SCOTTISH LAND COMMISSION
COIMISEAN FEARAINN NA H-ALBA

THE RANGE, NATURE AND APPLICABILITY OF FUNDING MODELS TO SUPPORT COMMUNITY LAND OWNERSHIP

SCOTTISH LAND COMMISSION
COIMISEAN FEARAINN NA H-ALBA

The Range, Nature and Applicability of Funding Models to Support Community Land Ownership

Authors: Duncan MacPherson, Faye MacLeod (Campbell Stewart MacLennan & Co), Josiah Lockhart (Firstport)

Acknowledgements: The authors would like to thank all those in the community landowning sector and those who support them who contributed their knowledge, experience and time that has enabled the development of this report.

This report should be cited as:

MacPherson, D., MacLeod, F., & Lockhart, J., (2019) The Range, Nature and Applicability of Funding Models to Support Community Land Ownership. Scottish Land Commission, Commissioned Report.

For further information on this project contact:
James MacKessack-Leitch
Scottish Land Commission, Longman House, Longman Road, Inverness, IV1 1SF
Tel: 01463 423 306

Contents

1 Executive Summary

This report was commissioned by the Scottish Land Commission (SLC) to scope the range of funding models available to, and being used by, community landowning groups.

The research is informed by the desire of the Scottish Government to make community landownership a normal option for communities across Scotland. Funding can be a barrier to achieving this goal and in an environment of limited public funding there is a need to consider alternative options.

The overall objective of this study was to scope the range of potential funding models that may be available to support community acquisition and development of land and building assets. In particular, the study was intended to inform the range of options available beyond direct government funding. The study was also intended to consider whether there are international examples of different ‘public interest’ finance models that could be applied to this context.

The study was conducted in the context of a rapidly growing community ownership sector, which is being promoted by Government policy through a combination of legislation and funding. The Scottish Land Fund is now in its third iteration with an annual budget of £10m per year for the period 2016-21. The Scottish Government reported that 403 groups owned 492 parcels of land totalling 562,230 acres in June 2017.

Methodology

The research work was undertaken in 3 steps:

- Identification of Models – the team sought to identify models over and above those identified in the brief for investigation through consideration of cases with which they were familiar; interviews with representatives of community landowners and representative bodies. The team also asked the representative bodies to encourage their members to participate in an on-line survey to which 70 responses were received. This process identified a range of non-public funding models available for use by community landowners in Scotland. One of the partners in the research, Firstport, used its international connections to identify a further 2 models that could be used in Scotland.
- Step 2: Assessment of Models – comprehensive semi-structured interviews gathered information on the funding models being used by community landowners, the advantages and disadvantages of each one and their acceptability to the community land sector. The interviews deliberately targeted groups who were known to have purchased and developed significant assets because of their ability to inform understandings of the benefits and disadvantages of particular models.

- Step 3: Development of Report – information gathered from researching the models and interviewing community asset owners were drawn together in order to:
  - Provide an overview of available funding options
  - Identify and distinguish actual and perceived constraints
  - Identify the appropriateness of particular models for particular situations
  - Propose actions for promoting and supporting alternative funding sources for community land and asset owners.
  - Identify regulatory constraints (e.g. OSCR) and those imposed by public agencies

Models

13 models are described which are currently available in the UK. These are:

- Charitable Funding
- Philanthropy
- Commercial lending
- Social Investment
- Lending in return for Guarantee of a Social Outcome
- Mutually Beneficial Arrangements between private and community businesses
- Private Investment
- Crowdfunding
- Community Shares
- Peer to Peer Lending
- Corporate Social Responsibility Funds
- Leveraging Assets Obtained by Nil Value Transfer
- Impact Bonds

The 13 models identified demonstrate that there is a wide range of options available to assist communities in the financing of their aspirations. Which model or combination of models to use in any situation will depend upon the particular circumstances of the community involved and of the development opportunity it is seeking to finance. Individual models are not mutually exclusive and a mix of models are often used by groups for financing projects.

Factors influencing Uptake

The fact that a particular model has been used does not indicate its wide acceptance in the sector or its applicability to a wide range of circumstances. In a number of cases the use of a particular model has been dictated or influenced by a range of factors including the non-availability of other models. The study identified seven factors influencing the choice of model:

- **Availability of Security.** Commercial lenders require security over assets in order to provide secured loans. This can be challenging for groups who have few assets, whose assets are of low value, or whose assets are not suitable for providing security (such as those in crofting tenure).
- **Availability of Capital.** Primary lenders will not lend 100% of required funding for a capital project as a rule. The borrower therefore requires to match fund this from other sources. Large community landowners with assets can use the capital sales and surpluses from income generating projects to invest. These options are much reduced or not open to owners of smaller assets.
- **Relative Availability of Types of Finance.** Community landowners as a rule seek public funding programmes first followed by charitable grants for funding either land purchase or project development. They will only then look to other funding models when public and charitable funding will not fund a project in full or in part, and if their own resources are insufficient to fill any funding gap.
- **Willingness to Take Risk.** Decisions to raise money via non-traditional and non-public funding models are taken by boards of directors. In order to consider these directors need to have a need, be aware of the opportunities and (in a number of models) be willing to risk their organisation's (and possibly their own) assets.
- **Capacity.** Organisations with a low capacity tend to be limited in their funding options to charitable giving, modest grant funding and (occasionally) philanthropic gifts. Organisations with a higher capacity can invest more resources in fundraising of all kinds and investigating options that are new to them.
- **Structure.** The majority of the organisations interviewed as part of this study operate as registered charities with trading subsidiary(ies) to undertake the activities that they are unable to undertake due to restrictions on charitable trading and/or they would like to safeguard the community owned assets from the potential risk of undertaking trading activities.
- **Investor Tax Relief.** The UK tax system offers various tax reliefs that are intended to encourage investment in UK businesses. In addition to the Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS) which are aimed at small to medium enterprises in the UK, an investment relief aimed at the social enterprise sector is also available in the form of Social Investment Tax Relief (SITR).

Three general factors influence the use of funding models:

- **National Policy Framework.** Government policy has played a significant role in the growth and development of land reform in Scotland and the sector continues to grow due to the continued political support provided by the Scottish Government. Whilst there was UK Government support for renewable energy, and in particular subsidies provided, community bodies in the Highlands and Islands of Scotland were able to benefit significantly from the development of renewable energy projects.

- **Support from Representative Bodies.** Representative bodies play an important part in mitigating the impacts of low capacity and increasing the capacity of their members. Interviewees spoke highly of the support given by Community Land Scotland (CLS), Development Trusts Association Scotland (DTAS), Community Energy Scotland (CES) and the Community Woodlands Association (CWA). The representative bodies have played an important role in developing and promoting the use of non-public as well as public funding models.
- **Support from Public Sector Bodies.** The public sector plays an important but variable role in promoting community land ownership. This variability occurs across time, geography and type of body.

International Models

The study has identified 2 models that are being used internationally that could be used in Scotland. These are:

- Founders Fund with a Repayment threshold
- Impact Investing with Social Return on Investment (SROI) Discount

In the first example repayments are only made after reaching a certain income threshold and in the second discounts are given on interest rates in return for certain social and environmental outcomes.

Conclusions and Recommendations

This study has shown that there are a wide range of funding models available to community landowning bodies. A number of community landowners have been innovative in their exploration and use of alternative models, helped by representative and public sector bodies.

Despite these success stories there is a widespread lack of knowledge on the true extent of the options available to community landowners.

When raising non-public finance communities logically seek those options which are easiest, cheapest and do most to keep local community control first. They then move on to models that are more complex, expensive and exert less community control in a form of hierarchy of descent. The exact model a group chooses depends upon a range of factors including the availability of assets to provide security, own capital, the relative availability of finance types, the willingness to take risk, capacity and structure of the organisation. In addition, the availability of representative body and public sector support provide context to the choices available.

Organisational capacity and willingness to take financial risk are important factors in determining whether an individual organisation will explore and use alternative financing models. High capacity organisations tend to be more entrepreneurial and use a wide range of financial tools, whereas low capacity ones will be much more conservative. The writers know from experience that the level of ability to understand and interpret financial information in many organisations is low. This is a significant barrier to good governance and the ability to make sound investment decisions.

The default setting for establishing a new community organisation is that of a charitable company limited by guarantee. This is not always the best model depending upon the type of business that the community is trying to develop.

To address the issues arising from this report we make the following recommendations:

1. Consideration should be given to making information on all funding models easily available to community landowners and development trusts. This could take the form of a website, book or booklet containing all the models, and flyers detailing each individual model.

2. Community groups should be given the opportunity to explore all of these models in a safe space. That would require information to be made available on each model and for the opportunities, constraints and risks of each model to be explained without any pressure being placed on groups to take them up taking into account financial as well as legal implications from the outset. A specialist funding conference, stands at specialist community networking events, and roadshows are all possibilities.

3. Support for broader thinking is needed across the sector in relation to finance. Community groups themselves, community advisers and professionals as a whole need to take the communities sector more seriously. They also need to consider from the outset some of the newer legal structures such as Community Interest Companies or Community Benefit Societies which have been created specifically to meet the needs of social enterprises as well as the more traditional Charity and Trading Subsidiary. This could assist groups in reducing the cost of administration and regulatory costs. As with recommendation one consideration should be given to making resources available in easily accessible formats to raise awareness of options.

4. Further research should be commissioned into alternative finance models. In particular the use of the 'Founders Fund with a Repayment Threshold' and 'Impact Investing with SROI Discount' models to establish how applicable they might be to community landownership in Scotland. A suitable approach may be to fund a research trip by representatives of DTAS/CLS/CWA/CES to see how these models are actually used by communities elsewhere.

5. There is a need for support to be delivered to communities beyond the acquisition of assets and in the first phase of development. There are many examples of targeted support by HIE for community groups requesting help, or where communities have been fortunate to obtain support for development posts, but not a universal support service that would in particular support communities to develop their board capacity and training as the sector continues to mature.

6. Consideration of the role of the forthcoming Scottish National Investment Bank in supporting community finance. In the year leading up to Autumn 2020, the Scottish Government will be establishing the Scottish National Investment Bank with a mission which includes investing in promoting inclusive growth through place-making and local regeneration.

With the emphasis on placemaking and a low carbon economy, we recommend that the Scottish Government consider inclusion of models of supporting community ownership through patient capital in the Bank's portfolio of programmes and products.

7. The tax system could be used more effectively to encourage greater levels of investment in the social enterprise sector. This could also encourage more investment into the community buyout and asset transfer market and for community asset development by providing specific tax incentives such as:

- Increasing awareness and refining the existing investor tax relief models ensuring that it is more easily accessed by social enterprises
- Higher levels of tax relief could be introduced for Social Investment Tax Relief to provide greater incentives to encourage investors to leverage more funding into the social enterprise sector
- Encourage use by the commercial arm of community organisations to access Enterprise Investment Scheme and Seed Enterprise Investment Scheme investment opportunities
- Capital gains tax relief for sellers on the gains generated on the sale of assets to community/charitable organisations within certain parameters
- Reduce the complexity of the VAT regulations with relaxation of the existing rules for community/charities, particularly in relation to land and buildings
- Providing greater levels of rates relief to community organisations beyond only registered charities
- Introducing a land value tax to encourage use of land and encourage more community use of the land
- Raise awareness of the benefits of gifting assets or cash to charitable organisations either during an individual's lifetime or as a legacy

2 Introduction

This report was commissioned by the Scottish Land Commission (SLC) to scope the range of funding models available to, and being used by, community landowning groups. The research is informed by the recommendations made by SLC to the Scottish Government in November 2018[1] to make community landownership a normal option for communities across Scotland. Recommendation 5 calls upon government to "Consider long term financial support beyond the immediate commitments to the Scottish Land Fund including capital and development funding". As part of the narrative of that recommendation the Commission recognises and welcomes the commitment of the Scottish Government to increasing community landownership through a range of public sector mechanisms; particularly through its commitment to the Scottish land Fund until 2021. However, it also states that the promotion of the community landownership should not be the sole responsibility of the public sector.

A new stakeholder group is in the process of being established to implement the recommendations. In order to inform the stakeholder group this research was commissioned to explore how alternative sources of community finance can be identified, promoted, and supported, and what can be done – particularly by public bodies – to enable such action.

2.1 Research Objectives

The overall objective of this study was to scope the range of potential funding models that may be available to support community acquisition and development of land and building assets. In particular, the study was intended to inform the range of options available beyond direct government funding. SLC expected these models to include, but not be limited to:

- Community shares
- Crowd-funding
- Peer-to-Peer lending
- Private investment and philanthropy
- Charitable funding
- Corporate Social Responsibility funds
- Commercial lending

[1] https://landcommission.gov.scot/2018/11/community-ownership-should-become-routine-option-for-communities-across-scotland-says-new-report/

The study was also to consider whether there are international examples of different 'public interest' finance models that could be applied to this context, for example lessons that could be drawn from conservation bonds, philanthropic giving and the social investment sector.

The study was to consider models of finance that could support both acquisition of land or buildings and subsequent development.

