JBWere

7 July 2011

The Secretary
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Secretary

Re: Senate Economics References Committee Inquiry "Mechanisms and Options for the Development of a Robust Capital Market for Social Economy Organisations"

Thank you for the opportunity to make a submission to the Senate Economic References Committee 2011 inquiring into mechanisms and options for the development of a robust capital market for social economy organisations.

For over ten years, JBWere has been a leading adviser to the philanthropic and community sector and seeks to offer its resources and knowledge to assist in the development and promotion of philanthropy and social investment in Australia.

Since 2009, JBWere has been majority owned by National Australia Bank, one of Australia's leading major financial institutions. NAB's commitment to address financial exclusion in Australia is core to NAB's corporate responsibility strategy and activities. JBWere shares NAB's concern that Not for Profit and community organisations often struggle to access financial products and services appropriate to their needs and aspirations, and commend their separate submission to this inquiry.

In the following submission, we have attempted to address the specific issues raised under the terms of reference for the inquiry as well as making some overall observations regarding the key issues that we believe need to be addressed to develop a social capital market in Australia.

JBWere is encouraged by the Government's interest in examining this matter and we are willing to be available for further consultation if and when appropriate.

Yours sincerely

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1. Social Capital Markets in Australia

The Not for Profit sector in Australia has seen significant growth and development over the past decade.

In recent times, there has been an increasing body of research that has documented these changes.

This work has contributed to a greater understanding of the need for financial products and services and the social capital requirements of community organisations in Australia.

The Productivity Commission's research report[1] has been an important resource providing detailed analysis of the sector and its growth. This report specifically identified key issues around access to capital and the provision of financial services to community sector organisations.

The sector is at an important transition point for a number of reasons, these include:

- A greater transparency and awareness by the community of what organisations within the sector do
- Increased engagement of people, resources and commercial providers to these organisations
- Significant growth of the sector due to the outsourcing of service delivery by government
- An increase in the overall level of giving and associated donor engagement over the past decade
- Significant development and innovation in international markets, noting particularly the intervention and leadership of the UK government to drive major change

All of these factors are combining to increase awareness that Not for Profit organisations need to be able to access social capital from sources beyond the traditional suppliers of this funding, ie government and philanthropy.

To develop a more robust social capital market in Australia, there needs to be clarity on what the demand for this capital is, how it is currently sourced, and what new alternatives or approaches could be considered.

By combining the skills and experience of commercial market intermediaries with a detailed knowledge of the challenges that Not for Profit organisations face in seeking social capital and access to appropriate financial services and products, there is a real opportunity to address the market failure that occurs between traditional Not for Profit funding sources (ie Government and philanthropy) and commercial markets.

When considering the issue of the Not for Profit sector's access to finance, there needs to be a paradigm shift in the way all participants think about how this access can be improved. By aligning the interests of all stakeholders, this will identify solutions that create significant social value.

In particular, we believe the utilisation of arbitrage bonds (as explained in section 4.3.3. of this submission) have the scope to dramatically change the way social and environmental programs could be funded in this country.

[1] Productivity Commission report "Contribution of the Not-for-Profit Sector" (January 2010) http://www.pc.gov.au/__data/assets/pdf_file/0003/94548/not-for-profit-report.pdf

2. Identifying the Financial Needs of the Social Sector in Australia

There are three broad areas that we would like to address in this submission:

1. What types of capital and finance are required
2. Sources of Not for Profit finance
3. Are Not for Profit organisations investment ready

2.1. What types of capital and finance are required

As with most things, there is not a one-size-fits-all solution to providing greater access to capital and financial services to Not for Profit organisations. Up until recently, discussion of this topic was very much focused on individual products or ideas, rather than systemic change. The importance of developing strong commercial intermediaries who are focused on providing comprehensive and coordinated offerings is a vital development required to bring about this change.

Many organisations in the sector have a history of deficit funded hand-to-mouth fundraising which has been a one-size-fits-all source of finance. As organisations grow, they are increasingly able to attract specific project or program based funding from Government or philanthropy.

As Not for Profits become more organised, have greater resources and become aware of the options available to them, they begin to source different types of capital and financial services from a variety of sources. These include:

- Day-to-day operating finance
  - Lease facilities for vehicles, property, equipment
  - Credit cards
  - Short term / overdraft debt
  - Insurance
- Longer term project or infrastructure capital
  - Debt finance
  - 'Nominal' social equity
  - Impact investment

    We define impact investment as a form of debt or equity investment where the investor accepts a discounted financial return, where the size of the discount is understood to represent the 'social' return component of the investment. This form of capital has traditionally been provided by philanthropic support at one end of the spectrum, where the discount is greatest, or commercial providers at the other end who have been willing to take even a small 'social' discount to satisfy other non-financial criteria of their investment mandate.
- In addition, Not for Profits are increasingly looking to professional service providers to manage their financial assets. These services include
  - Cash management
  - Wealth management services
  - Property management
  - Endowment establishment, governance and administration services

Many of these services are only available to medium-to-large organisations that typically generate some form of internally generated revenue, or have assets that can be used as security. Smaller organisations that have limited access to these forms of finance and credit options are therefore restricted to access funding primarily through donations, sponsorship or government support.

Currently in Australia there are well-documented examples of the financial exclusion faced by Not for Profit organisations looking to access capital; this is especially prevalent in small to medium size organisations.[2]

Over time, we believe that Not for Profit organisations should have the ability to access all the forms of appropriate funding that their for-profit counterparts have available to them; be they debt or equity instruments. However, to achieve this, the market needs to be developed and confidence needs to be built. Building this marketplace will involve:

- innovation
- incentive
- infrastructure
- intermediation

As confidence builds so will the supply and demand for a variety of different products and services which will in-turn build competitiveness, ensuring that informed Not for Profit organisations that demonstrate good governance and outcomes will attract financial support.

2.2. Sources of Not for Profit finance

There are five main sources of funding of Not for Profit organisations:

1. Government
2. Philanthropy
3. Income from fee for services provided by the Not for Profit or other commercial activities
4. Impact or social investors
5. Capital markets

For the purposes of this submission, rather than attempting to define or quantify the scale of funding provided by this classification, we would refer to Chapter 7 of the Productivity Commission's research report.[1]

Suffice to say that each of these sources have their own limitations and restrictions on what and how they can fund. In addition, the motivation for providing finance from each of these sources varies widely, whether that be to achieve a public policy objective at one end of the spectrum through to achieving pure commercial outcomes at the other.

The point being there is not a single type of 'social capital' required or one predominant source to provide it.

On the surface, this appears to be an obvious statement. However it is an important perception to address, as we have seen with the Giving Pledge (www.givingpledge.org), such actions can reinforce a perception that if the wealthy do not give, the Not for Profit sector will not be supported. This is a narrow and limiting perspective.

Likewise in Australia, the debate around how generous our wealthiest citizens may or may not be can be misinterpreted to suggest that if the rich do not give, our community sector will not be funded. Similarly, the argument is regularly made that, unless there is greater promotion of philanthropy or the Government creates new incentives to encourage private giving, the Not for Profit sector will be significantly impacted.

[2] Foresters Community Finance report, commissioned by National Australia Bank, "Finance and the Australian Not-for-Profit Sector" (March 2011) http://www.foresters.org.au/site/DefaultSite/filesystem/documents/Research%20Report%20Finance%20&%20Australian%20Not%20for%20Profit%20Sector%202011.pdf

To be clear, we **enthusiastically** support any effort or mechanism to encourage greater giving.

Philanthropy, however, will only ever be a small part of the funding picture and is best suited to those activities that cannot access the type of capital solutions we are addressing in this submission. We do not believe greater philanthropy is the panacea to opening up new pools of social capital. We would argue that the bigger issue is understanding **how** to match the needs of the sector more efficiently with all available sources of funding. If this can occur, it will greatly increase the amount of capital available.

2.3. Are Not for Profit organisations investment ready?

In many instances Not for Profit organisations need assistance and advice to become investment ready. This may include reorganising capital structures, improving balance sheets, educating key staff, reviewing services and offerings, improving cash-flows, reviewing governance practices and increasing transparency and accountability.

Not only will these actions assist Not for Profit organisations become ‘investment ready’ in the way they work with professional service providers, and improve their ability to tap into commercial markets, it has also proved very helpful in putting the same organisations in a much stronger position when seeking traditional philanthropic and Government funding.

This is an important step because whilst most Not for Profits are likely to want access to new funding streams and the financial services offered by capital market participants, these offerings may not be appropriate for all organisations if they are not ‘investment ready’, and philanthropy will still be a significant source of funding.

Determining an appropriate instrument be it debt, equity or something else is very important. Poor decisions or choices could result in severe consequences for the Not for Profit entity and investors alike.

