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15th DECEMBER, 2017

Executive Summary

Like any new market, impact investing¹ in Australia will grow faster with an effective catalyst. A go to place to help co-ordinate fragmented efforts, and support intermediation and demonstration of new approaches to solving our societal issues. International experience has shown the effectiveness of a national impact investment wholesaler in catalysing the market.

The Australian Government has taken some good first steps in support of impact investing both in initial policy moves in the 2017 budget and through supportive speeches and commentary from Ministers and Senators. There is now a significant choice to be made and that choice is in the hands of the Australian Government. The Government can continue to take incremental steps and not realise the impact investing markets potential, or it can enable a game-changing institution and unlock the opportunity to drive positive societal outcomes at scale. Australian communities need the Government to make the right choice.

Recommendation:

Create a step change in Australia's impact investing market by committing \$150m in 2018/19 to be matched by Australian financial institutions and other societally focused investors to establish Impact Capital Australia (ICA). ICA will be a game changing \$300m wholesale institution with the capital, mission and mandate to improve people's lives by driving the impact investment market in Australia to scale.

This submission outlines how the Australian Government can adopt an implementation-ready policy proposal to help drive the impact investment market to scale in Australia. It involves the establishment of a \$300m predominantly wholesale institution, Impact Capital Australia (ICA), as a partnership between the government, the private sector and the community sector.

A one-off \$150m of government capital to seed ICA would unlock a critical mass of investment and innovation that would deliver meaningful social, environmental, cultural, and economic benefits for Australians.

The path to impact at scale

A recent Australian Advisory Board on Impact Investing (AAB) field scan re-enforced that while there is strong appetite and potential for impact investing from a broad set of stakeholders, including governments, the market lacks scale. Significant gaps to growth remain, including gaps in the intermediary market. Other key gaps include: lack of origination capacity, lack of long term capital, viability of new/existing intermediaries and aggregators, misalignment of funding terms and incentives, mispriced risk and information asymmetries and under-developed secondary markets.

Capacity also needs to be built in impact management, measurement and risk assessment, and associated transaction structuring with the "right" capital. The involvement of private financiers, (including philanthropist), governments and the community sector necessitates significant cross-sector collaboration. These gaps and barriers to growth are not insurmountable and a go-to institution, such as ICA, which houses both flexible capital and extensive capacity would go a long way towards addressing many of these issues.

Experience from international markets illustrates that impact investment wholesalers, whether broadly focused or sector specific, can provide a catalytic effect in stimulating market growth.

Big Society Capital (BSC) the UK wholesaler was established in 2012 and over the last 5 years, has unlocked £1bn of capital for impact investing. Support for intermediaries has been a key driver of growth with the number of UK impact investing intermediaries managing over £50m going from only one in 2012 to seven in 2017.

The European Social Impact Accelerator, an EU focused fund of funds, invests in social impact funds targeting SMEs. Since it was established in 2013, it has helped to support 10 intermediaries in bringing new funds to market.

The Global Energy Efficiency and Renewable Energy Fund is sector specific and demonstrates the leverage of the wholesaler model. In 2016 its €154m of committed capital, through a fund of fund model, helped to unlock €2.4bn of private sector funds for energy projects. This created 5,000 jobs and brought energy to 308,000 developing market households.

The lessons from these international wholesalers' have been built into the design of ICA. It will be an independent organisation with a mission, investment mandate and sufficient catalytic capital at \$300m, to significantly accelerate market development.

As a predominantly wholesaler investor and market champion, ICA will also support two critical dimensions of the market that drive scale:

- the support of existing and new intermediaries through seed funding and capacity support; and
- the proving up of new and innovative business and financing models to address risk and pricing anomalies

The policy case for ICA

In an environment where government budgets are under-pressure two things are particularly critical:

- Maximising efficacy of government spending against policy priorities i.e. Better outcomes.
- Unlocking private capital for direction towards policy priorities i.e. More outcomes

More and better outcomes could be achieved with less money and result in savings to Government if effectively executed.

Recent policy announcements and Ministerial statements suggest the Government has recognised that impact investing has an important role to play in delivering these critical factors. They appear supportive of the market's development.

Game-changing policy, in establishing ICA, is now required to drive the impact investing market to a state of development where it can meaningfully contribute toward the Government's policy priorities.

A Government commitment of \$150m in 2018/19 would crowd in private capital immediately through a combined contribution from financial institutions including major Australian banks. The Government contribution could be structured as a grant and/or an approved investment.

ICA cannot be implemented to achieve its objectives without the Australian Government as a partner. There are a number of key reasons:

- Government is potentially both a key beneficiary and major participant in Impact Investing. The signalling effect of its early collaboration and commitment is therefore critical in instilling market confidence;
- In order for ICA to be self-sustaining, provide flexible capital and operate as a public good, it needs its own capital on the right terms. The private sector is prepared to partner with government to achieve this but would not be prepared to fund ICA alone; and
- The national nature of ICA's remit means the Australian Government is the more natural government partner to fund ICA. Once ICA is capitalised, there will be an important role for State governments in co-investment *with* ICA and its intermediaries.

The design for ICA is based on leading practice in market development and market and innovation policy. This proposal builds on the Government's initiatives to develop the social impact investment market in Australia, including the 2017 Budget measures. ICA also meets the Australian Governments Principles for Social Impact Investment.

The outcome areas which will be the focus of ICA's investment mandate include Government policy priorities in: housing; employment and training; healthcare and disability, childcare and; financial and community inclusion.

In pursuing the growth of intermediation and focusing on efficacy and efficiency of capital, ICA's work will be highly aligned with the objectives of Government around the delivery of both more and better outcomes for Australian communities.

ICA is implementation ready

ICA's design is based on a broad evidence base and is the product of a collaboration between cross-sector leaders, locally and globally. A three year process of robust co-design and planning has brought ICA to a point where it can be readily implemented.

ICA would be an independent, purpose-driven organisation with standards and processes that ensure accountability for proper and effective use of resources. Governance would be the responsibility of a highly experienced board utilising appropriate committee structures.

Other aspects of accountability and transparency such as performance monitoring and management and risk mitigation strategies, would all be essential in the formalisation of ICA policies on implementation.

A clear and accountable implementation plan has been developed for ICA. The plan has four stages with identified work-streams, milestones and time-frames:

- Stage 1: concept design;
- Stage 2: pre-funding implementation;
- Stage 3: formation and capitalisation; and
- Stage 4: post-funding implementation.

Stage 1 has been completed and Stage 2 has been progressed to the final stages. The next major milestone is securing capital commitments from significant stakeholders including the Australia Government.

An important aspect of ICA's implementation is pipeline development and this process has already commenced. This early identification of opportunities and adoption of initiatives around building pipeline, will accelerate the speed of ICA's market impact, once capitalised.

Conclusion

This year's pre-Budget submission focuses in on the highest priority action to achieve a breakthrough in enabling and supporting the market for impact investment, ICA.

ICA is not the only constructive step the Australian Government could take, or the only one that will be needed. However, it is the one that will make the biggest difference and is the measure most likely to put the market on a path to scale. ICA will change the game because it is unique. It exists not to make a surplus profit or compete against others in the market but to act as an independent, designated market champion with the capital and mission to grow the market.

The AAB and Impact Investing Australia welcome the opportunity to have input into this pre-Budget process. We urge the Australian Government to take up the opportunity for targeted action to fuel development of impact investment. Members of the AAB and Impact Investing Australia Executive will be happy to meet to discuss any aspect of this Submission and the design and analysis for ICA.

Introduction

This submission outlines how the Australian Government can adopt an implementation-ready policy proposal to help drive the impact investment market to scale in Australia. It involves the establishment of a \$300m predominantly wholesale institution, Impact Capital Australia, (ICA) as a partnership between the government, the private sector and the community sector.

A one-off \$150m of government capital to seed ICA would unlock a critical mass of investment and innovation that would deliver meaningful social, environmental, cultural, and economic benefits for Australians.

Impact investing can play a bigger role in helping the Australian Government meet growing demands to address social and environmental issues and contribute new solutions to complex challenges.

The Australian Advisory Board on Impact Investing (AAB) and Impact Investing Australia (IIA) welcome recent commitments by the Australian Government to encourage and support growth in impact investment.

Measures in the 2017 Budget to develop impact driven enterprises, trial innovative approaches to youth homelessness and new initiatives to finance affordable housing are welcome early steps. Recent speeches from the Treasurer and Minister for Foreign Affairs sent important signals to the field, including to international colleagues who noted the seriousness with which the Government is taking the opportunity.

The policy focus is timely as a recent field scan led by the AAB found that there has been a real shift in awareness of impact investing in the Australian market over the last three years, uncovering its significant potential. State governments, financial institutions, super funds, corporations, and the community sector are expressing an appetite to explore the opportunities.

