

# Working for Third Sector-led Social Investment and the Common Good

Senscot Discussion Paper ([www.senscot.net](http://www.senscot.net))

*Scotland has a vibrant social entrepreneurial environment. Senscot, in this discussion paper, is critical of the marketization of social investment suggesting an alternative model that they conclude fits the third sector ethos. Reprinted with permission.*

*This Discussion Paper was written and researched by Laurence Demarco and James Henderson and published by Senscot to promote further discussion.*  
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## 1.0 Introduction

In August 2012 Senscot circulated a discussion paper<sup>1</sup> expressing concern about the direction of social investment in the UK, particularly the growing emphasis on investor profit. This paper updates the discussion in the light of subsequent events and new thinking. The third sector generates much of the social capital which holds our society together, and it has an ethos quite distinct from either the state (public) sector or the private sector and market economy (section 2). To flourish our sector requires a flow of investment which understands and respects its mission and values: investment which is both patient (long-term) and bold, tolerating the inherent risk of innovation.

**A**s rehearsed in the earlier 2012 paper, Senscot believes that the style of social investment promoted by the UK Government – through Big Society Capital (BSC) and others – was designed by people unaware of both the nature and needs of our sector. This prediction has proven more or less correct, and there is a growing realisation that the payment of dividends to private investors is contrary to the ethos and realities of our sector's work: in effect, it's not going to happen (section 3).

Our 2012 paper also expressed surprise at the lack of resistance to the clumsy attempts of merchant bankers to marketise the third sector in England. Fortunately, there is now evidence from the past year that the fight-back is underway, and of the potential for new third sector-led initiatives (section 4). So we conclude by asking if – in the light of specific recent developments – a *Scottish model* of financing the third sector, and supporting the common good, is now emerging as an alternative to market-led thinking.

## 2.0: The fundamental importance of the third sector

2.1 A *distinctive sector*, what we now know as the third sector, has its origins in the charities, mutuals and voluntary organisations which flourished in the 19th century. Motivated by the compassion and solidarity of ordinary citizens, these initiatives provided respite from the extraordinary industrial expansion and harsh social changes generated by the market economy. Although to some degree ‘parked’ by the growth of state provision in the 20th century, the third sector has continued to change and thrive: witness, since the 1970s, the growth of the community sector; from the 1980s, the advance of community and social enterprise; while, the 2000s brought the increased emphasis on contracted public service delivery through the third sector. The social value of all this activity is explicitly endorsed by the state, with legislation affording fiscal benefits, and organisations eligible for this status are regulated – a distinctive sector<sup>2</sup>.

2.2 *Third Sector values and culture...* given the diversity of the third sector, a single agreed statement of values and approaches seems neither likely nor useful. However, in 2007, the Third Sector Network in England drafted eight ‘values and principles’<sup>3</sup>, from which we have extracted four broad narratives as a framework for supporting discussion of third sector values:

- Social justice and the protection of the planet as prerequisites of all activity;
- The Common Good will always trump individual gain;
- Independence from both the state and private sector interests;
- Democracy, accountability and transparency – are embedded traditions.

Taken together, these third sector values identify a space which is sometimes also referred to as ‘civil society’; the realm of the citizen, free to act outwith the control of the state or the constraints of market forces. Activity which, in 1948, Lord Beveridge described as one of the distinguishing marks of a free society.<sup>4</sup>

2.3 *The common good...* we are concerned here to assert the importance of the third sector and its contribution to the functioning of our society. The philosopher Michael Sandel, in his 2012 book *What Money Can’t Buy*, expresses concern that we, in the West, are moving from a market economy to ‘market societies’ which tolerate gross inequalities, and where the pervasiveness of market-based thinking comes to corrupt our commitment to human social values. At its core, third sector activity is the expression by millions of volunteers and activists of their concern for all in our society and our common future. The assumption that this spontaneous goodwill should be subjected to market forces is the fundamental error underlying government policy. Be in no doubt, the UK Government is trying to marketise both public and third sectors, and we need to talk about this.

