UKSIF
UK Sustainable Investment
and Finance Association

13th September 2013

Social Investment Tax Relief Consultation
Enterprise & Property Tax Team
HM Treasury
1 Horse Guards Road
SW1A 2HQ

E-mail: socialinvestmenttaxreliefconsultation@hmtreasury.gsi.gov.uk

Dear Anna and Virginia,

Thank you for the opportunity to comment on HM Treasury's and the Department for Business, Innovation and Skills' *Consultation on Social Investment Tax Relief.*

About the UK Sustainable Investment and Finance Association (UKSIF)

The UK Sustainable Investment and Finance Association (UKSIF) is the UK's membership network for sustainable and responsible financial services. We promote and support responsible investment and other forms of finance that advance sustainable economic development, enhance quality of life and safeguard the environment. We also seek to ensure that individual and institutional investors can reflect their values in their investments.

UKSIF was created in 1991 to bring together the different strands of sustainable and responsible finance nationally and to act as a focus and a voice for the industry. UKSIF's 250+ members and affiliates include financial advisers, charities and other NGOs, institutional and retail fund managers, pension funds, banks, research providers and consultants. For more information about UKSIF, please visit www.uksif.org.

Introduction

UKSIF welcomes the commitment by the Government to establish a social investment tax relief (SIR) to encourage funding and investment from private individuals that can be used to address social problems. Our response primarily addresses those issues raised in questions 4, 6 – 7, 8 – 9, 31 – 32 and 35, and is based on consultation with our members, some of whom are heavily involved in this sector, at a roundtable on the 3rd September 2013, as well as previous responses to: The Financial Services Authority's (FSA) consultation CP12/19 *"Restrictions on the retail distribution of unregulated collective investment schemes and close substitutes"* in November 2012, the Cabinet Office's *Red Tape Challenge: Civil Society – Social Investment* in September 2012 and our joint response to your previous consultation on *Tax-advantaged venture capital schemes with regard to community-based* *renewable energy* (September 2011). All these responses can be found on our website at http://uksif.org/policy/responses-representations/ .

UKSIF has long supported the introduction of tax incentives for social investments, including social enterprises, having considered it perverse that tax incentives should be available for investment in listed companies and in early stage venture capital but not in social investments. As the secretariat for the Social Investment Task Force, we supported the introduction of Community Investment Tax Relief (CITR) and we also called for and welcomed the government's decision last year to ensure that community-based renewable energy projects established as social enterprises were not excluded from Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCT) tax reliefs.

We feel that the government's proposals regarding SIR will move the social investment sector forward and this proposal, together with the other initiatives undertaken by the government, including the set-up of Big Society Capital and the outcome of the UK's Presidency of the G8 Summit in June 2013, sends a good signal to investors.

However, we feel there are some issues that the Government should continue to explore when designing and implementing the SIR including:

- The need to monitor the actual displacement of donations into investments for charities once the SIR is implemented
- The particular difficulties surrounding the estimation of gross assets, employees or turnover when it comes to the charity sector and some other social enterprises
- The fact that several activities which are typically excluded from benefiting from, for instance, EIS, such as lending or the provision of social care, are the kinds of services that social enterprises often provide
- The fact that unsecured debt instruments are a very popular choice of finance for e.g. charities yet would not be covered by this relief
- The necessity of working closely with the FCA, the Department for Business, Innovation and Skills, the Cabinet Office and other government bodies in order to ensure a joined-up approach to the policy and tax framework for social enterprises

Question 4: Are there any particular advantages or disadvantages to making charities eligible for the relief? In particular, is there a risk that donations to charities will be displaced into investments and what are the consequences of this?

Our members would broadly support including charities in the SIR as they play a key part in service provision in several sectors yet are in need of access to capital for growth. We note the response of Social Finance, one of UKSIF's members, who highlight a study in the US into impact investing by Hope Consulting which showed that – at least in the US – the risk that donations to charities would be displaced into investments was present for approximately 10% of donations.

There has been no equivalent study conducted in the UK but we would urge the government to remain conscious of this risk once the tax relief has been fully designed and implemented and to build in sufficient flexibility in its policy to allow for any tweaks should the displacement of donations into investments prove to be sufficiently high in practice.

Some of our members also noted that it might be helpful if charities' trading subsidiaries were included in the relief as this is a model used by an increasing number of charities.

Question 6: Would a size requirement of up to 250 employees be appropriate for the social investment tax relief, or should a lower limit be introduced initially?

Our members' views were mixed on this: some organisations stated that it made little sense to exclude larger charities as these were potentially where access to finance could produce the greatest impact and that several mainstream charities don't have the ability to secure significant size loans, while others noted that the relief's intention is to focus on those who have difficulties accessing finance, a group which tends to be smaller charities.

There were also concerns that social enterprises have so far been relatively labour-intensive and that a focus on the number of employees might therefore disproportionately impact the social enterprise sector.

Question 7: What are the benefits and disadvantages of using gross assets or turnover to measure size, and what would the appropriate limits be? Please provide reasons and evidence.

Our members had a range of views on this issue. A gross asset requirement was felt to disproportionately impact those property-backed institutions for instance in the social housing sector. This may be because even though in theory an organisation with assets should be able to access mainstream financing, those assets (such as housing) might play a vital part in their service provision and so they may be unwilling to risk using them as security. It was also noted that it can be difficult to estimate turnover for the charity sector.