They are also expressing concern that the potential could be missed without proactive steps to drive scale, and design for scaling impact as well as capital. The feedback reinforced that stakeholders are looking to the Government to take a more proactive and catalytic role in that process.¹

The challenges to achieving scale are familiar to new markets, and include a relative lack of: efficient and effective co-ordination; infrastructure; intermediaries, and capacity shortfalls. There is precedence across OECD countries that a combination of catalytic capital and signalling from government has a unique and powerful effect in demonstrating new models, enabling intermediaries and overcoming information asymmetries, well beyond the organic, transaction based growth the market can deliver alone.²

The Australian Government is uniquely placed to pull the policy lever required to make the shift from incremental to transformative change at scale. Recent developments, including growing interest in the UN Sustainable Development Goals (SDGs) and managing systemic risk, indicate the institutional market is shifting. The AAB's assessment, based on available data and the recent field scan, is that targeted market building by the government can unlock significant capital and fill gaps in the market infrastructure. Without that interest and momentum around impact investing will start to wane and ultimately, an important source of funding and innovation to address our societal issues may never reach its potential.

The work of the AAB has positioned Australia as an early and competitive leader in the impact investing market globally. This means a proactive commitment of \$150m by government to ICA at this time is not just about Australia's domestic outcomes but broader opportunities across the region. There is potential to attract new capital into Australia, to position it as a hub for investment into the region, and attract new sources of talent and capital to activity, research and development that provides social, environmental and cultural benefit.

¹ AAB Field Scan October – November 2017 (see Appendix 1)

² Wilson, K & Silva, F, 2013 *Policies for Seed and Early Finance: Findings from the 2012 OECD Financing Questionnaire*, OECD Science, Technology and Policy Papers, No 9

Part 1: The path to impact at scale

State of the impact investment market

The recent AAB field scan re-enforced that while there is strong appetite and potential for impact investing from a broad set of stakeholders, including governments, the market lacks scale. Significant gaps to growth remain, including gaps in the intermediary market.

Capacity needs to be built in impact management, measurement and risk assessment, and associated transaction structuring with the “right” capital. The involvement of private financiers, (including philanthropist), governments and the community sector necessitates significant cross-sector collaboration. These barriers are not insurmountable and a go to institution such as ICA which houses both flexible capital and extensive capacity would go a long way towards addressing these issues.

Impact investing is one way to mobilise additional resources to relieve pressure on Government budgets. Impact investment brings focus to measurable outcomes and sustainable impact for people, communities and the environment. This market is growing in Australia and across the globe. The recent AAB field scan found that activity and participation are growing in all parts of the ecosystem.

Impact Investing is already being used to finance initiative areas including the arts, aged care, community development, education, employment, health, environmental management, sustainable agriculture, renewable energy, justice, social housing and international development.

There is marked interest in the opportunities and challenges of meeting the SDGs. Sixty percent of respondents to the latest Global Impact Investment Network (GIIN) Survey indicated they were already tracking investments to the SDGs or planned to do so.³

The potential for growth is material and the Global Social Impact Investment Steering Group (GSG) has set a target of over US\$300bn in impact investments actively targeting new solutions by 2020.⁴ Market development internationally is accelerating rapidly. Outcome funds at scale ranging from US\$200m to US\$1bn are in development. Mainstream financial institutions through SDG alignment and other means are considering how impact can be factored into processes and/or products.

Estimates for the domestic Australian market by 2022 have been forecast at \$32bn.⁵ This does however assume Australian developments follow the trajectory of comparable countries including an active role of government without which the potential both within Australia and the region is unlikely to be realised. The 2016 Impact Investing Australia Investor Survey data indicated willingness from those already active in the market to invest a baseline of ~\$18bn in capital over the next 5 years, *provided* the right opportunities are available.

The findings from the AAB’s recently concluded field scan clearly point to growth in momentum; participation and activity. The market has entered a phase of more coordinated market development rather than early innovation. Potential is there for more significant growth. The findings reinforced conclusions from the Impact Investing Australia 2016 Investor Survey that those already active would like to do more and a greater number expect to mobilise in the next 3-5 years.

³ The GIIN Annual Impact Investor Survey, 2017 <https://thegiin.org/knowledge/publication/annualsurvey2017>

⁴ Ibid

⁵ Addis et al 2013; https://docs.employment.gov.au/system/files/doc/other/impact-australia_nov_2013_2.pdf

Participants across the board raised the opportunity and need for scale. There was a sense that much of the growth so far has been investor led and that there are greater opportunities to be realised with focussed effort to contributing new solutions and designing approaches that work to scale impactful activity and attract finance.

Participants underscored the need for more and multi-skilled intermediaries and for catalytic capital. They referred to the necessity to prove up more models, replicate what works and aggregate investment opportunities in a form that can engage investors. They were clear that they wanted to see more engagement and signalling from governments, including to provide catalytic capital and data that will be critical to supporting scale.

More background on impact investment and the state of the market is included in **Appendix 1**.

Addressing market gaps and driving scale

Key gaps in the market include: lack of origination capacity, lack of long term capital, viability of new/existing intermediaries and aggregators, misalignment of funding terms and incentives, mispriced risk and information asymmetries and under-developed secondary markets.

The trajectory of other markets, like the UK, shows a wholesaler such as ICA can support two key dimensions of the market that drive scale in this context:

- the support of existing and new intermediaries through seed funding and capacity support; and
- the proving up of new and innovative business and financing models to address risk and pricing anomalies

Emerging fields of market based activity and innovation exhibit a number of common challenges. These factors can push up the price and reduce the flexibility of finance. Impact investment adds the additional complexity of delivering social, environmental and/or cultural outcomes thus amplifying some of the gaps and challenges. Private markets do not readily promote delivery of public goods or optimal social and environmental outcomes. Data, where available, does not easily cross sector boundaries which further complicates pricing and tracking performance.

The key levers to overcome market failures, accelerate development and support more, and more effective, participation are well documented. Similar approaches have been successfully employed in fields such as venture capital, infrastructure investment, the corporate bond market, community finance and microfinance.

The evidence base is building that these approaches are similarly effective in growing impact investment. The UK's impact investment wholesaler, Big Society Capital (BSC) has demonstrated the scale and momentum effects driven by support of existing and new intermediaries; and the proving up of new and innovative business and financing models.

The GSG has recently established a working group to promote the development of national impact investing wholesalers. These efforts recognise wholesaler organisations as key market infrastructure that ground and accelerate development of impact investment.

National wholesalers are designed to support and grow intermediaries and act as market champions.⁶ Without the type of capital and capacity brought by a wholesaler initiatives in the market are likely to lack critical mass for some time, limiting self-sufficiency and inhibiting the opportunities for innovative models to scale. More details on the catalytic effects of international wholesalers on building the pipeline and growing the market can be found in Part 2 of this report, under [Proof of concept for a wholesaler](#).

⁶ Social Impact Investment Taskforce, 2014, and Notes of GSG Plenary Meeting, London, [unpublished] July 2015

In 2014, after extensive market consultation, the AAB, a National Advisory Board of the GSG, recommended in its strategy report, [Delivering on Impact](#), that a wholesale institution should be established for Australia. This was identified by the AAB as a key breakthrough action to deliver demonstrable impact, meaningful practice, and build a greater number of informed participants in the impact investing field.

Since early 2015, the AAB through its implementation arm, Impact Investing Australia, has been working to establish ICA as an impact investing wholesaler for Australia.

Proof of concept for a wholesaler

Experience from international markets illustrates that impact investment wholesalers, whether broadly focused or sector specific can provide a catalytic effect in stimulating market growth.

Big Society Capital, the UK wholesaler, was established in 2012 and over the last five years has unlocked £1bn of capital for impact investing. Support for intermediaries has been a key driver of growth with the number of UK impact investing intermediaries managing over £50m going from only one in 2012 to seven in 2017.

The European Social Impact Accelerator, an EU focused fund of funds, invests in social impact funds targeting SMEs. Since it was established in 2013, it has helped to support ten intermediaries in bringing new funds to market.

The Global Energy Efficiency and Renewable Energy Fund is sector specific and demonstrates the leverage of the wholesaler model. In 2016, its €154m of committed capital, through a fund of fund model, helped to unlock €2.4bn of private sector funds for energy projects. This created 5,000 jobs and brought energy to 308,000 developing market households.

The international experience: National wholesalers

Experience from international markets shows that a wholesaler investor and market champion is needed to drive market transition and stimulate growth in impact investing.