## 3.0: Marketising the third sector as current UK Government policy

3.1 There has been nothing covert about the UK Government’s aspiration to finance the third sector through profit-seeking private investment. The founding chair of BSC, Ronald Cohen, became cheerleader, and spoke of making social investment a new ‘asset class’ for international capital markets – a market, he claimed, of massive scale. He warned us we would need to change, most controversially by being prepared to pay dividends to investors. The third sector, as a value-driven and asset-locked entity, was replaced by the language of ‘social sector’, and deemed to embrace profit-driven companies with ‘social’ elements. Cohen spoke of a new ‘paradigm’ which would unleash the vast wealth of money markets to tackle social ills.<sup>5</sup>

3.2 *Marketisation and the public sector* ... simultaneously in England, the privatisation of the public sector has been gathering momentum, with ‘sweetheart’

deals for giant, outsourcing corporations like G4S, Serco, A4e, Capita and Atos.<sup>6</sup> The spread of ‘payment by results’ contracts further favours the target-driven, economies of scale and culture of the corporate sector over the third sector. Social impact bonds (SIBs) were introduced with much fanfare as a vehicle to enable private capital to gamble on the success of social ‘interventions’ – with the state paying dividends according to outcomes. The Coalition UK Government has continued to promote SIBs as a key vehicle for opening social investment to the private finance markets, with BSC to play a key role within this.<sup>7</sup>

- 3.3 Yet the recent birthday celebration of BSC was a surprisingly muted affair. The organisation is more modest now, more realistic. Chairman Cohen has gone, and with him the overblown rhetoric about a multi-billion asset class; while new Chair Harvey McGrath recognises that social investment is not a ‘silver bullet’ for all third sector organisations. If you read the small print of their 2013 annual report, you will learn that the total money that has reached frontline organisations by the end of 2013 was only £13m<sup>8</sup>. We also learned this month that the much vaunted inaugural Peterborough SIB will not be extended into a planned third phase.<sup>9</sup> The SIB model, overcomplicated and over expensive<sup>10</sup>, survives only on a UK Government funded life support system.<sup>11</sup> Yet if the UK Government policy for social investment can be seen as failing, those of us who seek to replace it must recognise why it is so, and seek alternatives.
- 3.4 Firstly, and much to its credit, the culture of the third sector rejects the idea of profit from working with people in distress, and we should not underestimate the effect of this embedded resistance.<sup>12</sup> But leaving moral discomfort aside, the overarching reason for the failure of government policy is the mismatch between the types of investment required and what’s been offered. The research has consistently shown that BSC’s supply of finance-led social investment simply doesn’t match the needs of community-based social enterprise and third sector organisations for a mix of small scale (up to £100k)

grants and patient capital, often as unsecured investment.<sup>13</sup>

- 3.5 *The new reality ...* current BSC Chair Harvey McGrath recently told a Westminster Civil Society All Party Group (May 2014) that products of ‘blended capital’ – a mixture of grant funding and loan – are better suited to third sector needs, with social investment as a ‘subset’ for the minority<sup>14</sup>. Interviews by social enterprise commentator David Floyd with former BSC Chief Operating Officer Caroline Mason (November 2013), and Chief Executive Nick O’Donohoe (February 2014) confirm that – after a two year detour – this penny has dropped.<sup>15</sup>

#### 4.0: Seeking third sector-led approaches: resistance and new horizons

- 4.1 The lack of explicit challenge to the UK Government’s social investment strategy has been disappointing – particularly from third sector leaders. Yet, there has now been some criticism of the general privatisation of the public sector: SEUK’s 2012 report *The Shadow State* has established the dangers of the corporate invasion of public service delivery and the curtailing of opportunities for the third sector;<sup>16</sup> whilst Cooperatives UK and the TUC have similarly clarified their concerns about the abuse of public service ‘mutualisation’ as a vehicle for privatisation.<sup>17</sup>
- 4.2: The current thinking of Locality has been particularly encouraging with, firstly, (then) Chief Executive Steve Wyler arguing (May 2013) that BSC and others are seeking to redefine social enterprise, through the language of the ‘social sector’ and social impact investment, in order to normalise the role of for-profit, private organisations within the social economy.<sup>18</sup> Most recently, Locality’s report<sup>19</sup> on ‘the diseconomies of scale’, and an advocacy for a ‘local-by-default’ approach to the provision of local services, is now showing how a very different language can be developed: one no longer concerned for targets and economies of scale that appeal to the corporate sector and market investment. Locality’s emphasis is on working with people to understand their purposes and needs, and to develop

their strengths, through locally-based approaches. Early days for such thinking, but an alternative approach concerned for third sector roles and values is coming into view.