There are significant challenges many Not for Profits face in seeking finance which include, but are not limited to:

i) Few organisations have adequate resources or access to appropriately skilled internal personnel to oversee relationships and transactions with commercial providers

ii) A lack of intermediaries who understand the sector and who have the knowledge and skills to facilitate outcomes between ‘buyers’ and ‘sellers’ of finance

iii) Under-developed understanding of risk, both for the Not for Profit and the finance provider

iv) Cultural expectations of what Not for Profits should or should not do, eg take on debt

v) Not for Profits have an inability to offer collateral to secure debt finance

vi) When successful, a Not for Profit outcome may not be ‘monetised’ and cannot therefore be used to pay back ‘commercial’ investors

3. The Role of Appropriate Intermediaries

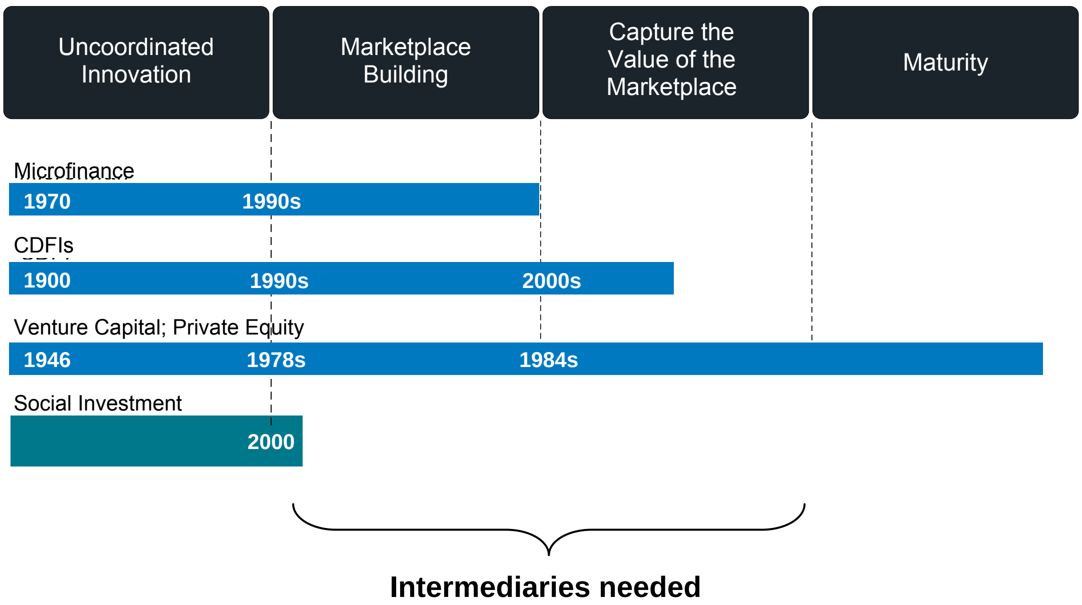
An examination of the history of developing markets across a range of activities and geographic locations highlights the importance of intermediation as a major factor in unlocking the capital that facilitates the growth of that market.

The Monitor Institute report[3] (page 62) identifies "lack of intermediation capacity as one of the most significant changes limiting the ability of investors to find and place capital in impact investment opportunities".

The same report highlights the development of specific capital markets and the role intermediaries fulfilled in moving these markets from the uncoordinated innovation stage through the phases of 'market place building', 'capturing value of the marketplace' right through to the creation of a mature market.

Key drivers for a new asset class

What needs to happen to grown the market?



Source: Monitor Institute (2009)

Intermediaries have been slow to develop due to lack of understanding about the size of the commercial opportunity and the Not for Profit sector grappling with the issues highlighted earlier around becoming investment ready.

It is becoming more evident that well-resourced commercial intermediaries need to be established and encouraged if we are to develop a robust social capital market in Australia.

These organisations need to be staffed by professionals who understand both the needs of all clients they are trying to serve as well as having the ability and authority to modify or tailor existing commercial offerings for the specific needs of Not for Profit organisations.

[3] Monitor Institute report "Investing for Social & Environmental Impact" (January 2009) http://www.monitorinstitute.com/impactinvesting/

As we have seen with international microfinance, the source of investment capital has changed as this sector has developed and investors have become increasingly comfortable with the growth and risk characteristics of the market. Within Australia, microfinance programs such as No Interest Loans Schemes traditionally funded by Government and philanthropic interests have seen significant commercial investment, for example NAB's commitment to microfinance programs which is in excess of $130m.

At the outset, providers of capital to international microfinance programs were predominantly philanthropic. As a greater understanding of the risk and return experience developed, microfinance organisations matured and sought impact or social capital (ie capital willing to accept a discounted financial return, with the understanding that the discount represents a social return acceptable to the investor). Now microfinance programs are substantially funded by commercial investors.

Over time, as Not for Profits have grown, commercial providers (with few exceptions) have struggled to deliver products and services that are compatible with the specific needs of the Not for Profit or are flexible enough to satisfy the requirements of all stakeholders.

In response to this, Not for Profit providers have emerged to try and address these issues by providing tailored solutions. The challenges that these Not for Profit providers have faced include how do they:

i) Generate sufficient return to cover the increased cost of the tailored solution

ii) Be of a size where they can provide an offering suited to the requirements of larger Not for Profits

iii) Achieve volume to look after a large number of customers

Larger organisations require a greater diversity of product and service offering and access to capital on a scale these newer players cannot easily provide. In addition, there is a need for providers who can offer a total solution rather than one-off products that result in Not for Profits having to use a portfolio of service providers. This results in the Not for Profit missing out on the economies of scale that an integrated provider can supply. The end result being often offerings of commercial providers are utilised which may be less appropriate but far more price competitive, resulting in sub-optimal outcomes.

This has lead to a mismatch of service offering and price, from provider to customer.

Another challenge that arises occurs when organisations that do not have sufficient experience or knowledge of the specific needs of Not for Profit organisations get drawn into providing services or capital that they are not set up to provide. Examples might include:

i) Philanthropic programs or ‘social’ enterprises being presented to the market as commercial investments

ii) A deposit taking organisation being asked to make ‘equity’ type investments or

iii) Not for Profits issuing capital instruments without appropriate market knowledge that can lead to mispricing of risk

All of these examples have the potential to lead to an erosion of trust and create justifications for providers and investors not to enter the market. Intermediaries who understand the challenges of this market will fulfil an important role in ensuring trust and confidence is built through the utilisation of the right products and services offered to appropriate and informed investors.

Apart from the challenges set out above, some of the new approaches being presented to the ‘market’ have required a paradigm shift in thinking to gain traction, eg encouraging philanthropists to think as ‘investors’, this can be a challenging shift for some who have operated from a particular framework or mindset over a long period of time. Again, experienced and informed intermediaries are important agents to educate, lead and participate in changing the approach to these challenges.

Often because these new approaches are presented out of context, they have been slow to win support.

Examples of this would include:

- Donors may be willing to donate capital to a capital campaign for a new building but are reluctant to lend funds at a discounted rate because ‘the risk is too high or the return not sufficient’ or
- Social sector organisations approach providers of capital with investment opportunities that have discounted coupons, expecting generic support from these ‘social investors’. Where these approaches have not considered the individual motivations of investors or the fact that their willingness to accept a ’social return’ via a discounted financial return is still strongly influenced by that investors’ association with or geographic connection to the project being funded, disappointing outcomes have occurred.
- A by-product of this outcome is the ‘social’ investor who has been approached, rather than investing in the opportunity at hand, takes the concept and tries to apply the technology, often with insufficient understanding, to another context where they have an association, only to result in another disappointing outcome. This is obviously counter-productive to developing successful case studies of this approach being applied successfully.

For this type of financing to be successfully supported, the returns to investors need to be made as commercial as possible. Furthermore, the social return needs to be measurable and identifiable so that a hybrid investor is able to assess what level of discount is appropriate for the social outcome achieved. An informed decision can then be made as to whether the return is appropriate for the term and risks being undertaken by the ‘investor’.

Intermediaries who understand this market will again be important to ensure that these opportunities are shown to those ‘investors’ who have a natural affinity with the project being funded.