Three examples of international wholesalers, their mandates and some of the impact they have created in their respective regions are provided. These wholesalers aim to build markets, not just write cheques. Their theory of change is that a strong layer of intermediaries will both draw other investors into the market and serve the diversity of impact driven demand. They are designed to ‘crowd in’ other investors rather than ‘crowd out’ intermediaries.⁷

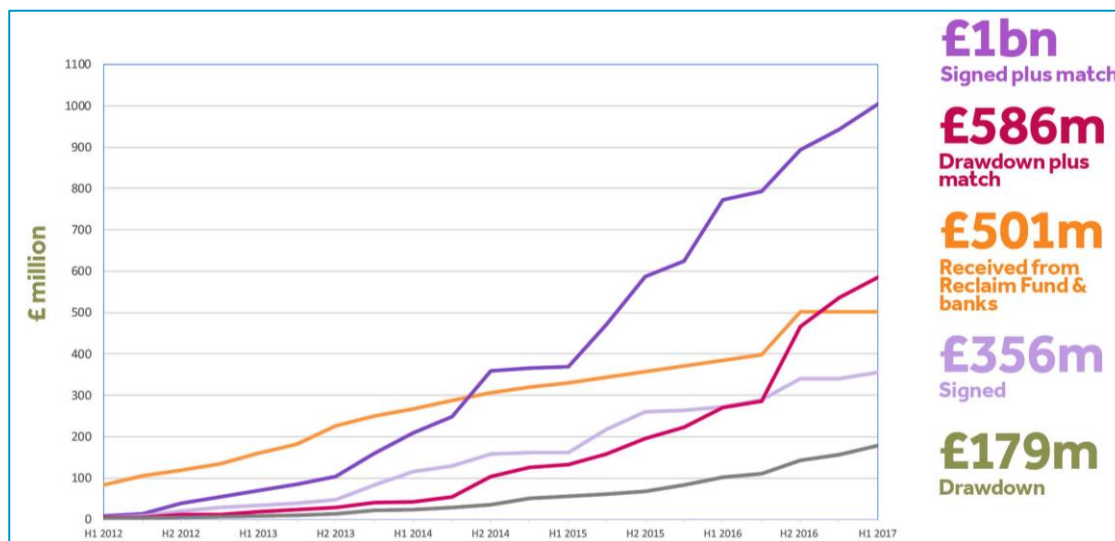
The AAB’s membership of the GSG has provided access to key executives at various international wholesalers. BSC in particular collaborated extensively in the design process for ICA. Lessons learnt from the UK experience, adapted for Australian market conditions, have been extensively incorporated into ICA’s design.

Big Society Capital, UK

In the United Kingdom, the 5-year track record of BSC provides evidence of both the direct multiplier effect and the broader market-catalysing effects that can be achieved when government acts as a first mover by co-investing in impact investment, (Figure 1). McKinsey analysis found that BSC’s impact represented a “*decisive shift*” in the UK impact investing market.⁸

⁷ GSG Wholesaler Working group draft materials Nov 2015 [unpublished]

⁸ Godsall, J & Sanghvi, A, 2016, *How Impact Investing can reach the mainstream*, McKinsey & Company

Figure 1: Big Society Capital's portfolio and leverage effect has built over the first 5 years of operation

Source: Big Society Capital Website, accessed 8/12/2017

Table 1: Snapshot Big Society Capital ⁹

Purpose	To improve the lives of people in the UK by connecting investment to charities and social enterprises.
Summary	Big Society Capital (BSC) is a wholesale institution that invests in UK social investment finance intermediaries. The intermediaries invest in charities, social enterprises and other social organizations.
Year Opened	2012
Geographic Limits	The United Kingdom
Source of Capital	Dormant banks accounts (up to £400m); Merlin Banks ¹⁰ (up to £200m)
Amount Held	£501m (up to £600m)
Amount Invested	£356m Signed / £179m Drawdown
Amount Co-Invested	£644m Signed / £407m Drawdown
Co-Investors	Social bank depositors (18%), charities and foundations (14%), government agencies (11%), international (10%), banks (4%), local government pension funds (2%), funds (1%) and other (40%)
Return Target	4% to 6%
Immediate Investees	Intermediaries (no restrictions on intermediary type)
Final Investees	Charities, social enterprises and other social organizations
Investment Tools	Into intermediaries: Debt and equity.

⁹ Retrieved from <https://www.bigsocietycapital.com>

¹⁰ Relates to Project Merlin - an agreement covering lending, bonuses and transparency between the UK (Cameron) Government and the UK's four biggest banks: HSBC; Barclays; Royal Bank of Scotland and Lloyds Banking Group.

European Social Impact Accelerator, EU

The experience of the European Investment Bank run Social Impact Accelerator is also supportive of the role of a wholesaler in stimulating impact investing market development.

The EU's €243m Social Impact Accelerator (SIA) is a fifteen-year fund of funds within the European Investment Fund that invests mostly in social venture capital funds. The SIA seeks a return competitive with general venture capital.¹¹ The SIA usually supplies between 7.5% and 50% of an intermediary's capital raising.¹² The SIA's intermediaries must raise the rest of the capital for that round through other sources. The SIA leverages non-SIA capital by strengthening, developing and enabling its intermediaries to complete their capital raisings rounds outside the SIA.

Table 2: Snapshot Social Impact Accelerator (SIA)¹³

Purpose	To establish a financial market for social entrepreneurship in Europe.
Summary	The SIA is a fund-of-funds that invests in European social impact funds. The social impact funds invest in social enterprises. The European Investment Fund manages the SIA.
Year Opened	2013
Geographic Limits	The European Union
Amount Held	€243m
Amount Invested	€105m
Amount Co-Invested	Up to 50%
Return Target	Over 5%
Immediate Investees	Social impact funds
Final investees	Small and medium-sized social enterprises
Investment Tools	Into intermediaries: Equity. Into final investees: Equity and debt.
Sources of Capital	Public & private financial institutions: European Investment Bank (€230m), European Investment Fund (€9m), Crédit Coopératif (€1m), Deutsche Bank (€1 m), SITRA (€1m) and Bulgarian Development Bank (€1m)

A focus on intermediary support

While wholesale investors differ by goals and context, the common thread is intermediary support. Both BSC and the SIA work closely with their intermediaries to hone their processes, sharpen their skills and structure investable products.¹⁴

BSC has since spent significant time and energy helping intermediaries organise their management, figure out their processes, foster pipelines, structure products and otherwise create entities into which BSC wants

11 GSG Wholesaler Working group Interview, Sept-Nov 2017 [unpublished]

12 Retrieved from https://media.sitra.fi/2017/05/30110707/EIF_Social_Impact.pdf

13 Retrieved from http://www.eif.europa.eu/what_we_do/equity/sia

14 GSG Wholesaler Working group Interview, Sept-Nov 2017 [unpublished]

to invest. With the help of BSC, as the UK market has matured, the number of intermediaries managing more than £50m jumped from one in 2012 to seven in 2017¹⁵. The SIA has followed the same path. It works closely with intermediaries and other partners to put together funds into which the SIA will invest.¹⁶

Creating impact in key areas of policy priority

BSC did not deliberately set out to align with government policy priorities. Unsurprisingly however, there is significant overlap between the societal issues that it is seeking to address and the UK Governments policy priorities. In the UK, employment, and enabling training and education, are key areas of policy focus as are social and affordable housing and affordable access to childcare. Table 3 below is indicative of the type of investments made by the intermediaries BSC has supported along with the outcome area targeted and the impacts achieved. It illustrates that, with a wholesaler in the market driving intermediation, the private sector can be mobilised to provide capital for social purpose with strong impact.

Table 3: BSC creating impact in key outcome areas

Outcome Area	Investment	Impact
Employment, training and education	Nesta Impact Investments invested £1m into GetMyFirstJob, an online service that matches young people to apprenticeships.	26,000 jobs and training opportunities created
Housing and local facilities	Golden Lane Housing raised £11m through a listed charity bond, purchased in part by the Threadneedle UK Social Bond Fund. Golden Lane Housing supplies supported, independent homes to people with learning disabilities.	2,000 people housed
Family, friends and relationships – Affordable Childcare	Big Issue Invest and Bridges Fund Management invested £1.25m into the London Early Years Foundation. The Foundation subsidises low-income spots by charging affluent parents more.	5,000 affordable nursery or childcare spaces offered

Source: Adapted from GSG Wholesaler WG materials, October 2017 using data retrieved from <https://www.bigsocietycapital.com>

The international experience: A multi-national wholesaler

ICA's design also draws upon lessons from other fields of market development.

