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# Social Enterprise Zones

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## 1. Executive Summary

There are many people and organisations far better qualified than politicians to ameliorate and reverse some of the most pernicious social trends in our communities that cause and perpetuate misery for far too many.

In other words, the state is not, contrary to the present Prime Minister's belief, the sole guarantor of fairness. To believe that an army of bureaucrats can solve the problems of the most under-privileged areas in the UK is to ignore the evidence of the last ten years. Inadequate measures have left large numbers of our fellow citizens trapped in spiralling deprivation. *Breakdown Britain* and *Breakthrough Britain*, the two volumes of the Conservative Social Justice Policy Group's report, have shown how poverty and desperation have turned into a vicious cycle of unemployment, addiction, crime and further poverty – diminishing families and neighbourhoods.

*Breakdown Britain* and *Breakthrough Britain* also show the concentration of such poverty and misery in certain areas of the country. Data is thick on the ground – be it from the Home Office, the Department of Communities and Local Government, or the British Crime Survey – that shows the degree to which people in the greatest need are concentrated in particular neighbourhoods. This is hardly surprising, given the evidence of wretchedness begetting more wretchedness; but coherent thinking about how to rescue neighbourhoods caught in cycles of deprivation has been less than evident.

In *Breakthrough Britain*, the Social Justice Policy Group makes a wide range of recommendations about steps needed to tackle such deprivation. In this Consultative Paper, we draw attention to one particular answer to the question of how to tackle endemic distress concentrated within particular communities. We believe that solutions to whole neighbourhood breakdown have to be local, because the problems are local; they are also complex and delicate and require a straightforward, practical and flexible response from those most fitted to deliver it: the **third sector**, with its ability to provide patient and knowledgeable help to our most deprived communities. This Paper incorporates research and recommendations on the third sector from *Breakdown Britain* and *Breakthrough Britain* (in Sections 4.2. and 4.3.), as well as the work of the Social Enterprise Zones Task Force, led by Rodney Lord and Harriett Baldwin; and in Section 4.4., we present the results of the Task Force's wide consultation on the best method of fulfilling David Cameron's pledge to establish Social Enterprise Zones.

*“Labour are creating a new class of decommissioned people. Individuals who should have been guided onto paths out of poverty have instead been shunted into life's sidings...How are we going to build the nation of the second chance? Here, I don't think that the voluntary sector has an important role to play. I believe that the voluntary sector has the crucial role to play...[I] have...seen how the voluntary and social enterprise sectors provide intensive, long term, holistic care to our vulnerable people. Above all, the care is personal...The public sector does a great job, but its targets and caseloads make it difficult to provide the necessary level of help... Social Enterprise Zones...will incentivize social action where it is most needed...Small community and voluntary groups who care for broken lives deserve financial support – the use of which isn't micromanaged...Communities are not created from the top down, but built from the bottom up. Conservatives will always promote a nation of enterprise, individual freedom and personal responsibility. But we must remember too that personal responsibility must be part of a shared responsibility.”<sup>1</sup>*

Our consultation has led us to believe that the best way to revolutionize the hopes and opportunities of individuals in the most troubled neighbourhoods, and hence those of future generations, is to help the

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<sup>1</sup> From 'Tackling Poverty in Britain Today': a speech by David Cameron, given to the Centre for Social Justice, 18<sup>th</sup> January 2006

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55,000 social enterprises that already exist, listening to their views instead of imposing our own; and to make it much easier for new social enterprises to start up. These enterprises vary enormously in both size and remit, but what they all have in common is that they are businesses, generating a substantial proportion of their own income, with primarily social objectives rather than being driven by the need to maximise profits for shareholders. Thus they change society for the better bit by bit, and with the untiring and experienced perseverance of those who understand the complex nature of each problem that they address, and of every person whom they help.

Social enterprises have local knowledge, motivation, flexibility and imagination, and we need to tear down the barriers that a centralist government has put in their way. These range from not transferring public services to the third sector in general, to the lack of prompt funding support. In particular, over-regulation has become a substantial drag on the smallest enterprises, which have become increasingly polarized from the largest. This disparity has been increased by the Government's tendency to funnel the majority of its funding to the bigger organisations, which has allowed them in turn to generate the publicity that ensures that they also get the lion's share of voluntary income. This is a trend which surveys make clear that the public finds concerning, as is the pressure on all charities to conform with the public sector, so that they risk becoming just another wing of the Government, thereby losing all the attributes that were so attractive and effective in the first place.

If, therefore, we are to do more to support social enterprise, there are many practical measures that would be of immense and immediate benefit. This paper lists many of those suggested by the Social Justice Policy Group, from social bonds to promoting volunteering at school; and from a less bureaucratic method of funding, especially for smaller organisations, to enhancing the third sector's voice in the Cabinet and in Parliament. Social enterprises can play an important role across the economy, providing solutions to a range of 21<sup>st</sup> century issues; these are explored in the reports of other Conservative policy groups. In this paper, we have considered specifically how social enterprise can be strengthened in the most deprived neighbourhoods, in which poor life-chances seem to multiply and move from one generation to the next. Enterprise Zones existed under the Thatcher Government, with the purpose of allowing the swift, unimpeded improvements to physical infrastructure that were desperately needed as a means of regeneration and creating jobs. We wish to emulate their success, but with social infrastructure instead.

By allowing local authorities to put forward neighbourhoods within their areas to become Social Enterprise Zones, we can help to reduce the financial and planning obstacles that social enterprises in the hardest-pressed neighbourhoods currently face, while keeping all decisions firmly local. External finance is clearly vital to this project, especially in areas with little access to their own local capital; and this paper looks at the possibility of a Community Bank, which would be in some ways analogous to a 'central bank' for Social Enterprise Zones; it would operate in partnership with existing social enterprise and community lending institutions, and the social enterprises they serve would be offered enhanced tax reliefs to attract funds into the most deprived areas. The Bank would also help social enterprises to find other sources of finance, including grant money, effectively streamlining the multifarious and confusing sources of finance available to the sector into a single conduit.

This 'patient capital', funding the work of social enterprises in Social Enterprise Zones, and drawn in with the help of tax measures similar to the venture capital reliefs developed by the Conservatives in the 1980s and 1990s, would give the smallest of social enterprises the chance to help transform Britain's most troubled neighbourhoods. In the longer term, such financial measures should be more than offset by the savings in public expenditure as those people whom Labour has allowed to be 'decommissioned' are given real opportunities to rejoin society, in neighbourhoods where crime, addiction and unemployment are no longer an unchangeable and accepted status quo. This would be a social dividend on a grand scale.

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## 2. Neighbourhood Breakdown

### 2.1. Multiple Deprivation

*Breakdown Britain*, the interim report of the Conservative Social Justice Policy Group, identifies a cluster of mutually reinforcing sources of deprivation:

- worklessness and economic dependence;
- family breakdown;
- drug and alcohol addiction;
- low educational attainment; and
- indebtedness.

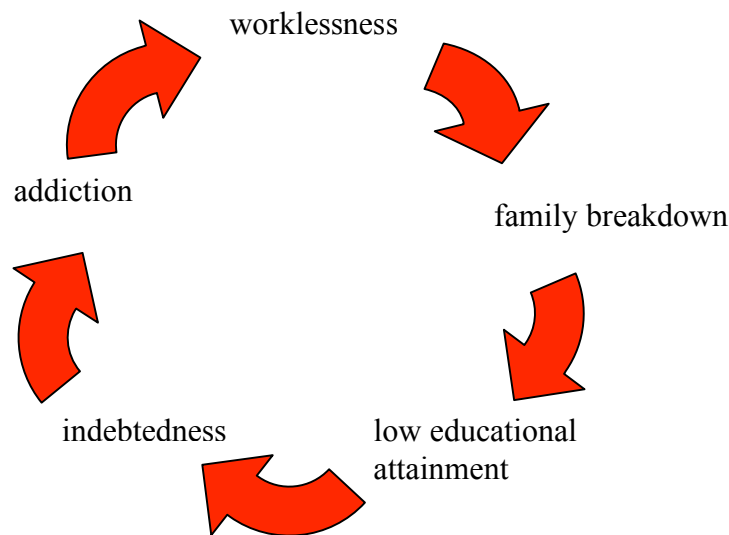
The evidence presented in *Breakdown Britain* highlights the strong connections between each of these sources of deprivation, and illustrates how destructive behaviour patterns can take root in families, with the behaviour of the parent mirrored in the behaviour of the child. Looking at substance misuse, the cycle may begin when one or both parents are drinking or taking drugs and are being abusive towards, or neglectful of, their children. In turn, those children are being propelled into substance abuse; substance misuse is likely to trigger truancy; truancy triggers educational failure; educational failure triggers unemployment; and unemployment is a very high risk factor for substance abuse. Furthermore, those on low incomes who get into debt find it almost impossible to pay off their debts, partly because of the appallingly high levels of interest they routinely pay on their loans. Financial worries often place enormous strain on family life, leading in turn to family breakdown. Theodora Ooms, who has written extensively on the problems facing low income families, succinctly summarises these pressures<sup>2</sup>:

*“Low income families, especially those who reside in poor neighbourhoods, are daily exposed to a variety of experiences that place extraordinary stress on the couple and family relationships. In addition to the constant stress of making ends meet financially, and of working in unstable, low paying jobs, they have the frustrations of living in sub-standard housing in poorly serviced neighbourhoods, without adequate transportation; and they and their children are continually in fear of crime and violence. Members of their immediate extended families may be struggling with depression, alcoholism or drug abuse, HIV/AIDS, or may be in and out of jail, or some combination of those problems. Domestic violence is more prevalent in low income households. In addition, black and other minority individuals are constantly exposed in the workplace or on the streets to incidents of racism and discrimination. Service providers who work with these couples note how often these accumulated stresses spill over into the home, and anger and frustration too often poison the relationship between parents and children.”*

In short, traps of multiple deprivation are a reality in Britain today. For those caught in such traps, one problem interacts with another, and then another, to produce eventually a malign spiral of social dysfunction. Poor prospects encourage drug abuse which in turn reinforces low motivation and poor performance in school. Lack of qualifications make it harder to get a job, giving the downward spiral another twist by increasing poverty and opening the door to crime. Partly as a result, young people find it harder to create lasting relationships, teenage pregnancy increases, and children are born into conditions in which the cycle is prone to continue.

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<sup>2</sup> Ooms T, 2002, ‘Strengthening Couples and Marriage in Low-Income Communities’ in Hawkins A et al, 2002, *Revitalising the Institution of Marriage for the Twenty-First Century*, Praeger



## 2.2. Statistical Evidence

The statistical analysis provided in *Breakdown Britain* bears out this anecdotal evidence – illustrating, for example, how connected educational failure is with almost every other aspect of social breakdown:

- Crime: 73% of young offenders described their academic attainments as nil.
- Health: 32% of young people who have been excluded from school have been involved in drug dealing.
- Family Breakdown: children who have experienced family breakdown are 75% more likely to suffer educational failure.
- Unemployment: 20% of children in care will still be unemployed the September after they leave school.
- Poverty: children in schools where many pupils are eligible for free school meals are 2.7 times more likely to be considered underperforming by Ofsted; and children from disadvantaged backgrounds are five times more likely to fail academically compared with their peers.

Manifestly, this spiral of social dysfunction traps individuals and families rather than whole communities. But there is strong evidence that families caught in such traps of multiple deprivation are concentrated in certain areas of the country.

## 2.3. Local Authorities

Even crude analysis at the level of individual local authorities is enough to suggest the degree of concentration of social breakdown. The figures for alcohol-related deaths, for example, provide stark evidence of the geography of social dysfunction. ONS statistics for the eight years from 1997 to 2004 show that the less prosperous London boroughs of Lambeth and Ealing had on average around twice the level of such deaths as the more prosperous London boroughs of Merton and Kensington & Chelsea over the same period:

Borough	Average Alcohol-related Deaths '97-'04
Ealing	35.5
Lambeth	34.5
Merton	19.5
Kensington & Chelsea	18.0

*Baker A and Rooney C (2003). Recent trends in alcohol-related mortality, and the impact of ICD-10 on the monitoring of these deaths in England and Wales. Health Statistics Quarterly 17, Pages 5-14.*

Similar analysis from the Home Office, using 2005/6 British Crime Survey data, shows that 12% of households in the most employment-deprived areas had been the victim of one or more vehicle thefts, compared with 7% of those in the least employment-deprived areas; and that 4% of households in 'hard-pressed' areas had been the victim of burglary, compared with 2% of households nationally. Much the same picture emerges when one looks at violent crime: people living in the most deprived areas of England and Wales are twice as likely to be victims of crime as those in the wealthiest areas.<sup>3</sup>

Inequality in health and education is also geographically concentrated. A National Audit Office report of 11 January 2006 concludes that one third of all failing schools are in the most deprived 20% of communities.<sup>4</sup> And the London Health Observatory report, published by the Office of National Statistics in 2004, shows that a child born in Canning Town in the East End of London has a life expectancy of eight years less than one born in more affluent Westminster.<sup>5</sup>

## 2.4. Neighbourhoods: Where the Focus Should Lie

The evidence of geographical concentration of multiple deprivation is, however, even stronger when a finer-grained analysis is performed. The Department of Communities and Local Government (formerly, The Office of the Deputy Prime Minister) has calculated indices of multiple deprivation for 32,482 Super Output Areas (SOAs) of the country (each containing an average of 1,500 individuals). This index looks at deprivation in terms of:

- low income;
- low employment rates;
- poor health;
- low educational attainment;
- barriers to housing and public services;
- poor living environment; and
- crime.