For each model considered, the study was to identify:

- A description of the funding model;
- The relative maturity of the model and examples of its application in the UK or internationally;
- Key governance implications of the funding model;
- Significant constraints and risks associated with the funding model;
- Commentary on its applicability to supporting community ownership of land and buildings.

2.2 Study Context

Community landownership is a rapidly growing sector of society and the economy which is being actively promoted by government policy. Successive Scottish Governments have passed several pieces of legislation to make it easier for communities to buy and own their own land.

The Scottish Land Fund is now in its third iteration with an annual budget of £10m per year for the period 2016-21. In its first 3 years it has made 123 awards to groups to buy land and buildings with a capital of value of £26,242,392 with capital grants of £21,434,085. Groups funded have subsequently levered in a further £17,550,186[2] in funding for post-acquisition development.

The Scottish Government reported[3] that 403 groups owned 492 parcels of land totalling 562,230 acres in June 2017.

The Development Trusts Association Scotland (DTAS) carried out a detailed members' survey in 2016 which reported that 220 members owned assets worth £89.4m and employed 751 people. Aggregate reported turnover was £50.3m with £21.1m (42%) of that being self-generated or trading income. A repeat survey this year is expected to show significant increases in turnover and self-generated income.

---

[2] This is likely to be a significant underestimate as some groups will only report on their funding success in End of Year reports

[3] https://www.gov.scot/publications/estimate-community-owned-land-scotland-2017/pages/1/

3 Methodology

The research work was undertaken in 3 steps and a brief summary of what was involved at each stage is set out below:

- Step 1: Identification of models
- Step 2: Assessment of Models
- Step 3: Development of Report

3.1 Step 1: Identification of Models

The brief identified the following models for investigation:

- Community shares
- Crowd-funding
- Peer-to-Peer lending
- Private investment and philanthropy
- Charitable funding
- Corporate Social Responsibility funds
- Commercial lending

At the start of the process the team sought to identify additional models for investigation through consideration of cases with which they were familiar; interviews with representatives of 14 community landowners and interviews with representative bodies Community Land Scotland (CLS), Community Energy Scotland (CES), Community Woodlands Association (CWA) and Development Trusts Association Scotland (DTAS).

The team also asked the representative bodies to encourage their members to participate in an on-line survey. For this purpose, Firstport used a data analytics tool incorporating an online form-building platform with a range of features that simplifies the process of building applications and surveys, data capturing and analysis. Seventy responses were received.

Interviews were also carried out with stakeholders with an interest in this area. This included lenders specializing in social enterprise such as Social investment Scotland as well as high street banks to find out if they were developing innovative models or were aware of others doing so. Support agencies including Community Enterprise and the Scottish Community Re:Investment Trust were also interviewed. Public sector groups who assisted included HIE and the Scottish Land Fund. The Office of the Scottish Charity Regulator (OSCR) was also approached to discuss whether there may be any prospect of altering regulations for the community sector to allow charitable organisations more latitude in financing and to limit the need for complex structures.

Firstport is co-located with Challenges Worldwide. Since 1999 Challenges Worldwide, have worked in over 40 countries across the world supporting people and enterprises to work together to help their community have better access to goods, services and money. As a strategic delivery partner of Firstport, Challenges Worldwide contributed their perspective and helped Firstport identify relevant international examples of community ownership in the countries they work in as well as comparing and contrasting funding models for post-acquisition development.

Additional models identified by the team prior to tender and as a result of this process include:

- Leveraging assets obtained by discounted/nil value transfer to raise finance
- Mixed versions of different models
- Lending in return for guarantee of a social outcome
- Mutually beneficial financial arrangements between private businesses and community-based organisations where funding can be provided to a community group by a private business in return for working collaboratively.

3.2 Step 2: Assessment of Models

The information required for step 2 was gathered as part of the same process for step 1. Comprehensive semi-structured interviews gathered information on the funding models being used by community landowners, the advantages and disadvantages of each one and their acceptability to the community land sector.

The interviews deliberately targeted groups who were known to have purchased and developed significant assets because of their ability to inform understanding of the benefits and disadvantages of particular models. The online survey attracted responses from a larger number of smaller asset owners (often single buildings) which has helped to produce a fuller picture of the sector as a whole.

Team members researched the models to:

- Assess the relative maturity of each model, by researching how widespread its use and acceptance is in the UK or abroad.
- Identify which models tend to be favoured in specific situations e.g. land purchase, stage of maturity of organization, capital/asset strength of community body, type of asset being developed.
- Identify what role public sector funding and support may have had in facilitating the uptake of specific models and whether any geographical variations in such support can be identified as influencing model adoption e.g. between local authorities or Highlands & Islands Enterprise/Scottish Enterprise areas of Scotland.
- Consider the implications it has for governance (including charitable status), constraints and risks (actual and perceived) associated with it.

- Make an assessment of its relevance. Team members considered issues such as those in the bullet point above, the cost of finance, the complexity of structures required, limitations of usefulness imposed by time constraints, and implications on security of land ownership in making this assessment.
- Consider the interaction between different funding models and to identify what reasons certain funding models have been investigated but not taken forward by groups

3.3 Step 3: Development of Report

Information gathered from researching the models and interviewing community asset owners were drawn together in order to:

- Provide a comprehensive overview of available funding options
- Identify and distinguish actual and perceived constraints
- Identify the appropriateness of particular models for particular situations
- Propose actions for promoting and supporting alternative funding sources for community land and asset owners.
- Identify regulatory constraints (e.g. OSCR) and those imposed by public agencies

These elements are illustrated with examples, either actual or hypothetical.

4 Models

4.1 Charitable Funding

Description

This model involves the raising of funding from charitable bodies who disburse grants and occasionally loans. Charitable funding can be sought in part or in full for particular projects. The process requires the completion of application forms which can vary in complexity and would normally require the applicant to provide a business plan where larger sums of capital or revenue funding are required. Charitable funders will give to other bodies where the applicant's project objectives align with that of the funder. Some will only provide funding to bodies who are registered charities themselves, whereas others will fund groups that are not registered charities but whose aims or specific project goals are considered to be charitable.

Maturity & Examples

This model is mature and has been used by a wide range of community landowners to purchase or develop land. The Directory of Social Change estimates that over £5bn/yr is available from the 2000 largest grant making trusts in the UK[4]. Charitable funding is commonly used to match fund public sector awards to supplement or complete a funding package. Charitable funding tends to be a small proportion of very large funding packages where there is an economic as well as a social impact but can comprise 100% of funding of smaller funding packages (typically less than £10,000), particularly where these are of a social or environmental nature.

Key Governance Implications

The restriction (or perceived restriction) of charitable funders to supporting only charities has encouraged many community groups to register as charities. This brings them under the oversight of the Office of the Scottish Charity Regulator (OSCR) which has the potential for compliance issues, particularly where groups are involved in economic development projects which are outside the activities that charities are allowed to undertake without jeopardising their charitable status,

Significant Constraints & Risks

The targeted nature of charitable funding acts as a constraint upon the range of activities that can be funded through this source. A significant proportion of charitable funders focus their support upon more disadvantaged groups within society or more disadvantaged areas of the country. Others are bound by their trust deed to only act within, or predominantly within, a particular geographical area. Access to the funds of

[4] https://www.dsc.org.uk/publication/the-directory-of-grant-making-trusts-201819/

grant making trusts is constrained by a lack of knowledge of their availability. Finding funding opportunities is easier than it used to be with online funding search tools available[5] but many groups are unaware of the funding opportunities available to them. Others may be aware of opportunities to search for funding but lack capacity or time to complete multiple searches and funding applications.

Risks are generally low with this form of funding. If the group accessing the funds spends them in accordance with the conditions of the grant there is little risk of being asked to return the funds, even where outcomes do not meet expectations. There is a risk however that groups that have access to significant resources of this nature become dependent on them. This can cause great difficulty if the source of funds is greatly diminished or terminates at any point in time.

Applicability to supporting community landownership

Charitable funding has been of significant assistance to supporting community land ownership, both for purchase of land and for its development.

The Isle of Eigg Heritage Trust, the Knoydart Foundation, the North Harris Trust and the Assynt Foundation all received significant support from environmental charities to purchase their land. A wide range of groups have accessed charitable funding for community, social and environmental projects.

4.2 Philanthropy

Description

This model involves the giving of money from a donor (private individual or corporate) to a beneficiary community to pursue social purposes. The boundary between what is perceived as ordinary charitable giving and philanthropic giving is a matter of some debate. For the purposes of this discussion giving is considered to be philanthropic by its size and/or its regularity over a long period of time.

Maturity & Examples

Philanthropy has a long history of wealthy benefactors in society supporting individuals, groups or causes that align with their own interests. In the community landowning sector there has been some history of certain groups receiving considerable donations.

Example 1: The Isle of Eigg Heritage Trust received a donation of £750,000 from 1 individual and were able to claim gift aid of £250,000 making £1,000,000 towards its appeal to purchase the island.

---

[5] See for example https://fundsonline.org.uk or https://fundingscotland.com

Example 2: In 2018 the North West Mull Community Woodland Company (NWMCWC) purchased the Isle of Ulva. Marketed at offers over £4m NWMCWC would have to find in excess of £200,000 in private sources to complete a funding package (assuming a Scottish Land Fund intervention rate of 95%). Lachlan Macquarie a former Governor of New South Wales who formally adopted the name of Australia for the continent was born on Ulva. NWMCWC therefore approached Macquarie Bank to see if it would make a donation to the community purchase of Ulva. The Macquarie Green Investment Bank arm of the Macquarie Group agreed to donate £500,000 towards the purchase and redevelopment of the island.

Example 3: One individual has given several thousand pounds to one community landowner in recent years because of his love of wild landscapes and his appreciation of the community's management of its landscape.

Key Governance Implications

Depending on whether conditions are attached to philanthropic gifts and the nature of those particular conditions will dictate whether there are any governance issues to be considered. The community group must ensure that the conditions do not compromise their agreed aims and objectives.

Significant Constraints & Risks

The primary constraint for this model is that it requires the alignment of interests of the philanthropic donor and the recipient community. The philanthropist requires to be satisfied that the purpose to which the money will be put agrees with their own particular interests. This is not dissimilar to the requirements of grant funders, but recipients may be completely unaware of the philanthropic opportunity, or once aware the criteria for making an award may be very opaque.

Applicability to supporting community landownership

Examples 1& 2 demonstrate that philanthropy can be highly applicable to community land purchase situations in specific circumstances. In example 1 the purchase of the Isle of Eigg would not have happened without the support of the principal donor. In example 2 the large donation enabled the purchase of the island without debt and has provided a capital sum for development. The provision of the £500,000 donation will have been taken into consideration by the Scottish Land Fund in its decision-making process. The lack of such a sum of money may have led to a different outcome in the award decision. Philanthropic giving can be critical in a time sensitive situation where an organisation has a limited amount of time to raise funds as there is a lot less, if any, due diligence required or restrictions imposed by the donor.

While philanthropic giving can play an important role in specific circumstances it is unlikely to play any role in the majority of community landownership scenarios. Most community purchases do not have specific social or environmental circumstances that will attract the attention of philanthropic givers. The normalisation of community landownership will lead to less publicity for any one community purchase proposal outside of the immediate area it affects and in an environment in which there are many acquisitions each year it makes it harder for individual voices to be heard.

Philanthropic giving could not fill the gap in public funding if for example the Scottish Land Fund were to close. This is demonstrated by the fact that when there was no Scottish Land Fund in the period 2006-2011 the number of community acquisitions dwindled. (See 6.3 below)

Inheritance tax can result in a significant level of tax becoming payable on a person's estate after death at a rate of 40%, which can be relieved by legacies being made to charity, and this could be more widely encouraged to assist the community landowning sector. Similarly, gifts to charities during an individual's lifetime by way of cash or assets can also result in tax relief which may mitigate a capital gains tax liability.

4.3 Commercial Lending

Description

Mainstream lending takes the form of overdrafts and loans which may be unsecured or secured. Unsecured lending tends to be for smaller sums and at relatively high interest rates. Secured lending can be for much larger sums and at lower rates than unsecured lending. While lending interest rates can be lower than some social investors, they are often secured against assets of the organisation and/or the assets of the company director/ charity trustees.

Maturity & Examples

Commercial lenders are happy to lend to community organisations as long as their due diligence of the business plan and financial projections stack up and meet their lending criteria and the project will deliver sufficient return to provide sufficient cover over the debt repayments required in a similar fashion required by a commercial borrower.

Example: One organisation where significant commercial lending has been used is the community landlord Sealladh na Beinne Moire, which owns 93,000 acres covering Eriskay, South Uist and part of Benbecula. An overdraft was provided by a commercial bank at the time of the buy-out to assist with cashflow and give the community time to complete its own fundraising target, and a further loan was taken to finance the purchase of a building for the organisation with a commercial bank. Another loan facility of £7.4m was provided by another lender to help fund a £10m windfarm project. These lenders have required significant levels of security to be provided to as part of the facility agreements.

Key Governance Implications

Mainstream banks provide access to loan and overdraft facilities to organisations of all types and almost any legal structure.