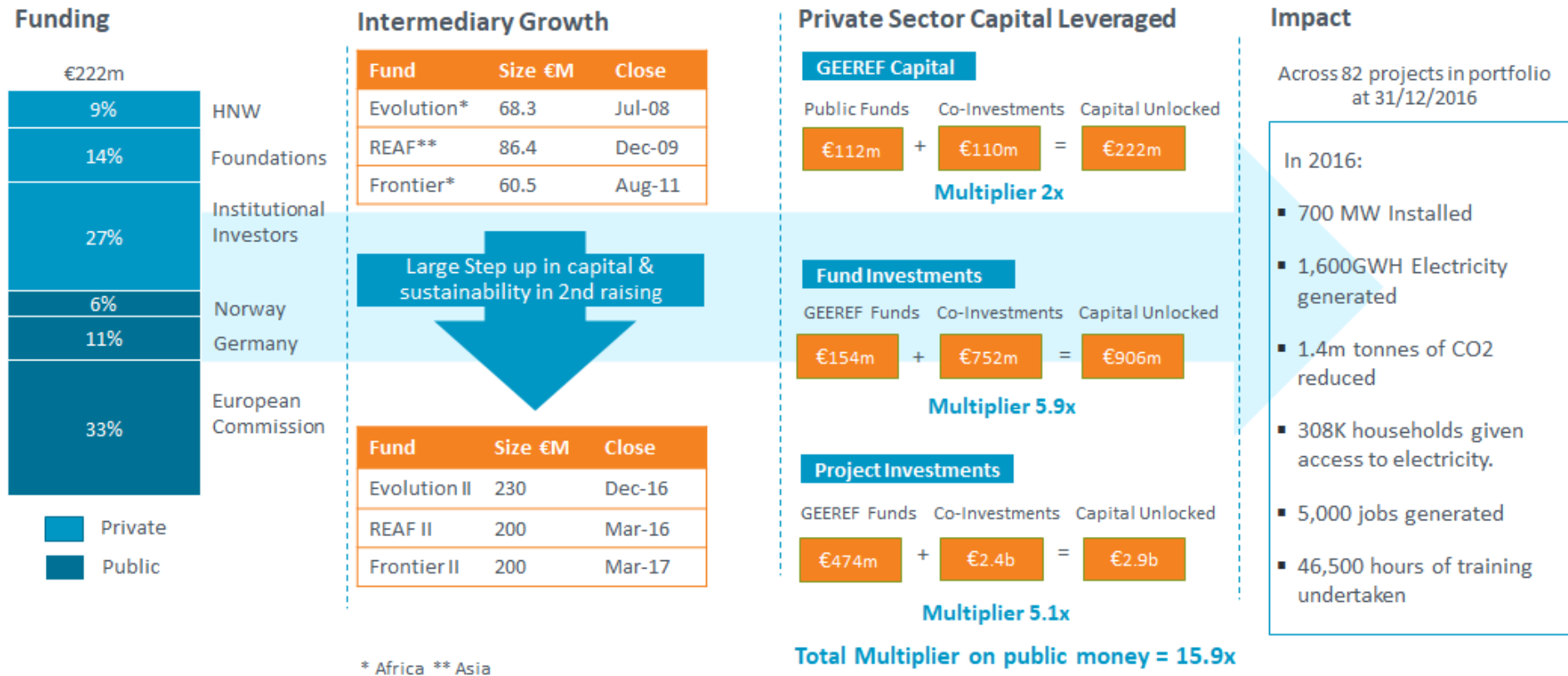
One such example is the Global Energy Efficiency and Renewable Energy Fund (GEEREF). Launched in 2008, GEEREF is an innovative fund of funds catalysing private sector capital into clean energy projects in developing countries and economies in transition. In April 2017, the Green Climate Fund, currently chaired by the Australian Department of Foreign Affairs & Trade, approved a US\$265m investment in GEEREF Next, a further capital raising for GEEREF. GEEREF is advised by the European Investment Bank.

The multiplier effect of GEEREF on both impact and finance is significant, (**Figure 2**). At the fund level, GEEREF's €154m of commitments have unlocked €906m in total capital, a multiplier of 5.9x. At the project level €2.4bn is unlocked from fund commitments of €474m, a multiplier of 5.1x on project funding and 15.4x on total GEEREF commitments.

Beyond the environmental benefits, GEEREF has also contributed technical expertise and capacity development to supported funds, as well as enabled increases in jobs, training and access to power for developing market beneficiaries.

¹⁵ Retrieved from <https://www.bigsocietycapital.com/impact-report/impact-market>
¹⁶ GSG Wholesaler working group Interviews Sept-Nov 2017 [unpublished]

Figure 2: GEEREF intermediary support and leverage effect 2016



Source: Impact Investing Australia, 2017 from information in GEEREF Impact Report 2016

Significantly, the GEEREF support has also helped the intermediaries build track record which together with the growth in the market has resulted in a major step up in capital raised in their second approach to the market.

The experience from other fields and from impact investing in other jurisdictions was distilled to identify the hallmarks of a successful wholesale investment fund. These features have been integrated into ICA’s design. Additionally, Australia has its own lessons and experience to draw on.

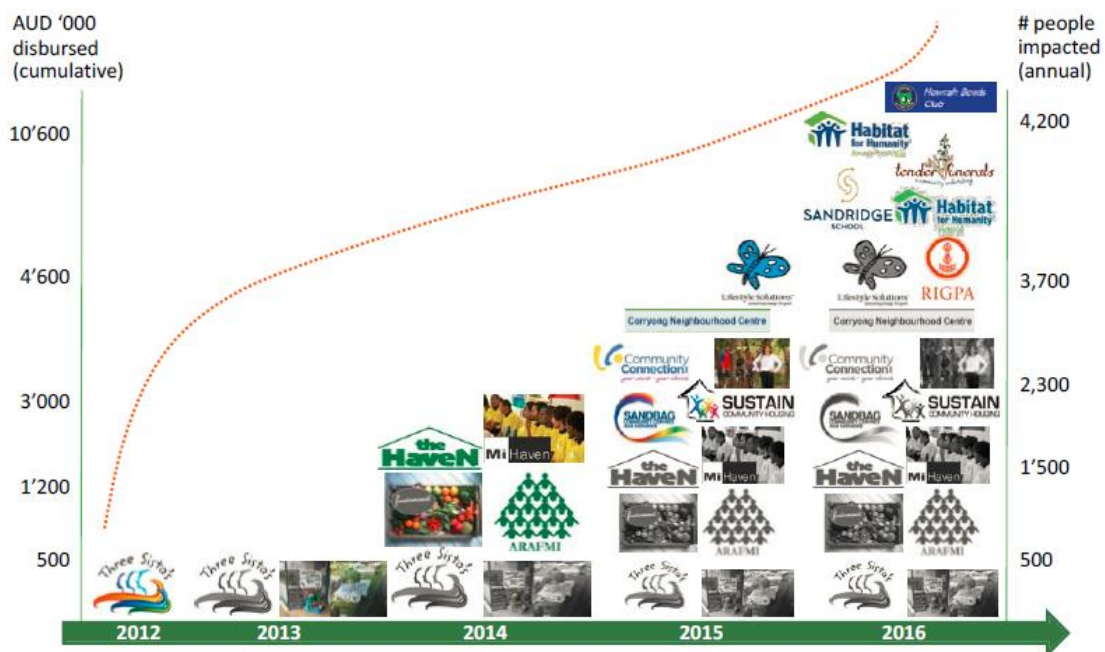
The Australian experience

The Australian experience also illustrates a multiplier effect generated from catalytic capital. Like the experience of international wholesalers, acceleration of momentum was particularly marked post 3-5 years of operation, (for example **Figure 3**). The key difference between the Australian and overseas experience has predominantly been in the scale of the initial capital and therefore the impact that it was possible to generate.

In 2011, the then Australian Government launched the Social Enterprise Development and Investment Funds, (SEDIF). These funds granted a total of \$20m to cornerstone 3 new investment funds to provide appropriate finance to social enterprise.

The 5 year evaluation of SEDIF found that for the \$20m investment of public monies, there were strong direct effects on capacity building and scaling social impacts for 64 SEDIF financed social enterprises, and modest indirect effects on developing capacity of 424 social enterprises. The evaluation recommended *‘That future policy developments give consideration to the suggestion raised by multiple interviewees, including some SEDIF co-investors and impact investment specialists, to establish a wholesale impact investment fund to support scalability of impact investing in Australia.’*¹⁷

Figure 3: Social Enterprise Finance Australia¹⁸ investing for Impact



Source: SEFA Impact Report 2016

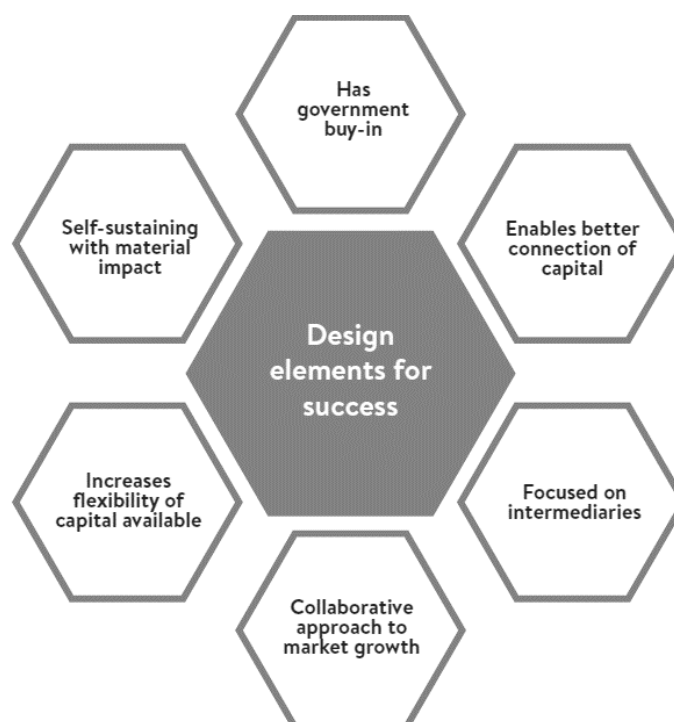
17 SEDIF Evaluation Report, 2016

18 Social Enterprise Finance Australia (SEFA) one of the SEDIF funds

Key components of successful wholesalers

There are numerous differences between the wholesaler examples provided both in terms of goals and context. Market size and stage are critical, as is the problem the wholesale investor wants to solve. A wholesale investor that aims to grow the overall market will differ from a wholesale investor that wants, for example, to specifically support early stage social enterprises or a specific issue such as clean energy. Notwithstanding different market context and forms, there are some common elements that all these wholesalers share that have been critical to their success, (Figure 4).