3.1. Resources intermediaries can provide

Intermediaries have well-developed services, expertise and systems in place for existing commercial markets. This infrastructure has the ability to be modified and utilised to fast-track the development and market penetration of impact investments. Such services, expertise and systems include:

Legal and Compliance

- contracts
- anti-money laundering
- information memorandums
- product disclosure statements

Marketing

- branding
- distribution
- market engagement
- collateral
- education material
- online positioning

Custodial Services

- coordinating the settlement of all transactions
- collecting and filing all mail correspondence regarding the portfolio (holding statements, dividend statements, entitlements and special offers, etc.)
- banking and recording all income received from investments
- completing all paperwork and associated administration for any corporate actions (entitlement offers, etc.)
- maintaining a full transaction and taxation registers tracking transactions executed

Systems

- trading systems (buy, sell)
- custodial systems
- reporting systems

Reporting

- valuation reporting
- unit pricing
- performance reporting (financial – social)
- benchmarking
- online reporting
- portfolio valuation reporting

Financial Advisers

- client engagement
- distribution networks
- matching products to clients with appropriate risk profiles (know your client, know your product)

Intermediaries are well-placed to develop financial instruments, run models to determine expected risks and returns and test the market demand for the product. There is also a role to develop opportunities that meet the needs of both the Not for Profits seeking capital and the needs of those providing the capital.

Achieving an appropriate balance of risks with combinations of financial and social return will be important to ensure adequate demand from potential investors.

Intermediaries will play a critical role in educating and informing the market of opportunities to build out demand for impact investments.

JBWere regularly host events across our Australian network that are aimed at informing and educating potential market participants. In addition, we publish educational articles (see Appendix 3) and research on impact investing. All these initiatives are aimed at building awareness of impact investing with the view to creating demand for existing and future opportunities.

Providing capital to Not for Profit organisations will come with certain risks that will, in many cases, be higher than those seen in traditional commercial transactions. On the other hand, as we have seen with microfinance, the investment risk is actually lower than comparative 'commercial' lending. This only further illustrates the need for a real understanding by those providing capital of understanding the risks involved, so capital can be priced accordingly.

Intermediaries will play an important role in communicating to investors the risks associated with various impact investments. The presence of experienced intermediaries involved in this process will provide confidence to investors that the investments are legitimate and sound and that the investment risk has been adequately explained and understood. Utilising the trusted names of intermediaries will provide confidence in the investments and will play a key role in building out demand for impact investments.

Most intermediaries fall under the licensing system of the Australian Securities and Investment Commission and hold an Australian Financial Services Licence. They also fall under the Financial Services Reform Act and the Corporations Act (2001) and come under the watchful eye of the Australian Prudential Regulation Authority. These regulatory authorities help ensure that consumers of financial services are protected and that the financial systems integrity is maintained.

Further to this intermediaries that have to comply Anti-Money Laundering and Counter Terrorism Financing Regulations Act (2008) and have in place mechanisms to protect against money laundering.

The Government should ensure that those participating in developing and selling impact investment opportunities comply with the aforementioned bodies and regulation.

3.2. International Intermediary Case Study: J.P. Morgan's (America) Social Finance Unit

J.P. Morgan's (America) Social Finance Unit is a good example of an international intermediary helping to develop and service impact investment opportunities. This unit provides investment and capital markets services to social enterprises, funds, foundations, non-governmental organisations and development financial institutions. The unit looks to achieve both a social and financial return. Launched in November 2007, as part of J.P. Morgan's Investment Bank the group serves to provide expertise and client contact for social impact investment opportunities.

Source: http://www.jpmorgan.com/pages/jpmorgan/investbk/solutions/ssf

4. Where to from Here

To develop a robust social capital market and to provide the returns required to support the significant investment this market development will require, financing of the sector needs to move from a 'cottage industry' approach to a more coordinated and transparent market place.

This means encouraging and creating more commercial financial products and services tailored to the specific needs of the Not for Profit sector, and creating investment opportunities that attract capital from a wider source of potential investors.

This does not mean turning Not for Profits into businesses. It does mean creating solutions and providing capital in a professional and sustainable manner; the reasons for this include:

i) The more commercial the activity, the greater the specialist resources committed by commercial providers, because the business case will be there to support it

ii) The more commercial the investment opportunity, the quicker these opportunities will get to scale and achieve the desired outcomes

"Not all Not for Profits should grow significantly. Nevertheless, in instances where a social entrepreneurial model has shown results and has the infrastructure and plan to support growth, growth capital should be available to support what is working." (Michele Jolin, Innovating the White House, Stanford Social Innovation Review, Vol. 6 No. 2, 2008)

As capital becomes available more opportunities will arise for Not for Profit organisations to review their business models to place themselves in a better position to attract capital from commercial markets. Over time the diversity of social business models and impact investment opportunities will increase as this market matures. This process will also drive efficiencies within the community sector helping to fast track sustainability and community impact. As attractive social business models are rewarded with demand from investors, this will result in significant growth in capital available to the sector.

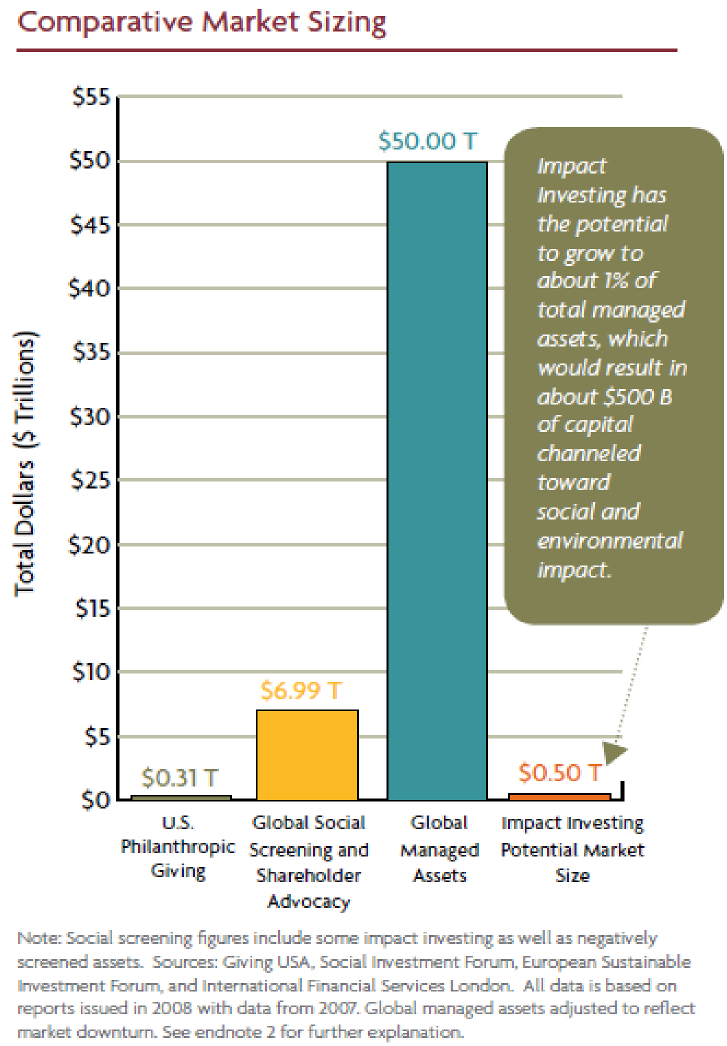
4.1. Tapping into commercial capital pools

Philanthropic capital pools are tiny when compared with the capital in commercial markets.

The Monitor Institute report[3] suggests that in 2008 US philanthropic giving was approximately US$300bn. In Australia, the equivalent amount is estimated to be AU$10bn. These numbers were in the context of global managed assets of US$50trillion.

If growing philanthropic capital markets was to be the major source of finance for the substantial needs of the Australian Not for Profit sector, the finance required to fund the organisations addressing arguably the largest and most significant social and environmental challenges that face our communities, would never be sourced.

As argued above, if we are able to encourage those participants best placed to provide capital to do so in the most sustainable way and to tailor existing offerings specifically to meet the needs of the sector, the capital available for these goals would increase substantially.



Source: Monitor Institute (2009)

4.2. What has worked – GoodStart Childcare Limited: a case study

In Australia, the recent 'GoodStart' transaction has rightly been heralded as a landmark social impact investment. A notable characteristic was the way different types of capital were sourced from different providers to achieve the overall funding requirement.

There were a number of other significant factors that contributed to the success of this transaction:

- The GoodStart consortium was well-placed to lead the transaction as it understood and was able to make the case for the social and economic benefits of the transaction. (In addition, some of the Not for Profit consortium participants and investors took on the role of intermediary by advocating for the transaction, bringing the skills an intermediary would have otherwise brought to position, transact and 'sell' this offer to the market.)
- The consortium was 'investment ready' in that it had the leadership, experience and skills to understand the market and organise the financial markets expertise to win a competitive bid for the assets against highly commercial competitors.
- GoodStart was able to bring together an appropriately experienced board, ongoing governance structures and a well-qualified management team to take the enterprise forward.