Governance risks for community land owners can be high due to the requested security, particularly when loans are secured against the directors/trustees directly. As with other types of borrowing, this route is only available if governing documents allow it, and the company must ensure it can service the debt through a sustainable business model and positive cash flow.

Significant Constraints & Risks

Commercial lending can require significant levels of security to be provided which may limit the organisation's ability to borrow further sums if it identifies subsequent projects without additional work and costs to renegotiate with the existing lender.

The borrower exposes the community organisation to all the risks associated with commercial lending and the assets of the organisation are exposed to a higher level of risk in a commercial lending situation.

Applicability to supporting community landownership

Although many offer specific charity and/or community association options, a number of commercial banks are currently exploring the specific needs of social/community enterprises. In the meantime, most community land owners use corporate or community banking facilities.

This model is particularly appropriate for financing projects that will develop a strong income stream as noted in the example above. In most cases it is not suited for the purchase of land without strong revenue streams because of the high value placed on land for non-economic purposes. However, where an asset is bought with a strong income stream it may be possible to finance borrowing costs, particularly where there is a proportion of grant funding in the package.

4.4 Social Investment

Description

Social Investment refers to investment from institutional investors (state-backed or private) with a specific remit to support community, social, and/or environmental outcomes. Predominantly issuing loan financing, these institutions measure portfolio performance in both financial and social outcomes. Examples of Social Investors in Scotland are Social Investment Scotland, Resilient, and Big Issue Invest. As the largest, Social Investment Scotland has invested £63m in over 300 organisations across the country.

Social Investors will often be more willing to work with communities who do not have the assets to secure against the financing.

Maturity & Examples

This is a growth area from a funding perspective with many examples of Social Investment Scotland in particular featuring in the funding models identified through this research. This funding does usually attract a higher level of interest and is often a means of closing a funding gap or covering short term cashflow shortfall, particularly where delays are encountered in the delivery of a project.

There are a number of examples of wind turbine projects taking a longer period of time to reach the stage of being operational which have benefited from SIS providing a bridging loan and done so in quite a short space of time as they have a good understanding of community projects and the funding challenges faced.

Key Governance Implications

In order to access social investment, trustees of community organisations have to ensure their governing documents allow them to take out loans.

Significant Constraints & Risks

Interest rates are generally higher than commercial lending rates with this form of lending which can make it more challenging to service debt.

As with any debt financing, there is an inherent risk to organisations who are unable to generate enough income to continue to service loan payments.

Applicability to supporting community landownership

For community landowners, this is a very relevant form of financing and, in many cases, is the first port of call after grant funding options have been exhausted.

4.5 Lending in Return for Guarantee of a Social Outcome

Description

This model involves the lending of money by one body to another in return for the promise of delivering an outcome favoured by the lender. The lending would normally be carried out on favourable terms (i.e. less than market rate or with an indeterminate date of repayment) for the borrower. The lender may or may not take security. It requires the purposes of the borrower and the lender to be aligned.

Maturity & Examples

This is a model that has been developed relatively recently within the social enterprise sector. It is relatively immature as its use is not widespread and knowledge of it as an option is very limited amongst both potential borrowers and lenders.

Example 1: The West Harris Trust (WHT) purchased a crofting estate from the Scottish Ministers in 2010. At the time it was not possible to source funding from the Big Lottery Fund to buy property that was already publicly owned. As part of the funding package local housing development agency Tighean Innse Gall (TIG) loaned £22,000 to WHT. One of WHT's key priorities was to release land for housing opportunities. Therefore, the loan was made on the condition that it would be repaid using income from the sale of house plots.

Example 2: In March 2019 the Assynt Foundation secured a six-figure interest-free loan[6] from Wildland Limited while it secures working capital from other sources.

Key Governance Implications

This form of lending does not require a particular form of company structure and therefore there are no significant governance implications.

Significant Constraints & Risks

The major constraint upon this form of lending lies with the willingness to lend or otherwise of a party with surplus funds. If a lender were to move from occasional lending to making it a core part of their business it would need to apply for a credit licence.

The key risk for the borrower is that of not having the ability to repay, as with any form of borrowing. This risk can be attenuated however by being able to borrow on more favourable terms than may be received from a commercial lender.

Applicability to supporting community landownership

In the right circumstances this model can be used to support both land purchase and development. The West Harris Trust example noted above enabled the community to purchase its land and proceed to develop it for community benefit.

4.6 Mutually Beneficial Financial Arrangements Between Private and Community Businesses

Description

Mutually beneficial arrangements between private and community businesses can range from the provision of rental premises by either organisation to the other on beneficial terms to providing loan arrangements, trading agreements or more complicated Joint Venture arrangements. The variety is only limited to the creativity and motivation of both parties to enter into arrangements which are mutually beneficial. The

6 https://www.pressandjournal.co.uk/fp/news/highlands/1695203/estates-help-from-danish-billionaire-to-protect-land-in-sutherland

significant feature of these mutually beneficial arrangements is that they are generally commercial in nature.

Maturity & Examples

There are a broad range of models that can be seen in practice with growth in the last ten years with the increase in community land ownership and groups looking to create financially self-sustaining community owned entities with commercial income streams.

Community ownership is generally looking to have socially and economically beneficial outcomes for local communities, therefore the provision of rental opportunities for businesses in the local area will deliver economic benefit for the community group as well as a secure income stream. Many of the larger estate buyouts include commercial tenants leasing business units, quarries, fish farm shore sites, piers etc which helps stimulate the local economy and provide employment. In the case of new business rental opportunities there can be a number of mutually beneficial arrangements created such as a rent-free period to help stimulate new businesses in the area, ensuring that rents are maintained at a fair level or offering a rent-free period in return for the tenant undertaking leasehold improvements and development of their unit.

In other circumstances communities can come to agreement with private companies who wish to access the resources of the community in return for providing up-front capital or loans that the community may be lacking.

Example 1: Comrie Development Trust has provided some business units with a rent-free period whilst the tenants were undertaking improvements at their own expense.

Example 2: North West Mull Community Woodland Company entered into an arrangement with a forestry management company whereby it provided loan funding to the group and took an enhanced management fee from the commercial arrangement for the sale of wood. This reduced the risk to the Woodland Company of commercial borrowing as it was linked to the sale arrangements for the wood.

Key Governance Implications

These arrangements are generally on a commercially trading basis and are usually undertaken by a subsidiary company of the community owned entity. This arrangement ensures that the company does not run into problems of exceeding the allowed trading limits for charities and also safeguards the community's assets from the potentially risky aspects of trading activities.

Significant Constraints & Risks

Mutually beneficial arrangements between communities and businesses can restrict the level of profitability achievable by the community through the often, increased cost of finance required by the business providing the finance.

The risk for the community and the business is due to the potential inability to repay, particularly if income is delayed or lower than anticipated from the commercial arrangement.

Applicability to supporting community landownership

There is scope for community landowners to significantly develop more mutually beneficial arrangements between both parties where the landowner has a commercial opportunity that they may not have access to the funding to take forward, or where they wish to limit their risk exposure by sharing the project with another business.

4.7 Private Investment

Description

Private Investment is generally characterised as funds given from a person classed as a High Net Worth Individual or a Self-Certified Investor to an organisation with the anticipation of a financial return either through loan interest or dividend. Although private investment by way of loan can be accessed by any type of organisation allowed to take on debt, Private Investors can gain social investment tax relief (SITR) on their investment if the community has set up a Community Interest Company, a Community Benefit Society with an “asset lock,” or a charity which can be either a company or a trust. Depending on organisations structure, private investments can be made either as loans or equity shares.

Relatively new, the SITR scheme was introduced in 2014 with less than 75 investments to date. As such, there are relatively few case studies related to community ownership. The added difficulty for community asset owners is that Social Investment Tax Relief is not eligible if the majority of trade of the company is dealing in land or property development.

Equity Investment through the SITR scheme, currently only applicable to Community Interest Companies limited by shares, brings the governance issue of having additional owners, sometimes from out with the community.

Despite this, a small number of community land owners have successfully accessed private investment through the SITR scheme.

Maturity & Examples

Private investment is the predominant source of funding for growth in capitalist societies. It is not widely used in the community land sector due to the desire to retain the benefits of ownership within the sector itself. However, it can unlock revenue streams that would otherwise not have been possible for a group with constraints on its own capital and borrowing options.

Example 1: With a lack of community space in the area, KLAS Care wanted to provide premises to provide childcare throughout the day as well as offer community groups, services and local people spaces to meet, engage and interact, which they have used to convert and renovate new premises - a disused janitor's lodging on the grounds of East Fulton Primary School. Set up as a community interest company, KLAS care was able to raise £170k to help renovate the property and start the enterprise.

Alongside a SITR investment from 4 private investors, the funds included £40,000 from Social Investment Scotland, and a grant from Firstport/the Big Lottery Fund.

Example 2: North West Mull Community Woodland Company entered into a joint venture with a turbine supplier for their community hydro project, with the supplier bearing significant capital costs in return for a share of revenues.

Key Governance Implications

In order for a community landowner to qualify for private investment, their governing documents (or those of a subsidiary) have to allow them to take on debt or issue shares.

Significant Constraints & Risks

As with any debt, this brings with it the risk of having to generate enough income to service the debt over time, which becomes harder the larger the loan gets.

Applicability to supporting community landownership

The model is applicable to community landownership in circumstances where investment is required, it is difficult or impossible to find from other sources and the community trusts the investor in question and is happy with the proposed deal.

4.8 **Crowdfunding**

Description

Crowdfunding is the practice of funding an organisation or project by raising money from a large number of people who each contribute a small amount without the promise of a financial return. Predominantly crowdfunding is performed through the use of online platforms such as *Crowdfunder*, *Kickstarter* and *Indiegogo*.

Maturity & Examples

With early platforms launched in the late 2000's, crowdfunding has become a common method for raising capital.

Example 1: Isle of Ulva Purchase- The North West Mull Community Woodland Company raised £37,224[7] from 546 supporters using a crowd funding platform.

Example 2: Although not a community land owner, Gorgie City Farm, a community enterprise manages four acres of land owned by the City of Edinburgh Council on a long lease. In 2016, when facing the need for restructuring Gorgie City Farm launched a crowd fund to re-capitalise the enterprise and invest in site infrastructure. Over a period of six weeks the community organisation raised over £100k through a mix of online platforms and a media campaign using print and social media.

Key Governance Implications

As there are no debt implications to crowdfunding, there is minimal governance risk to this method as income is generally treated as donations.

Significant Constraints & Risks

Organisations considering this route do need to consider fees charged by online platforms. Often, crowdfunding is seen as a one off and can rarely be achieved to the same level twice in succession. As such, anyone considering this method must time their crowdfund appropriately.

Applicability to supporting community landownership

Community land owners who can clearly define their community and assess the value of their "social capital" will find this a helpful method for raising initial funds for their project. It will not be possible to repeat this on a regular basis due to the limits of the generosity of donors.

4.9 Community Shares

Description

Enterprises that are established for community benefit sell shares to raise capital for businesses that deliver community benefit. The investors receive limited interest on the money that they lend to the business.

Maturity & Examples

There is a long history of community co-operatives raising working capital for community shops through this model. It has only recently come to prominence in Scotland as a way of funding renewables and other projects. Community Shares Scotland states that since

[7] https://www.justgiving.com/campaigns/charity/northwest-mull/ulvabuyout

2009 almost 100,000 people have invested over £100m to support 350 community businesses throughout the UK[8].

DTAS have worked for some time on developing the community share model and has been successful in obtaining approval by the Financial Conduct Authority for hybrid model rules that enable two classes of shares that allow the ability to have community representation for a nominal share value and also a separate share class designed to attract funding from larger investors.

Key Governance Implications

Community shares can only be issued by co-operatives and community benefit societies (Bencoms). Community landowners need to establish a Bencom either to deliver the project or to lend its raised capital to the landowning body or its subsidiary running the enterprise. Bencoms can be established with a requirement to donate all profits to the community landowning body.

Significant Constraints & Risks

In this model risk is transferred from the community body to the shareholder. There is no requirement for the level of due diligence that a mainstream bank for example would make a condition of its loan. However the prospectus for the share offer needs to clearly outline the opportunity and the risks for potential investors. There is a considerable risk of loss of community confidence if a business were to fail and local people were to lose their investment.

Applicability to supporting community landownership

A range of community renewable projects and community shops have been part or fully funded through these offers. In theory community shares can be used to fund any form of social enterprise.

4.10 Peer to Peer Lending

Description

Peer to peer lending is a form of lending that allows individuals to lend directly to other individuals or businesses without the use of a bank. The lending is conducted through specialist lending platforms on the internet. This form of lending offers opportunities to lenders to achieve higher interest rates than by placing money on deposit with banks. It offers borrowers the opportunity to borrow from alternative sources of finance which may be beneficial to their situation.

---

8 http://communitysharesscotland.org.uk/find-out-more/what-are-community-shares

Maturity & Examples

Peer to peer lending is now a well-established part of the market with a wide range of lenders. Lending of this nature in 2017 was estimated at £1.4bn to individuals and £2bn to businesses[9]. It does not however appear to have been used to any great extent by community landowners. None of the respondents to the online survey had used peer to peer lending. Of the interviewees Mull and Iona Community Trust are currently intending to raise £180k for Phase two of its Tobermory Business Park. Any shortfall to this target will be covered by a business loan from SIS.