Figure 4: Key Elements of successful wholesale funds¹⁹



19 : Impact Investing Australia, 2015 adapted from Addis, R (2015). *The roles of government and policy in social finance* in Nicholls et al, *Social finance*, Oxford, UK

Part 2: The policy case for ICA

Overview of ICA and how it works

ICA is game changing infrastructure conceived to scale the impact investment market in Australia. It is designed to be independent, with a mission, investment mandate and sufficient catalytic capital at \$300m, to significantly accelerate market development.

As a predominantly wholesaler investor and market champion, ICA could provide seed capital to new impact funds, and bring tools and “know-how” to the structuring of products including the measurement of outcomes.

Our recommendation is for government to commit \$150m in 2018/19 which would be matched initially by a combined contribution from financial institutions including major Australian banks. The Government contribution could be structured as a grant and/or an approved investment

Detail on the vision, mission and mandate designed for ICA is provided in **Appendix 2**. This section provides a brief overview of its two key roles: investor and market champion.

As an investor, ICA will focus ~80% of its activity on finance for existing and new intermediaries. In its capacity as a wholesaler or fund of funds, ICA will invest in funds seeking to enter the impact investing market or those looking to grow in key impact sectors. ICA will also retain ~20% of its capital for investment **directly** into transactions that promised socially impactful, innovative and scalable solutions. It would “crowd-In” rather than “crowd-out” capital with direct investments which would not typically attract first mover capital from other sources.

Impact driven organisations and initiatives need access to capital on appropriate terms while on the investor side there is an increasing pool of capital seeking impact. The most efficient way to match demand and supply is through effective and appropriately skilled intermediaries delivering a variety of investment products that work for different types of issues and organisational requirements.

ICA is designed to provide a long-term committed platform that can have a catalytic effect to stimulate intermediaries and, through them, demand and deal pipeline. Funding by ICA in this way creates a much more significant multiplier effect, (discussed in more detail below).

In addition, without the availability of capital from an institution such as ICA, innovative ideas developed by intermediaries will struggle to find investors willing to go first on acceptable terms or who can appropriately price impact risk and return. When initiatives consistently don’t get off the ground, the cycle acts as a disincentive to others.

ICA’s investment mandate will have three central elements: clear impact, financial viability and contribution to market development. ICA will have the scope to be the first mover, providing flexible and appropriate terms and sending important signals to build market confidence and attract other investors. Its investment process will attribute value beyond financial returns to the social and market development dividends of new funds and products entering the market.

As a market champion, ICA could facilitate market development by proactively identifying opportunities and tackling barriers. Its combination of capital and collaborative approach will see it quickly become a go to place for new ideas and opportunities. ICA’s proactive allocation of capital to initiatives designed to achieve diversity, innovation and growth will underpin its influence in setting benchmarks for rigorous design and impact measurement.

ICA will also have a role in raising awareness and shifting mindsets. Areas it could tackle include: the cultural aversion to debt of socially motivated organisations; the simplification of investment jargon; a

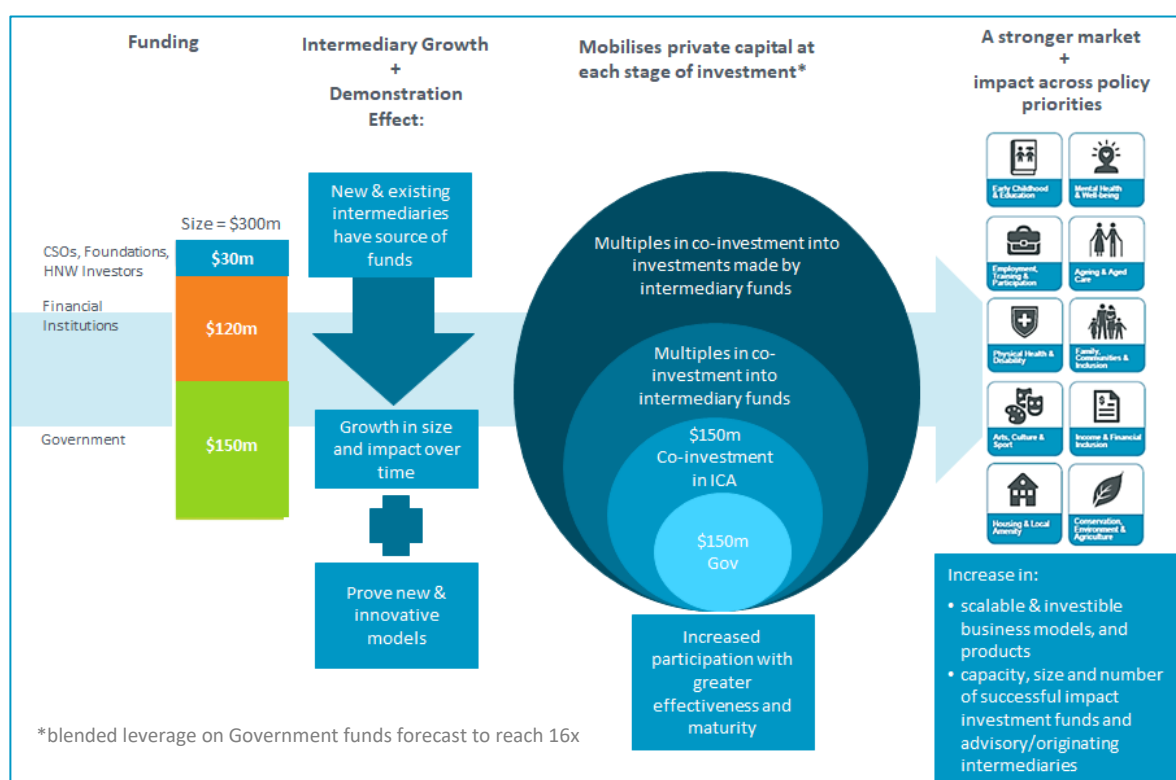
framework for understanding of the true costs and risks relating to impact; inexperience in blending philanthropic and investment capital; and the evolution of a new mainstream investment paradigm where impact is evaluated alongside financial risk and return.

In an environment of low trust in institutions, including governments and the banking sector, ICA represents a unique opportunity to demonstrate positive and collaborative action for the benefit of our communities. ICA will foster stakeholder collaboration and embody a multi-sector approach to impact investment. Its approach will include co-design and the convening of stakeholders to develop societally impactful, innovative and scalable solutions, particularly in more complex areas where the market may not go on its own.

The unique aspect of a wholesaler such as ICA is that its mandate seeks to ‘grow the pie’ rather than compete for a ‘slice of the pie’. Intermediaries already active in the market cannot fulfil this role. Their focus primarily is on developing their own businesses rather than encouraging and supporting other intermediaries and market infrastructure. Unless they have the benefit of their own significant capital reserves, they will also struggle to invest in ongoing development of new investment products or complex large transactions without further support being available.²⁰

ICA’s multiple layers of co-investment will create a material multiplier effect on the Government’s \$150m contribution. As **Figure 5** demonstrates, at each stage of investment more private capital is unlocked for public benefit. While in a tight budgetary environment the leverage on government capital is incredibly important, so too is its efficacy. In addition to the capital unlocked, support of intermediation enables the attraction of talent and capacity building. Measurement and monitoring of intermediary impact also places focus on what is being achieved for the money spent. This support of intermediaries will ultimately multiply the opportunities in the field and lead to additional ways of delivering more and better outcomes for our Australian communities including through new solutions to complex issues.

Figure 5: ICA creates a multiplier effect



Source: Impact Investing Australia, 2017

20 Addis, R, McCutchan, S and Munro, P, 2015, *Blueprint to Market: Impact Capital Australia*, Impact Investing Australia

The policy case

In an environment where government budgets are under-pressure two things are particularly critical:

- Maximising efficacy of government spending against policy priorities ie. Better outcomes.
- Unlocking private capital for direction towards policy priorities ie. More outcomes

More and better outcomes could actually be achieved with less money and result in savings to Government if effectively executed.

Recent policy announcements and Ministerial statements suggest the Government has recognised that impact investing has an important role to play in delivering these critical factors. They appear supportive of the market's development.

Game-changing policy, in establishing ICA, is now required to drive the impact investing market to a state of development where it can meaningfully contribute toward the Government's policy priorities.