The most deprived area in England identified by this index in 2004 was area E01006559 in Liverpool. It was ranked 91st most deprived in terms of income, 35th for employment, 49th for health, 310<sup>th</sup> for education, training and skills, 21,270th for housing and public services (the measure most directly related to government spending), 152nd for living environment, and 275<sup>th</sup> for crime.<sup>6</sup>

<sup>3</sup> Walker A, Kershaw C, Nicholas S (2006) Home Office Statistical Bulletin 'Crime in England and Wales 2005/06' 12/06, Table 5.05

<sup>4</sup> National Audit Office DfES 'Improving poorly performing schools in England' HC 679 Session 2005-2006, 11 January 2006

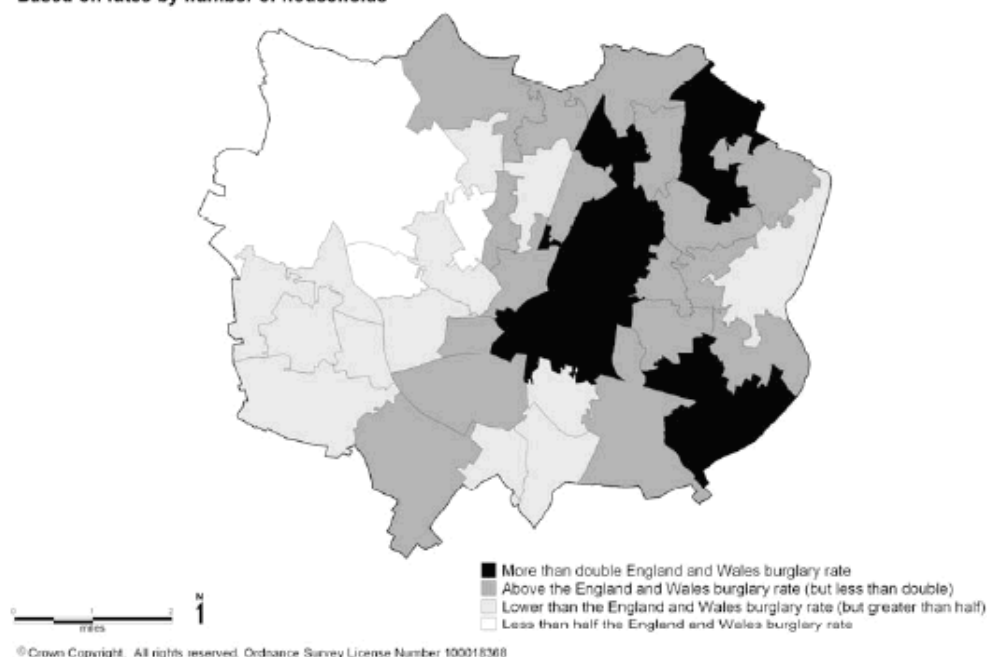
<sup>5</sup> Department of Health 'Choosing Health: making healthier choices easier', 16 November 2004

<sup>6</sup> www.odpm.gov.uk/indices

The same pattern of neighbourhood (as opposed to local authority) concentrations of social breakdown emerges when fine-grained analysis is applied to particular elements within the general pattern of social dysfunction identified in *Breakdown Britain*. In its analysis of the 2006 British Crime Survey, the Home Office Statistical Bulletin notes<sup>7</sup>:

*“It is important to remember that crime rates can vary considerably within regions. For example, Figure 7.4 shows a map of domestic burglary rates for 2003/04 in Coventry CDRP in the West Midlands Region. In 2003/04, the domestic burglary rate for Coventry CDRP was 233 offences per 10,000 households, 28% higher than the rate for England and Wales as a whole. However, as the more detailed presentation of burglaries in Figure 7.4 shows, there are marked variations within this CDRP. Areas shaded black represent domestic burglary rates in excess of double the rate for England and Wales as a whole, and the white areas are less than half the overall rate:*

**Figure 7.4 Domestic burglary (2003-2004) in Coventry CDRP, by Middle Super Output Areas**  
Based on rates by number of households



*In the case of Coventry CDRP, these variations in burglary rates closely reflect levels of deprivation and the nature of the housing stock. The areas with the highest rate of burglary are characterised by high levels of deprivation and high proportions of social housing. The area to the far north-east of the CDRP has been classified as one of the most deprived areas in England and Wales, and has received funding under the New Deal for Communities programme. Conversely, the area in the north-west which shows a low burglary rate is affluent, with low-density, high cost housing stock.”*

The same picture emerges when one considers non-crime disparities between neighbourhoods in one local authority area.

Within the area covered by Liverpool City Council, there lies – as we have seen – what is measured as the most deprived neighbourhood in England; and the Liverpool local authority area also contains three others of the ten most deprived neighbourhoods (in addition to one highly deprived neighbourhood that lies just outside the local authority area). Notably, all of the remaining neighbourhoods measured as being within the ten most deprived in England are in one other city –

<sup>7</sup> Walker A, Kershaw C, Nicholas S (2006) Home Office Statistical Bulletin ‘Crime in England and Wales 2005/06’ 12/06, p114

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Manchester. To the naïve observer, this data might suggest that policy could focus sensibly on specific local authority areas. But closer inspection confirms what any city-dweller in fact knows: that neighbourhoods geographically close to one another may nevertheless have markedly different social characteristics.

The two maps below show the configurations of deprivation for, respectively, Liverpool<sup>8</sup> and Oxfordshire<sup>9</sup>. More particularly, they show two neighbourhoods (Church Ward in Liverpool, and Northfield Brook Ward in the City of Oxford) which are ranked, respectively, as the 12,778<sup>th</sup> and the 12,844<sup>th</sup> least deprived wards in England in the DCLG index of multiple deprivation. The fact that (as the shadings on the maps show) the first of these neighbourhoods is one of the least deprived in Liverpool whilst the other is one of the most deprived in Oxford is entirely compatible with the fact that each is similarly deprived (or, if one prefers, similarly affluent). Any policy that is focused on local authority areas rather than on neighbourhoods will inevitably miss these crucial and fine-grained differences.

The conclusion is inescapable: although traps of multiple deprivation catch particular individuals and families in a cycle of poverty and misery, those individuals and families are highly concentrated not only in particular local authority areas of the country but also – and more significantly – in particular neighbourhoods, containing an average of 1,500 individuals. It has sometimes been observed that all politics is ultimately local. Certainly, given the geographical concentration of social deprivation, the politics of poverty-relief, if it is to be effective in its aim of lifting people out of these traps, must be sufficiently local to focus on the neighbourhood.

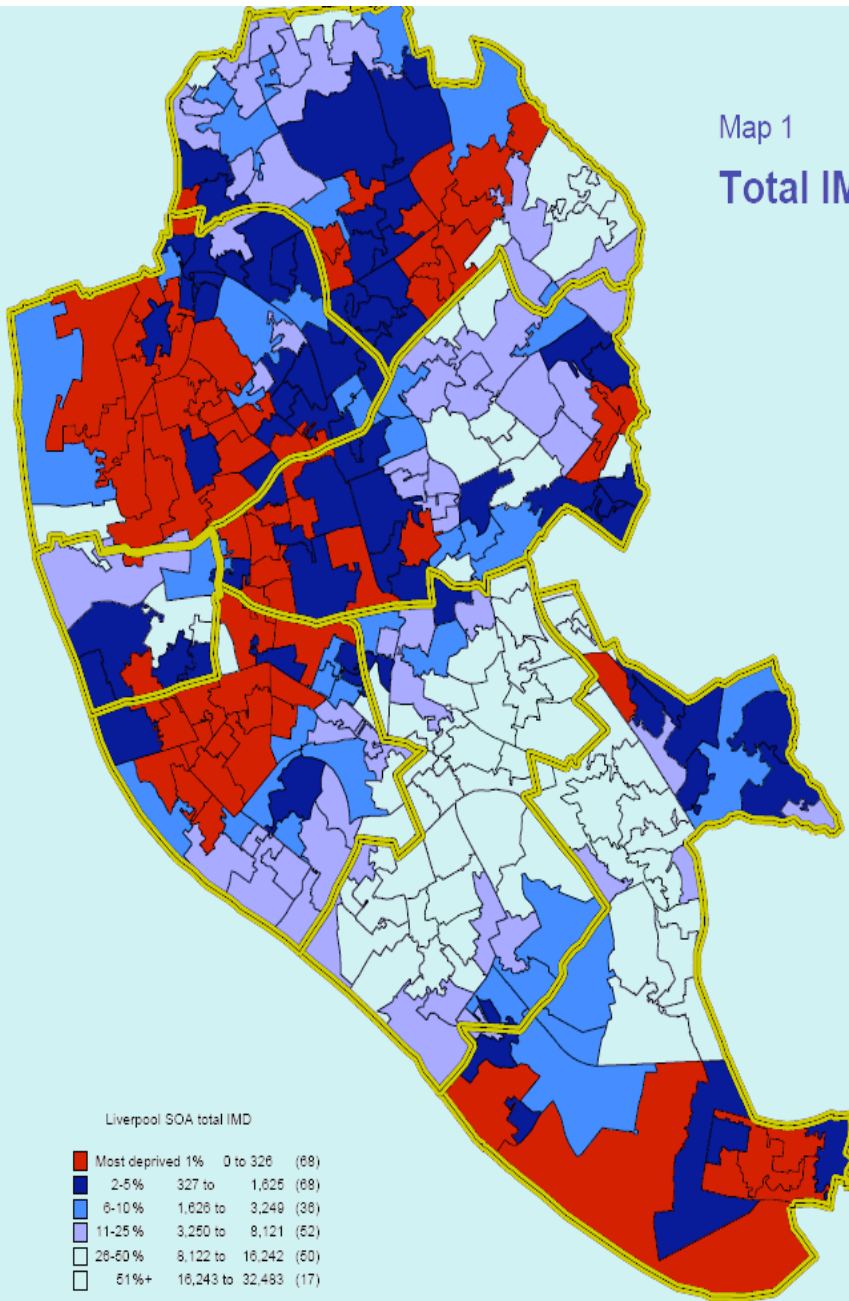
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<sup>8</sup><http://www.liverpool.gov.uk/Images/tcm21-64385.pdf>

<sup>9</sup>[http://portal.oxfordshire.gov.uk/content/public/OCP/UO/themes/poverty/oxfordshire\\_soa\\_imdscore\\_nat\\_dc.gif](http://portal.oxfordshire.gov.uk/content/public/OCP/UO/themes/poverty/oxfordshire_soa_imdscore_nat_dc.gif)

Map 1

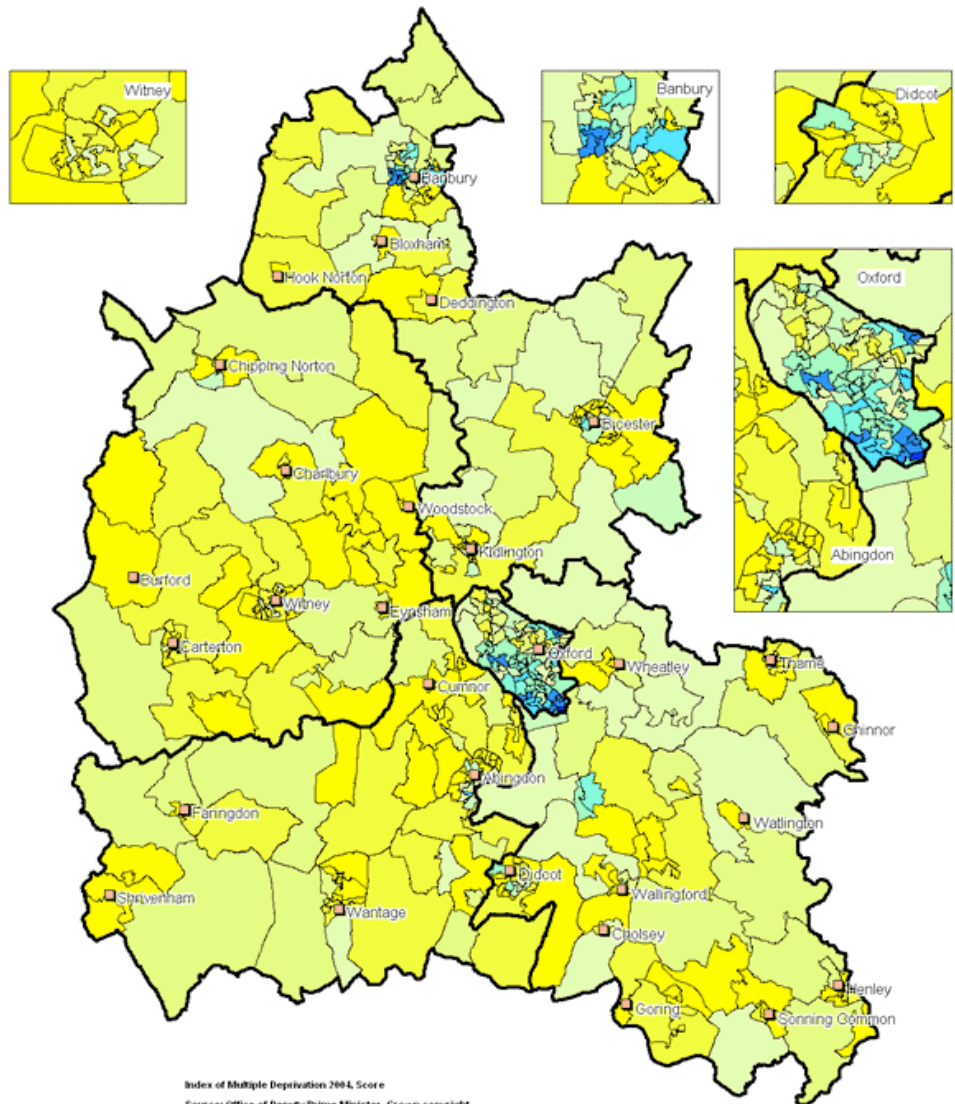
## Total IMD for Liverpool



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# Index of Multiple Deprivation 2004