- The transaction required sophisticated hybrid investors who were willing to accept a discounted coupon in return for the ‘social dividend’ that had been explained and understood. This social dividend was represented by the discount that an equivalent investment would have been expected to generate.
- To get to scale, the transaction required a commercial investor, NAB, who committed debt capital on commercial terms as philanthropic and hybrid capital pools did not have the resources to provide the capital required.
- A major reason this transaction was successful was that those involved had significant understanding of the various capital markets – philanthropic, hybrid and commercial – and were able to price each tranche opportunity to achieve the desired outcome.
- GoodStart was able to work with Government to achieve the funding and other involvements required.

There are other examples in the Australian context that have not been as successful because either

i) the pricing was wrong for the particular market the offering was being pitched to, or

ii) the issuer lacked sufficient understanding of the motivations of those providing the capital, and what would attract them to accept a discounted return.

These examples provide a strong argument for the need of capable, well credentialed intermediaries who can understand the financing needs of this market and work to facilitate transactions with appropriate parties on suitable terms and conditions.

4.3. Opportunity for Government

The emergence of a range of ‘social impact bonds’ in Australia provides a timely opportunity for Government to take a new concept to scale quickly and as a cornerstone investor potentially play an important role in redefining the scale of social finance in Australia. If successful, this would provide crucial impetus in attracting new players and investment of resources into this activity.

This is particularly relevant given the alignment of the following key factors:

- Successful international precedent
- A growing awareness and engagement of investors to allocate capital to the Not for Profit sector
- Government appetite to develop this market
- Prevailing market conditions supportive of increased supply of appropriately priced ‘bond’ products

Traditionally, financing of the Not for Profit sector has been seen primarily from the perspective of the Not for Profit organisation.

International experience suggests one of the key drivers for the emergence of impact investment bonds is the involvement of Government which is constantly looking for funding solutions to address the challenges of financing ever growing social policy priorities in the face of increasingly challenging fiscal conditions.

In addition, the Global Financial Crisis (GFC) has provided challenges for Government in terms of supporting financial markets and institutions that are grappling with refinancing obligations in the face of these uncertain credit markets.

This is obviously a major focus of the Australian Government as ensuring a stable, liquid and well-funded financial system is fundamental to a strong and growing economy.

In addition, these difficult global conditions in financial markets are providing an increasing number of international and domestic, institutional and private investors who have an appetite for high yielding, highly rated Australian Government issued securities.

As the Australian Government looks to return to surplus in the next few years, liquidity of Australian issued securities could naturally be expected to decline. However, as the Budget papers 2011-12 outlined[4], the Government indicated it understood the importance of maintaining a liquid and efficient bond market for investors who require exposure to Government bonds for portfolio mandate reasons. The Government also recognises the significant value of maintaining a diversified investor base, including passive investors to absorb any unexpected increase in issuance. As such, various forms of social bonds could become an important tool of Government to assist in maintaining liquidity in this market.

These factors combined provide potentially attractive opportunities for Government which include:

- A framework to support the issuance of bonds that can finance the Not for Profit sector and associated infrastructure
- Tapping into private sector savings including international institutional investment markets to provide liquidity for the Australian bond market

4.4. Three types of social or impact bonds

There are three forms of 'social investment' bonds that could be utilised by Government as described above.

4.4.1. Infrastructure bonds

Infrastructure bonds are often unsophisticated, unrated, unsecured bonds issued to raise longer term physical infrastructure capital. The coupons on products brought to market to date have tended to be heavily discounted in comparison to commercial equivalents with the significant discount on the coupon being justified as an appropriate 'social' dividend.

By their nature, the distribution of these opportunities has been limited to investors that have a personal or direct connection with the entity raising the capital. To date, the offerings made in this category have struggled to raise capital from a wider group of potential investors.

Although several of the recent offerings have received a higher profile, it is worth noting this type of instrument has been used in private transactions for many years, and as such is a proven concept.

To the earlier point regarding making these opportunities 'as commercial as possible', issuers of this type of offering have called for the discount to be recognised and offset by some form of incentive, via other compensation such as offering a franking credit on the interest paid. Without such compensation the attraction of these instruments to a wider range of investors is likely to be limited.

As an aside, although not widely understood, for certain classes of investors (eg Private Ancillary Funds) the social discount can potentially be mitigated by an offset against other distribution obligations. (Anecdotal feedback would suggest this feature, applicable only to PAFs, is not widely understood.) From a policy perspective, to encourage the greatest impact, this 'return relief' for such investments would be most effective if provided on a product basis and not by class of investor.

Another approach the Government could consider to create 'relief' for the social discount, and to make this form of social infrastructure bond more attractive to a wider group of investors, would be to make the coupon tax-free. This could be regulated by limiting the ability to issue this form of instrument to those organisations with DGR status. Again this becomes a product-based feature rather than being offered to a limited class of investor.

If the price/coupon is competitive, these instruments could be then offered to the broader market. In addition, as intermediaries develop, a secondary market could develop along lines that are not dissimilar to the US municipal bond market.

This form of security may be then used by Government to provide liquidity in the Commonwealth Government Securities market in line with the objectives set out in the budget papers, and in line with calls from market participants to develop securitised debt markets in Australia.

[4] Budget Strategy and Outlook 2011-12 Budget Paper No.1 Statement 7 "Future of the Commonwealth Government Securities Market" http://www.budget.gov.au/2011-12/content/bp1/html/bp1_bst7-03.htm

4.4.2. Social impact bonds

Another form of 'social bonds' emerging in Australia have been described as social impact bonds.

The NSW government has been working on this concept in Australia following successful implementation internationally.

These instruments have been successfully used in the UK, and the US Government has recently instigated the $1bn Impact Investment Fund (see http://www.whitehouse.gov/omb/factsheet/paying-for-success).

Early indications suggest this type of instrument could develop into a meaningful funding pool to supplement or replace a wide range of government funding of social and environmental programs in Australia, as well as potentially providing an alternative funding source for Government funded research.

Although still very much at an exploratory stage in Australia, depending on the utilisation of Government guarantees and coupon offered, traditional investors in Government bonds may be attracted to this type of investment.

4.4.3. Arbitrage bonds

This form of bond, although proposed in several forms by JBWere Philanthropic Services, has not yet been used in Australia. However, we believe it has the scope to dramatically change the way certain social and environmental programs could be funded in this country.

Currently, demand for high yielding AAA rated Government paper in strong from both domestic and international investors, which provides the context for an instrument targeted to tap into this demand.

An arbitrage bond in its simplest form works as follows. This example makes the following assumptions about price and volume of issuance (note that these levels are indicative only):

	Quantum	Yield
Medium Term Note (MTN)	$500m	5%
Bank Securities Portfolio	$500m	7%

Stage 1

- Special Purpose Vehicle (SPV) is established and issues a ten-year Medium Term Note (MTN) guaranteed by the Government
- The SPV invests the funds raised by the MTN in a portfolio of fixed income securities issued by one of the major four Australian banks, but arguably could be extended to more for portfolio or other reasons

Stage 2

- The bank pays a coupon on the securities to the SPV
- From the proceeds, the SPV pays the coupon to the MTN investors
- The difference between the coupon earned on the securities paid on the MTN could be used to provide an annuity payment to the social organisation, program or research project that is the focus of this particular bond

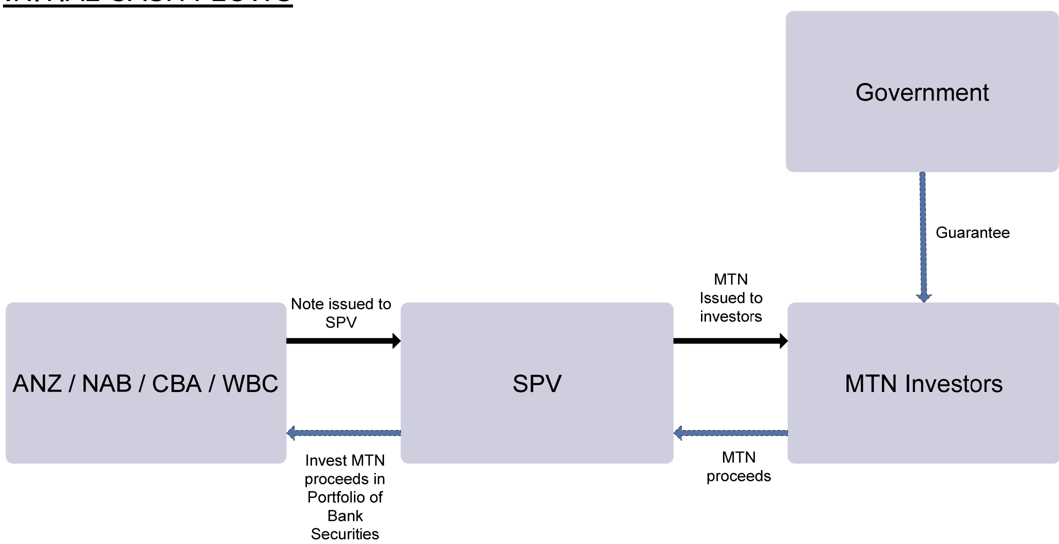
Stage 3

- At year ten (or other agreed maturity date), the securities are redeemed by the banks and the SPV issues the proceeds to repay the MTN
- The ultimate outcome being the tax pay is relieved of any repayment or funding obligation via this instrument

