive to reduce its administration costs and increase its efficiency.
40. However, the OTS should recognise that large amounts of administration are required to undertake a wide range of activities such as the engaged investor approach and we do not believe that the £6.5m indicated would be proportionate to this continued scale of activity. Although it is important to reduce the cost of administration this should not take place at the expense of the Fund's effectiveness.
41. It is also worth noting that the true value of the contract needs to be understood in the context of a wider disposition towards loan finance, a more constructive commissioning environment and a healthy third sector. It is important that the Fund manager places sufficient emphasis on continuing to provide an appropriate level of support to organisations already receiving funding. If this is not provided there may be unnecessary failure of organisations and the services they provide.

How should the OTS measure that the delivery aims of the Fund are being met by the Fund manager.

42. The primary measurement for the Fund should be the success of the services being delivered. As stated earlier this requires the Fund manager to play a role in supporting a framework for organisations to measure their social output. Additional measurements could be the number and value of contracts won by an organisation.
43. The Funds objective is to demonstrate how third sector organisations can help transform public services in England, and as such its impact is wider than simply those organisations that are successful in applying to the Fund for investment. In measuring the new organisations that enter the market, it is important to consider that this will include third sector providers that do not access the Fund, but have been aided by an improvement in the commissioning environment. One useful indicator maybe the number of organisations making applications to Futurebuilders, and how this is relevant to the sector they operate within. The Coalition would also suggest measuring the additional value of finance leveraged.
44. To measure the development of new services, the Fund manager should look to report on the number of funded organisations that are delivering services that were not previously available within their area.
45. The Coalition also proposes the creation of a separate social enterprise classification, to enable the easy identification of both the number social enterprises that access the Fund and the value invested in social enterprises. This would provide an assessment of the success of the Government's policy of achieving greater social enterprise involvement.
46. The Coalition would suggest that although the OTS should aim to collect this data to help monitor and evaluate the success of the fund rather than to be used as contractual targets. Whilst targets work toward driving efficiency and improvement in the quality of service, short term financial assessment is unlikely to reveal the true impact of the Fund. Many of the benefits of the Fund are likely to be more visible over a longer period, of at least three to five years, where organisations are able to deliver a diverse range of services and generate tangible impacts.

What measures should the OTS seek to adopt to ensure that the Fund manager meets appropriate financial targets?

47. The Coalition recommends that the OTS takes a light touch approach to monitoring and targets, which is flexible and sensible enough to ensure that the money is not committed unwisely or in haste.
48. The Coalition also believes that the Fund should do more to encourage a funding mix. Leveraging a range of investments should help capitalise social enterprises and add value to the Fund. In line with previous comments regarding the amount of the Fund invested in assets, the Coalition particularly supports moves that would encourage a match funding approach to loans on property.
49. Whilst working towards a reduction of overhead and administration costs should be the goal of any organisation, the Coalition would urge the OTS to consider a proportionate management cost, given the involved nature of the investment approach.

Recommendations

- The Coalition recommends the definition of public service based on 51% income paid for by the public sector is revised to ensure that the fund is accessible to social enterprises that generate income from other markets as well as providing public services.
- The primary measurement of the Fund's success should be social benefit. In order to evaluate social benefit the Fund manager should support organisations in implementing a framework for social accounting or social return on investment.
- The Fund manager should seek to work with all existing funders, including social lenders and high street banks, to provide a mixed financial package where appropriate. Leveraging of finance will add value to the Fund.
- Whilst the government is right to seek a reduction in the administration costs, the Coalition recommends that the administration required in implementing an effective engaged approach is recognised.

**SEC Policy team
August 2007**