Key Governance Implications

Trustees of community organisations have to ensure their governing documents allow them to take out loans.

Significant Constraints & Risks

The amount of borrowing that can be raised will be constrained by the lenders' perceived risk of the organisation and the project. This form of lending is unsecured and therefore risks lie with the lender.

Applicability to supporting community landownership

It has the potential to provide a useful alternative source of investment for community landowners.

4.11 **Corporate Social Responsibility Funds**

Description

Corporate Social Responsibility (also known as Environmental and Social Governance) covers the actions taken by companies to act responsibly towards their local communities, wider society and the environment over and above that required by law. Corporate Social Responsibility Funds may come from fixed annual payments or a percentage of profits from the company and can also include money raised by company employees acting as volunteers. These funds are disbursed locally and further afield to achieve social and environmental outcomes.

Maturity & Examples

CSR Funds are now commonplace, and a wide range of community and environmental groups access them.

Example: Lambhill Stables actively engage with a range of corporate clients looking to carry out corporate social responsibility activities. They earn £5-6,000 per year by

[9] https://www.statista.com/statistics/370647/lending-value-p2p-alternative-market

charging £35-£55/person/day for hosting volunteers. These range from one partner sending 10-15 people 2-4 times per year to another sending over 100 people once a year.

Key Governance Implications

CSR Funds should have no implications for governance.

Significant Constraints & Risks

The funds may be disbursed according to specific criteria as per grant funding programmes. They are often constrained to the specific community in which a company works and therefore will only be available to a limited number of community groups.

Applicability to supporting community landownership

They are likely to provide a modest but locally useful source of finance.

4.12 Leveraging Assets Obtained by Discounted/Nil Value Transfer

Description

In certain circumstances community landowners obtain assets for less than market value which can be a percentage discount from as little as 5% up to 100% where the asset has been acquired by way of a gift or for a nominal sum of say £1. This is a good opportunity for a community to obtain access to assets that they would otherwise require significant fundraising efforts to obtain.

Maturity & Examples

As community asset ownership has increased, there have been increasing number of estates and assets being gifted to communities, but the ability to use the value of the assets acquired for 'Nil' appears to be limited due to the often limited value of the assets in the first place due to limited asset value or opportunities to generate revenue or existing liabilities in relation the assets, particularly where the land is under crofting tenure.

The research identified examples of communities that have received assets as gifts for £1 but did not identify any that have subsequently raised finance using the asset as security. This was despite enquiring of local authority contacts and groups with wide knowledge of the sector such as DTAS. It is possible however that such examples exist in Scotland, particularly in relation to single buildings. The difficulty in finding examples is likely to be reflective of a general aversion to borrowing within the sector (see 5.4 below).

Comhairle nan Eilean Siar has a history of selling surplus assets such as former schools to community groups at discounted prices. While officers were not aware of any groups using these assets to leverage loans they were aware of examples of groups using the value of the land to leverage grant funding for development projects that required a community contribution from one or more funders.

The use of even modest discounts of say as little as 5% have been useful to communities in undertaking initial land purchases as the value of the discount can represent the community's own contribution and be sufficient to unlock Scottish Land Fund grant support for the acquisition.

Key Governance Implications

Any assets acquired by a community place responsibilities on the organisation for good stewardship and to use and develop those assets for the benefit of the community and this is still the case for assets acquired at a discount or 'nil' value. For the previous landowner disposing of an asset to a registered charity for 'nil' value or discount, they will benefit from eliminating or reducing potential capital gains tax on the sale of their asset which can make a charitable structure attractive.

Significant Constraints & Risks

Many landowners are looking to obtain a return for their assets and very few will be willing to transfer assets on the basis of a discounted or 'nil' value basis.

Whilst acquiring an asset for a discounted or 'nil' value can be attractive, the potential liabilities must be carefully considered to ensure that they are fully understood along with the potential related costs, which can increase risks for a community.

Applicability to supporting community landownership

The transfer of assets at a discounted or 'nil' value to communities creates a significant opportunity for greater levels of community land ownership for a minimal cost to the public sector and the communities themselves.

4.13 **Impact Bonds**

Description

Impact Bonds are a tool to help facilitate social, environmental, or community based impact through an impact investment model. Social/community Investors invest in a project at the beginning for a set period of time and receive payments based upon the results of the project. There are a number of versions of impact bonds, with Social Impact Bonds (SIBs) and Community Impact Bonds being the most common.

Maturity & Examples

Although not a commonly used model in Scotland, this model is frequently used across Europe both in public commissioning and at a small community based scale. The UK government and the National Lottery Community Fund have produced guidance[10] on Social Impact Bonds in the UK. There are around 30 currently in operation in the UK.

Example 1: Bridges Fund Management created the Bridges Social Impact Bond Fund[11] with a range of investors including Big Society Capital, European Investment Fund and The Prince of Wales's Charitable Foundation. This fund has supported almost 30 outcomes contracts, approximately half of which are in the UK. It provides working capital to Career Connect a charity supporting disadvantaged teenagers. If young people improve behaviour and attendance at school, gain qualifications and move on to further education or employment the Department for Work and Pensions Innovation Fund makes payments to the programme. In 2015 the programme was so successful that it became one of the first SIBs in the world to over-deliver against its social objectives and repaid all the loan capital (plus interest) to its social investors.

Example 2: – SITRA Social Impact Bond (Finland) – Occupational Well-being. In the SITRA model, Private and institutional investors invest into a SIB which in return uses the funds to commission 4 workplace health and wellbeing providers to provide services for public sector employees. Public sector employers than track the reduction in sick days across their workplace and pay 175 euros back into the bond for each reduced sick leave day. Capital and returns from these payments are then repaid to the original investors.

Key Governance Implications

In most cases, the organisation managing the bond commissions another to produce the social and/or environmental impact. Getting the legal structuring for impact bonds is key, especially where it is regulated by the Financial Conduct Authority.

Significant Constraints & Risks

Models of Impact bonds can often be complex and confusing and there are risks associated with communities not taking appropriate legal and financial advice to ensure their governance can appropriately manage a bond offer. Likewise, there are risks related ensuring the social and/or environmental performance are delivered in line with the bond offer.

Applicability to supporting community landownership

This is an under used mechanism for raising capital that community landowners should explore and, if structured correctly, provide an opportunity for communities and other

[10] https://www.gov.uk/guidance/social-impact-bonds

[11] https://www.bridgesfundmanagement.com/for-investors/bridges-social-impact-bond-fund/

organisations to invest in each other for fixed periods. It is a model that conceptually fits well with communities' aspirations in that it is outcomes based, rather than process-driven. Therefore, it can empower communities to be flexible in their approach to achieving desired outcomes and be tailored to meet individual community needs and cultures.

4.14 Summary

The 13 models identified above demonstrate that there is a wide range of options available to assist communities in the financing of their aspirations. Which model or combination of models to use in any situation will depend upon the particular circumstances of the community involved and of the development opportunity it is seeking to finance. Influences upon choice are discussed further in sections 5 & 6. At this point it is important to note that individual models are not mutually exclusive and that a mix of models are often used by groups for financing projects. Land has been bought with a mix of grant funding, crowdfunding and philanthropy. Renewables projects have been financed by a mixture of community shares, commercial borrowing and social impact borrowing. Construction projects have been and are being financed through a combination of grants, social impact lending and peer to peer lending. The uptake of individual models varies considerably but as the examples in this section have shown the ingenuity of community groups to devise innovative funding mechanisms is not in question. Appendix 1 uses a case study approach to illustrate how one community landowner, the West Harris Trust, used a number of the funding models identified here to purchase and develop its land assets.

The 13 models are summarised in the table below:

	Model	Description	Limitations	Suitable for
1	Charitable funding	Raising funds from charitable bodies who disburse grants and occasionally loans	Limited availability beyond registered charities or those who meet fundable activities criteria	Registered charities and other eligible organisations who align with funders objectives
2	Philanthropy	Giving of money from a donor (private individual or corporate) to a beneficiary community to pursue social purposes	Alignment of interests of the donor and the recipient community	Organisations with social or environmental outcomes which are important to particular philanthropists
3	Commercial lending	Mainstream lending in the form of overdrafts and loans (secured and unsecured)	Lender usually has security requirements and commercial lending can increase risk for a community group	Financing projects with a strong income stream and assets to offer as security
4	Social investment	Investment from institutional investors (state-backed or private) predominantly issued as loan financing	Interest rates are generally higher than commercial lending	Communities who do not have assets to secure finance against
5	Lending in return for guarantee of a social outcome	Lending of money by one body to another in return for the promise of delivering an outcome favoured by the lender	Willingness to lend or otherwise of a party with surplus funds	Funding support for communities with land purchase and development
6	Mutually beneficial financial arrangement between private and community businesses	Generally commercial arrangements between private and commercial businesses such as rental arrangements, loan or trading agreements	Can restrict the level of profitability achievable by the community through the often, increased cost of finance required by the business providing the finance	Community landowners with commercial opportunities where they may not have access to finance to take forward or can share risk

	Model	Description	Limitations	Suitable for
7	Private investment	Funds given from a person classed as a High Net Worth Individual or a Self-Certified Investor to an organisation with financial return through loan interest or dividend	Risk of having to generate enough income to service the debt over time	Where investment is difficult to source, an investor may be willing to lend for financial return
8	Crowdfunding	Raising money from a large number of people who each contribute a small amount without the promise of a financial return	Often seen as a one off and can rarely be achieved to the same level twice in succession	Community organisations where they can assess the value of their 'social capital'
9	Community shares	Enterprises which are established for community benefit sell shares to raise capital for businesses that deliver community benefit. The investors receive limited interest on the money that they lend to the business.	Can only be issued by co-operatives and community benefit societies. Risk of loss of community confidence if a business were to fail and local people were to lose their investment.	Community shares can be used to fund any form of social enterprise
10	Peer to peer lending	Peer to peer lending is a form of lending which allows individuals to lend directly to other individuals or businesses without the use of a bank. The lending is conducted through specialist lending platforms on the internet.	The amount of borrowing that can be raised will be constrained by the lenders' perceived risk of the organisation and the project	Alternative source of investment for community landowners

	Model	Description	Limitations	Suitable for
11	Corporate social responsibility funds	Corporate Social Responsibility covers the actions taken by companies to act responsibly towards their local communities, wider society and the environment over and above that required by law. Corporate Social Responsibility Funds may come from fixed annual payments or a percentage of profits from the company and can also include money raised by company employees acting as volunteers.	Often constrained to the specific community in which a company works and therefore will only be available to a limited number of community groups.	Locally useful source of finance for community groups
12	Leveraging assets obtained by discounted or nil value transfer	In certain circumstances community landowners obtain assets by way of a discount on the market value or by gift or for a nominal sum of say £1.	The potential liabilities must be carefully considered to ensure that they are fully understood along with the potential related costs, which can increase risks for a community	Opportunity for greater levels of community land ownership for a minimal or reduced cost to the public sector and the communities themselves
13	Impact bonds	Impact Bonds are a tool to help facilitate social, environmental, or community based impact through an impact investment model. Social/Community Investors invest in a project at the beginning for a set period of time and receive payments based upon the results of the project.	Models can often be complex and confusing and there are risks associated with communities not taking appropriate legal and financial advice to ensure their governance can appropriately manage a bond offer.	This is an under used mechanism for raising capital that community landowners should explore and, if structured correctly, provide an opportunity for communities and other organisations to invest in each other for fixed periods

5 Factors Influencing Uptake of Specific Models

The previous section outlined the wide range of financial models that community landowners have adopted or could adopt to deliver their objectives. They have shown themselves to be flexible, innovative and entrepreneurial in their approaches to financing. However, the fact that a particular model has been used does not indicate its wide acceptance in the sector or its applicability to a wide range of circumstances. In a number of cases the use of a particular model has been dictated or influenced by a range of factors including the non-availability of other models. This section explores those factors that have been identified during the course of the research from the subject interviews and the online survey.

5.1 Availability of Security

Commercial lenders require security over assets in order to provide secured loans. This can be challenging for groups that have few assets, whose assets are of low value, or whose assets are not suitable for providing security (such as those in crofting tenure). The ability to access secured lending therefore favours those community landowners that have valuable assets. These high value assets can range from large areas of land of low value to individual buildings on small parcels of land with high value. Low value sites in remote areas (typically island situations) can be hard to secure lending against because the cost of building may be greater than the open market value of the finished building.

5.2 Availability of Capital

Primary lenders will not lend 100% of required funding for a capital project as a rule. The borrower is therefore required to match fund this from other sources. Where grant funding is not available, not sufficient to fill a funding gap, or not sufficient to minimise borrowing to an extent that would be reasonably repayable the community group requires to supply its own capital. Large community landowners with assets that they can sell (e.g. house sites) can use the capital sales to reinvest in other projects and match fund borrowing requirements. Alternatively, they can use surpluses from income generating projects to invest in one project at a time as capital resources become available. These options are much reduced or not open to owners of smaller assets.