SOAs ranked across England  
Source: ODPM



Index of Multiple Deprivation 2004, Score  
Source: Office of Deputy Prime Minister, Crown copyright.  
Source: 2001 Census, Output Area and Ward Boundaries, Crown copyright, Oxfordshire County Council Licence No LA076885  
Crown copyright material is reproduced with permission of the controller of HMSO.  
SOAs are Super Output Areas, a statistical geography developed for the Census  
Produced by Oxford Consultants for Social Inclusion, www.ocsis.co.uk, January 2005



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## 3. Good Intentions, Poor Delivery

### 3.1. The Last Ten Years: Intentions

Over the past ten years, the present Government has – to its credit – recognised both the importance of traps of multiple deprivation and the extent to which the individuals and families caught in these traps are concentrated in certain areas. Large amounts of money have been spent on a raft of schemes and initiatives, many of which have been focused on specific neighbourhoods. These include:

- the Neighbourhood Management Scheme;
- the Neighbourhood Renewal Fund;
- the Neighbourhood Support Fund;
- Neighbourhood Wardens;
- the Coalfields Scheme;
- the Community Champions Scheme;
- the Community Chest Scheme;
- the Community Empowerment Scheme;
- the New Deal for Communities;
- Action Teams for Jobs;
- the Active Community Fund;
- Community Legal Service Partnerships;
- the Crime Reduction Programme;
- the Playing Fields and Community Green Spaces Initiative;
- the Excellence in Cities Initiative;
- the Creative Partnership Scheme;
- the Safer Stronger Community Fund;
- the Liveability Fund;
- Health Action Zones;
- Healthy Living Centres; and
- Sports Actions Zones.

How much real difference have these well-intentioned schemes made to those caught in traps of multiple deprivation, and to the neighbourhoods within which the victims of these traps are most likely to live?

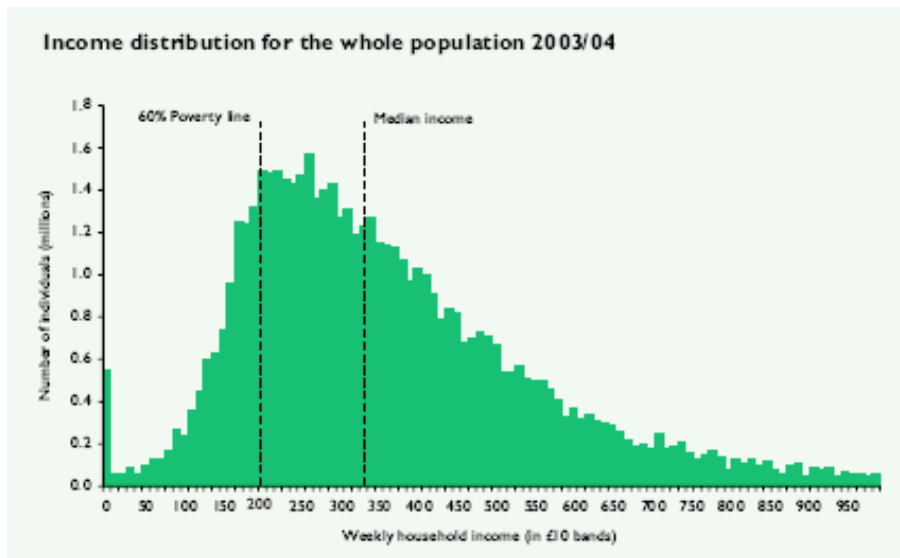
It is not, of course, possible to give a definitive answer to this important question. As Chou En-lai once remarked when asked whether the French Revolution had been a success, it is too early to tell. But the early signs are not particularly encouraging.

### 3.2. Definition of Poverty

If we take the Government's own measures of poverty as a crude proxy for traps of deprivation, the figures are stark. On the face of it, poverty rates have fallen since 1997. However, the simplistic way in which the figures are calculated conceals a much darker picture. Detailed analysis undertaken by the Conservative Social Justice Policy Group shows that much of the Government's success is based on moving families from just below the poverty line to just above it – for the people left behind, poverty is deeper than ever.

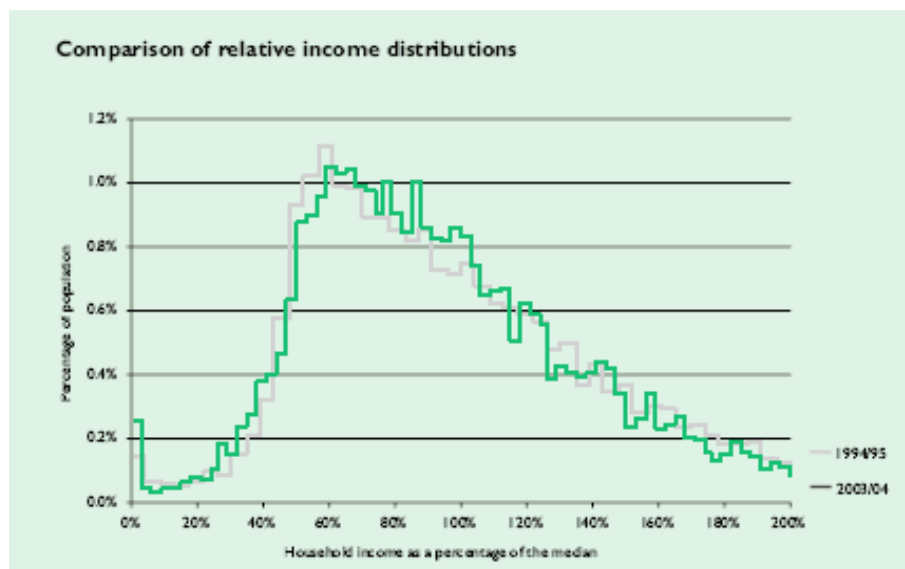
The Government defines poverty by means of a poverty line – dividing the country into simple categories of poor and not poor. This threshold is set at 60% of median household income, the median

being the point at which half the population earns more and half the population earns less. This is illustrated by the following chart which shows the number of people falling into each £10 band of household income:



Source: Department of Work and Pensions

Because a large number of people are clustered around the poverty line, a small income boost targeted at households just below this threshold can result in an apparently dramatic fall in the number of people living in poverty. There is strong evidence that this is exactly what has happened. Using Government figures obtained through the House of Commons Library, the 1994/95 income distribution for families with children was plotted against that for 2003/04. This ten year comparison is shown below:



Source: Greg Clark MP's calculations, based on Department of Work and Pensions figures.

This demonstrates that, in the area around the 60% poverty threshold, income distribution has been shifted forward just enough to put the peak marginally *above* the threshold instead of just *below* it. It is a different story at the bottom of the scale, where there are more individuals, not fewer, with incomes of 40% or less of the median. Thus, while there are fewer people *just below* the poverty line, there are more people *significantly below* the poverty line.

Unsurprisingly, the Government has not emphasised the plight of the poorest of the poor, focusing instead on the overall poverty figures. But even here progress has been exaggerated through careful

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selection of baselines. Typically a comparison is made with the late-1990s rather than with the mid-1990s, when poverty rates hit a low point for that decade. Thus, ten year comparisons from the mid-1990s show a smaller improvement than that highlighted by the Government.

Recent government *Households Below Average Income* (HBAI) figures for 2005/06, published in March of this year, give no more reason for optimism than earlier data. Indeed, they suggest that deep poverty (and hence, in all likelihood, other elements of multiple deprivation) is becoming more entrenched.

The HBAI figures came after the IFS calculated that 3.5 million families would be worse off as a result of Mr Brown's 2007 budget.

As the IFS reports, the number of people in relative poverty (living in households with less than 60% of the median income) rose between 2004-05 and 2005-06 from 12.1 million to 12.7 million, measuring incomes after housing costs (AHC); and from 10 million to 10.4 million, measuring incomes before housing costs (BHC). This is the first rise in relative poverty since 1996-97 (AHC) or 1998-97 (BHC).<sup>10</sup>

What is clear is how short term government thinking has been on this issue. The narrow statistical focus on an arbitrary poverty target, followed by complacent trumpeting of supposedly major reductions in poverty, has obscured the scale and nature of the problems that have yet to be tackled.

### 3.3. Whom have the Schemes Reached?

It is, of course, possible – and it is very much to be hoped – that these disturbing trends will be reversed by the current array of government initiatives. But, in addition to the aggregate outcome-data on deep poverty, there are worrying signs that many of the schemes and initiatives have not been constructed in a way that is likely to lift the most deprived families and neighbourhoods out of multiple deprivation. One interesting example is provided by the Action Teams for Jobs project, which is aimed specifically (and laudably) at helping to secure jobs for those who were either economically inactive, had never worked, or faced multiple barriers to labour market participation. Analysis has now shown, however, that many of those who have been found work under this project had in fact either been jobless for less than six months or were new entrants to the labour market, who were claiming Jobseeker's Allowance and were accordingly not amongst the hardest to help. Similar doubts have been raised about the client group actually helped by the equally well-intentioned Excellence in the Cities programme, the Creative Partnerships Scheme (the evaluation of which states that “at school level...the young people who attended Creative Partnerships activities tended to be less disadvantaged than those in the same schools”<sup>11</sup>), and some of the Sure Start programme (which seems to have been particularly effective for children of medium to high ability rather than for those who are struggling<sup>12</sup>). Indeed, even the former Prime Minister Mr Blair has acknowledged the weakness of programmes like Sure Start as a tool for helping those in the hardest-pressed neighbourhoods to escape from the traps of multiple deprivation: “Sure Start has been brilliant for those people who have in their own minds decided they want to participate. But the hard to reach families, the ones who are shut out of the system...they are not going to come to places like Sure Start.”<sup>13</sup>

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<sup>10</sup> Brewer M, Goodman A, Muriel A, Sibieta L ‘Poverty and inequality in the UK: 2007’ IFS Briefing Note No.73

<sup>11</sup> Eames A, Benton T, Sharp C, Kendall L ‘The longer term impact of Creative Partnerships on the attainment of young people’ National Foundation for Educational Research, February 2006, p7

<sup>12</sup> “These programmes seem to have had limited and small effects: beneficial effects on the least socially deprived families and adverse effects on the most disadvantaged families” – Belsky J, Melhuish E, Barnes J, Leyland A.H, Romaniuk, H & the National Evaluation of Sure Start Research Team, ‘Effects of Sure Start local programmes on children and families: early findings from a quasi-experimental, cross sectional study’ British Medical Journal, June 2006, p6

<sup>13</sup> Unscripted remarks at the launch of Labour's ‘Let's Talk’ initiative, The Guardian, 16 May 2006

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In other cases, these initiatives have suffered from bureaucratic obstacles. The Home Office's evaluation of the Crime Reduction Programme, for example, noted that "by the end of year three of the CRP...[the] level of activity is well below the original expectations...In addition, as indicated, some of these initiatives are showing high implementation failure rates." Interestingly, but disturbingly, the same report indicated that "many of the CRP's companion social policy initiatives (e.g. New Deal for Communities) have experienced very similar problems."<sup>14</sup>

Other projects, including Health Action Zones, Healthy Living Centres, the Playing Fields and Community Green Spaces Initiative and the Community Legal Services Partnerships, have either been discontinued following a pilot-scheme, or quietly have been 'merged', or 'mainstreamed', into other services after a relatively short period – suggesting that they have not been regarded by the Government as outstandingly successful. One evaluation report on the Health Action Zones suggested that their direct impact on their stated target (health inequalities) was minimal because of the short time frame of the initiative as well as limited resources.<sup>15</sup>

### 3.4. Cost-Effectiveness of Schemes

It is difficult to ascertain the true cost of many of these projects, but it seems clear that it is not negligible. The Liveability Fund provided £89 million over three years (2003 to 2006) to help local authorities to achieve innovations in transforming the quality of public spaces<sup>16</sup>; the funding for the Stronger Safer Community Fund – aimed at tackling crime, anti-social behaviour and drugs, at empowering communities, and at improving the condition of public spaces – totalled £208 million for 2006/07<sup>17</sup>; and 2006/07 spending on the Neighbourhood Renewal Fund – designed to enable England's most deprived local authorities to improve services, with the expressed intention of "narrowing the gap between deprived areas and the rest of the country"<sup>18</sup> – was £524 million.<sup>19</sup> These are, by any standards, significant sums of money. Given the worryingly poor overall outcomes so far as deep poverty is concerned, the accumulated evidence of spirals of social dysfunction compellingly presented in *Breakdown Britain*, the continual anecdotal evidence of serious social breakdown in specific neighbourhoods, the accompanying statistical evidence of concentrations of deprivation in those neighbourhoods, and the considerable questions raised about the effectiveness of many of the schemes, it is at the very least open to doubt whether this money has been spent as effectively as anyone would wish.