At our member roundtable on this consultation, the point – as highlighted in our response to Question 6 – that it would seem odd to exclude larger players which could really add to the impact that social enterprises are making in several vital areas, was repeated frequently.

We would recommend that the Government explore this issue further.

Question 8: Would it be appropriate to exclude particular activities from the social investment tax relief, in order to keep the tax relief well-targeted, or would the existing regulation of the qualifying organisations be sufficient? If the Government does introduce exclusions, should specific organisations be entitled to the social investment tax relief that are not currently able to access the venture capital reliefs, for example organisations delivering social care, or arts based organisations? Should any additional exclusions apply? Please give reasons.

We understand the need to avoid the potential for damage to the credibility of the proposed tax relief for social enterprises by ensuring abuse of the system is minimised.

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However, currently there are a broad range of services that are typically undertaken by social enterprises that are often excluded by other tax reliefs such as the EIS and VCT and which our members think should be included. These include: health care and social care (such as managing nursing homes) or providing legal and lending services. Property was highlighted as a 'grey area' by our members, with some pointing out that there are some charities like Mencap, who adapt properties to meet the needs of specific individuals.

Similarly, our members noted that organisations like Community Development Finance Institutions (CDFIs) are engaged in lending activities which benefit their community and often underpin important local services, but would be excluded under most tax reliefs.

Question 9: Do you agree with these general principles governing the scope of the investment instrument as a means to ensure that the tax relief for social investments is well-targeted and focused on appropriately high-risk investments?

One aspect of the SIR highlighted by our members is that if, as the proposals currently state, the rate of return must be dependent on the financial performance of the organisation, this would exclude conventional debt instruments. Yet for many organisations in the social enterprise sphere, including charities, an unsecured loan can often be the most cost-effective and straightforward option. Recent research conducted by Big Society Capital alongside the City of London showed that quasi-equity arrangements made up only 0.2% of the total social investment market (by value) in 2011/2012 while 'conventional debt investments' made up about 95% with unsecured debt forecast to make up 58% of the demand for social investment by 2015[1].

Question 31: What are the barriers that currently put investors off investing in the social enterprise market?

There is clear evidence that 'ethical' or 'green' – which can also reasonably be extended to include social – considerations are increasingly taken into account by retail clients and the public more generally when considering how to invest their money. This is based both on feedback from our financial adviser members and UKSIF/YouGov research for National Ethical Investment Week 2012, the UK's 'Sustainable Investment Week' which indicates strong retail investor interest[2]:

- **45%** of UK adults with savings or investments want **at least some of those to take green and ethical considerations into account**, with **15%** wanting **all their investments to do this**.
- **46%** of UK adults want to **put at least some of their investments into 'impact investments'** such as social enterprises, which produce both a financial and a social or environmental benefit.
- **55%** are interested in **knowing more about 'impact investments'**.

However, our members continually tell us that this demand for 'sustainable' investment – such as investment into social enterprises, isn't being tapped.

[1] Big Lottery Fund, Big Society Capital, HM Government, City of London Corporation (2013): *Growing the Social Investment Market: the landscape and economic impact*
[2] UKSIF/YouGov figures, National Ethical Investment Week 2012.

One reason given is that member feedback indicates the cost of meeting financial promotion requirements not designed or appropriate for small-scale social investments inhibits the provision of these opportunities to socially motivated investors.

For instance, the FSA consultation paper on *Restrictions on the retail distribution of unregulated collective investment schemes and close substitutes* failed to mention social investing or client investment objectives that go beyond financial aims or the potential to introduce a pre-defined cap on investments by ordinary retail investors into non-mainstream pooled investment products with social aims. Although we understood the very legitimate concerns that prompted this paper, we were disappointed at this omission, which was retained in the resulting FCA guidance.

We note that the suggested tax relief for investment in social enterprises should interest financial advisers who can then sell it to their clients. Furthermore, we feel that the decision to model the tax relief on the EIS is a good one as this is something that financial advisers are familiar and comfortable with. But we would urge HM Treasury and the Department of Business, Innovation and Skills to work closely with the Cabinet Office and the FCA in order to ensure coherent messaging and signals regarding the Government's commitment to social investment, including investment in social enterprises.

Question 32: What is the loss to the economy from underinvestment in the UK social enterprise market?

UKSIF sees social investing – including investment in social enterprises – as a sub-set of modern sustainable and responsible investing, where the distinctive characteristic is the motivation of seeking a social impact as well as financial returns.

Social investment and social enterprises therefore have a vital part to play in supporting a move to a more sustainable UK economy, with business models that not only provide a financial return to investors but also invest in and support local communities.

In order to enable social enterprise to do so, however, they require support and we feel the SIR will play an important part in encouraging investors to consider social as well as financial returns when making investment decisions.

Question 35: What type of investor is likely to drive an increase in social investment, and are they targeted by the policy as is currently outlined? If not, what would be needed to bring them into the policy?

There has been increasing interest from institutional investors in social investment and, although understandable, this policy fails to target what could be an important source of funding for social enterprises.

Our institutional members tell us that they are currently examining impact investment options – including investment into vehicles providing loans and equity to social enterprises– but an important limitation is the lack of liquidity in this market.

We would recommend that the Government examine policy options for supporting the creation of a social investment product that appeals to both the institutional and the retail market.

I trust that the comments above are self-explanatory but please do contact us should you require any further information or clarification.

Yours sincerely,

Simon Howard

Chief Executive
The UK Sustainable Investment and Finance Association (UKSIF)