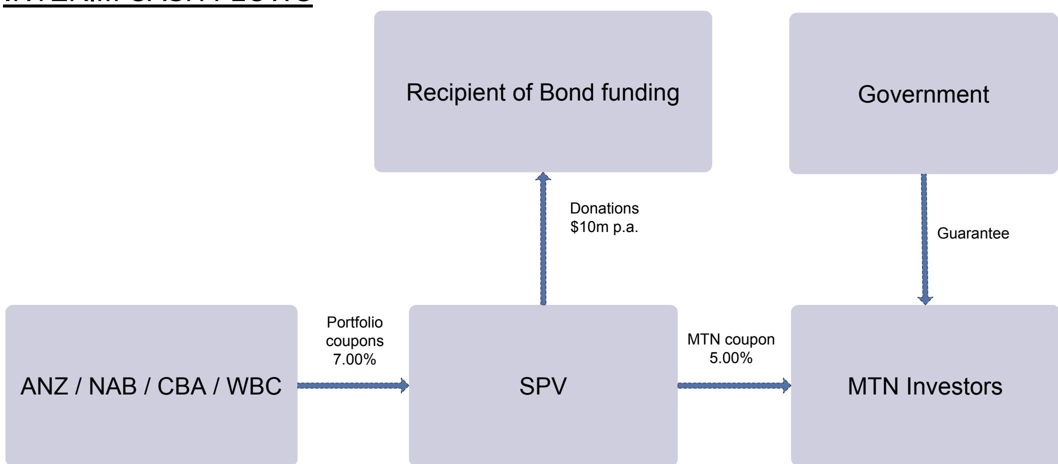
Refer to JBWere Arbitrage Bond – Conceptual Diagram below

JBWere Arbitrage Bond – Conceptual Diagram

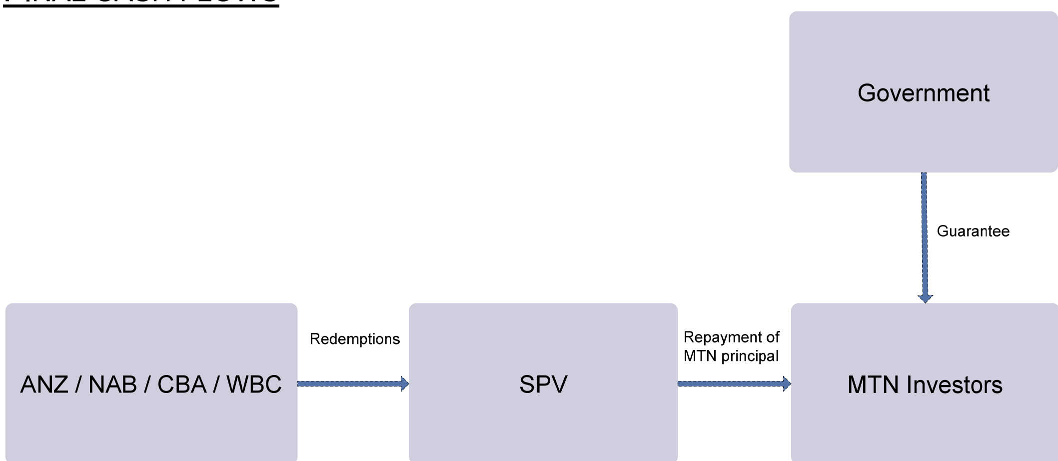
INITIAL CASH FLOWS



INTERIM CASH FLOWS



FINAL CASH FLOWS



Appendix 1.
Responses to Specific Issues the Inquiry raised as topics the Committee will examine

Government actions that would support the potential for social economy organisations involved in the delivery of government services to access capital markets

There are a number of specific initiatives the Government could consider to stimulate greater access to capital by Not for Profit organisations. These would include:

i) Government social debt instruments

Government plays an important role as an issuer in capital markets and thus in social capital markets has a natural role to play by facilitating the issuance of social investment opportunities for investors. Government acting as a reliable source of capital for Not for Profits on appropriate terms would provide an important catalyst for further impact investments as investors look take on more risk, be it social or financial. The implementation of government social financing instruments could include:

- **Government Social Debt** – issuing government debt to fund social enterprise
- **Government Guaranteed Securities –** government backing to provide confidence to investors
- **Government Seed Capital –** for Not for Profits looking to secure funding from capital markets, this government funding could help cover operating and transactional costs associated with developing a financial instrument, and provide confidence as a cornerstone investor.

"Government investments should not replace current funding streams, they should fill important gaps and catalyse funding by foundations, the private sector, and individuals" (Michele Jolin, Innovating the White House, Stanford Social Innovation Review, Vol. 6 No. 2, 2008)

ii) Government matched funding

For start up social investments the involvement of Government can add significant value and confidence by matching private investment or contributing as a participating investor.

This was utilised by the Commonwealth through the GoodStart Childcare investment in the ABC Learning Centres where it contributed a $15m loan to assist in the purchase. This assistance provided by the government, in this instance has:

- provided potential investors with confidence the government was supporting an innovative solution;
- the investment kept the centres running and care available to beneficiaries;
- helped to provide a solution that provided a social outcome, with the centres run with the view to providing sustainable and accessible education;
- the government is not out of pocket with the loan to be repaid.

iii) A risk rating system agency financial instrument

The government could fund an independent Not for Profit rating agency for impact investments, helping to provide transparency and accountability in the market, protecting and informing investors.

Independent evaluation of criteria for the rating agency could include:

- Social Impact
- Financial Return
- Risk

Such criteria could be used to derive a rating or a series of ratings under each heading to allow investors to be able to adequately compare investments and match them to their needs. Further information could be housed to include:

- Key facts
- Product promotional material
- Product Disclosure Statements or Information Memorandums
- Application Forms
- Information on suitable investors (i.e. retail or wholesale investors)
- Provided Details
- Links to the underlying Not for Profit's website

A rating agency could utilise **The United Nations Global Compact Principles for Social Investment (PSI)** as guiding principles. For organisations looking to engage in social investment – whether it be financial or not financial – they are encouraged to comply with the following PSI have principles:

- **Purposeful**: Purposeful social investment is grounded in a limited set of priorities about which the funder is knowledgeable and committed, and for which the funder is reasonably assured to play a positive role and does not negate or unnecessarily duplicate the efforts of other contributors.
- **Accountable**: Accountable social investors take responsibility for the intention and unintentional effects of their funding, and embrace the concepts of transparency and self-assessment.
- **Respectful**: Respectful social investment has due regard for the local customs, traditions, religions, and priorities of pertinent individuals and groups.
- **Ethical**: Ethical social investment is a reflective practice that employs only legitimate and constructive means in order to achieve its proper ends, in accordance with applicable laws and accepted international norms of behaviour.

Source: http://www.unglobalcompact.org/AboutTheGC/tools_resources/leaders_summit_2010.html

iv) Online Information for market participants:

Data collected as part of a risk rating system could also be used as an education and information portal for market participants. A portal for impact investing hosted by the Government or an independent ratings agency could support education of participants in the details of the impact investment market, by providing:

- Information on available investments
- Information on investment principles (risk, returns, diversity)
- Information on impact investing success stories
- Information for potential Not for Profits looking to access capital through financial markets

An online reporting mechanism of Not for Profit instruments could also provide assistance to Not for Profit organisations in selecting the most appropriate structures for their circumstances and provide insight into what has and hasn't worked for likeminded organisations.

v) Government reporting and research on impact investments

There is an important role Government could play in encouraging the funding of independent research into social investment to help encourage innovation and report back to the Not for Profit sector on how such investment is being used to access capital markets.

This could become increasingly important as market and products develop and the diversity of offerings and providers increases.

The ability to source and research international initiatives in social investment is also likely to help accelerate development of the domestic impact investment market.

vi) Promoting accountability and transparency in the Not for Profit sector

The move of Government to for the Australian Charities and Not-for-Profits Commission is a step in the right direction creating standards in terms of reporting, accounting and legislation governing Not for Profit organisations.

Capital markets will demand accountability and transparency on behalf of Not for Profit organisations as investors want to know what they are investing in. Creating a standard set of accounts for Not for Profit organisations would also assist in this process, enabling investors to compare apples with apples.