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<sup>14</sup> Homel P, Nutley S, Webb B, Tilley N 'Investing to deliver: reviewing the implementation of the UK Crime Reduction Programme' Home Office Research Study 281, December 2004, pp60-61

<sup>15</sup> 'Lessons from Health Action Zones' Health Development Agency Briefing No.9, June 2004, p2

<sup>16</sup> House of Commons Written Parliamentary Question, Rt Hon Oliver Letwin MP to Yvette Cooper MP, date answered Monday 26<sup>th</sup> February 2007

<sup>17</sup> House of Commons Written Parliamentary Question, Rt Hon Oliver Letwin MP to Phil Woolas MP, date answered Thursday 8<sup>th</sup> February 2007

<sup>18</sup> <http://www.neighbourhood.gov.uk/page.asp?id=611>

<sup>19</sup> House of Commons Written Parliamentary Question, Rt Hon Oliver Letwin MP to Phil Woolas MP, date answered Thursday 25<sup>th</sup> January 2007

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## 4. The Social Responsibility Approach

### 4.1. The Social Enterprise Model

Those wedded to direct central government schemes as the basic model for addressing issues of social deprivation may argue that any lack of effectiveness in current schemes and initiatives is due either to particular failings that can be ironed out as more experience is gained, or to limited local coordination, which can be addressed by the Government's introduction of Local Area Agreements and the planned new tier of neighbourhood councils in the cities. How far these hopes will be realised in practice remains to be seen.

There is, however, another possible method of relieving social deprivation in hard-pressed neighbourhoods, apart from well-intentioned and highly funded government schemes. This method is based on the idea that, to have a sustained impact on poverty and multiple deprivation, there needs to be significantly more bottom-up and genuinely locally based activity: people in hard-pressed neighbourhoods being encouraged and enabled to take responsibility for improving their own and their neighbours' social and environmental circumstances.

The fundamental thought here is that the waste of human talent represented by those who are trapped in multiple deprivation in our hardest-pressed neighbourhoods is a scandal and a tragedy; and that the process which produces the downward spiral of interacting problems can also be used to reverse it, creating instead an upward spiral where success in tackling one problem can begin to help in tackling others. In preparing this report, we have heard several inspiring stories of disadvantaged young people who have been able to make something of their lives. For instance, the young man who went from crack dealing on his west London estate to university; or the derelict council housing accommodation refurbished by unemployed youngsters in Bradford.

Among the most potent engines for achieving the changes which are needed are Britain's 55,000 social enterprises. Social enterprises are businesses, generating a substantial proportion of their own income, with primarily social objectives rather than being driven by the need to maximise profits for shareholders and owners. Examples range from Jamie Oliver's Fifteen group of restaurants, training unemployed youngsters in the restaurant trade; to the housing group Impact Community Developments, which provides shelter for excluded young people in Bradford; and to Community Foster Care in the West Country, which trains unemployed people to become foster carers, so meeting two separate needs: for jobs, and for foster care.

#### What is a social enterprise?

"A social enterprise is a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners.

"Social enterprises tackle a wide range of social and environmental issues and operate in all parts of the economy...

"Social enterprises are diverse. They include local community enterprises, social firms, mutual organisations such as co-operatives and large scale organisations operating nationally or internationally. There is no single legal model for social enterprises."

*Social Enterprise*, DTI, 2004

"The Bank of England, in its report on financing, distinguished social enterprises from other organisations in the social sector by saying that, in addition to social objectives, they should have "at least some income from trading, or be intending to develop some income from trading within the next year."

*The Financing of Social Enterprises*, Bank of England, 2003

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The best social enterprises are particularly effective at achieving social change. They bring together the enthusiasm and ambition of social entrepreneurs with the disciplines of business. They also tend to be more dependable than alternative providers because they generate their own income rather than relying on government grants.

Of course, social enterprises alone (even in combination with other third sector organisations) cannot reverse the spiral. Government programmes, local authorities and the private sector all have an essential role to play. Nor are social enterprises concerned only with tackling the relief of poverty and deprivation. Nevertheless, third sector activity, and in particular the social enterprise approach, is often among the best able to tackle traps of multiple deprivation, combining (as it can) local knowledge and motivation with flexibility and imagination.<sup>20</sup>

#### **Where do social entrepreneurs come from?**

“At the Skol Centre for Social Entrepreneurship we offer an elective in Social Entrepreneurship in the context of the MBA, which is proving anything but marginal. A third of MBAs [at the Saïd Business School] study Social Entrepreneurship... Demand is coming mainly from younger people. It seems they are less content now to see trade-offs between straightforward commercial activity and their personal interests, and are wanting to make some sort of contribution. Typically these are high achievers.

There is a second sort of social entrepreneur who typically has had some sort of experience of social deprivation or exclusion themselves which has acted as a spur...”

*Rowena Young, Director of the Skol Centre of Social Entrepreneurship at the Saïd Business School at Oxford*

#### **An education for life**

“Most of the staff we’ve got here have come from a disadvantaged or homeless background, and yet commercially they are sounder than most people, though none of them has been to university. If I was going to set up a business tomorrow I would use them all.

“Coming into contact with a social enterprise rubs off on our clients to help them become enterprising employable people. If a charity is seen to have a government grant then our clients also tend to sit there and expect a handout.

“The council spent a fantastic amount of money on a 64-unit development of bedsits and they never could fill it because people didn’t really want that. It fitted all the criteria laid down by the housing corporation, but it didn’t really fit what the community wanted... We have consistently had a waiting list and been 95% full for the last 8 years... Communities are full of different people with different issues but the council has built just one type of property to satisfy one type of person. Any good business keeps close to its customers.

“The council had two problems: difficulties with young people and boarded up blocks they didn’t know what to do with. I came along with one good solution, to take over and refurbish the blocks and house the homeless youngsters... There are other housing associations with similar problems. But we have had to wait months and months, until they were absolutely desperate and a property was semi-derelict, before they would release it to us.”

*Nigel Delaney, Chief Executive of Impact Community Developments, Bradford.*

## **4.2. Barriers to Social Enterprise**

The ability of social enterprise, and of the third sector more widely, to help the most hard-pressed communities is at present impeded by the barriers which are placed in its way by government.

These barriers do not arise from ill will on the part of the present Government towards social enterprise or the third sector as a whole. The Treasury has recognised that social enterprise and third

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<sup>20</sup> See, for example, work by US researcher Professor Lester Salamon, Johns Hopkins University

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sector organisations provide a service that is often of higher quality, more efficient, more equitable and more personalised than that delivered through either public or private delivery. Hilary Armstrong (the former Cabinet Minister with direct responsibility) has said<sup>21</sup>:

*“Some people simply lack the capacity to access and exploit [public] services however far they reach. Others have developed through experience an intrinsic mistrust of the state... For these groups, a greater use of the charitable and voluntary sector will be crucial since such groups can fulfil these specific public policy objectives of reaching out much better than publicly run services.”*

Indeed, in recent years the third sector, and social enterprise in particular, has received unprecedented attention from government and the political establishment. One consequence of this has been the creation of an Office of the Third Sector (adopting a proposal in the Conservative Party’s 2001 Green Paper ‘Sixty Million Citizens’). Ed Miliband, then Minister for the Third Sector and now Hilary Armstrong’s successor as Minister for the Cabinet Office, appeared to have understood that the third sector is uniquely qualified to help the vulnerable, when he told an ACEVO summit recently (June, 2006):

*“You [the third sector] have the ability to reach out to many groups and individuals that the Government cannot reach... you are innovators in a way that the Government and private sector is often not... you have led the way in innovating in public services and beyond...”*

However, for all the rhetoric, the Third Sector Working Group report in *Breakdown Britain* shows that the Government’s record in supporting the third sector leaves much to be desired, particularly in two fundamental respects.

First, although the value of the third sector’s work in combating poverty is clearly evident, the Government still does not support it enough, or perhaps even trust it enough, to deliver the sort of remarkable outcomes it is capable of. Not only has the Public Accounts Committee condemned the slow rate of transfer of public services to the third sector in general, but time and again the Working Group highlights the lack of funding support for the third sector’s work in fighting poverty, and the problems with payment terms, length of contracts, full cost recovery, tax, and other excessive regulations that are particularly hindering the sector.

The Government’s target of increasing the volume of public services provided by the third sector by 5% by 2006 should be met, but has been described as ‘not a very demanding’ goal by the Public Accounts Committee, which called on the Government to set a ‘more meaningful and stretching target’.

Last year, an ACEVO survey of 74 TSO chief executives found that progress towards achieving full cost recovery had got worse since 2002: almost 80% felt that the situation had either got worse or stayed the same – and overall, more felt that it had got worse than better.

A recent NCVO survey of TSOs found that 55% of respondents had not had statutory funding agreed promptly for the current financial year, and several were still waiting to reach agreement months after funding was supposed to start. 47% had not had funding agreed in advance, meaning that they were forced to draw on their reserves.

According to the Charities Tax Reform Group, irrecoverable VAT costs UK charities between £400 and £500 million each year.

*Breakdown Britain, Volume 6, Page 11: Denying the vulnerable a second chance: undervaluing Britain’s third sector in the fight against poverty, December 2006*

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<sup>21</sup> Hilary Armstrong MP, ‘Social inclusion means tough policies’ *The Guardian*, 5<sup>th</sup> September 2006

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The Working Group’s findings are in line with public opinion. A recent YouGov poll for the Group found that 75% of the interested public believe that the Government should provide more funds to the sector, and also that red tape and regulations are inhibiting third sector organisations.

Second, when it does involve the third sector in such crucial work, the Government appears to forget the attributes that attracted it to the third sector in the first place. These include its independence, enthusiasm, innovation, commitment and diversity. Instead, in the commissioning process, the Government (which is now the biggest funder of the third sector, providing 38% of its £26 billion of income) frequently uses contracts to direct requirements in such a detailed way, places such tight controls on the programmes, and awards contracts to so few, large organisations<sup>22</sup> that it runs the risk of shaping a third sector in the image of the public sector – the very result it wanted to avoid in the beginning.

*“I don’t think statutory organisations always understand voluntary organisations... They seem to feel that they can intervene at a very detailed level, on the nature of the operation.”*

Stuart Etherington, NCVO

*“It is felt within the third sector that commissioning should mean commissioning the organisation to deliver what it delivers. However, it would appear that within local government commissioning means commissioning the organisation to deliver the government agenda and specification.”*

Charles Drew, Amber

*“61% of those who responded to our survey believed that regulation inhibited social innovation. Prescriptive and overly protective approaches to regulation are leading to loss of diversity in the sector and greater conformity in the way people and organisations operate.”*

Better Regulation Taskforce

*Breakdown Britain, Volume 6, Denying the vulnerable a second chance: undervaluing Britain’s third sector in the fight against poverty, December 2006, p12*

It is often the smaller third sector organisations and social enterprises with very local roots that are most likely to be able to identify and tackle the specific, local problems of the hardest-pressed neighbourhoods. As the Institute of Volunteering Research put it, in a submission to the Conservative Social Justice Policy Group, “the advantage of smaller organisations may well be the degree to which they are rooted in the locality”. Such enterprises and groups, by being closer to their community, and involving more local volunteers working on specific local projects, inevitably generate significant social capital in the communities they serve – creating support networks in communities, building horizontal ties across society in activities like prisoner-befriending schemes, and linking third sector organisations with official institutions. Professor Bob Holman illustrates the effect that this can have on community engagement, citing the example of FARE’s (Family Action in Rogerfield and Easterhouse) AGM, which attracted many more local residents than were in attendance at a local political party’s meeting.

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<sup>22</sup> The Conservative Social Justice Policy Group notes that smaller charities make up 87 per cent of Britain’s third sector, but receive just 5.4 per cent of its income

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## Finding a job

“Where we differ from the job centre is we go out into our community and we ask, persuade, cajole, talk people round, encourage them, support them into the idea that employment is a viable alternative to benefit and crime. It’s easier coming from us because we have the same education and background and live in the same place and face the same problems. When some of the boys see that people they live with are working, it suddenly all seems possible, and then they try much harder. The key thing with young people is to get at the people who are slightly older than they are. When you get boys who are 26 or 27 into work it impacts an entire family in a way that youth work won’t. Those kids look up to the older members of their family. So when their dad, uncle or cousin is working, then all of a sudden it seems like the done thing. And people in work almost always advocate education to the children in their world.”

“The key thing in our job club is we don’t chase people around too hard, we make them work for it. Our motto is: we’ll do nothing for you, but will help you do anything. For instance, in the past when we did training we used to do it for free. We still do it for free, but in order to make the take-up higher we charge them a £20 deposit which is returnable so long as you turn up. If you turn up and pass you get the deposit back, if you turn up and fail you get your deposit back. If you don’t turn up we keep it. To my surprise not only has the number of people dropping off decreased drastically but more people want to sign on in the first place. I say to them now you’ve paid the £20 you’ve got rights: you can moan! We are trying to give the power back to them, make them take charge of their own lives. Locally that’s far easier to do than to write a policy nationally.”