- 4.3: *In Scotland*, the Scottish Government is generating a policy landscape more receptive to third sector values and third sector-led development. The Government Economic Strategy 2011<sup>20</sup> clearly establishes the third sector and social enterprise as key partners in working for more equitable economic development – with over £190m being committed to support its Enterprising Third Sector Action Plan between 2008-2014 (Scottish Govt website – various). Its approach to public service reform – given public spending cuts and changing demographics – has not been to turn to the commercial markets and privatisation, but instead to recognise the role of preventative approaches and the third sector. One particular commitment has been through ‘public social partnerships’ in which public and third sectors work together with local service users to design suitable services; once piloted and evaluated, these can then be commissioned through an open tendering process.<sup>21</sup> Further, the Scottish Government has side-stepped SIBs and is choosing, for instance, to invest £8m in the (Scottish) Social Growth Fund, which is enabling Social Investment Scotland to provide loan products responsive to third sector needs.<sup>22</sup>
- 4.4: *The Scottish Community Re-investment Trust (SCRT)* ... Senscot is now involved in the development of this Trust which is concerned to make the Scottish third sector less reliant on investment from either the state or the commercial sector, so giving it more control over its own future. The investible assets of Scotland’s third sector have been calculated to be in the region of £4.25bn<sup>23</sup>, and 10% of this amount (£425m) would be sufficient to justify a new third sector banking institution, while even 1% (£42.5m) of strategically placed deposits would transform our sector’s influence and role. Yet these third sector deposits are mainly held in financial institutions that have little understanding or interest in

our sector’s mission. At the same time, all our research (and that of others) confirms that the sector’s development is being restricted by the lack of suitable investment, particularly relatively small amounts of risk or patient investment.<sup>24</sup>

- 4.5: The intention, therefore, is to create the SCRT with a stated mission: *to establish an intermediary owned and controlled by the Scottish third sector that seeks both to harness our sector’s collective assets and expertise and to provide a family of financial services relevant to our sector’s needs.*<sup>25</sup> The Trust will:
- provide opportunities for third sector organisations to invest in and support the development of the wider third sector;
  - support the development of suitable financial services and products, and promote financial literacy and increasing financial expertise within the third sector;
  - progress its plans through its commitment to third sector values and ethos, and in collaboration with the sector through its Board, membership and networks.
- 4.6: *Working for Third sector-led investment* ... the SCRT’s vision is of a mutualised framework, wherein financially robust organisations with substantial reserves, can elect to ease the supply of risk seed capital to the next generation of social innovators. No-one disputes that our sector controls the financial resources to implement this strategy, but there is a question about its will to do so: can our thousands of disparate organisations feel sufficient shared identity to act with collective purpose? This is a big question but one, Senscot feels, deserves to be asked.

The third sector is experiencing a shift in its political and economic environment. Potentially, it may be undergoing a significant transformation in its shape, its role and its relationship with both public and private sectors. By failing to effectively harness our own substantial resources, our sector is more exposed than necessary to the vagaries of political ideology and ‘market fundamentalism’. If we can commit to work together – we ourselves can determine the future.

<sup>1</sup> Note: view Senscot 2012 Social Investment paper at: [www.senscot.net/view\\_art.php?viewid=12660](http://www.senscot.net/view_art.php?viewid=12660).

<sup>2</sup> Note: Rory Ridley-Duff and Mike Bull's (2011) *Understanding Social Enterprise: theory & practice* explores the development of the third sector in the UK. Steve Wyler's (2009) *A History of Community Asset Ownership* – view [www.locality.org.uk/resources/history-community-asset-ownership](http://www.locality.org.uk/resources/history-community-asset-ownership) – and John Pearce's (1993) *At the Heart of the Community Economy*, look more closely at the development of community social enterprise.

<sup>3</sup> Note: view details of Third Sector Network's thinking at: [www.navca.org.uk/news/view-article/values](http://www.navca.org.uk/news/view-article/values).

<sup>4</sup> Note: see for instance Barry Knight's article in the Fabian Society report *Beveridge at 70*, view at: <http://www.fabians.org.uk/publications/beveridge-at-70/>

<sup>5</sup> Note: see, for instance, Ronald Cohen's 2014 speech *Revolutionising Philanthropy – Impact Investment*, view at: [www.cass.city.ac.uk/\\_data/assets/pdf\\_file/0003/209775/LM-CLP\\_Sir-Ronald-Cohen-Jan-14.pdf](http://www.cass.city.ac.uk/_data/assets/pdf_file/0003/209775/LM-CLP_Sir-Ronald-Cohen-Jan-14.pdf).

<sup>6</sup> Note: see, for instance, Zoe Williams' 2012 report *The Shadow State for Social Enterprise UK*, view at: [www.socialenterprise.org.uk/uploads/files/2012/12/the\\_shadow\\_state\\_3\\_dec1.pdf](http://www.socialenterprise.org.uk/uploads/files/2012/12/the_shadow_state_3_dec1.pdf).

<sup>7</sup> Note: see, for instance, the UK Government aspirations within its web-information on SIBs, view at: [www.gov.uk/social-impact-bonds](http://www.gov.uk/social-impact-bonds), and BSC's aims for SIBs and related market structures in its *Annual Report 2012*, view at: [www.bigsocietycapital.com/sites/default/files/pdf/BSC\\_AR\\_AW\\_forwebsite.pdf](http://www.bigsocietycapital.com/sites/default/files/pdf/BSC_AR_AW_forwebsite.pdf).