5.3 Relative availability of types of finance

As a general rule, community landowners seek grant finance as the first option for funding either land purchase or project development. Their first choice is public funding programmes followed by charitable grants, which often act as supplementary funding sources to public ones in completing a funding package. In doing so community landowners are acting rationally and reasonably by seeking to minimise cost to themselves and to receive public support for delivering public goods. They will only then look to other funding models when public and charitable funding will not fund a project in full or in part, and if their own resources are insufficient to fill any funding gap. The most common reason given in the online survey for not taking up other finance options was that the project had been funded from non-commercial sources.

Often the assets being taken on by a community group are no longer in use due to difficulties arising from the availability of capital and revenue funding being provided to local authorities and other public agencies and the communities face the same difficulties in taking on such assets and would not be in a position to do so without grant assistance.

Commercial Lending

A majority of the telephone interviewees had accessed commercial bank lending for commercial projects. In an era of low interest rates this is generally the favoured form of borrowing for those groups that are able to access it. The two most common types of projects funded were renewables and affordable housing.

Some interviewees expressed frustration that mainstream banks do not take charitable community companies seriously. There was a perception that they seem to struggle with understanding community-led enterprise and sometimes equate “charitable” with “amateurish”. A high proportion of interviewees who had borrowed had done so from Triodos or Charity Bank, indicating that mainstream lenders are difficult to engage for the community land sector.

Those who borrowed to deliver renewables projects found that the willingness of state-backed lenders REIF and SIS to commit funds was an important factor in convincing the primary lender to agree to fund the project with 1st ranking security. Mainstream banks initially struggled to understand the renewables sector and the guaranteed income that Feed-In Tariffs provided. Borrowers for these projects thought that due diligence was excessive, costing tens of thousands of pounds.

Lenders are easier to engage for lending on property because this is traditionally a strong focus of their lending and is the sector in which they have most experience and understanding. Borrowing for building or renovating housing is confined to a relatively small number of landowners who have either inherited housing stock or have started in a modest way to build new houses with assistance from the Rural & Islands Housing Fund.

Community Shares

The need to find match funding for bank lending or as an alternative to bank lending has led a number of groups seeking to use community share offers. The highest profile of these have been for community renewables projects with several raising many hundreds of thousands of pounds. In most cases these offers have been used to raise funds to match fund borrowing needs but there are cases where the share offer has been so successful that no borrowing has been required e.g. Applejuice (Applecross) Ltd raised £780k to install a micro-hydro scheme.

A key attraction for community landowners in using share offers is the prospect of greatly enhancing community buy-in to a project and of enhancing the sense of, and commitment to, community ownership locally. It also has the benefit of maximising the benefit to the local economy with interest payments being distributed within the community, rather than to remote investors in corporate lenders.

Those interviewed who had been involved in community share offers stressed that a huge amount of work needed to be put into preparing the share offer and promoting it, in order for it to be successful. Such a requirement favours groups with significant capacity (See 5.5 below)

The success of renewables share offers were due in part to generous interest rates (4-5%) and tax incentives (See 5.7 below). The principle behind share offers from Bencoms is that the rate offered should only just be sufficient to attract the resources required. Interviewees suggested that with the removal of certain tax incentives and more modest returns on renewables projects going forward it is likely that future offers will raise smaller amounts of funding. They also believed that communities would probably have scope for one successful share offer and that future ones would be less successful due to the limited savings available locally.

Other models

The primary purpose of communities taking control of land and assets is to maximise the benefit of their management and development to the local community. There is therefore an understandable reluctance on the part of communities to engage in joint ventures with private capital, because part of the profits from a venture will be lost to the community. If a community landowner can develop an enterprise from its own resources, or with the aid of resources that enable it to retain the surpluses (or profits) generated it will do so.

Where the community is unable to fund a project it has a choice: it can either not proceed with a project or seek to deliver it with the aid of external capital. Some groups will choose the former on principle and in the hope that circumstances will change in the future. Others will take a more pragmatic view and judge that part of a cake is better than no cake at all. There is not necessarily a right or wrong approach in any given situation but a choice to be made on the basis of financial return, level of community control, community acceptability, community benefit, and consideration of short, medium and long term timescales. Some of these factors add layers of consideration to a choice that would not necessarily be factors in private or corporate decision making.

5.4 **Willingness to Take Risk**

Decisions to raise money via non-traditional and non-public funding models are taken by boards of directors. In order to consider these, directors need to have a need, be aware of the opportunities and (in a number of models) be willing to risk their organisation's (and possibly their own) assets.

Of the 70 respondents to the online survey 27 stated that they had not considered any commercial funding models. Of these 10 gave the reason that they had no need and 13 that they either had made a policy decision not to borrow or were sceptical of taking on debt. Of those who had considered alternative funding models 8 stated that they had decided not to proceed because they did not want to take on debt.

5.5 Capacity

The capacity of an organisation depends upon the amount of officer/director time available and the skillsets (individually and collectively) of the personnel involved. Organisations can increase their capacity by learning from experience, training personnel, recruiting officers and directors with particular skills and through buying-in expertise in the form of specialist advice.

Organisations with a low capacity tend to be limited in their funding options to charitable giving, modest grant funding and (occasionally) philanthropic gifts. Organisations with a higher capacity can invest more resources in fundraising of all kinds and investigating options that are new to them.

The community land or asset owning sector in Scotland is relatively young in terms of its growth with the Land Reform Act in 2003 really having kickstarted the sector with support, particularly in the form of grants, having been focused on the acquisition of assets and development support for the first few years. Whilst there are often paid employees, these organisations are driven by voluntary boards who find themselves delivering significant financial projects which often result in communities taking responsibility for the delivery of services which were previously delivered by the public sector but without ready access to the staffing and resources of these organisations.

5.6 Structure

The majority of the organisations interviewed as part of this study operate as a Registered Charity with trading subsidiary(ies) to undertake the activities that they are unable to due to restrictions on charitable trading and/or they would like to safeguard the community owned assets from the potential risk of undertaking trading activities.

Charities are generally exempt from paying corporation tax on profits, and often this is cited as being one of the main reasons that community organisations have decided to register as a charity. Many community groups however are not generating much if any profit, particularly in the early days, therefore would not be paying corporation tax anyway and could delay registering as a charity until a much later point in the process once they can identify that charitable structure is indeed the most appropriate format for their organisation. This is likely to reduce the compliance costs associated with the preparation of charity accounts.

Many community organisations also cite that they can fundraise and obtain income in the form of donations as a registered charity. However, reviewing the accounts of such organisations reveals that a lot of community companies are receiving grant income that is not restricted to only being available to charitable organisations. The development staff of community organisations are also often so busy delivering specific projects that they do not have the time to fundraise in the way that had been originally anticipated.

There are restrictions on the level of tax-free trading that can be undertaken by a charity and it often becomes necessary for an organisation to create a trading subsidiary to undertake its social enterprise activities which are beyond the low level of trading activities permitted by a charity. This adds an additional layer of administration and compliance and additional costs that could be avoided by considering another legal structure that may be more agile and appropriate for a social enterprise rather than having two entities in the form of a charity and trading subsidiary.

As part of this research OSCR have confirmed that their position in relation to social enterprises remains as it has been in the past and that funds can only be used by a charity for development in very limited circumstances:

'The charitable purpose 'the advancement of citizenship/community development' does include urban and rural regeneration. In our recently revised Meeting The Charity Test Guidance, we say that 'to be charitable, a regeneration organisation will normally need to demonstrate that an area is in need of regeneration, and that its activities will cover a broad spectrum of regeneration work'.[12]

The guidance goes on to include the following examples of activities that could fall under regeneration:

- providing education, training and re-training opportunities and work experience, especially for unemployed people
- providing financial or technical assistance or advice to new businesses or existing businesses where it would lead to training and employment opportunities for unemployed people
- providing land and buildings on favourable terms to businesses in order to create training and employment opportunities for the unemployed'

[12] Email to Community Land Scotland from OSCR of 29 September 2015 and confirmed to Faye MacLeod by OSCR on 18 March 2019 as still the same position.

Community Interest Companies and Community Benefit Societies can be used as well as the charitable company structure. Community Interest Companies were introduced in 2005 designed to provide a model for social enterprises, whilst Community Benefit Societies serve the broader interests of the community. Both these models enable share/loan funds to be raised for the organisation whilst giving a return to those advancing the funds to the organisation. This is particularly useful where the projects being taken forward will generate sufficient income to cover the required interest payments but might not be able to fund the whole project through a commercial lender.

In the example of Sealladh na Beinne Moire, the 93,000 acre community owned estate of Eriskay, South Uist and part of Benbecula, they are simply a Company limited by guarantee with trading subsidiaries. Their Memorandum and Articles have been written in such a way that they could become a registered charity relatively quickly and this has been considered a number of times in the last 12 years. However, the scale of their operations, particularly the income from their 9.6MW windfarm and the fact that the organisation wishes to support economic development and to cross subsidise loss making parts of the Estate’s operations for the benefit of the community as a whole means that this would be difficult to do within the limitations of a charitable structure.

In the situation of Coimhearsnachd Barraidh agus Bhatarsaidh (Barra and Vatersay Community Ltd) the organisation is currently considering converting their charitable company to a Community Interest Company in order to reduce the regulation and cost of undertaking an annual group audit which results in additional costs of around £6,000 per annum which would not be necessary if they were a CIC. This organisation has a 1MW wind turbine which increases the company’s turnover thus requiring an audit on an annual basis.

It appears that there can be some difficulties encountered with commercial funders due to pre-conceptions that charities are amateurish and they can struggle to obtain commercial funding for this reason. Often the alternative loans they can access are at relatively high interest rates which significantly disadvantages this sector.

Many groups are advised from the outset that a registered charity will be the best option for their community aspirations without necessarily considering the organisation’s future activities and the potential restrictions that charitable requirements will place on the charity, particularly in terms of VAT. This is a complex area which is discussed further in Appendices 2(Legal Structure) & 3 (VAT).

5.7 Investor Tax Relief

The UK tax system offers various tax reliefs that are intended to encourage investment in UK businesses. The way in which tax relief is given, and the conditions that need to be satisfied, vary considerably. In the majority of cases, relief is only available for investment in a trading company, and shares will generally need to be held for a period of time to benefit from the relief. Another common condition is that where the investment takes the form of shares, they are in an unquoted company.

In addition to the Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS), which are aimed at small to medium enterprises in the UK, an investment relief aimed at the social enterprise sector is also available in the form of Social Investment Tax Relief (SITR).

SITR has been used in particular in relation to community share issues, but there is also an example of EIS and SEIS being used to attract investment to the commercial wind turbine project undertaken by Urras Oighreachd Ghabhsainn, although since EIS was accessed for this particular project, relief has been withdrawn for renewables projects. There is scope for these existing investor reliefs to be considered for other suitable commercial projects being taken forward by communities as a means of leveraging in further funding.

Appendix 4 provides a summary of the main features of these three investor tax reliefs.

6 General Factors Influencing Financing Capability

6.1 National Policy Framework

Government policy has played a significant role in the growth and development of land reform in Scotland and the sector continues to grow due to the continued political support provided by the Scottish Government in particular, so it has to be acknowledged that the sector will continue to be influenced by politics and funding models will also be impacted in a similar way. This is particularly apparent in relation to the UK Government's approach to renewable energy. Whilst there was UK Government support for renewable energy, and in particular subsidies provided, community bodies in the Highlands and Islands of Scotland were able to benefit significantly from the development of renewable energy projects. The subsequent reduction in support by the UK Government has resulted in most renewable projects not already in receipt of subsidy income no longer being financially viable.

6.2 Support from Representative Bodies

Representative bodies play an important part in mitigating the impacts of low capacity and increasing the capacity of their members. They do this through providing advice, sharing information and providing networking opportunities. They can also host programmes that promote government policies or schemes of relevance to their sector and have the ability to access people in positions of authority, whether in the public or private sectors.

Interviewees spoke highly of the support given by Community Land Scotland (CLS), Development Trusts Association Scotland (DTAS), Community Energy Scotland (CES) and the Community Woodlands Association (CWA). Their support was valued in the early stages of organisational life when new groups were unclear how to proceed. In more mature organisations they are still valued for providing important background information which feeds into decisions about managing and developing assets. Mature organisations also benefit from specific assistance to overcome barriers to project development. One organisation cited the assistance of CES in helping to address a planning issue that could have prevented a community hydro scheme from progressing.

The representative bodies have played an important role in developing and promoting the use of non-public as well as public funding models e.g. DTAS has received funding to deliver a programme to promote community shares and CES formerly delivered the Community and Renewable Energy Scheme (CARES) programme.

6.3 Support from Public Sector Bodies

The public sector plays an important but variable role in promoting community land ownership. This variability occurs across time, geography and type of body.