There is no market from which governments are completely absent. The policy announcements in the 2017 Budget, release of the Social Impact Investment Principles (the Principles) and public statements from the Treasurer and other Ministers supportive of enabling and growing impact investment in and from Australia are welcome developments.

However, there is more to do for the Government to take up the Financial System Inquiry recommendation that it play a *'catalytic role both in facilitating the functioning of the ecosystem and targeting actions to trigger its further development.'*²¹

A proactive role for governments in building the market builders is well-recognised in impact investing and in other fields of market based activity. That role includes providing catalytic capital and incentives to encourage greater participation. The public value created will go beyond economic market effects. It will include outcomes and impact for vulnerable groups and communities and bring focused attention to contributing new solutions. ICA is specifically designed to execute on the Government's market building role.

Governments have well-recognised roles as market stewards, removing barriers to participation and ensuring the regulatory environment facilitates market activity and an appropriate level of accountability. ICA will contribute to this role by tackling key barriers to entry. It will also help set expectations and standards for accountability for impact thereby mitigating risk of 'impact-washing'.

Governments also have an established role as market participants and this can be a powerful way to unlock and direct capital to areas of policy priority. A clear theme that came through in the AAB field scan is that practitioners are looking for signals from the Government. They will welcome prudent utilisation of public monies to encourage more private capital into areas of need where current market conditions discourage investment. As a specialist wholesaler in impact investing, an investment from ICA could create signals around credibility of impact alongside providing flexible capital. Both elements will make it more attractive for other investors to participate resulting in better outcomes and more reach.

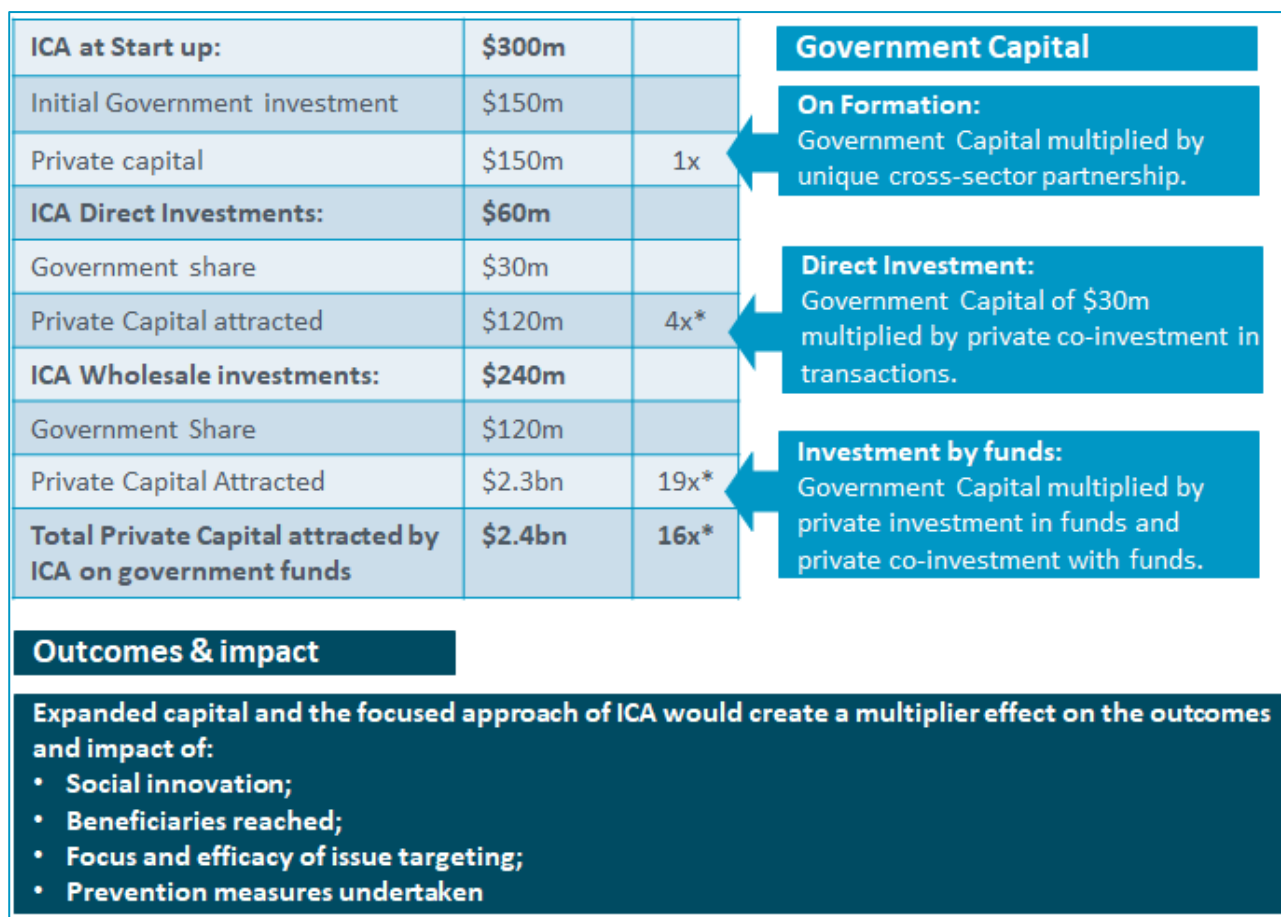
ICA is designed to reduce areas of long term dependency on public funds and is structured to maximise capital and non-capital resources from other sources. It will attract new sources of private capital and expertise to help drive new investment and innovation across key areas of policy priority and into targeted communities.

²¹ Financial System Inquiry Report, 2014

It has been mission-oriented State investments that have, time after time, and over national boundaries, proved effective in driving individual sectors in the innovation economy... writ large, the strategic State interventions that have shaped the market economy over generations have depended on grander themes – national development, national security, social justice, liberation from disease – that transcend the cultures of welfare economics and the logic of market failure²²

The Government will be a clear beneficiary of ICA through delivery of greater public value from improved outcomes and a multiplier effect on public funding. **Figure 6** illustrates an example of the multiplier effect that could be achieved with ICA.

Figure 6: Dimensions of the Multiplier Effect of ICA²³



Source: Impact Investing Australia, ICA Implementation Deck October 2017

Benefits of ICA will also flow to a broad range of stakeholders including:

- Australian communities and the economy through greater resource availability for social purposes, new approaches to solving entrenched problems and greater transparency and accountability for outcomes;
- Investors such as banks and intermediaries from ICA, as a market champion, being prepared to go first, unlocking new capital and creating new opportunities for investment with impact;
- The social and environmental sectors from improved access to a wider range of funding and finance options;
- Philanthropists and Foundations from the potential to achieve more impact from strategic use of grants and investment capital.

²² Janeway, W, H, 2013, *Doing Capitalism in the Innovation Economy: Markets, Speculation and the State*, Cambridge University Press

²³ See Appendix 2 for further analysis

Government is an essential partner

ICA cannot be implemented to achieve its objectives without the Government as a partner. There are a number of key reasons:

- Government is potentially both a key beneficiary and major participant in impact investing. The signalling effect of its early collaboration and commitment is therefore critical in instilling market confidence;
- In order for ICA to be self-sustaining, provide flexible capital and operate as a public good, it needs its own capital on the right terms. The private sector is prepared to partner with government to achieve this but would not be prepared to fund ICA alone; and
- The national nature of ICA's remit means the Australian Government is the more natural government partner to fund ICA. Once ICA is capitalised, there will be an important role for State governments in co-investment *with* ICA and its intermediaries.

ICA is designed to occupy a unique position as an independent organisation formed in partnership between the Australian Government, leading financial institutions and the community to operate as a public good. The trust and signalling effect will not be achieved without a cross-sector partnership in which Government is engaged.

ICA's remit needs to be national to have the intended effect. Government has a major stake in, and is a major beneficiary of, improving outcomes for people and communities. The outcome areas identified for ICA to operate relate to areas of national and shared government responsibility. Without government as a partner, the capacity to drive activity toward those areas will be reduced. If government is not at the table, its access benefits in learning and capability will be limited at best.

The Government capital will provide a degree of confidence to other investors in ICA such that:

- the risk adjusted return (i.e. Pricing) for co-investors will be reduced;
- Capital will flow which would otherwise not have been made available, (e.g. Banks will not typically provide debt to a fund of funds, particularly in a market still developing);
- Co-investment is enabled on terms that will not otherwise be possible, (e.g. Longer timeframes more aligned with market need).

Government funding in ICA's capital stack has a number of consequences. Most significantly, capital that if alternatively sourced would be too expensive could be offered by ICA on appropriate terms for impact directed activity and organisations. Additionally, ICA will be able to take a portfolio approach that reaches more impactful opportunities and still become self-sufficient over time, rather than only doing those transactions that target significantly higher hurdle rates of return.

The government contribution is also structured to enable ICA to undertake and facilitate design for new and more impactful opportunities within its operating budget. This will increase the collaborative effort and innovation to contribute new solutions, design for scale and reach issues that the market alone is unlikely to tackle.