<sup>8</sup> Note: BSC Annual Report 2013 (p41) notes that in total commitments to £148.9m for 30 investments had been made at 31 December 2013, with 19 investments of £47.9m having been signed, and £13.1m drawn down, view at: [www.bigsocietycapital.com/sites/default/files/BSC\\_AR\\_2013.pdf](http://www.bigsocietycapital.com/sites/default/files/BSC_AR_2013.pdf).

<sup>9</sup> Note: the Peterborough Prison offenders project will now be further funded through the UK Government's 'Transforming Rehabilitation' programme, view Civil Society article (May 2014).

<sup>10</sup> Note: the Yunus Social Business Centre at Glasgow Caledonian University's recent paper on SIBs (McHugh, et al. 2013) establishes a wide range of technical and policy concerns; whilst even the more supportive Social Market Foundation (Keohane, Mulheirn & Shorthouse, 2013) recognises their complexity and set-up costs.

<sup>11</sup> Note: the UK Government has now announced backing for Youth SIBs worth £30m (May 2014): [www.gov.uk/government/news/30-million-boost-to-improve-the-lives-of-britains-most-vulnerable-young-people](http://www.gov.uk/government/news/30-million-boost-to-improve-the-lives-of-britains-most-vulnerable-young-people).

<sup>12</sup> Note: various research reports from 2012 and 2013 have highlighted this culture clash: Duffy (2012); Gregory, Hill, Joy & Kean (2012); Baker & Goggin (2013); Gregory (2013).

<sup>13</sup> Note: various research reports and commentaries from 2012 and 2013 establish this clash between third sector demand and BSC/social investment supply: see the four reports in Note 12 above; Henry & Craig (2013); Davison (2013); Davison & Heap (2013); see also Senscot 2013 report in Note 23.

<sup>14</sup> Note: view at: [www.thirdsector.co.uk/news/1294363/Social-investment-is-not-silver-bullet-sector](http://www.thirdsector.co.uk/news/1294363/Social-investment-is-not-silver-bullet-sector).

<sup>15</sup> Note: see David Floyd's interviews with: Caroline Mason at: [www.beanbagsandbullshit.com/tag/caroline-mason](http://www.beanbagsandbullshit.com/tag/caroline-mason); Nick O'Donohoe at: [beanbagsandbullshit.com/2014/02/28/report-from-emerging-market](http://beanbagsandbullshit.com/2014/02/28/report-from-emerging-market).

<sup>16</sup> Note: see Note 5 above for details.

<sup>17</sup> Note: see Cooperatives UK and TUC news release and report at: [http://www.uk.coop/pressrelease/tuc-and-co-operatives-uk?utm\\_source=Linx+293+-+29+August&utm\\_campaign=linx293&utm\\_medium=email](http://www.uk.coop/pressrelease/tuc-and-co-operatives-uk?utm_source=Linx+293+-+29+August&utm_campaign=linx293&utm_medium=email).

<sup>18</sup> Note: see Steve Wyler's blog (13.05.13) at: <http://locality.org.uk/blog/powerful-engine-pieces-lying-floor/>

<sup>19</sup> Note: see Locality's report at: [www.locality.org.uk/our-work/policy/diseconomies-scale](http://www.locality.org.uk/our-work/policy/diseconomies-scale)

<sup>20</sup> Note: Scottish Government Economic Strategy 2011, view at: [www.scotland.gov.uk/Resource/Doc/357756/0120893.pdf](http://www.scotland.gov.uk/Resource/Doc/357756/0120893.pdf)

<sup>21</sup> Note: see *Public Social Partnerships on the Ready for Business* website: [www.readyforbusiness.org/programme-offering/public-social-partnerships](http://www.readyforbusiness.org/programme-offering/public-social-partnerships)

<sup>22</sup> Note: Scottish Government and BSC have provided £8m each to establish a £16m growth funded to be managed by Social Investment Scotland, view details at: [www.socialinvestmentscotland.com/news-and-events/16m-investment-scotlands-third-sector/](http://www.socialinvestmentscotland.com/news-and-events/16m-investment-scotlands-third-sector/)

<sup>23</sup> Note: data from SCVO's *State of the Sector 2014* report, view at: <http://www.scvo.org.uk/wp-content/uploads/2014/04/SCVO-Sector-Stats-2014.pdf>

<sup>24</sup> Note: view Senscot and the Scottish Community Banking Trust 2013 report for market research in Scotland: [www.senscot.net/view\\_art.php?viewid=16013](http://www.senscot.net/view_art.php?viewid=16013).