6.3.1 HIE/SLF Support

The variability across time and geography can be illustrated using data showing purchases since 1996, when HIE started supporting community groups to purchase land. In the period 1997-2001 there were 29 purchases in the Highlands & Islands and none in the rest of Scotland. During the period of the 1st Scottish Land Fund (2001-06) this rose to 141 with 3 times as many in the HIE are as the Scottish Enterprise area. The presence of the nationwide fund stimulated a large increase in community purchases across the country but with more than three quarters in the Highlands & Islands where HIE was able to match fund purchases in a way that SE could not do.

The replacement of SLF by Growing Community Assets (GCA) by the Big Lottery Fund for the period 2006-12 saw a steep decline to 44 purchases nationwide, showing the impact of the loss of a dedicated funding source and structure to support community landownership. The 4-year period of SLF 2 saw the trend reversed with 58 purchases but with more than two thirds of these in the HIE area. In the current iteration SLF 3 with an increased annual budget from £3m to £10m and an expansion to include urban areas the number of purchases has risen to 123 in a 3-year period. In 2017-18 purchases in the Scottish Enterprise area exceeded those in the HIE area for the first time.

It is important to note that HIE support has not been solely limited to funding for purchase of land. It has also played important roles historically in the provision of funding for development projects and in revenue support for Local Development Officers (LDOs) either working directly for community landowners or based in an area and available to them. In general interviewees were very appreciative of this support but expressed concern that reduced budgets and the significant scaling back of support for LDOs was leading to a significant loss in capacity.

6.3.2 Local Authority & Other Public Body Support

Support provided by local authorities can be very variable. Authorities with a high level of actual and potential community ownership such as Comhairle nan Eilean Siar (CnES) and Highland Council have provided financial help and officer support to purchase and development of assets on a systematic basis. Some authorities which have much less knowledge and experience of the sector are perceived by community groups to be considerably less supportive. Some comments received via the online survey spoke of the frustration of groups who wished to own their assets but were given a long lease instead by the local authority. Groups in a lease situation are likely to be much more constrained in their financing options than those who own property. The support offered by local authorities as a whole may improve over time with the impact of the Community Asset Transfer regulations. It is notable that the average discount on valuation of 23 local authority assets to date under CAT has been 38%. As was noted with HIE above the ability of LAs to provide financial support to groups has diminished significantly in recent years as authorities have had to retrench due to continued budget cuts.

The CAT provisions of the Community Empowerment (Scotland) Act 2015 also apply to a wide range of public bodies termed Relevant Authorities (RAs). All RAs[13] have a duty under Section 95[14] of the Act to produce an annual report by 30th June each year detailing information on a range of elements including the number of requests, their outcome, any action taken to promote the use of asset transfer requests, and any action taken to support a community body in the making of an asset transfer request. A review[15] of the reports for 2017-18 by Glasgow Caledonian University on behalf of the Scottish Government found that not all reports had been submitted, the purpose for which Asset Transfer Requests (ATRs) were made was not included in all reports and "Consideration of how to support and promote ATRs to marginalised groups was lacking across the majority of the annual reports." These findings indicate that a number of public bodies have a considerable amount of progress to make in providing a supportive environment to communities wishing to own assets. More positively the report highlighted that a number of RAs highlighted capacity building for staff on ATR processes and there was a good example setting ATR support within the broader approach of the authority to participation and engagement.

---

13 http://www.legislation.gov.uk/asp/2015/6/schedule/3/enacted

14 http://www.legislation.gov.uk/asp/2015/6/section/95/enacted

15 https://www.gov.scot/publications/independent-evaluation-of-community-empowerment-act-parts-3-and-5-interim-findings/

7 International Models Not Yet Used in Scotland

International financing models which are not frequently used in Scotland for community ownership largely fall into two general types, democratised finance and future oriented finance. In addition, many of these models incorporate some measure of social and/or environmental measurement in order to articulate a double, or often triple, bottom line.

In Democratised Finance, people are given control over how their assets (e.g. land, buildings, financial capital) are leveraged and invested. More familiar models in this category include community shares, credit unions, and peer to peer micro lending. In some countries this model has been expanded to include community owned loan deposit guarantee schemes (First Nations Market Housing, Canada), new insurance schemes to empower co-ownership of transport (Sharing Economy Insurance, Canada), and alternative currencies to translate social and civic capital into usable currency (Wara, Germany).

Future Oriented Finance, on the other hand, is based upon converting future savings on social and/or environmental health budgets into long term patient capital invested today. The most common model this is social impact bonds. There are, however, alternative models in operation across the globe including an insurance fund protecting coral reefs in Mexico paid for by tourist operators in the area (Reef+Beech Insurance Fund), the introduction of Climate Smart Agriculture metrics to agriculture investment management in Kenya, and a property upgrade company in the USA financing environmental upgrades financed through future savings on insurance premiums (My Strong Home).

Although there are hundreds of methodologies for measuring social and environmental impact, three of the leading measures are Social Return on Investment, Global Impact Investment Ratings System (GIIRS), and the B Impact Assessment.

Two financing models currently underused in Scotland, which could offset both concerns of communities as well as introducing evolved types of capital are described below.

7.1 Founders fund with a repayment threshold

Description

Some global impact investment funds base repayment holidays and implement variable interest rates based upon annual turnover of community/social enterprises. For example, an organisation could be granted a repayment holiday until they reached a threshold of £100k turnover at which time they would begin repayments at a low interest rate. As their turnover grows above £500k their interest rate would grow at an agreed ratio. In this manner the affordability of the loan is based upon the health and stability of the organisation.

Maturity & Examples

Although common method of investment international the tech sector and universities, this method is not frequently used in the UK. It is, however, similar to how student loans are administered.

Key Governance Implications

As with any debt financing, there is an inherent risk to organisations who are unable to generate enough income to continue to service loan payments. Organisations also need to ensure their governing documents allow them to take on debt.

Significant Constraints & Risks

There are significant risks in this model for both investors and organisations. Although this often gives companies a longer repayment holiday and lower initial interest rate, as the turnover of a company grows the interest rate can grow higher than commercial rates. Likewise, investors need to manage a risk around investees never crossing the repayment threshold.

Applicability to supporting community landownership

This type of impact investment could provide a viable alternative to other funding models for community ownership as it allows the community organisation is given longer to reach sustainability.

7.2 Impact Investing with SROI discount

Description

Some global impact investment funds employ a social accounting method to discount the capital repayment based upon a social return, potentially reducing the overall total repayment of debt. Methodologies for measuring the financial value of impact often follow the Social Return On Investment (SROI) model. SROI, a model standardised by Social Value UK[16], is a social impact measurement tool that measures social value and applies a financial value proxy metric for each type of social impact (e.g. £30k for each job created).

Maturity & Examples

Currently not a common example in Scotland, a number of international investment funds, primarily in Europe and the USA, employ this method.

Example: Rabobank Impact Loan. Currently delivering an Impact Loan programme in partnership with the European Investment Bank, Rabo bank manages a 250 million euro

[16] http://www.socialvalueuk.org

facility for SMEs in the Netherlands selected for quality marks for environmental and social performance.

In the Impact Loan, the interest rate discount is described as both “a reward for frontrunners in sustainability and an incentive for them to keep up the good work.”

For a business to qualify for an impact fund, they must have less than 3000 employees and possess one of the 47 quality marks (i.e. Forest Stewardship Certification, Cradle to Cradle, Demeter, etc…)

Key Governance Implications

As with any debt financing, there is an inherent risk to organisations who are unable to generate enough income to continue to service loan payments. Organisations also need to ensure their governing documents allow them to take on debt.

Significant Constraints & Risks

Organisations considering this route need robust impact measurement systems as well as matrixes to define social return on investment. Without a formal system that can translate social and/or environmental impact into a financial figure this type of investment does not work.

Applicability to supporting community landownership

This type of impact investment could provide a viable alternative to other funding models for community ownership as it not only has a potential discount on total loan value, but also encourages community landowners to focus and develop social and environmental impact.

8 Conclusions & Recommendations

This study has shown that there are a wide range of funding models available to community landowning bodies. A number of community landowners have been innovative in their exploration and use of alternative models, helped by representative and public sector bodies. Cumulatively they have raised tens of millions of pounds in external finance to deliver significant revenue streams and social benefit to their communities.

Despite these success stories there is a widespread lack of knowledge on the true extent of the options available to community landowners. It is commonplace for community trusts to learn of individual models by word of mouth from a neighbouring trust or wider networking opportunities. Such mechanisms are highly valuable but highlight the fact that there is no single place that communities can go to identify what combination of models may be best suited to their own circumstances.

When raising non-public finance communities logically seek those options that are easiest, cheapest and do most to keep local community control first. They then move on to models that are more complex, expensive and exert less community control in a form of hierarchy of descent. The exact model a group chooses depends upon a range of factors including the availability of assets to provide security, own capital, the relative availability of finance types, the willingness to take risk, capacity and structure of the organisation. In addition, the availability of representative body and public sector support provide context to the choices available.

Two additional models have been identified that are being used internationally but not in Scotland to date. This study was not able to study these in depth, but they appear to offer additional financing options and are worthy of further investigation.

Organisational capacity and willingness to take financial risk are important factors in determining whether an individual organisation will explore and use alternative financing models. Capacity is determined by the combined skills and knowledge of the directors/trustees and staff. High capacity organisations tend to be more entrepreneurial and use a wide range of financial tools, whereas low capacity ones will be much more conservative. The writers know from experience that the level of ability to understand and interpret financial information in many organisations is low. This is a significant barrier to good governance and the ability to make sound investment decisions. Many community organisations look to minimise the use of external professionals where possible to minimise costs, and in particular viewing accountants as necessary simply to fulfil annual compliance requirements. However, there is a need to develop more financial advisory support from the accountancy profession beyond simply preparing annual accounts and tax returns to better support community organisations. This will require communities to seek advisory support on an ongoing basis (at a reasonable cost) and encourage the accountancy profession to view the communities and charities sector as a genuine growth area of business which is not simply looking for free support.

The default setting for establishing a new community organisation is that of a charitable company limited by guarantee. This is not always the best model depending upon the type of business that the community is trying to develop.

8.1 Recommendations

To address the issues arising from this report the following recommendations have been identified:

1. Consideration should be given to making information on all funding models easily available to community landowners and development trusts. This could take the form of a website, book or booklet containing all the models, and flyers detailing each individual model. This could potentially be done along the lines of a partnership model between the Scottish Government and one or more representative bodies that has been used successfully for other initiatives.

2. Community groups should be given the opportunity to explore all of these models in a safe space. That would require information to be made available on each model and for the opportunities, constraints and risks of each model to be explained without any pressure being placed on groups to take them up taking into account financial as well as legal implications from the outset. A specialist funding conference, stands at specialist community networking events and roadshows are all possibilities.

3. Support for broader thinking is needed across the sector in relation to finance. Community groups, community advisers and professionals as a whole need to take more seriously the communities sector. They also need to consider from the outset some of the newer legal structures which have been created specifically to meet the needs of social enterprises such as Community Interest Companies or Community Benefit Societies as well as the more traditional Charity and Trading Subsidiary. This could assist groups in reducing the cost of administration and regulatory costs. As with recommendation 1 consideration should be given to making resources available in easily accessible formats to raise awareness of options.

4. Further research should be commissioned into alternative finance models. Particularly the use of the 'Founders Fund with a Repayment Threshold' and 'Impact Investing with SROI Discount' models, to establish how applicable they might be to community landownership in Scotland. A suitable approach may be to fund a research trip by representatives of DTAS/CLS/CWA/CES to see how these models are actually used by communities elsewhere.

5. There is a need for support to be delivered to communities beyond acquisition of assets and in the first phase of development. There are many examples of targeted support by HIE for community groups requesting help, or where communities have been fortunate to obtain support for development posts, but not a universal support service that would in particular support communities to develop their board capacity and training as the sector continues to mature.

6. Comprehensive efforts should be made to ensure that there is a supportive environment across all public bodies for normalising community ownership. The Scottish Government should engage with COSLA and local authorities to identify and promote best practice within local authorities (including their ability to lend surplus funds to community landowning groups). The Scottish Government should further engage with all Relevant Authorities under the Community Empowerment Act to ensure that they fulfil their reporting obligations under the Act, and to identify and promote best practice in dealing with Asset Transfer Requests.

7. Consideration of the role of the forthcoming Scottish National Investment Bank in supporting community finance. In the year leading up to Autumn 2020, the Scottish Government will be establishing the Scottish National Investment Bank with a mission which includes investing in promoting inclusive growth through place-making and local regeneration.

With the emphasis on placemaking and a low carbon economy, we recommend that the Scottish Government consider inclusion of models of supporting community ownership through patient capital in the Bank's portfolio of programmes and products.