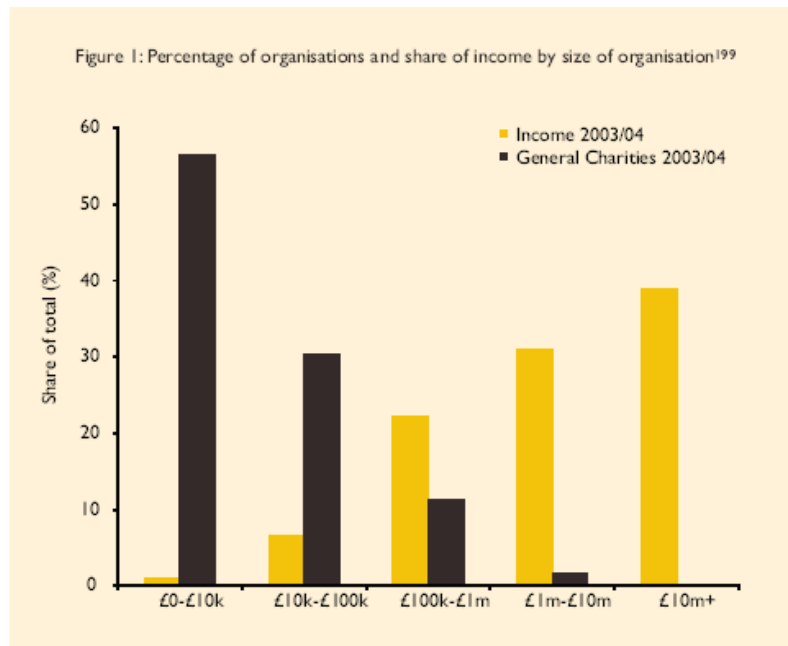
*Shaun Bailey, founder of My Generation, West London.*

Despite this, analysis of income trends shows that smaller third sector organisations have been marginalised increasingly over the past 10 years, with their share of total voluntary and statutory income falling 30% during that period. The Charities Aid Foundation concludes that smaller charities may be becoming unsustainable. In public sector work, smaller third sector groups, including a large number of small social enterprises, are being crowded out by big charities because of the increasing award of statutory contracts to large scale providers. In addition to this, increased government regulation, especially in relation to competitive tendering rules, is having a negative impact on smaller organisations that do not have the resources to pass the tests of government commissioning authorities.

Apart from losing out on government-funded work, smaller organisations are also suffering a fall in their non-statutory funding, as larger social enterprises and charities, with a greater profile and fundraising abilities, take a greater share of the income.

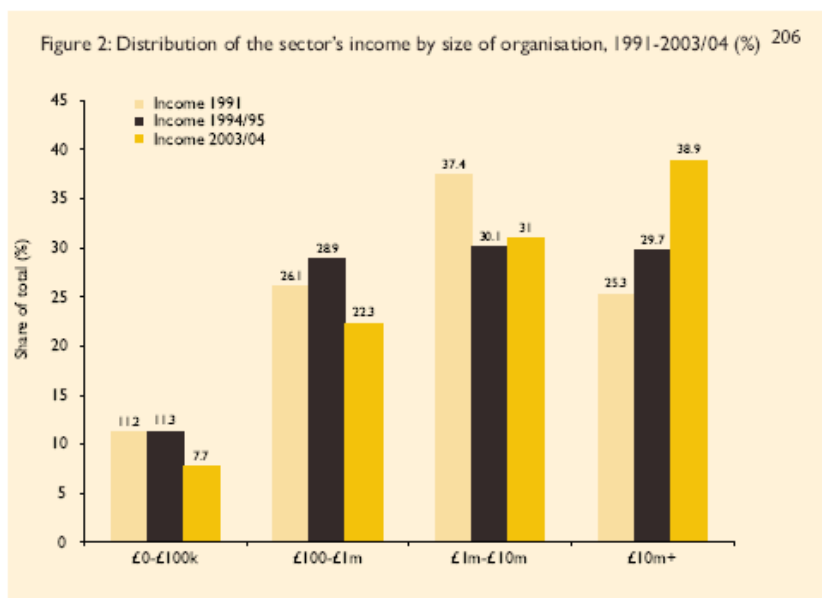
Generally, smaller organisations are also suffering disproportionately under the present complex tax system; and the regulatory burden is now such that smaller social enterprises find it increasingly difficult to establish themselves.

It is disturbing to see how, on so many different fronts, smaller third sector community organisations appear at present to be under considerable pressure.



Source: NCVO, UK Voluntary Sector Almanac, 2006, p54

Using charities as a proxy for the whole third sector, and looking first at income, 87% of charities currently have an income of under £100,000 a year (see Figure 1). But the share of the UK's total charitable income enjoyed by those smaller charities has *fallen* by over 30% in the last ten years<sup>23</sup> (see Figure 2), while the share of income enjoyed by those charities with an income of over £10 million a year has *increased* by over 30%.



Source: NCVO, UK Voluntary Sector Almanac, 2006, p55

In a similar trend, the total income enjoyed by smaller charities with under £100,000 of income fell by £110 million between 2002 and 2004, whilst charities with incomes of over £1 million grew by over £800 million (see Figure 3).

<sup>23</sup> See UK Voluntary Sector, an analysis of charities characteristics by stratified income, Russell White, Conservative Social Justice Policy Group, [www.povertydebate.com](http://www.povertydebate.com)

Figure 3: Total income by size of organisation, 2002/03 and 2003/04 (£million)

	Under £10k	£10-£100k	£100k-£1m	£1m-£10m	Over £10m	All
2002/03	290.8	1,845.20	5,411.10	7,656.40	9,939.20	25,272.70
2003/04	289.2	1,736.60	5,882.80	8,171.70	10,233.20	26,322.60
Total change (%)	-0.6	-5.9	6.2	6.7	3	4.2
Total change (£million)	-1.6	-108.6	341.7	515.3	294	1,049.90

This substantial and growing polarisation of income has been noted with understandable concern. Thus Stuart Etherington, Chief Executive of the NCVO, in a hearing before the Conservative Social Justice Policy Group in July 2006<sup>24</sup>:

*“I think there’s clearly a polarisation between the large and the small. The big get bigger and the small get smaller, a bigger gap growing...”*

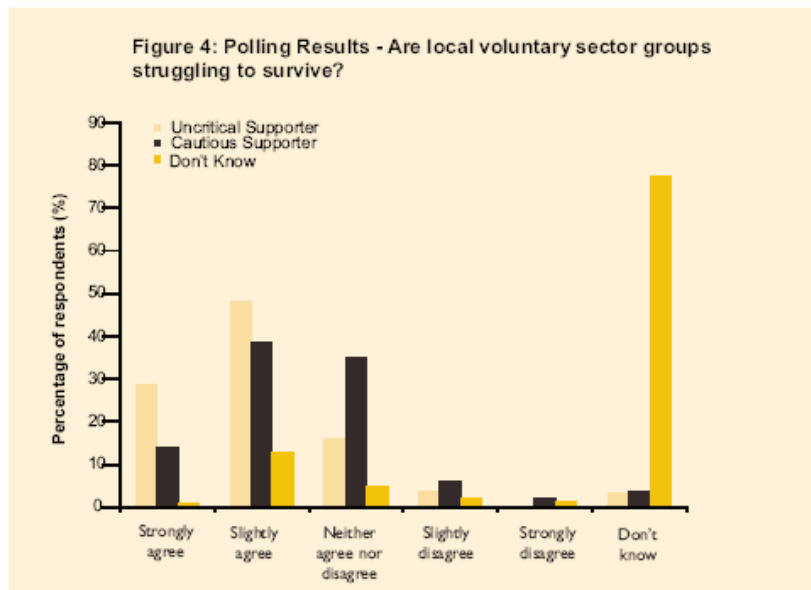
Les Hems, development director of Guidestar, similarly commented to the Third Sector Working Group, in September 2006:

*“Small charities are being outgunned by their bigger rivals in the fundraising game.”*

Most blunt of all is the alarming conclusion of the Charities Aid Foundation:

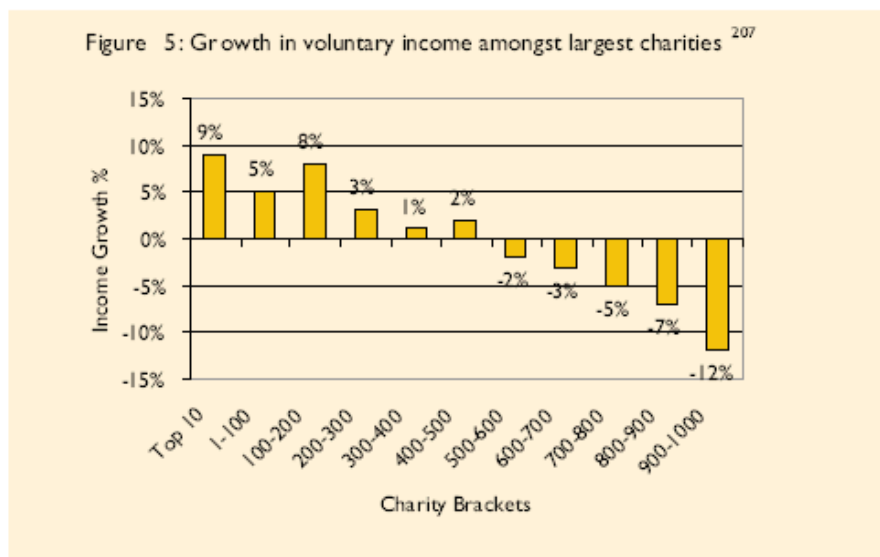
*“At a time when voluntary income is showing modest above-inflation growth, the fall in income in smaller charities demonstrates a polarisation that, if it continues, may in future result in smaller charities becoming unsustainable.”*

The Charities Aid Foundation’s view is shared by the knowledgeable general public. In a YouGov poll for the Conservative Social Justice Policy Group, 75% of the public interested in and supportive of the third sector said that they believed that local third sector groups are struggling to survive (see Figure 4).



<sup>24</sup> Echoing the 2006 NCVO Almanac, State of the Sector: “our evidence suggests that this concentration of resources is becoming more acute over time”, p6

In terms of voluntary income, it is clear that the top larger charities are increasing their share of voluntary income at a fast rate. The growth of income from fundraising events was 16% for 2004/05, with the top ten mega-charities obtaining 80.3% of their income from voluntary income sources, in contrast to the charity sector average of 44.9%.<sup>25</sup> This trend looks likely to continue on present growth figures (see Figure 5).<sup>26</sup> The reasons for the larger charities' increasing dominance in fundraising are easy to imagine – namely, greater fundraising budgets, and therefore greater public awareness of, and habitual giving to, larger charities; and an inability of smaller charities to make headway in the face of pressure from larger rivals.



CAF, *Charity Trends 2006* (CAF, London), 2006, p24

Analysing the dwindling income of smaller charities, it is clear that the polarisation is similar whether the income is coming from the general public or grant-making private institutions by way of voluntary income, or from the statutory sector. This strongly suggests that the same patterns apply in the case of social enterprises (for which the data is currently less comprehensive).

In terms of statutory income, while its overall volume has increased dramatically as a share of all charitable income over the past ten years (from 28% to 31.1% – see Figure 6), it seems clear that again its distribution is polarised to the benefit of the larger charities. Thus, the NCVO's 2006 Almanac states:

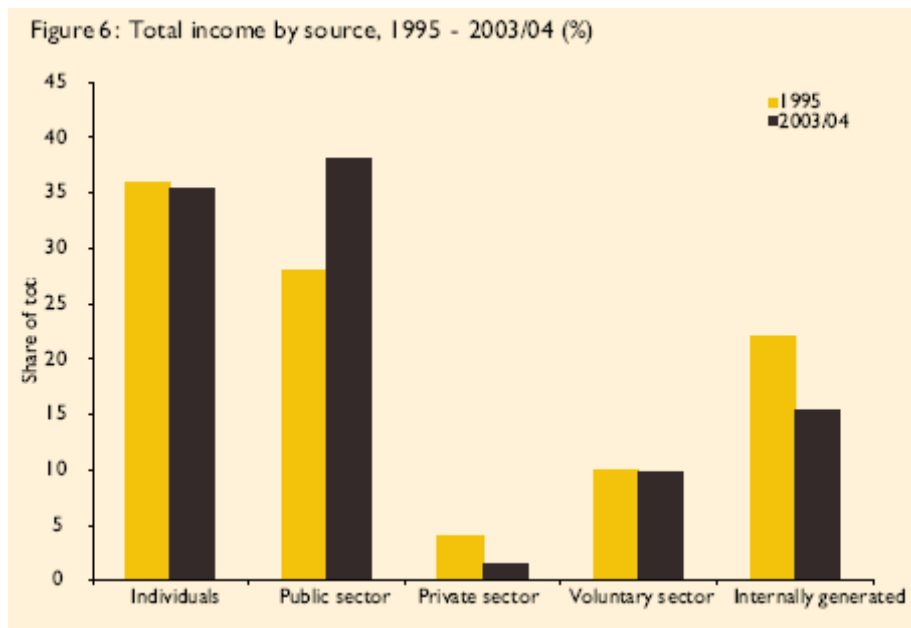
*“Our evidence indicates that statutory funding has increased from approximately £3.2 billion in 1991 to £10 billion in 2003/04. Our analysis suggests that over two-thirds (68.8%) of statutory resources flow to general charities with incomes of over £1 million; in other words, government funding broadly correlates with the distribution of total income.”*

Further, in its written submissions to the Third Sector Working Group, the NCVO states:

*“NCVO’s research shows that small and medium size voluntary organisations are not yet benefiting from the increase in statutory resources flowing to the sector as a whole.”*

<sup>25</sup> See UK Voluntary Sector, an analysis of charities characteristics by stratified income, Russell White, Conservative Social Justice Policy Group, [www.povertydebate.com](http://www.povertydebate.com)

<sup>26</sup> There are also indications that, at the top of the charity tree, there is little movement in terms of rankings by income – which itself indicates a possible lack of dynamism



Source: See *UK Voluntary Sector, an analysis of charities characteristics by stratified income*, Russell White, Social Justice Policy Group, [www.povertydebate.com](http://www.povertydebate.com)

In the meantime, in relation to the statutory sector, it is easy to see that there will be some degree of tension between central and local government’s aspiration to deliver a standardised and cost-efficient professional service in certain areas, and the smaller third sector organisations’ lack of financial resources, training, capacity, and economies of scale.