Incentives to support investment in this sector

"Government policy plays an important role in influencing the decisions that philanthropists and commercial investors make. Two of the most powerful tools that government policymakers wield are tax policy and regulation, each with its own point of leverage for spurring (or inhibiting) investment in the social space." (Chertok, Hamaoui & Eliot, The Funding Gap, Stanford Social Innovation Review, Vol. 6 No. 2, 2008)

Incentives used internationally

United Kingdom

Community Investment Tax Relief

A tax relief available to individuals and corporate bodies investing in accredited Community Development Finance Institutions (CDFIs), which then in turn provide finance to qualifying profit-distributing enterprises, social enterprises or community projects.

The tax relief available to the investor is five per cent per annum of the amount invested in the CDFI and may be claimed in the tax year in which the investment is made and in each of the four subsequent years.

Source: http://www.bis.gov.uk/policies/enterprise-and-business-support/access-to-finance/community-investment-tax-relief

United States

Community Reinvestment Act

The Community Reinvestment Act is intended to encourage depository institutions to help meet the credit needs of the communities in which they operate, including low- and moderate-income neighbourhoods, consistent with safe and sound operations. It was enacted by the Congress in 1977.

Source: http://www.federalreserve.gov/communitydev/cra_about.htm

Making better use of the sector's own financial capacity, including practices relating to purchases of products and services and use of reserve capital

The use of Not for Profit organisations reserve capital

Using the financial reserve capital of Not for Profit organisations to invest in impact investments should be approached cautiously. The surplus capital of Not for Profit organisations is increasingly being deployed in capital reserves which are invested and the income is used to fund recurrent expenditure. For many Not for Profit organisations, reserve capital income is the only source of income that is not subject to conditions placed by the funding party (ie Government or philanthropy). It is therefore important that this reserve capital is invested prudently to meet the risk profile, capital and growth requirements of each individual organisation.

Whilst some impact investments will be suitable for investment from Not for Profit organisations it is important that reserve capital is not exposed to undue risk in the pursuit of a social return. The ramifications of such actions would be to the detriment of the investing organisation and has the potential to negatively impact on their ability to deliver their primary objectives. It may also significantly impact their ability to raise funding from traditional fundraising sources.

Impact investments should only be utilised if they meet the risk parameters of the organisation and comply with the governance policies in place (i.e. investment policies, investment committee charters).

Some organisations may be in a financial position to justify taking on additional risk through an impact investment in order to leverage support from their existing supporters and to enhance their social outcomes.

Making better use of the corpus of philanthropy foundations and trusts to make investments in Australia's social economy organisations, expand socially responsibility investments and impact investments and any current barrier to their investment

Those charged with managing invested capital on behalf of philanthropic trust and foundations are obligated to investment in line with the statutory 'code of conduct' Prudent Person Rule found in each State and Territory's Trustee Acts.

All investments, whether they have a social impact or not, will have varying levels of risk associated with them. Therefore, different forms of impact investments will not be suitable for Trusts and Foundations as they provide an inappropriate balance of risk and return when considered in the light of the objectives of the trust.

In supporting the development of impact investments, consideration would need to be given to how such instruments are structured so as not to breach the obligations of trustees.

Focusing on foundations and trusts will exclude the majority of the market. Impact investments should be for all investors, including:

- superannuation funds
- trusts and foundations
- individual investors
- managed funds
- pension funds
- insurance funds
- common funds

If the supply of impact investment products can be built up to meet the needs of all investors then the social outcome of an impact investment market will be maximised. To do this the investments and professionalism of the market and its participants needs to hold up against traditional and existing non-impact investments.

Policies, practices and strategies that affect the availability of capital markets for social economy organisations on social innovation, productivity, growth and workforce issues in these sectors

Not for Profit accounting & reporting practices

In order for capital markets to be fully engaged, impact investments need to be subject to the same scrutiny that regular investments come under. Transparency and being subject to rigorous analysis will help to provide confidence to investors committing capital to these opportunities.

As previously mentioned the Government's move to create the Australian Charities and Not-for-Profits Commission will hopefully go a long way to standardising the reporting practices of Not for Profit organisations. Transparency and accountability through a standard set of accounts are essential for developing successful (determining value, pricing, risk, structure etc) investment instruments.

Attracting and retaining experienced personnel

"Beyond training a management team, even hiring the right people is harder in Not for Profits. Salaries in the Not for Profit sector are typically not competitive with those in the commercial sector, yet the need for management talent is just as great." (Silverman & Taliento, What Business Execs Don't Know – but should- About Not for Profits, Stanford Social Innovation Review, Summer 2006)

The Not for Profit sector faces considerable challenges in attracting and retaining experienced and qualified personnel. This is primarily because they are unable to match incomes paid to employees of their for-profit counterparts. This is obviously a particular challenge as developing and issuing financial instruments is often a complex task that requires the use of individuals with the appropriate skills. To date these skills have often been provided pro bono by individuals willing to donate their skills.

Intermediaries can be utilised to help alleviate this issue.

Not for Profit capital structures

There is little doubt that most Not for Profit organisations will want to access this new form of capital. However, for Chief Financial Officer's and Boards of Not for Profit organisations significant consideration will need to be given to their capital structure; as debt may not be sustainable for many organisations.

Whilst impact investment need not be limited to debt instruments, it is important that appropriate instruments are developed to meet the organisations needs without placing the entity under undue duress.

Measuring impact investments

A question that is raised time and time again in the Not for Profit sector is how does one measure social impact. This is an important when considering impact investments, where investors may be asked to give up financial return or take on extra risk in order to increase the social outcome. As previously mentioned an independent rating agency of peak body of the sought may help partially overcome this hurdle, though it is unlikely to completely resolve the issue.

Reputational risk of intermediaries & charities

Intermediaries are likely to play an important role in building a market for impact investments and making capital markets available to Not for Profit organisations. In doing this they will take on a large reputational risk as they put their brand names to untried, innovative and entrepreneurial instruments. For the Not for Profit organisations and investors participating there will be a similar reputational risk.

Government measures to encourage, support and back new initiatives will build confidence in investments which will help elevate concerns over reputational risk from both intermediaries, investors and Not for Profit organisations.

Avoiding a disjointed & sporadic approach

In the United States, the evidence points sporadic and disjointed successes in the impact investing space. For impact investing in United States of America "the industry remains beset by inefficiencies and distortions that currently limit the impact even in areas where impact investing should be viable (such as healthcare delivery, slum upgrading, agriculture development and educations)." (Antony Bugg-Levine, Impact Investing: Harnessing capital markets to drive development at scale, Beyond Profit, May/June 2009)

The government in the United Kingdom has played a key role in setting the agenda for impact investing and has put in place measures to encourage and support market participants. This initiative is likely to offset the distorted approach to impact investing seen elsewhere, and encourage a coherent market to form. This however has some years to play out before any concrete evidence will be available as to its success.

Appendix 2.
International Government & Peak Body Initiatives

Social Investment Task Force's (SITF)

The Social Investment Task Force (SITF) was established at the request of HM Treasury in April 2000 to carry out an urgent but considered assessment of the ways in which the UK could achieve a radical improvement in its capacity to create wealth, economic growth, employment and an improved social fabric in its poorest communities.

The SITF has continued to meet periodically to monitor progress and consider ideas to take the social investment agenda forward.

The SITF has released a series of reports over a ten year period, and in April 2010 release its final report, reviewing, what has been achieved and suggesting areas for further policy development

Source: http://www.socialinvestmenttaskforce.org/

Community Development Finance Association (CDFA) & Community Development Finance Institutions (CDFI)

A United Kingdom initiative the Community Development Finance Association (CDFA) represents Community Development Finance Institutions (CDFI), which provide loans and support to help people and businesses to create prosperity in their communities.

Most CDFIs operate within the United Kingdom's most disadvantaged communities. They provide loans and support to lend money to businesses, social enterprises and individuals who struggle to get finance from high street banks and loan companies.

Source: http://www.cdfa.org.uk/about-cdfis/what-is-a-cdfi/

Big Society Bank

In the United Kingdom, where the Government announced the establishment of the Big Society Bank, which will be funded by £400m from dormant bank accounts and will provide capital for the social sector.

Source: http://www.cabinetoffice.gov.uk/news/big-society-bank-could-back-social-isas-everyday-savers

The Global Impact Investing Network (GIIN)

The Global Impact Investing Network was begun in October 2007, culminating from the Rockefeller Foundation gathered a small group of investors to discuss the needs of the emergent impact investing industry.

Soon this international peak body organised a number of initiatives, including the creation of a global network of leading impact investors, the development of a standardised framework for assessing social and environmental impact, and a development of a working group of investors focused on sustainable agriculture in sub-Saharan Africa.