8. The tax system could be used more effectively to encourage greater levels of investment in the social enterprise sector. This could also encourage more investment into the community buyout and asset transfer market and for community asset development by providing specific tax incentives such as:

- Increasing awareness and refining the existing investor tax relief models ensuring that it is more easily accessed by social enterprises
- Higher levels of tax relief could be introduced for SITR to provide greater incentives to encourage investors to leverage more funding into the social enterprise sector
- Encourage use by the commercial arm of community organisations to access EIS and SEED investment opportunities
- Capital gains tax relief for sellers on the gains generated on the sale of assets to community/charitable organisations within certain parameters
- Reduce the complexity of the VAT regulations with relaxation of the existing rules for community/charities, particularly in relation to land and buildings
- Providing greater levels of rates relief to community organisations beyond only registered charities
- Introducing a land value tax to encourage use of land and encourage more community use of the land

- Raise awareness of the benefits of gifting assets or cash to charitable organisations either during an individual's lifetime or as a legacy

9 Appendices

9.1 Appendix 1 – Case Study

Sections 4, 5 and 6 considered the range of models available and the specific and general factors affecting community landowners' ability to use these models. The following case study illustrates how these factors interact in the case of one community landowner, the West Harris Trust.

The Trust was formed in 2008 as a charitable company to pursue the purchase of 3 contiguous crofting estates belonging to the Scottish Government. It succeeded in purchasing 7225ha (17853 acres) of land which was home to 119 residents in January 2010 after a funding struggle for the **£59,000** purchase price. The original Scottish Land Fund had finished, and BIG Growing Community Assets was unwilling to fund the purchase of publicly owned property. Modest contributions from HIE and CnES left a funding gap which was filled by a **£22,000 loan from Tighean Innse Gall, in return for a commitment to release land for housing.**

Renewables Projects

At purchase the only guaranteed income was £1800/yr in croft rents. Therefore, the directors knew that they had to focus their attention on income generating projects in order to create a sustainable business that could generate real benefits for local residents. An initial plan to build a hydro scheme using a combination of a £380k Big Lottery Fund award and of loan finance from the Co-op bank had to be shelved due to 2 factors: the UK Govt ruled that communities could not receive both grant and Feed-In Tariff (FIT) on the same project; and the Co-op bank got into financial difficulty and withdrew from lending. Instead of employing staff and developing new projects from the profits of the hydro scheme the Trust was allowed to use the BIG funding to employ staff and develop alternative projects that would deliver similar outcomes.

The Trust invested in 3 wind turbine projects of gradually increasing size, with projects led by a subsidiary West Harris Renewables Limited (WHRL). First in 2012 was a 5kw wind turbine funded by local fundraising and a **loan at 5% interest** from the Energy Saving Trust (EST). The Trust was eligible for this loan because the energy from the turbine was being used to make the building it fed less reliant on fossil fuels. The second turbine was installed in March 2014 and was not eligible for an EST loan. It was a larger 50kw turbine funded by income from the sale of house plots to new residents and a **£210,000 loan at 8%** from Social Investment Scotland. (The Trust's mainstream bank was unable to assist because it required the Trust to have revenues equivalent to 25% of the repayments available from other streams – something not possible with only £1,800/yr in rents.) The turbine performed well despite an initial breakdown and the Trust decided to invest in a second turbine linked to a proposed multi-purpose community building to be funded by a grant package from a range of bodies. By 2015 FIT rates were falling and while the project was profitable, the need to pay back a loan over 10 years would not have been viable at an interest rate of 8% from SIS. However, the Trust was now aware of the benefits of **community share offers** and the potential to raise money at 4-5% interest. This was researched and a Bencom established by a local development officer employed by the Trust and part-funded by HIE.

At this point a second breakdown in the 50kw turbine and a disappointing level of service to repair it led the directors of WHRL to take the view that they could not in good conscience recommend that the local community invest in shares in a project that would have question marks over its longevity. Risking their community's money would be very different to risking a lender's. An alternative newly developed 100kw turbine was identified but it had a higher capital cost and the lack of a track record meant it was also not suitable for a community share offer. Locked out of grant funding, traditional commercial lending and community shares the Trust then considered **private investment.** It agreed a deal with 2 private investors who operated a Limited Liability Partnership (LLP) for investing in renewables projects. WHT created a new subsidiary and established an LLP with the private LLP as a partner. The private investors funded the installation of the turbine in 2016 with an agreed profit share between the 2 parties.

At the same time that the 100kw wind turbine project was being developed, an opportunity arose for private investors operating an EIS investment fund to enable the building of the original hydro scheme. Discussions lasted well over a year and during this time a community share offer also became a possibility. WHT had significant capacity in board and staff thanks to skills in engineering, building and accountancy. However, that capacity had its limits and was largely being taken up in the wind and building projects. Therefore, it was agreed that WHRL would take shares in a joint venture with the investment fund. The EIS investors wish to withdraw by 2020 and WHRL is working to raise money through **commercial lending** based on actual production figures to take complete control of the scheme.

Community Projects

Parallel to the Trust's actions on the renewable energy front it worked on delivery of social benefit projects from its inception. WHT received institutional support from HIE, being accepted on to its account management programme in 2012. The agreed plan included support to develop a multi-use community building incorporating business space and support for a graduate placement post to develop new business activities. At purchase the community had no dedicated community space, no affordable housing for rent, no affordable plots for self-build and no available business space. The Trust could not deliver such projects without public sector support because it was starting without capital and a combination of high build costs and low rents in a remote location meant that the market alone could not deliver solutions.

The Trust installed a pontoon and shore base using **BIG and LEADER funds** in 2013. It then purchased the local two classroom school in 2014 after its closure using part of the BIG grant initially earmarked for the hydro project, allowing it to move its office on to its own land. Comhairle nan Eilean Siar (CnES) agreed to a large discount on the valuation in return for WHT developing a business plan that demonstrated it would deliver economic benefit from community ownership.

The support of partners enabled WHT to develop a 500m² community building incorporating community space, restaurant, wedding venue, office space, studio space and campervan stances. The project concept was conceived in 2011**,** construction started in 2015 and the completed building was opened in early 2017**.** The £2.1m project was almost completely grant funded by the public sector with a small amount of charitable funding support. During construction, funding from the Scottish Government's Low Carbon Infrastructure Transition Programme (LCITP) enabled WHT to research, plan and put the correct legal structures in place that enabled the 100kw wind turbine to supply electricity to the new building and 6 neighbouring houses built by Hebridean Housing Partnership in 2016.

The ability to provide self-build housing opportunities was constrained at a site in Luskentyre by the need to extend the water main and divert power lines. The Trust had 1 guaranteed purchaser for 1 of 3 plots in 2015 but did not have the capital to carry out the infrastructure improvements first. Banks would not lend on land still in crofting tenure and which could not be decrofted until it was sold to plot purchasers. Therefore, CnES agreed to lend money to WHT at 1% over base rate in return for security to enable the work to be carried out. The Trust has since sold all 3 plots and repaid the loan in full.

The above narrative shows how the Trust has been able to secure significant public sector resources to deliver public goods for projects that would not deliver a free market return. It also shows that the Trust has been successful in using a range of alternative financial models to finance revenue-generating projects. It has been excluded from traditional bank lending due to its lack of start-up capital, limited initial revenue streams and assets being held in crofting tenure. However, it has successfully used social impact lending from SIS and, when this was not appropriate, different forms of private sector investment to deliver projects. Preferential lending from the voluntary sector to buy the estate and from the local authority to enable housing development has also played an important role. Other important factors in successful development have been institutional support from public sector partners and the skills available in board and staff. The combination of available financial models, public sector support and local determination has enabled the trust to develop significant revenue streams, provide important community and business infrastructure, create employment opportunities and raise the population from 119 to 143.

9.2 Appendix 2 - Legal Structure

Legal structure is an important framework for all organisations and comprises two key elements:

- Legal form – the type of organisation it is in the eyes of the law
- Governing document – how it plans to work and govern itself

There are a range of structures available to community groups for the operation of not for profit organisations such as:

- Unincorporated associations
- Company limited by guarantee
- Charitable trusts
- Scottish charitable incorporated organisation (SCIO)
- Mutual societies:
    - Registered societies, including:
        - Co-operative societies; and
        - Community benefit societies
    - Credit unions
    - Building societies
    - Friendly societies
- Community interest companies

9.2.1 Incorporation

Becoming incorporated gives an organisation a legal identity of its own (separate from the individuals involved). This means that it can:-

- hold property and enter into contracts
- borrow money
- defend or take legal proceedings

Being incorporated offers board members protection against unlimited personal liability. If the group wants to employs someone or wants to enter into a contract concerned with buying or leasing property, then becoming incorporated would be a sensible route to take.

An unincorporated organisation can be attractive to its management committee in terms of its relative simplicity from a reporting perspective. However, if an organisation is not incorporated, then the members of the voluntary management committee can have unlimited personal liability in the event of the organisation failing, and this consideration often outweighs the downside of incorporation which is slightly more complex with additional legal and accounting reporting requirement which generally cost organisations more to comply with.

9.2.2 Company Limited by Guarantee

The most common legal form used by community groups is a Company Limited by Guarantee. The company is formed by a group of Directors or Members but their liability is limited to the amount contributed to the company on incorporation, often £1.

Where there is a membership structure, Directors are usually elected the company's membership.

Companies Limited by Guarantee must be registered with Companies House and require Articles of Association, and can if they wish apply for charitable status, but its Articles must be approved by the Scottish Charity Regulator.

9.2.3 Charitable Status

Charitable status is a separate consideration from setting up the legal structure of an organisation, although the choice of legal structure can determine whether the organisation has the ability to apply for charitable status.

Advantages:

- Charities are generally exempt from paying corporation tax on profits, but there are restrictions on the level of tax-free trading that can be undertaken.
- Can attract private and corporate donors who support registered charities.

Disadvantages:

- Compliance with charity legislation.
- Strict rules for financial reporting and dealing with restricted funds and reserves.

Overall consideration:

For community companies, the trading restrictions can outweigh the benefits of charitable status, and each organisation must consider its likely future activities before making a decision on charitable status.

9.2.4 Scottish Charitable Incorporated Organisation

A new legal form called a Scottish Charitable Incorporated Organisation (SCIO) was introduced in 2011 to provide a separate legal identity with limited liability without the need to comply with the complexities of company law so that they only have to deal with the Scottish Charity Regulator (OSCR) rather than the dual reporting to Companies House and OSCR required by companies.

9.2.5 Regulated Societies

Since the coming into force of The Co-operative and Communities Benefit Societies Act 2014 (the "Act") on 1 August 2014, the legal entity known as Industrial and Provident

Society no longer exists. The Act consolidates previous industrial and provident legislation, replacing the 'industrial and provident society' legal form with two new legal forms:

- A Co-operative Society; and
- A Community Benefit Society

Prior to 1 August 2014, all societies registered under the Industrial and Provident Societies Act 1965 (or its predecessors) were legally referred to as 'industrial and provident societies', whatever they called themselves. From 1 August, existing societies are now known as 'Registered Societies'.

Any new societies registered on or after 1 August will be referred to as either a Co-operative Society or a Community Benefit Society.

There are important distinctions between the two legal forms:

Co-operative Societies

Co-operative Societies are formed primarily to benefit their own members, who will participate in the primary business of the society. They must also fulfil the following conditions:

- Community of interest - there should be common economic, social or cultural needs or interest amongst all the members of the co-operative.
- Conduct of business - the business will run for the mutual benefit of the members, so that the benefit that the members obtain will stem principally from their participation in the business.
- Control - control of the society lies with all the members, exercised by them equally and not based on the amount of money each members has put into the society.
- Interest on share and loan capital - where part of the business capital is the common property of the co-operative, members should receive only limited compensation (if at all) on any share or loan capital which they subscribe.
- Profits - if the rules of the society allow profits to be distributed, they must be distributed among the members in line with the rules.
- Restriction on membership - there should normally be open membership. This should not be restricted artificially to increase the value of the rights and interest of current members, but there may be grounds for restricting membership in certain circumstances, which do not offend co-operative principles.

Community Benefit Societies

Community Benefit Societies are formed primarily to benefit people who are not members of the society and will not participate in the primary business of the society. They must also adhere to the following:

- Conduct of business - the business must be run primarily for the benefit of people who are not members of the society, and must also be in the interests of the community at large. It will usually be charitable or philanthropic in character.
- Interest on share and loan capital - it will be unusual for a community benefit society to issue more than the nominal share capital (normally £1 share per member). Where it does issue more than nominal share capital or where members make loans to the society, or both, any interest paid must not be more than a reasonable rate necessary to obtain and retain enough capital to run the business.
- Profits and assets - the society's rules must not allow profits or the society's assets to be distributed to the members. Profits must generally be used to further the object of the society by being ploughed back into the business.
- Dissolution - the society's rules must not allow assets to be distributed to its members on dissolution. The rules should state that on dissolution the assets should be transferred to some other body with similar objects.

How BenComs operate

Some key characteristics of BenComs are as follows:

- They are set up with social objectives to conduct a business or trade.
- They are run and managed by their members.
- They must submit annual accounts.
- They can raise funds by issuing shares to the public.
- They can be established as charities, providing they have exclusively charitable objects that are for the public benefit, allowing them to raise capital through public grants and charitable trusts.

BenComs are not to be confused with co-operatives. Co-operatives operate for the mutual benefit of their members and may or may not be a social enterprise, depending on their activities and how they distribute their profits. Co-operatives cannot be established as charities.

BenCom registration

To register as a BenCom, the organisation must demonstrate social objectives and reasons for registering as a society, rather than a company.