In these circumstances, and in the current climate of public sector savings, it is not difficult to see why smaller third sector organisations have found themselves crowded out: for example, in the recent award of public sector contracts to assist the long term jobless into work, through Jobcentre Plus New Deal. A4E, a large private supplier, acknowledged the complaints of smaller non-statutory competitors in this regard, and Tomorrow’s People, a significant third sector organisation with wide national reach, commented in September 2006:

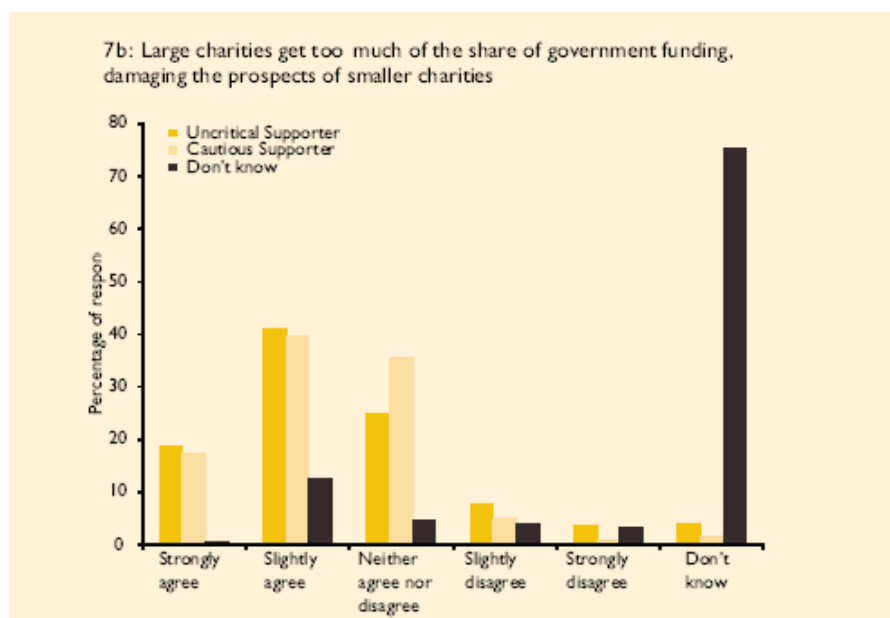
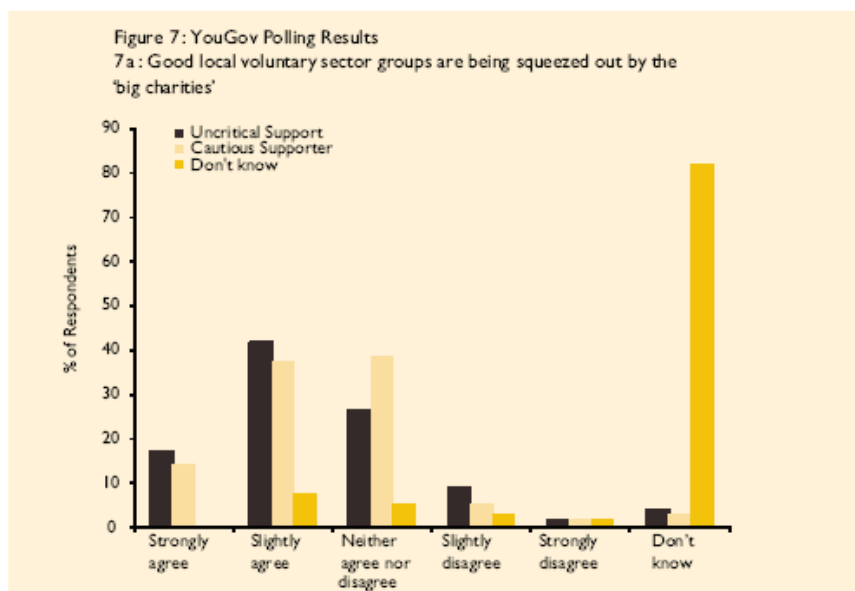
*“There’s definitely a move by government to have fewer providers holding larger contracts, which has a negative impact on many organisations in our sector.”*

Similarly, St Mungo’s, a provider of drug and alcohol treatment in London, gave evidence to the Working Group in the following terms:

*“...In most areas, local authorities are selecting a small group of preferred providers; and in most contracts they will only commission one lead agency.”*

And in the field of money advice, nearly 90% of recent government grants to the third sector from the Financial Inclusion Fund have gone to the national Citizens Advice Bureaux Federation, together with some partners.

From polling conducted by YouGov for the Conservative Social Justice Policy Group, this is a trend the public appears to be picking up on. Two polls (see Figure 7 and Figure 7b) show that, of those polled who were interested and supportive of the third sector, a significant majority (approximately 70%) thought both that local third sector groups were being squeezed out by big organisations, and that big organisations got too large a share of government funding, damaging the prospects of smaller groups.



Naturally, one area which acts as a brake on the ability of the smaller organisations to survive and thrive is in the commonly acknowledged growth in regulation.<sup>27</sup> This is an area which disproportionately affects smaller third sector organisations (just as it does smaller businesses), as they often lack the resources to cope. Some of this particularly affects the areas that we are most concerned about – such as stringent legislation affecting the use of volunteers in drug misuse treatment. As Sir David Arculus’s Better Regulation Taskforce report found:

*“61% of those who responded to our survey believed that regulation inhibited social innovation. Prescriptive and overly protective approaches to regulation are leading to loss of diversity in the sector and greater conformity in the way people and organisations operate.”*

We have heard from many organisations in the family, addictions, joblessness, and indebtedness fields. They describe the length of time taken to comply with government tendering processes (20 days in some cases, for only modest proposals); the bureaucratic and micro-managing nature of some government programmes (such as Supporting People); and the burdensome nature of the increasing

<sup>27</sup> See Better Regulation Taskforce, ‘Better Regulation for Civil Society’, November 2005

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CRB, health and safety, and employment regulations. Regrettably, the Government completely failed to respond to the Better Regulation Taskforce's recommendations within the specified two month period, and indeed responded only in November 2006, over a year later. This would seem to indicate that the Government does not take the Taskforce recommendations seriously.

Consultation with third sector organisations also provides anecdotal evidence of the excessive regulation entry cost for new, smaller, innovative groups. Thus, when asked by the Conservative Social Justice Policy Group how easy it would be for a small provider to start up in their area, responses included:

"It would be very difficult indeed. The principal obstacles would be getting sufficient financial support to start operations; finding an affordable building and getting planning permission; getting referrals if they required funding. It could only continue if its donor base was sufficient to maintain its revenue stream, and would probably face local authority opposition if worked with a socially excluded client group. It would not be eligible to bid for SP [Supporting People] money if it was not already an SP provider, and would not be able to get PCT commissioning until it had a track record/evidence base..."

*St Mungo's, London*

"Very difficult. Tenders are competitive...Also, infrastructure costs, with all that SLA demands, are considerable, and this would make it very difficult for a small organisation to deliver; and they would be very expensive as a result."

*CAN, Northampton*

"We have been undertaking such an initiative in Southend, and it has been anything but easy. The level of funding has not been adequate to get the service properly operational, and securing accommodation was a difficult task."

*ADAS, Harlow*

"Issues of compliance (health and safety, employment legislation) would make it very difficult for a small organisation to get started."

*Aquarius, Birmingham*

"Very difficult as commissioners rarely commission services without a proven track record."

*Mainliners*

These downbeat responses are a long distance from the welcoming environment we would like to see, particularly in a field like drug addictions, which is crying out for the help of more, smaller third sector organisations, with their effective client-intensive approach.

One other related aspect of regulation, which unduly affects smaller third sector organisations, is the tax system. Not only do they suffer from the unfairness of irrecoverable VAT (as other larger third sector organisations do), but the Finance Act (No. 2) also recently abolished an exemption on non-qualifying expenditure worth £10,000 to small charities. And as the widely respected Charity Tax Reform Group put it:

*"Smaller charities often lack the resources to pay professional advisers and as a result find it difficult to take advantage of some of the legitimate means of reducing their tax burden."*

Finally, it would be wrong to leave this subject without commenting on a significant movement that currently assists small organisations. This is the partnerships between large and small third sector bodies, encouraged by central government and local government commissioners. Such schemes, when they work, often help smaller organisations to learn valuable management skills, whilst bringing the bigger organisations closer to the communities they need to help. Examples of the many that exist across the country include Capitalise (a debt advice scheme launched in the summer of 2006 across

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London, through the leadership of Toynbee Hall), Barnardos and Off the Record (helping young people in Bath), and Addaction and Action for Change (drug treatment in Brighton). The approach of Addaction, as expressed to the Conservative Social Justice Policy Group in September 2006, is to be applauded:

*“Addaction aims to ensure that it develops relevant complementary partnerships or joint services with appropriate organisations so that service users’ needs are addressed holistically. Priority areas for partnership working include ethnic minority organisations, domestic violence agencies, young people’s services, employment, housing... As an organisation we are keen to develop more organisations to support smaller organisations (such as ethnic minority providers) that do not have the infrastructure to compete.”*

However, there is a danger that with the increasing ‘contract culture’ in the third sector, smaller organisations will feel compelled to agree partnerships with larger organisations solely to secure statutory funding. In doing so, smaller organisations may be forced to comply with overly prescriptive contracts.

### 4.3. Supporting the Third Sector

In its second report, *Breakthrough Britain*, the Conservative Social Justice Policy Group put forward a series of recommendations, aimed at increasing the ability of third sector organisations to live up to their full potential as agencies that can help lift individuals, families and neighbourhoods out of multiple deprivation. These recommendations are now being debated within and beyond the Conservative Party. They include:

#### *Making Gift Aid easier to claim*

To make it easier for TSOs to reclaim Gift Aid, a certain percentage, perhaps 80%, of all individual donations could be assumed to come from taxpayers, and qualify for Gift Aid without the paperwork currently needed to ‘opt-in’. This simplified system would generate a sizeable increase in fundraising revenue for many charities.

#### *Launching a ‘Trustmarking’ website*

An independent website could be created to accredit the work of smaller poverty-fighting TSOs, and to promote giving to them. Run as a social enterprise, the site would help funds flow to those charities getting good results. Initially, donations to trustmarked TSOs through the site would attract Enhanced Gift Aid at double the normal rate. A fixed fund of £50 million would generate an extra £150 million for participant TSOs.

#### *Introducing Charitable Remainder Trusts*

Charitable Remainder Trusts (CRTs) could be introduced as tax-efficient vehicles for planned giving. These would enable a person to donate assets whilst receiving tax benefits and an income stream from them. Many assets such as second homes could be transferred to charities during their owners’ lifetimes.

#### *Boosting Corporate Social Bonds*

To raise levels of corporate giving, a drive could be launched to increase the number and value of Corporate Social Bonds. These raise funds from companies who forego capital growth and interest income on their investments, but are guaranteed it all back after five years. Accumulated capital growth and interest is invested in local projects.

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### *School Giving Vouchers*

Through this one-off initiative to help instil habits of charitable giving, all Year 6 pupils in England would be issued with a £5 giving voucher each term. After presentations on the work of poverty-fighting and other TSOs, they would donate their voucher to the charity of their choice.

### *Preventing accumulation of excessive reserves*

Charities are currently holding reserves of approximately £35 billion. The Group recommended that the Charity Commission should do more in this area to uphold fairness, protect the reputation of the sector, and maximise the amount of Gift Aided public donations being put to work by charities – by tightening the guidance that currently allows some TSOs to hold excessive reserves.

### *Launching a 'V Card' to boost volunteering*

A V Card reward scheme could be introduced to engage young and socially excluded people in volunteering. Member charities would record the types and amount of volunteering done by participants, who would earn credits that could be redeemed for hard benefits such as concert tickets. This card would also record achievements that could be used by holders to build a CV.

### *Promoting volunteering in poverty-fighting areas*

Continued government funding for agencies such as CSV, Volunteering England and V, which promote volunteering and provide volunteering opportunities, could be made conditional on them doing more to increase the number of those volunteering to work with poverty-fighting charities and socially excluded groups.

### *Volunteering at school*

To encourage young people to contribute to their communities, volunteering schemes could be introduced in schools. In time allocated to PSHE, Year 9 pupils could all be asked to design social action projects, vote on the most popular, and then execute it. Good citizenship is best learned through practising it.

### *Strengthen the Compact*

To ensure charities get a fair deal in funding and other areas, multi-year funding, prompt payment and full-cost recovery could be enshrined in legislation. Whitehall's 'Compact Champions' could operate at Grade 2 instead of Grade 3, and Local Area Agreements could include evidence of progress towards full Compact implementation by members of the Local Strategic Partnership.

### *Greater third sector delivery of public services*

Spending Reviews could set out how each department, and government as a whole, would give the third sector the maximum opportunity to deliver services. Crude targets should be avoided and, to ensure innovation and diversity in services, commissioning should be reformed to reverse the trend towards ever larger contracts. Also, the next round of Local Area Agreements should be required to include strategies on maximising third sector delivery of services.

### *Less bureaucratic and prescriptive funding*

Government funding, especially contracts, could be far less prescriptive, stating expected outcomes while respecting TSOs' capability to determine how best to achieve these, rather than micro-managing the sector. Increased use of schemes that improve outcomes data, from the National Outcomes Programme and the PQASSO standard to trustmarking, could help here. More standardised contracts could help reduce excessive reporting burdens.