Source: http://www.thegiin.org/cgi-bin/iowa/home/index.html

Charity Bank

Charity Bank operates as a regulated charity and a bank in the United Kingdom with currently over £50m in deposits. Since the bank launch they have lent over £130m in loans of which £85m has been repaid to date and a loan default rate of just 0.5%.

Investment into Charity Bank can be made through acquisition of shares in the bank (dividends payable to charitable organisations only and no secondary market).

Source: http://www.charitybank.org/

Community Development Financial Institutions Fund

Formed under the United States Department of Treasury, the Community Development Financial Institutions Fund through monetary awards and the allocation of tax credits, the CDFI Fund helps promote access to capital and local economic growth in urban and rural low-income communities across the nation.

Through its various programs, the CDFI Fund enables locally based organizations to further goals such as: economic development (job creation, business development, and commercial real estate development); affordable housing (housing development and homeownership); and community development financial services (provision of basic banking services to underserved communities and financial literacy training).

Source: http://www.cdfifund.gov/what_we_do/

International product initiatives

International Finance Facility for Immunisation Bonds

The International Finance Facility for Immunisation's (IFFIm) inaugural bonds were issued in London on 14 November 2006 and raised US$1bn. The IFFIm saw an opportunity to utilise these country pledges to raise money in capital markets through a bond issuance to support and bring forward vaccination programmes. Since 2006 the bonds have been issued within the Japan, Australian, United Kingdom and Eurobond markets and have raised more than US$3bn.

Source: http://www.iff-immunisation.org/bond_issuances.html

Gray Ghost Ventures

Gray Ghost Ventures (GGV) is an impact investment firm dedicated to providing market-based capital solutions to entrepreneurs who are addressing the needs of low-income communities in emerging markets. Depending upon the need and opportunity, the organisations serves as creator and manager, sole funder, lead investor, co-investor, general partner or limited partner in operating companies or investment funds. GGV's focus areas include: microfinance, social venture investment and affordable private schools.

Gray Ghost Ventures has also created the Indian School Finance Company to provide capital to low-cost private schools across India, a significant and successful impact investment in its own right.

Sources: http://www.grayghostventures.com/about.htm
http://www.isfc.in/

Shorebank International

Shorebank International (SBI) started in 1988, SBI has delivered services and solutions that extend access to capital to un(der) served individuals, households and entrepreneurs globally. SBI current focuses on moving beyond access to credit to expanding the range of financial services and products for those who have difficult accessing banking services. This includes:

- designing and delivering savings products for low to moderate income people
- tapping new technologies to extend access to financial services and products
- exploring financial services to promote renewable energy and energy efficiency
- expanding access to housing finance, including traditional mortgages and housing microfinance;
- building successful small business banking units in the Middle East, Africa and South Asia, as well as in other parts of Asia, Eastern/Central Europe, Latin America and the Caribbean.

Source: http://www.sbksbi.com/

Root Capital

Root Capital is a Not for Profit social investment fund that is providing finance for grassroots businesses in rural areas of developing countries. The organisations provides capital, delivers financial training, and strengthens market connections for small and growing businesses that build sustainable livelihoods and transform rural communities in poor, environmentally vulnerable places.

Since the company launched in 1999, they have provided $256 million in credit to 320 small and growing businesses in 30 countries. They have maintained a 99% repayment rate from their borrowers and a 100% repayment rate to investors in Root Capital.

Source: http://www.rootcapital.org/

Not for Profit Finance Fund

Not for Profit Finance Fund (NFF) has been involved in the provision of millions of dollars in loans to Not for Profits and looks to improve how money is given and used in the Not for Profit sector. The fund has been in existence since 1980.

Source: http://nonprofitfinancefund.org/about-nff/what-we-do

Domestic product initiatives

GoodStart Childcare Limited

GoodStart is a partnership between four Not for Profit organisations which came together to purchased 678 Learning childcare centres from the insolvent ABC Learning Centres Ltd. This unique non profit alliance between Mission Australia, Benevolent Society, Brotherhood of St. Laurence and Social Ventures Australia raised $165m from a National Australia Bank loan, Commonwealth Loan of $15m, an estimated $2.5m from the participating Not for Profit organisations(subordinated notes) and an estimated $27.5m private capital (estimated to pay back a 12% annual coupon to investors).

Source: http://www.childcare.com.au/goodstart-childcare-limited

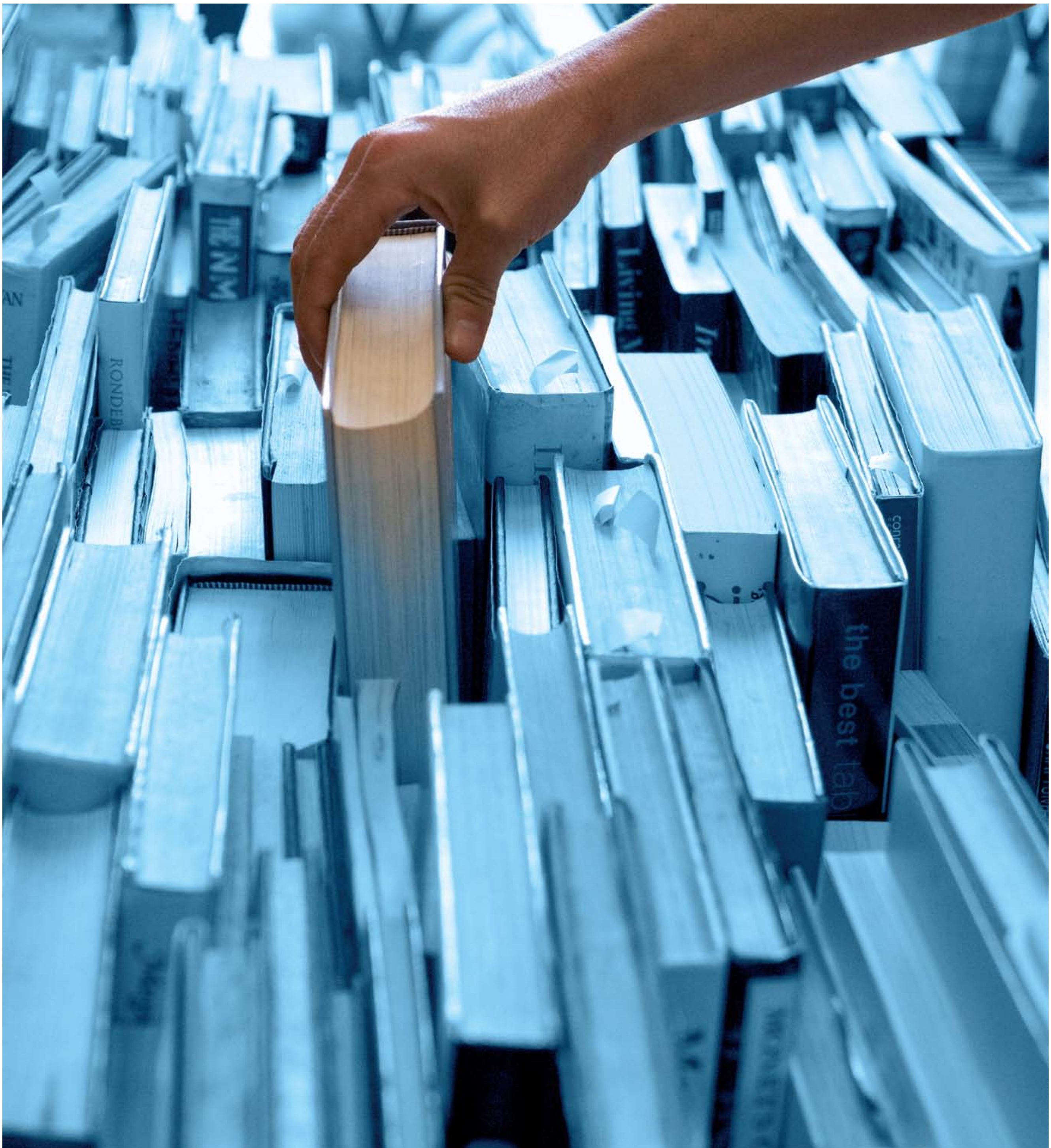
Hepburn Wind

Hepburn Wind will be the owner and operator of Australia's first community owned wind farm, at Leonards Hill, just south of Daylesford Victoria. Investment in Hepburn Wind will generate income through the sale of the renewable electricity generated by the wind farm. A total of $12,940,210 will be raised with an expected 9,507,441 shares to be issued at $1.

For shareholders there is an expected return of 6% in year one .

Source: http://hepburnwind.com.au/

Appendix 3.
What is Impact Investment?