Asset locks

Charitable BenComs must have an asset lock. Non-charitable BenComs can apply an asset lock, which protects their assets for the future benefit of the community. BenComs that do so may only convert to a Community Interest Company (CIC).

9.2.6 Community Interest Company (CIC)

Companies which do not have charitable status can find it difficult to ensure that their assets are dedicated to public benefit.

A CIC is a relatively new type of company (the legal form was established in 2006), designed for social enterprises that want to use their profits and assets for community good. They have the flexibility and certainty of the company form, but with special features to ensure that they are working for the benefit of the community.

What are the differences between CICs and charities?

- Charities must be established exclusively for charitable purposes, but a CIC can be established for any lawful purpose, as long as their activities are carried on for the benefit of the community
- Charities have certain tax advantages that CICs do not have
- In return for those advantages, charities are subject to more onerous regulation than CICs
- The CIC legal form was specifically designed to provide a purpose-built legal framework and a 'brand' identity for social enterprises that want to adopt the limited company form
- CICs are free to operate more 'commercially' than charities

Community Interest Test

To become a CIC, an organisation would need to satisfy the regulator that its purposes could be regarded by a reasonable person as being in the community or wider public interest. It will also be asked to confirm that access to the benefits it provides will not be confined to an unduly restricted group.

The Asset Lock

'Asset Lock' is a general term used to cover all the provisions designed to ensure that the assets of the CIC (including any profits or other surpluses generated by its activities) are used for the benefit of the community.

This means that, subject to the CIC meeting its obligation, its assets must either be retained within the CIC to be used for the community purposes for which it was formed, or, if they are transferred out of the CIC, the transfer must satisfy one of the following requirements:

- It is made for full consideration (i.e. at market value), so that the CIC retains the value of the assets transferred;
- It is made to another asset locked body (a CIC or charity) which is specified in the CIC's memorandum or articles of association;
- It is made to another asset locked body with the consent of the Regulator; or

- It is otherwise made for the benefit of the community

The asset lock prohibits CICs from distributing their assets or profits to members, except to the extent permitted where CICs issue equity. The lock will not prevent CICs from using their assets efficiently in pursuit of community benefit; for instance, they will be able to use assets as collateral for finance.

Equity Finance

CICs can issue capped investor shares so that investors have the possibility of making a modest return which will be restricted in order to ensure that the main beneficiary if the CIC is the wider community.

Advantages of being a CIC:

- as a corporate body, a CIC can hold property and borrow money in its own name
- flexible options for trading for community benefit without private gain
- personal liability of members is limited
- two tier structure for decision making allowing democratic input from members including the chance to vote on election/re-election of the board of directors
- asset lock ensures that profits/assets are retained by the community
- directors may receive limited payment (if the CIC's constitution or Articles permits)

Disadvantages of being a CIC:

- may incur some setting up costs (legal fees)
- dual reporting to both Companies House and the CIC Regulator including statutory filing of Annual Accounts along with annual CIC Report
- cannot apply for charitable status

Most suitable for

A Community Interest Company (CIC) is most suitable for groups who:

- want to trade for the benefit of a specific community (as long as any current constitution permits them to do so)
- can prove that their activities and services will benefit the community
- want to limit the personal liability of members
- want to run/lease/manage/own community assets such as shops, garages, day care centres
- do not have charitable purposes and are not seeking charitable status (in Scotland a CIC is not eligible to be a registered charity itself)
- are existing charities who want to set up a trading arm (the trading arm, which would not have charitable status itself, could be a CIC)

9.3 Appendix 3 - VAT

Charities and community groups are subject to the same VAT rules as any other organisations, although there are a number of reliefs and exemptions available specifically for charities.

When a charity buys goods and services they will normally have to pay VAT just like anyone else.

A charity must register for VAT if its turnover for the previous 12 months from 'taxable business activities' is above the VAT threshold (£85,000 annual threshold from 01/04/17). If there are no business activities or business activities are exempt from VAT, an organisation cannot register for VAT.

If an organisation is registered for VAT but make some exempt supplies, the business is partly exempt. It is not possible to reclaim VAT on purchases that relate to exempt supplies, so calculations of VAT on exempt supplies, VAT on taxable supplies and another calculation of VAT partly for the taxable supplies and partly for the exempt supplies must also be carried out, as well as calculating the business and non-business split.

Partial exemption results in additional work for a group and also increases the risk of not getting the VAT calculations right. A number of groups have assumed that VAT does not apply to them as a charity, or that as a charity they will be entitled to full recovery of VAT on build project and there area example of groups who have subsequently had costly VAT liabilities and/or professional costs in unpicking their VAT situation.

VAT recovery on supplies of land & buildings

Supplies of land and buildings, including leasing or renting, are normally exempt from VAT meaning that no VAT is payable, but the entity making the supply cannot normally recover any of the VAT incurred in relation to the supply of land and buildings. However, it is possible to opt to tax land, so that once opted to tax, all supplies made in relation to the land and buildings will normally be standard-rated and recovery of the VAT incurred in making those supplies is allowed.

The construction of buildings intended to be used by a charity solely for non-business purposes can be zero-rated subject to certain criteria being met.

If it is intended that part of the building will be let out to other organisations who are not themselves a charity, then the building will not meet the criteria of being used 'solely for non-business purposes'. Up to 5% of non-qualifying use can be ignored.

Where the building is used partly for charitable purposes and partly for trading (such as a shop) it will not qualify for charitable zero-rating unless the charitable element of the building is independent of the non-charitable part (e.g. an Annex to a building rather than an extension).

If within 10 years of construction the building is subject to a change of use (or change of use to part of the building) which does not meet the relevant charitable activities, then a VAT charge would be applied to the building.

The scale of build projects often result in groups seeing VAT recovery as a method of helping to fund their build project, however the complexity of the VAT rules in relation to land and buildings and the likely partial exemption position of a community organisation does result in a complicated VAT position for these groups to manage through a build project and for the subsequent 10 years after completion.

VAT treatment of mixed sources of income

Where an organisation is involved in a mix of activities which are subject to VAT as well as exempt and outside the scope activities, it finds itself in a VAT partial exemption situation which will result in not all input VAT being recoverable and the additional administrative work involved in performing VAT partial exemption calculations on a quarterly and annual basis.

9.4 Appendix 4 – Investor Tax Relief

Social Investment Tax Relief (SITR) is the government's tax relief for social investment which encourages individuals to support charities and social enterprises.

Social Investment Business[17] produced a report 'WHAT A RELIEF! A review of Social Investment Tax Relief for charities and social enterprises' in January 2019 which it had commissioned to report on how best SIB could support charities and social enterprises to make more and better use of Social Investment Tax Relief (SITR)

How is SITR used?

SITR can be deployed in three ways. The two main models are:

- A. Discretionary investment agreements with investment managers marketed as SITR loan funds. Intermediary organisations set up SITR funds enabling investors to invest into organisations selected by the fund managers
- B. A charity or social enterprise creates its own investment and seeks investors directly

In addition:

- C. Social Impact Bonds – companies set up to deliver Social Impact Bonds can be eligible for SITR if they receive accreditation from the Cabinet Office.

In practice, 'B' splits into two broad strands and 'C' is an option that relates to Payment by Results contract funding rather than risk finance for ongoing business activities.

As a result the main SITR products currently on offer to investors are:

- 1) SITR Funds – Intermediary organisations set up SITR funds enabling investors to invest into organisations selected by the fund managers
- 2) Crowdfunding platforms – an organisation seeks direct investment from individual investors (including retail investors) through a website which ensures that the offer complies with relevant financial regulations
- 3) Private offers – an organisation creates its own investment offer (after receiving appropriate legal advice) and makes it available to individual investors including High Net Worth Individuals (HNWIs).

---

[17] *Social Investment Business is a UK registered charity and trading company that offers loans, grants and other financial products to charities and social enterprises. SIB manages one of the largest social investment portfolios in the UK. Its foundation pioneered community investment in the UK and, to date, has leveraged over £30 million from corporate and public sector organisations.*

What has happened so far?

A report published by HMRC in May 2018 identifies that the estimated dealflow figure for the periods 2014-15, 2015-16 and 2016-17 was £83.3 million (based in Treasury estimated of the cost of the relief), however only £5.1 million was actually raised by 35 charities and social enterprises. In that same period.

In the SIB report, they identify that for SITR to function, 3 conditions need to be in place:

- Individual investors want to invest
- Charities and social enterprises are willing and able to use the kind of investment that is on offer
- The rules of the relief are fit for purpose

Five Key Challenges for SITR

Lack of awareness from charities and social enterprises

Slow pace of legislative change – for example the increase in the SITR eligible investment into a single organisation from £300,000 to £1,500,000 was announced in 2016 for implementation from 6th April 2017 but did not come into force until November 2017.

SITR is not fit for purpose – SITR has been evolved from EIS aimed at mainstream SMEs and does not specifically meet the needs of charities and social enterprises.

Process challenges – the experience of seeking SITR has been negative with a general feeling that HMRC are not adequately resourced to respond to the currently relatively small demand.

Lack of pipeline or mismatch between supply and demand -

The SIB report identified that SITR has not been a major success, but that there is potential for it to meet some of the demand for risk finance in the social investment market.

The report's recommendations are:

Government should:

- 1. Recognise that charities and social enterprises are not the same as mainstream businesses and – as a result – a copy and paste model of a mainstream tax relief will not work effectively for them
- 2. Amend legislation to enable the relief to be more easily used by charities with trading arms

- 3. Extend its positive work on nursing and care homes to set up an accreditation scheme for all currently excluded activities – including property, leasing and community energy – if they are being carried out for a demonstrable social purpose
- 4. Give investors 50% rather 30% relief to bring SITR into line with SEIS rather than EIS
- 5. Develop a model process for applying for Advance Assurance, registering investments, and administering payments, which is accessible for small charities and social enterprises with limited administrative capacities.

Voluntary sector/Social investment infrastructure organisations should:

- 6. Promote and create awareness of both the existence of SITR and ways that charities and social enterprises can make use of it
- 7. Use networks to promote awareness of SITR amongst voluntary sector support agencies including CVSs and other local bodies
- 8. Provide access to relevant legal and other professional support that would enable charities and social enterprises to create their own offers
- 9. Collect and publicise all available data in formats that are comprehensible to Government, potential investees and potential investors.

Wholesale and intermediary social investors (including trusts and foundations) should:

- 10. Develop and fund support programmes for charities and social enterprises to create investment offers and connect with potential investors
- 11. Provide match funding for SITR eligible investments - either via platforms or to support direct offers.

Seed Enterprise Investment Scheme

The Seed Enterprise Investment Scheme (SEIS) offers tax efficient benefits to investors in return for investment in small and early stage startup businesses in the UK. SEIS was designed to boost economic growth in the UK by promoting new enterprise and entrepreneurship.

Some key features are:

- SEIS investors can place a maximum of £100,000 in a single tax year, which can be spread over a number of companies.
- A company can raise no more than £150,000 in total via SEIS investment.
- Investors cannot control the company receiving their capital, and must not hold more than a 30% stake in the company in which they invest.
- Investors can receive up to 50% tax relief in the tax year the investment is made, regardless of their marginal rate.
- The company seeking investment must be based in the UK, and have a permanent establishment in the British Isles.

- The company must have fewer than 25 employees. If the company is the parent company of a group, that figure applies to the whole group.
- The company must be no more than two years old.
- The company must have assets of less than £200,000.
- The company has to trade in an approved sector – generally not in finance or investment, for example, a property company can't raise capital through SEIS.

Enterprise Investment Scheme

The Enterprise Investment Scheme (EIS) is designed to help small UK companies raise money to grow. It works by offering generous tax reliefs to individual investors when they buy shares in a qualifying company and when they sell them after a minimum period.

Important features:

- Overall maximum investment of up to £1 million per year that is eligible for tax relief.
- Individual investors must not have more than a 30% interest in the company, must not get preferential shares and must not have any other form of connection or controlling interest in the company.
- UK companies that aren't listed on a stock exchange, are considered 'small' (i.e. have assets of £15 million or less before shares are issued) and have no more than 250 full-time employees are usually eligible to seek investment through the scheme.
- Investors that buy shares in a qualifying EIS company will get 30% income tax relief on the cost up to £1 million, which is offset against the individual's Income Tax bill for the year in which the investment was made.
- The shares must be held for three years from the date of issue though or the tax relief will be clawed back.
- The scheme also allows investors to 'carry back' all or part of the investment in one tax year to the preceding tax year so long as the limit for EIS relief is not exceeded in that year.
- Investors making a qualifying EIS investment can also benefit from Capital Gains Tax (CGT) exemption.
- There is no CGT charged on any gain made through EIS shares as long as they are disposed of after the minimum three-year holding period on which Income Tax relief was given.
- Paying CGT can be deferred when a gain is invested in shares of an EIS-qualifying company (even if the investor is connected).
- The gain can be from the disposal of any kind of asset but the investment must be made one year before or three years after the gain occurred.

- If EIS shares are disposed of for a loss at any time, the loss can be offset (after Income Tax relief already given) against income for that year and the previous year.