### *Assessing the burden of irrecoverable VAT*

Charities are unable to reclaim up to £500 million incurred annually on activities in pursuit of their charitable objectives. Finding the money to tackle this injustice would be very difficult. Further

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research is needed to establish whether reform would benefit significantly TSOs of different types and sizes, and how many changes might be phased in.

#### *Shifting from direct to indirect statutory funding*

Government funding of the third sector could include much more indirect funding (including tax relief, voucher schemes, asset transfer, match funding and community endowments) to balance the current overwhelming emphasis on top-down contracts and grants. The distinction between direct and indirect funding could be hardwired into all statutory funding and strategies implemented by every public funding body, in order to facilitate this shift.

#### *Introducing voucher schemes*

Progressively empowering users of government-funded services with the ability to choose between providers could help to drive up standards and ensure diversity of provision. Vulnerable people who are overcoming problems such as homelessness and addictions could be endowed with vouchers to acquire housing-related support throughout England. New relationship and parenting education programmes worth £166 million annually could be funded by a voucher scheme, enabling choice between third sector providers.

#### *Enabling more opportunities to take over under-used public assets*

Legislation is needed to make it easier for TSOs to initiate the transfer of under-used public assets such as neglected buildings, and to do so from all public bodies rather than just local authorities. The Government's £30 million Community Asset Fund could be doubled to help TSOs take on these assets.

#### *Community Growth Trusts*

Smaller TSOs with significant growth potential could apply for the new legal status of Community Growth Trust. This would entitle visionary social entrepreneurs, faith based organisations, and community groups to deliver an increasing range of public services to their community as a reward for proven competence.

#### *Community Foundation Challenge Fund*

A new £50 million Challenge Fund could significantly boost the giving of grants to poverty-fighting TSOs, through the national network of 55 Community Foundations. The Foundations' track record indicates that they could generate an additional £100 million in private sector giving, creating a Fund total of £150 million. Invested in an endowment, this would enable £7.5 million of grants to be distributed annually to poverty-fighting groups in perpetuity.

#### *More effective use of National Lottery funds*

National Lottery money to good causes could be reformed to ensure more funding reaches smaller charities, especially those tackling the causes and consequences of poverty. At least half of the Big Lottery Fund (BIG) funding could be allocated to lightly prescribed, demand-led programmes. A new £100 million funding stream, *Fair Share Plus*, would provide expendable endowments of £1 million to around 100 communities to tackle social problems. Lottery funding for good causes also needs to be protected from further Olympic-type raids.

#### *Enhancing the third sector's voice in Cabinet and Parliament*

Increasing the third sector's status in Westminster is important, as society becomes ever more dependent on it to tackle poverty and to provide second chances. Therefore, the Minister of the Third Sector should have Cabinet rank, and there should be a Third Sector Select Committee to scrutinise the work of the department, in a similar manner to other departmental select committees.

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### *Creating a level playing field for faith based organisations*

There is increasing evidence that effective faith based organisations (FBOs) are being discriminated against by statutory funders, with the vulnerable people they serve losing out as a result. Legislation could be introduced to allow religious and non-religious charities to compete for public funding on equal terms, after a review of laws that FBOs consider are being used unfairly against them; and a faith standard could be used to help FBOs achieve the highest standards in serving clients from all backgrounds.

### *Establishing a Third Sector Institute*

The evidence base for policy making on many third sector issues can be patchy. An incoming government should heed calls for a third sector equivalent of the Institute for Fiscal Studies to be established, by funding up to half its costs. Conducting a detailed mapping exercise to establish a much fuller picture of the extent and impact of state funding on the sector would be one of the body's first research projects.

## 4.4. Social Enterprise Zones

The general measures proposed for consideration by the Conservative Social Justice Policy Group in Section 3.3 are designed to enable social enterprises and other third sector organisations to overcome many of the barriers identified in Section 3.2. But there is also a need for particular action to make it easier for third sector organisations, and especially social enterprises, to flourish in the hardest-pressed neighbourhoods, where families caught in traps of multiple deprivation are concentrated. Twenty-five years ago, the Thatcher Government tackled the economic and physical dereliction of the former London docklands and other run-down areas by creating Enterprise Zones in which developers and other agents of change received special incentives. The result was a notable success. Regeneration of these areas was fast-tracked, renewing neighbourhoods and creating jobs.

The challenges of today have less to do with physical infrastructure than with social infrastructure. But the principle of concentrating resources and encouragement in the areas most in need remains powerful. That is why David Cameron has promised to introduce Social Enterprise Zones, where social enterprises can be properly enabled and all unnecessary obstacles to their effectiveness removed.

As identified in Section 4.1. of this report, social enterprises are businesses, generating a substantial proportion of their own income, with primarily social objectives rather than being driven by the need to maximise profits for shareholders and owners. The combination of business ethos and social commitment can make them particularly effective in tackling social problems.

In an opinion survey we carried out among social enterprises<sup>28</sup>, more than four fifths of respondents supported this idea. An even greater preponderance said they should be applied flexibly rather than defined according to a grid imposed by Whitehall. This concern was also reflected in their comments that “bureaucracy” and “control freak government” were among the main obstacles experienced in their day to day operations.

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<sup>28</sup> We are grateful to the Social Enterprise Coalition (SEC) for giving us access to its members for the purpose of this survey

### Changes which social enterprises would like to see from Government

“Fiscal acknowledgement of the social benefit derived from the work of social enterprises.”

“Wider understanding of Community Interest Companies plus tax aid, like charities.”

“Let those best able to deliver to deprived communities do it, rather than looking for a one size fits all approach.”

“Break large public sector contracts into smaller bite-sized chunks that SMEs, and particularly social enterprises, can compete for.”

“There are too many sources of funding requiring very different criteria—amazingly complex and contradictory if you don’t know how to play the funding game. Some are for small amounts but require huge amounts of paperwork—remember many social enterprises are led by volunteers.”

“More consultation about local and regional strategies. ‘Third Sector’ does not mean third class.”

“Simplified approved supplier procedure [by local authorities and primary care trusts]. We are not all big companies.”

“Social Enterprise Zones would encourage the growth of socially responsible businesses across all areas for the benefit of deprived communities which suffer from lack of services and minimal employment opportunities.”

*Responses from the survey conducted by the Conservative Policy Review among Social Enterprise Coalition members, Nov 2006.*

Social deprivation is not something that can be measured easily. Aspects of it are all too clear from statistics – the number of children leaving school with no qualifications, incidents of violent crime, joblessness – but the interaction of these, which leads to disadvantaged communities, is less easy to pin down. What is clear is that you know it when you see it.

We believe the right way to identify areas of special need is by making them self-selecting. Local authorities or other competent local bodies should be asked to propose neighbourhoods for Social Enterprise Zone status, where social enterprises would have special privileges.

The key is to keep decisions local. Statistics designed to measure deprivation can give useful information, but they are no substitute for observing the reality on the spot. By making Social Enterprise Zones self-selecting, many potential problems regarding borderlines and the assessment of relative need will be avoided.

#### 4.4.1. Investing in Success

Having enabled local authorities to identify the neighbourhoods of greatest need, how can we best release from its shackles the power of social enterprises (SEs) in those neighbourhoods? The biggest single obstacle facing SEs – and the most striking contrast between SEs and their commercial counterparts – is their lack of access to external finance. A survey carried out by Taylor Nelson Sofres for the Bank of England<sup>29</sup> a few years ago showed that, out of a sample of 200 SEs, nearly a third identified difficulties in obtaining external finance as the greatest barrier to expanding trading – considerably more than the 7% of equivalent commercial enterprises that considered external finance a problem. “Access to external capital is the number one issue for social enterprises,” a banker confirmed.

<sup>29</sup> ‘The Financing of Social Enterprises: A Special Report by the Bank of England’ May 2003, p26

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This is not only a problem of supply. Many SEs, especially smaller ones and start-ups, prefer grant money to debt or equity on the grounds that, although it is usually short term and often hedged with restrictions, it does not have to be repaid or serviced and can therefore be applied entirely to social ends. SEs tend to be culturally averse to borrowing. As one accountant specialising in social enterprises told us: “It is often difficult to persuade my clients of the advantages of gearing up”. In the case of equity, many SEs fear that sharing ownership may result in dilution of their social aims.

#### **Capital ideas**

“We are under capitalised, and that’s one of the disadvantages of the social enterprise model, and to some extent is going to limit our growth. We don’t have the equity. For instance, we’d find it extremely difficult to put together enough money to set up a depot on a speculative basis on the expectation that we’d win work in that area subsequently. We are a bit beyond the hand to mouth stage, but still some way from sitting on what I would regard as a comfortable pile of assets... The answer is you’ve just got to persuade the banks to lend you the money. If we were something a little bit fluffier than we are, that might be harder. So I think there is a role for pump priming funding.”

“I’ve become very market oriented in recent years, and I think one of the problems with a lot of social enterprises is that they don’t understand that there is a market and they are not owed any favours.”

“Trading profits against quality is difficult. One of the advantages of the social enterprise model is that the orientation is more towards the social objectives and less towards the economic returns. We aim to make a profit, but we are not a profit maximising business. As a result we provide better quality services than if we were.”

*Stephen Sears, Chief Executive of ECT Group, a transport and recycling enterprise.*

However, there clearly are real limitations on the availability of finance for the social enterprise sector. Banks can be reluctant to lend to enterprises which find it difficult to offer collateral or personal guarantees on loans. They may also be afraid of damage to their reputation, if they have to call in a loan and are then blamed for the demise of a social enterprise doing popular work in the community. Meanwhile, equity investors are often put off by the prospect of below market returns, and by potential difficulties in exiting from their investment.

The Bank of England’s conclusion was that there was indeed an unmet demand for “patient capital”<sup>30</sup>. This could be either debt or equity, or some combination of the two, but would in any case be long term and at sub-market rates. The need for such finance was often greatest at the point where a social enterprise was starting up or attempting to expand. This was borne out by our own research. Asked what the biggest hurdle in setting up his own social enterprise was, one entrepreneur told us: “The £5000 it cost in lawyers’ fees and accountants. In the end someone paid for that out of his own pocket. Without that, there would have been no enterprise.”

#### **4.4.2. A Community Bank**

We are led to the conclusion that there is a strong case for attaching special privileges to the provision of finance for social enterprises in disadvantaged areas. Social enterprises produce great benefits for the community, which are not always recognised in the tax system. It is appropriate to acknowledge this by giving help where it is most needed.

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<sup>30</sup> Ibid, p49

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One possibility is a Community Bank which would help social enterprises to find the external finance they require. This Community Bank would be in some ways analogous to a ‘central bank’ for Social Enterprise Zones; it would operate in partnership with existing social enterprise and community lending institutions, and the social enterprises they serve would be offered enhanced tax reliefs to attract funds into the most deprived areas. The Bank would also help social enterprises to find other sources of finance, including grant money, effectively streamlining the multifarious and confusing sources of finance available to the sector into a single conduit.

The Bank’s purpose would be to achieve specific goals in the disadvantaged areas it served, and it would go about this task proactively, seeking out social enterprises to carry it forward, or even helping to set up new ones relevant to the tasks in hand. Where there was a need for complementary action, it would try to arrange for the appropriate voluntary bodies, or arms of the public sector, to provide it.

The new Bank would aim to offer a professional range of services to the sector, and to do that would need to have sufficient scale. To help in marketing the sector to potential investors, it would need to achieve a high profile.

At the same time, however, the new Bank must also be very local in its approach. Unless it understands the local environment and the local challenges, it will not be able to use its skills to best advantage.

#### 4.4.3. A Pre-determined Total of Tax Relief

To encourage local authorities, or local community groups, to propose Zones or communities of interest which would attract tax relief, the total amount of relief allocated to the programme would need in the first instance to be limited. This would act as an incentive for councils and others to come forward and bid for their share.

Projects would, in effect, have to compete for tax advantages, helping to ensure that the most resources went to the most disadvantaged communities. Within the overall pot of tax relief allocated by the Treasury, it would be the responsibility of the Community Bank to make the necessary choices.

The principles on which the Community Bank would identify Social Enterprise Zones should be subject to consultation. Statistical evidence such as the Government’s Index of Multiple Deprivation would provide useful quantitative data, based on measures such as housing conditions, educational attainment, employment levels, poverty and crime. But the selection process could not be mechanistic, and would need judgement on the part of the Bank.

Provided there was an obvious need, the quality and effectiveness of the social enterprise or enterprises involved would be the most important criteria. There would be no point in putting resources into a Social Enterprise Zone if there were no effective social enterprises to make use of them, though it would be part of the Bank’s responsibility to encourage the development of such SEs.

This implies that the Bank would need both to identify the types of need in the relevant areas or communities of interest, and to consider the track record of providers in tackling them, or their proposals for doing so. In some instances, the case might be made less by the activities of the enterprise itself, than by the surpluses which it generated for effective social support in disadvantaged areas.

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#### 4.4.4. Tax, Security and Liquidity

Investments made through existing social enterprise and community lending institutions in social enterprises within the areas designated by the Community Bank as Social Enterprise Zones would attract tax relief. An obvious way of achieving this would be a scheme similar to the venture capital reliefs introduced and developed by the Conservative Party in the 1980s and 1990s. These have been both attractive to investors and effective in encouraging new ventures, to the benefit of the economy. There is no reason why, suitably adapted, they should not also be effective in developing the social economy.