JBWere

What is Impact Investment?

By Christopher Thorn

Over many generations there have been people willing and able to give. However, there haven't always been the mechanisms to make capital available for a social purpose. Arguably if this capital could have been made available in broader ways than via the traditional construct of 'philanthropic grants', we would have seen greater progress in addressing some of society's most pressing issues.

In the first half of the 20th century, Australia saw a surge of traditional foundations. Many were established as will trusts due to favourable tax treatment conditions and are mainstays of today's organised philanthropic sector.

More recently the JBWere Philanthropic Services team has witnessed a shift in preference to giving in one's lifetime via vehicles such as Private or Public Ancillary Funds such as the JBWere Charitable Endowment Fund. These vehicles have the potential to significantly change the nature and demographic of giving in this country. Their increased utilisation also reflects recognition from Government (through changes in legislation and tax advantages) of the importance of encouraging private funding to support the community sector.

Today we are witnessing the emergence of another exciting opportunity for Australians to support the community sector in the form of 'Impact Investment'. This opportunity is being built on the back of strong international precedent and experience.

'Impact Investment' is any investment that generates for investors a combination of financial and social return, where the intent of the investment is primarily for a social purpose. Primary intent is important in otherwise distinguishing a similar investment made predominantly for commercial return that may have the bi-product of a social return. By definition we are talking about a spectrum of investments that sit in a range between being purely philanthropic at one end of the spectrum and commercial at the other end. We refer you to the Monitor Institute report 'Investing for Social & Environmental Impact', published in 2009. A copy of the report can be found at **www.monitorinstitute.com/impactinvesting**.

'Impact Investment' facilitates actions to address social and environmental issues by providing access to capital pools not normally available for this type of activity. The creation of investment opportunities and other forms of intermediation with commercial capital markets has led to significant benefits being achieved for the community now and potentially mitigating the cost of such social issues going forward.

A social investor may be willing to take a lower than normal market return for the risk they are taking on, in return for generating a 'social' return that may not be measured in the same form as a traditional investment. It should be pointed out that 'Social Return on Investment' is also not a new concept. However, social investors are now becoming more comfortable in giving up part of their financial return in acknowledgement of generating this social return.

'Impact Investment' offers capital markets and/or social investors a different way to think about the 'social' value created over and above that of traditional measurement of investment return. It offers an opportunity for investors to support their community with funds they may not have been comfortable 'giving away' or that they had otherwise flagged for traditional investments. This additional source of funding is particularly important in times of uncertainty, as we have recently witnessed during the global financial crisis, when the demand for non-profit services was high but the willingness of individuals to part with capital was low.

'Impact Investment' has opened up 'new' capital markets to the non-profit sector. Industries like micro finance have seen significant growth via intermediation which has opened up access to capital beyond traditional grant funding to millions of those otherwise excluded from formalised capital markets. Another example of this access to deeper pools of capital for a community benefit is the International Finance Facility for Immunisation (IFFIm) Immunisation Bonds, a case study for which can be found below (see **www.iff-immunisation.org** for more information).

Over time, as 'Impact Investment' matures, we would not be surprised to see non-profit organisations evolve into stronger, more sustainable organisations. However, as 'Impact Investment' develops, so potentially will competition for capital amongst participants. This will create new challenges in how non-profit organisations work with other organisations, how they demonstrate the impact of their outcomes and whether they should even continue to exist or contemplate merging with other organisations.

We anticipate difficult and sometimes confronting discussions and decisions that we shouldn't shy away from. Social capital markets will demand efficiencies, accountability and transparency in non-profit organisations seeking funding. Such scrutiny may be a different experience from that which these organisations are currently used to from more traditional funding sources such as philanthropy or government funding.

Although challenging (and definitely not always the most appropriate funding source in all situations) such access to finance can be a positive stimulus to promote sustainability within the non-profit sector, breaching the gap between for-profit and non-profit.

'Impact Investment' has the potential to form part of any investment portfolio: be it a superannuation fund, personal investment portfolio, trust, charitable trust or managed fund. While it is not a replacement for philanthropy, nor the 'silver bullet' that solves every funding challenge, it does have the potential to complement and diversify the funding sources for non-profit organisations and allow supporters to further aid the community sector with capital otherwise not intended to deliver social outcomes.

Case Study **Immunisation Bond**

The Problem

Leading up to 2006, each year nearly 30 million infants born in developing countries weren't immunised against preventable diseases; more than 2 million would die on a yearly basis*. The provision of vaccines such as for hepatitis B, yellow fever and Hib, can help countries strengthen the fight against these preventable diseases. The most effective way to suppress these diseases is through mass vaccinations, something that required the sourcing of immediate and substantial capital.

The Initiative

European countries (United Kingdom, France, Italy, Spain, Sweden and Norway) had pledged various amounts of funding annually over a 10 year period. The International Finance Facility for Immunisation (IFFIm) saw an opportunity to utilise these country pledges to raise money in capital markets through a bond issuance. This innovative financial mechanism aimed to provide US$4 billion in disbursements between 2006 and 2015 to help protect more than 500 million children from preventable diseases through immunisation*.

Today the money continues to be raised in the capital markets, with the bonds to be repaid over a 20 year period, under the terms of legally binding agreements.

The bonds offer investors:

- competitive market rates;
- highly rated AAA bonds;
- backed by mostly AAA rated governments;
- a virtually zero-risk investment that also saves lives; and
- the comfort of Goldman Sachs and Deutsche Bank as the two lead managers for the inaugural bond issue.

According to the IFFIm the investors in the bonds include:

- central banks and official institutions;
- fund managers;
- pension funds;
- retail investor;
- banks; and
- corporations and insurance companies.

The Outcome

The IFFIm states that the bonds have raised more than US$ 3 billion*, with the bonds heavily over-subscribed. The financing plan accelerated contributions from donor countries, helping to bring 10 years of immunisation programs forward. This effectively locked in aid flows, which are usually erratic due to their dependence on annual budgets and political influence. The direct benefits seen through the bonds included:

- strengthening immunisation and healthcare delivery systems;
- boosting coverage with established vaccines (against diphtheria, tetanus, pertussis, tuberculosis, measles, and polio);
- introducing under-used vaccines where needed (hepatitis B, Hib and yellow fever);
- creation of a polio vaccine stockpile to protect against future outbreaks;
- ensuring immunization safety; and
- accelerating the development of, and affordable access to, priority new vaccines for developing countries (e.g. against rotavirus and pneumococcal disease).

By assuring stable, predictable and coordinated cash flows, the bonds look to help governments reach the nearly 500 million children that miss being immunised each year*.

The bonds demonstrated the power of capital markets to effect change in the community sector, helping to raise capital and bring forward change in an efficient, accountable and transparent manner.

* International Finance Facility for Immunisation

Information for this case study was sourced from **www.iff-immunisation.org**

About the Author

Christopher is the Executive Director of the firm's Philanthropic Services team, where his primary responsibilities include raising awareness of philanthropic issues, providing advice on investment and capital management to individuals and organisations wishing to implement a philanthropic strategy, and fostering relationships between interested parties in order to facilitate the giving process. Christopher has a long term interest in social finance and has participated in and hosted roundtables and forums on this topic. He also overseas research by JBWere's Philanthropic Services.

Christopher joined JBWere in 1984 and worked in Melbourne as a Retail and Institutional Adviser. In 1993 Christopher moved to New York as Vice President Institutional Sales. Upon returning to Australia in 1996 he was appointed Manager of JBWere's Queensland business, until returning to Melbourne in 2001. He was made a partner of JBWere in 1997.

Christopher has held a variety of senior management roles within JBWere's Private Wealth Management business, including business integration and strategy. In 2002, Christopher established the firm's Philanthropic Services division.

Christopher is a member of the Philanthropy Australia Council, Chairman of ShareGift Australia, the MLC Community Foundation Advisory Committee and the JBWere Charitable Endowment Fund Investment Committee, President of the Camberwell Grammar School Foundation and a member of the Centre for Social Impact Melbourne Advisory Council.

The JBWere Philanthropic Services team is committed to contributing to the ongoing development of the philanthropic and the non-profit sectors in Australia and New Zealand. Our team has been an integral component of JBWere's wealth management offering since 2001.

We work with individuals, families and businesses to help them develop and implement strategic philanthropy goals that meet their particular family, legacy, tax or financial situation.

We also work with non-profit clients on governance, on how to maximise investment outcomes and on how to appeal to donors. In further support of our clients, we conduct and compile research on best practice in the non-profit space and share these findings with our clients. Additionally, our team provides capacity-building seminars and events that provide educational opportunities for non-profit staff and board members.

To find out more about how the JBWere Philanthropic Services team can help you, please contact:		
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