Investors in Venture Capital Trusts (VCTs) currently receive up-front tax relief on the whole sum invested of up to 30%, so long as the investment is held for a minimum of 5 years. They also enjoy relief on any income, and on capital gains. Similar reliefs could be extended to investments in social enterprises within Social Enterprise Zones, with the attraction of an additional slice of tax relief over and above the £200,000 ceiling attaching to investments in VCTs.

VCTs are precluded from investing in property companies. In the case of social enterprises, a Conservative government might consider relaxing this restriction.

There are currently three other venture capital schemes, the Enterprise Investment Scheme, Corporate Venturing Scheme, and Venture Capital Loss Relief. If there were a demand, these could also be adapted to raise money for social investment. The Corporate Venturing Scheme, in particular, might have a role to play in helping social enterprises to mentor others in the sector.

Key to attracting capital will be investors identifying with the projects which are being financed. Because a social enterprise's primary mission is to generate returns for society rather than for its owners, providers of long term capital to the social sector are generally asked to accept sub-market financial returns. In addition to the tax relief on offer, the balance is made up by the "social return" on the investment.

Ideally, "patient capital" should be found among the members of the community in which the social enterprise is operating, and where the social return is most obvious to investors. But in the most disadvantaged communities there may be little or no local capital available. In that case, capital needs to be raised from outsiders, and there is evidence that some investors, particularly high net worth individuals, are indeed prepared to consider investments which deliver part of their return in the form of a "social" dividend.

Clearly, however, they need to be made fully aware of the nature of the social dividend they are receiving. This argues in favour of direct investment in specific projects rather than pooled investment, though investment through funds designated for Social Enterprise Zones in general should also be available to those investors who prefer them.

In the absence of competitive financial returns, the security and liquidity of investments would be particularly important. There is some evidence that lending to SEs is less risky than lending to their commercial counterparts,<sup>31</sup> partly because of the level of local commitment on which SEs can usually depend.

As to liquidity, patient capital is by its nature long term. However, one of the challenges of the new Bank in dealing with quasi-equity investments would be to help the sector to develop a periodic

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<sup>31</sup> See, for example, Bank of England op.cit. p43

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bargain-matching service between investors who want to sell and those who want to buy. Existing institutions such as Triodos Bank have already experimented successfully with such arrangements.<sup>32</sup>

#### 4.4.5. Costs

The amount of tax relief to be made available would have to be determined at the time, depending on what circumstances permitted. The total resources made available to social enterprises as a result would be a multiple of that figure.

The accompanying table gives some illustrative figures. If, for instance, the initial total of tax relief were £50 million, then the new capital provided by 40% taxpayers, if fully relieved, would be £125 million. At a lower average tax rate, correspondingly more money could be raised. If unclaimed assets are to fund social investment (as opposed, for example, to the present Government deciding to use such assets to fund the Olympics), then it would be natural to use this money for the purpose of building further the tax relief available to investment in social enterprises within Social Enterprise Zones, rather than using it to establish a separate Social Investment Bank.

£mn			
Tax Relief	10	50	100
Capital Raised	33	167	333
Debt	33	167	333
Total Increase	67	333	667

On the basis of this new capital, social enterprises could raise at least the same amount of loan finance, bringing the total increase in resources to £250 million, or over £300 million if tax relief were capped at 30%. This represents a worthwhile and cost-effective addition to the resources deployed against social problems in our most disadvantaged communities.

From the point of view of the Exchequer, much of the cost would be offset over the longer term by savings in public expenditure. Indeed, a really successful attack on the spiral of drug addiction, educational failure, unemployment and crime would pay for itself many times over. None of this can be taken for granted, but there is no doubt that, as one social entrepreneur put it, “happiness is cheaper”.

#### 4.4.6. Planning and Premises

In addition to offering tax reliefs, the Enterprise Zones introduced by the Conservatives in the 1980s helped entrepreneurs by simplifying planning controls. In the same way, Social Enterprise Zones should recognise the benefits of social enterprise by facilitating the planning permissions on brownfield land needed by SEs.

At present social enterprises often find planning permission problematic, in part because there is no recognition of them in existing planning policy as a distinct category of business. As a result, planning

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<sup>32</sup> Ibid, p55

<sup>33</sup> Assumed average tax rate relieved of 30%. Columns may not sum due to rounding

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authorities tend to treat them as commercial businesses, taking little or no account of the potential social gains from their activities.

There are a number of ways in which SEs could be given special status. Simplest and fastest would be for central Government to issue a national planning policy statement. This could direct local authorities to take account of, and give substantial weight to, the community benefits to be derived from social enterprise, when considering planning applications from SEs.

Under existing law, it should also be possible to ease the planning constraints on brownfield land within a Social Enterprise Zone through the grant of blanket planning permission for development by social enterprises, under a local development order (LDO), made under section 61A of the Town and Country Planning Act 1990. The national planning policy statement envisaged above could direct local authorities to make provision in their local development documents for social enterprises, and for the use of LDOs to support them in Social Enterprise Zones.

A more radical approach would be to amend the existing secondary legislation, so as to give social enterprises special privileges in planning law. For instance, the Town and Country Planning (Use Classes) Order 1987, which identifies changes of use which do not require planning permission, might be amended to support changes of use involving social enterprises. And to facilitate new build on brownfield land, an additional part covering development by social enterprises could be added to the Town and Country Planning (General Permitted Development) Order 1995. We suggest these options might be held in reserve.

In a complementary move to easing the planning process, local authorities and other public sector bodies should be encouraged to make under-used property more readily available to SEs. Evidence collected in the course of our investigation suggests that finding premises is one of the biggest problems facing social enterprises, especially start-ups.

An incoming Conservative government could make a start by circulating a request to local authorities, for them to look favourably on providing properties for SEs where these were available on brownfield land. Where councils were unable or reluctant to identify such assets, the Community Bank might be able to assist SEs in locating them and negotiating with councils.

Facilitating change of use, for instance from residential to social enterprise, would help to smooth the way for transfers of property from local councils to SEs. It could also help to facilitate the provision of premises by private sector companies. Increasingly, companies are recognising that they may have a corporate interest in helping to solve social problems; and one way in which they can contribute is by finding premises for social enterprises, either on a temporary or semi-permanent basis.

#### 4.4.7. A Fairer and More Efficient Social Enterprise Sector

In evaluating our research, two issues have emerged as particularly important to many social enterprises, wherever they are operating. One is their relationship with charities. The other is the process of contracting to provide services to local authorities, or to other parts of the public sector.

The benefits to social enterprises of registering as charities are considerable:

- profits from any trade carried out by a charity are free of tax, if the profits are applied solely for the purposes of the charity, and the trade is exercised in furtherance of the primary purpose of the charity;

- chargeable gains made by a charity, for example on disposal of a property, are tax-free;
- charities do not pay tax on bank interest received;
- charities do not pay stamp duty land tax;
- at the local level, charities are entitled to a mandatory 80% relief; from the unified business rate, which the local authority has discretion to increase to 100%;
- for donors, gifts by companies and organisations paying corporation tax are tax deductible; and
- for individuals, donations attract Gift Aid relief under which the charity can recover the tax from the Exchequer.

These tax advantages obviously have persuaded many social enterprises to register as charities.<sup>34</sup> Charitable status can also be helpful in reassuring customers, staff and the community that the enterprise is fully committed to its social goals.

But there are also considerable disadvantages to an SE in adopting charitable status. Respondents to our survey cited among the drawbacks: the initial expense, the restrictiveness of the regulations, the difficulty in getting good trustees, and problems in being taken seriously as a trading enterprise. One said forthrightly: “A social enterprise should aim to be a real business with social aims, so there is no need for charitable status.”

The cost of registration with the Charity Commission is much higher than the cost of registering a limited company, and the requirement to make annual returns means that this regulatory burden continues.

Charitable status can also have a strong influence over business strategy. Charity law imposes strict rules about a charity’s purposes. This means that if a charitable social enterprise wants to offer an additional type of social service, say to provide childcare as well as an employment service, or if it wants to provide these services in a neighbouring area as well as the original one, it will find it difficult to remain within the rules.

A third problem is governance structure. Ultimate power in a charity rests with an independent board of trustees. No matter how well intentioned the board may be, it will often be several steps behind the SE’s chief executive, who will typically be the prime mover behind the enterprise. Moreover, the most ambitious and effective managers tend to be the ones who chafe most at charitable constraints.

#### **Uncharitable thoughts**

“Far too much of the money we and lawyers make from advising social enterprises is for creating artificial legal structures and relationships, which wouldn’t need to exist if there were tax reliefs for non-charity social enterprises.”

“I think extending tax reliefs would encourage people to set up social enterprises. The absence of reliefs is keeping a lot of people operating within the charity sector who would otherwise be inclined to work in a less regulated way.”

“The charity sector itself is being distorted by the presence within it of a lot of organisations which aren’t what most people would see as charitable organisations but as businesses... Creating social wealth is fine, but from the point of view of public perception there’s a case for narrowing the charity sector back down to good works and fund raising.”

*Eddie Finch, Buzzacott: Accountants advising social enterprises.*

<sup>34</sup> Of the 200 SEs surveyed by the Bank of England, 60% said they had charitable status, op.cit. p17

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#### 4.4.8. A Limited Tax Relief

We suggest that a Conservative government should consider extending some limited tax relief to all social enterprises that meet certain criteria, whether they are charities or not. To prevent abuse in what is a diverse and sometimes ill-defined sector, it would probably be appropriate to confine the relief to SEs organised in the form of Community Interest Companies (CICs). CICs have their own regulator to ensure their community purpose, and are forbidden to transfer assets into the private sector.

Compared with commercial firms, social enterprises often find it difficult to pursue a long term business strategy, because of their limited access to capital. One way to alleviate this problem would be to allow them to set aside a Community Interest Reserve which, provided that it was applied to community purposes, would not be taxed. If the transfer were irreversible, ring-fencing the relief would be relatively easy.

So long as they could be administered satisfactorily, the cost of such reliefs to the Exchequer might be quite small, as some of the reliefs are already being obtained (less satisfactorily) via links with charities. And, as noted above, successful social enterprises often give rise to public expenditure savings in the form of lower welfare benefit and other costs.

#### 4.4.9. Government Contracts

Another issue which arouses strong feelings among many social enterprises is the process of contracting with local authorities and other public sector bodies. Public service delivery, including the Government's contractual relationship with the private sector, is being examined elsewhere in the Conservative Policy Review process, but it is important that SEs' needs and concerns are understood.

Among the complaints are that local authorities do not understand or trust social enterprises to deliver high quality services; that approved supplier procedures and other bureaucratic requirements are unnecessarily complicated; and that the government requirement to aggregate contracts, in order to obtain the best value, effectively shuts out many SEs who are too small to compete.

##### **Contracting with local authorities**

"Social enterprises do face problems in negotiating contracts with local authorities to provide services. A lot of these social enterprises start from a community voluntary basis, and within any local authority there's a perception that they are still dealing with the community and voluntary group, when actually they should be thinking about it in a more business-like manner. But sometimes social enterprises do themselves no favours, because if they have come from the grant funded sector they can find it difficult dealing with all the documentation and making themselves tender-ready."

"Any successful social enterprise needs an entrepreneur, and that vision and entrepreneurship has to come from within the organisation itself... Occasionally people come to me looking for answers on how to fund raise better, and when that happens I re-direct them to other people. I'm here to look at marketable ideas."

"Special support for social enterprises is mainly desirable at the incubation stage...later on it may be less important."

"We sell our services under contract to five other London boroughs as part of our commitment to develop our own entrepreneurship."

*Amanda Lewsey, Head of Social Enterprise Support Unit at London Borough of Havering.*

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Authorities like Havering, with specialist units to encourage social enterprises, would admit that some SEs are not yet “contract ready”. Indeed, to make them so is one of the authority’s aims. But central government also has a responsibility to avoid policies (such as aggregating contracts) which prevent social enterprises from competing effectively.

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## 5. Conclusions

Social enterprises have a huge role to play in tackling the problems in our most disadvantaged communities. While the state has an important contribution to make, social enterprises bring the advantages of local knowledge, entrepreneurial energy, and a more sophisticated approach than the “one size fits all” solution.

We believe an incoming Conservative government should seek to encourage social enterprises, particularly in the most disadvantaged areas, by setting up Social Enterprise Zones where SEs can enjoy special privileges. This builds on the success of the Enterprise Zones set up by the Thatcher Government in the 1980s, which helped to reinvent London’s Docklands as a world financial centre.

In the case of Social Enterprise Zones, rather than central government taking the initiative, local authorities should make the case for the communities in their area which need help.

To help SEs find the capital they need, the government should offer attractive tax reliefs to lenders and investors, along the lines available to venture capital trusts. The total amount of tax relief available in any one year would be capped, encouraging local communities to come forward with proposals.

A new Community Bank would administer the tax relief scheme on behalf of government, selecting the Social Enterprise Zones from amongst the proposals put forward by local authorities, and ensuring that existing social enterprises and community lending institutions channel money raised under the tax-favoured scheme to social enterprises in the Zones. It would also work proactively to identify SEs for existing financing institutions to work with in the Zones; combine grants and other available funds in the financing mix for priority projects; and state publicly the outcomes it hoped would be achieved in the projects financed. In doing this, it would complement the work of existing institutions.

Social enterprises have the power to bring new hope to disadvantaged communities. This report outlines a Conservative way forward.

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## Members of the Policy Group

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*We are grateful to the following, who were among those we consulted. They bear no responsibility for our recommendations.*

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<sup>35</sup> Said Business School, Oxford