The AAB concluded in 2014, *'There is enough capital and talent to make a significant difference to social issues; they need to be deployed differently to achieve a better result'*.²⁴ The experience across the globe has been that proactive steps are needed to achieve that shift. Even where there is willing capital in the market, the literature indicates that *'It is as if impact investors are lined up around the proverbial water pump waiting for the flood of deals, while no one is actually priming the pump'*.²⁵

²⁴ Addis, R, Bowden, A and Simpson, D, 2014, Delivering on Impact: The Australian Advisory Board Strategy for Catalysing Impact Investment, Impact Investing Australia

²⁵ Bannick, M and Goldman, P, 2013, Priming the Pump: The Case for a Sector Based Approach to Impact Investing, Omidyar Network

In Australia, the issues are magnified because there is a relatively thin venture capital and private equity market. Hurdle rates to mobilise institutional investment are high, and yet it is necessary to engage these investors if impact investment in this country is to achieve scale.

Policy alignment

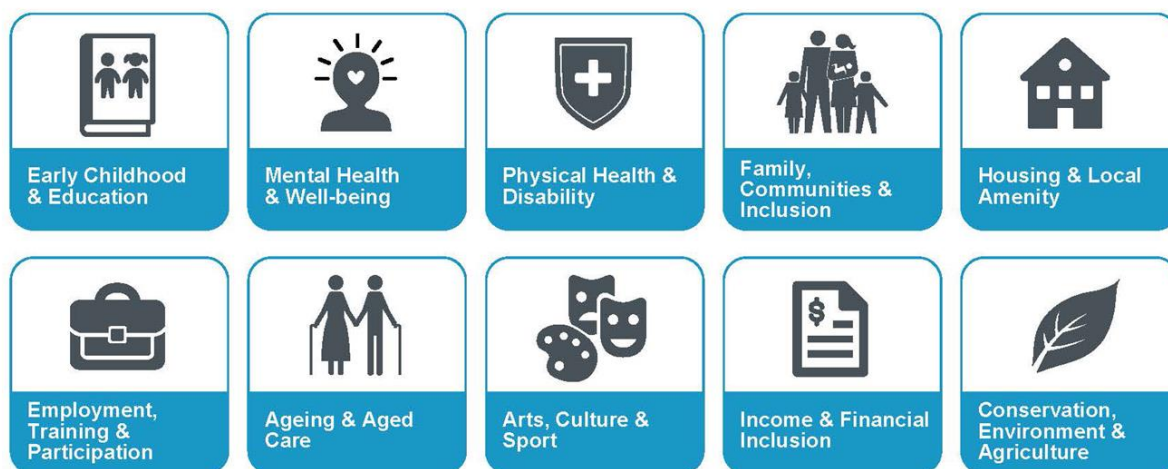
The design for ICA is based on leading practice in market development and market and innovation policy. This proposal builds on the Government's initiatives to develop the social impact investment market in Australia, including the 2017 Budget measures and the Australian Governments Principles for Social Impact Investment.

The outcome areas which will be the focus of ICA's investment mandate include Government policy priorities in: housing; employment and training; healthcare and disability, childcare and; financial and community inclusion.

In pursuing the growth of intermediation and focusing on efficacy and efficiency of capital, ICA's work will be highly aligned with the objectives of Government around the delivery of both more and better outcomes for Australian communities.

ICA's investment focus will be on the outcome areas in **Figure 7**.

Figure 7: ICA's targeted outcome areas



These outcome areas incorporate many aspects of the key policy priorities of the Australia Government. The broader enablement of the impact investment market by ICA is that these areas will support Government policy priorities as follows:

- *Fairness, Security and Opportunity*: The development of a robust for purpose or social enterprise sector enabled by greater access to capital through ICA, will support inclusive economic and jobs growth;

Place based investment in particular will be supported where opportunities exist to improve the flow of capital to communities that have experienced significant under-investment or withdrawal of industry. This will be further enhanced by increased investment availability in social services infrastructure;

- *Delivery of essential services in healthcare, housing, disability support and employment:* ICA will enable:
 - greater efficacy of government capital in service delivery by targeting outcomes with each dollar invested;
 - private co-investment delivering both more capital and better results through measurement;
 - innovation in service delivery through collaboration of cross-sector actors.

Measures to encourage market-based approaches could also encourage competition and facilitate access to quality services for all parts of the community.

- *Tackling cost of living pressures* in areas such as housing affordability, childcare and power prices. A key focus of ICA will be on scaling innovation around new structures and models including private co-investment and cross-subsidisation to deliver more affordable options in these areas at scale. ICA will also provide significant stimulus to unlock private capital for housing and social infrastructure. This will encourage a range of intermediaries and approaches to meet increasing demand for affordable stock particularly in key areas of reform such as disability support and aged care.
- *Government lives within its means.* There is growing budgetary pressure around social issues which the government and philanthropy alone cannot continue to meet. Through unlocking private capital, ICA is intended to create a multiplier effect for government capital estimated at over 16x on fully invested capital. A [drilldown on this multiplier](#) is in **Appendix 2**.

While ICA will operate domestically, it will send a strong market signal supportive of foreign policy priorities to encourage private sector partnerships, innovation and enterprise development in the Indo-Pacific and improve outcomes for women and girls. It is complementary to the recently announced Emerging Markets Impact Investment Fund and the Investing in Women and Pacific Rise initiatives.

Apart from its alignment to policy priorities, ICA's design is also consistent with the Government's Principles of Social Impact Investing. A detailed analysis of ICA against each of the Principles is set out in **Appendix 3**.

Part 3: ICA is implementation ready

Clear and accountable design

ICA's design is based on a broad evidence base and is the product of a collaboration between cross-sector leaders, locally and globally. A three year process of robust co-design and planning has brought ICA to a point where it can be readily implemented.

ICA would be an independent, purpose-driven organisation with standards and processes that ensure accountability for proper and effective use of resources. Governance would be the responsibility of a highly experienced board utilising appropriate committee structures.

Other aspects of accountability and transparency, such as performance monitoring and management and risk mitigation strategies, would all be essential in the formalisation of ICA policies on implementation.

ICA is good policy, which has been through a multi-stage, robust co-design and planning process and can be readily implemented.

ICA's design has been informed by: Australian market soundings led by the AAB in 2014 and 2017; the Financial System Inquiry; and the evidence and literature base for market design and innovation from sources including the OECD, G8 Social Impact Investment Taskforce and GSG; and the practical experience of the European Investment Bank and BSC. The blueprint, policy design and modelling for ICA is already informing work in other countries, including Japan and Canada.

ICA is designed to function as an independent, purpose-driven organisation with standards and processes that ensure accountability for impact, proper and effective use of resources and financial sustainability. It is critical that ICA's governance is rigorous, accountable, and transparent across dimensions of its implementation and operation.

ICA's structure will reflect the collaboration between the Australian Government, financial institutions and community and embed its independence and a mission lock that hard wires in its purpose.

Governance implementation will be the responsibility of a highly experienced board and management team. The governance structure allows for stakeholder interests to be represented and appropriate expertise to be brought into Board Committees as required. An experienced group of cross-sector leaders is already providing stewardship and support for ICA (see **Appendix 6**).

Performance monitoring is built into the design and will be reflected in contracting arrangements. An assessment of key risks and sensitivities and associated mitigation strategies has been informed by understanding of the Australian market for impact investment and the international experience. A risk management matrix is included in **Appendix 2**. As an entity in receipt of public monies, ICA will also be subject to requirements for Australian National Audit Office oversight and compliance with privacy and other applicable laws.

More background on the design, structure and governance principles is set out in the **Appendix 2**.

Implementation plan

A clear and accountable implementation plan has been developed for ICA. The plan has four stages, (Figure 8), with identified work-streams, milestones and time-frames:

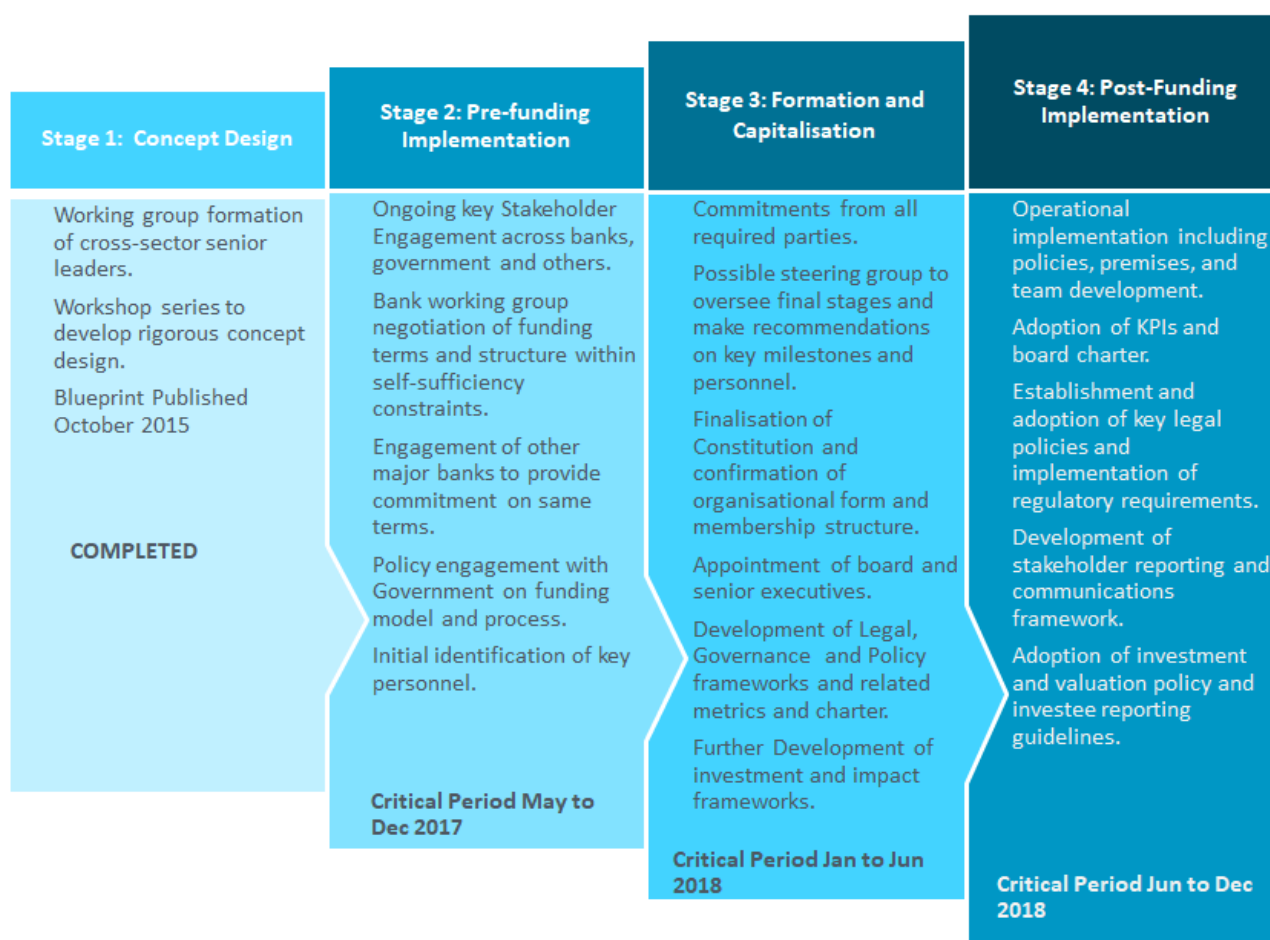
- Stage 1: concept design;
- Stage 2: pre-funding implementation;
- Stage 3: formation and capitalisation; and
- Stage 4: post-funding implementation.

Stage 1 has been completed and Stage 2 has been progressed to the final stages. The next major milestone is securing capital commitments from significant stakeholders including the Australian Government.

ICA's implementation plan anticipates a proposed funding partnership which includes the Government. This partnership will specifically meet the Social Impact Investing Principles and the seven key principles under the Commonwealth Grant Rules and Guidelines including integrated governance arrangements to mitigate risk. Performance monitoring is also built into the design and will be reflected in contracting arrangements.

Further information on the implementation plan and work-streams is included in (Appendix 2). A summary of the approach is shown in Figure 8.

Figure 8: ICA has a clear implementation plan broken into 4 stages



Source: Impact Investing Australia, 2017

Stages 3 and 4 of the implementation plan include developing ICA's operational policies and frameworks. These will embed systems of risk identification and management, planning and performance reporting and other processes necessary to ensure that ICA will secure and comply with an appropriate Australian Financial Services Licence and associated prudential regulation.

Implementation process

The acceleration of ICA's implementation would take place once funding is secured. In the first instance, implementation would likely fall under the remit of a steering group which would report to all key stakeholders and be tasked with critical milestones such as board and senior executive appointments, the adoption of the constitution and key policy developments including the board charter.

Once appointed, ICA's implementation would be transitioned to the board and senior executives. At this stage adoption of key policies would be formalised and operational implementation would be accelerated.

Ensuring accountability, transparency and the appropriate rigour in the related governance and communication framework is a critical aspects of the implementation process.

An implementation process is proposed for Stages 3 and 4 to facilitate efficient and effective implementation of the design and enable each of the contributing parties, including the Australian Government, to meet their respective approval, governance and accountability requirements.²⁶

It is proposed a small high calibre implementation steering group be established to oversee Stage 3 and the transition to Stage 4 of the Implementation Plan. The Steering Group will consult with, and report to, nominated officials in Government, the participating financial Institutions and the AAB. They could be supported by a small implementation team.

The Steering Group will be asked to make recommendations on key implementation milestones including: Board and Committee appointments; process and candidates for key personnel; design and adoption of a Board Charter; more detailed design of key policies and; finalisation of the investment mandate. The Steering Group could also propose or respond to implementation milestones for Stage 4. It is anticipated the Board and Executive team will be appointed during Stage 3.

During Stage 3, further work could also be carried out on the options for structuring the Australian Government capital contribution to ICA and to work through any further government approval processes. This could include providing support and materials for any Ministerial or other delegate briefings; Cabinet process or matters related to appropriations and; if applicable, design grant guidelines.

At the beginning of Stage 4, it is anticipated governance will transition to the ICA Board and executive team. There will still be work to do before doors open and operations commence. During this phase, ICA will report to clear milestones and time lines. Once the milestones have been achieved, ICA will be operation-ready and will commence operations in accordance with its internal policies and procedures.

Once operational, ICA will report to funders and investors, including Government, on financial and impact performance. It will also report publicly both in accordance with the requirements for a public company under the Corporations Act and on its societal impact.

ICA is designed to run for an initial 10 year period. A progress review is planned after 5 and 10 years of operations. On current modelling, it is anticipated the ramp up of the investment portfolio to full allocation will take approximately 5 years. An option for extension (by agreement) at the end of year 10 will allow for accumulated funds to be utilised to extend the operations of ICA or undertake an agreed program of

²⁶ Including requirements of the Public, Governance, Performance & Accountability Act 2013 and Rules made under that Act and, to the extent applicable, Commonwealth Grants Rules & Guidelines 2017.

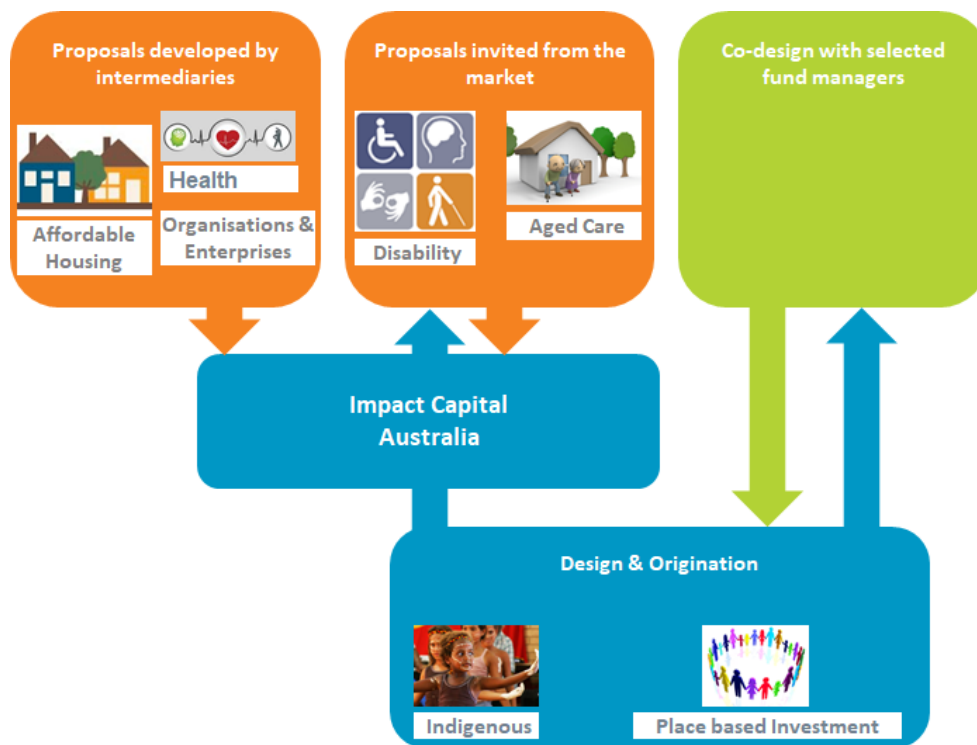
further work within mandated areas of operation based on an assessment of the needs and opportunities at that time.

Pipeline development

An important aspect of ICA's implementation is pipeline development. The early identification of opportunities and adoption of initiatives around building pipeline, (Figure 8), will accelerate the speed of ICA's market impact, once capitalised.

Pipeline development will consider the [different types of impact investments](#) which relate to: infrastructure and property assets; organisations and enterprises; and service delivery as illustrated in **Appendix 2**.

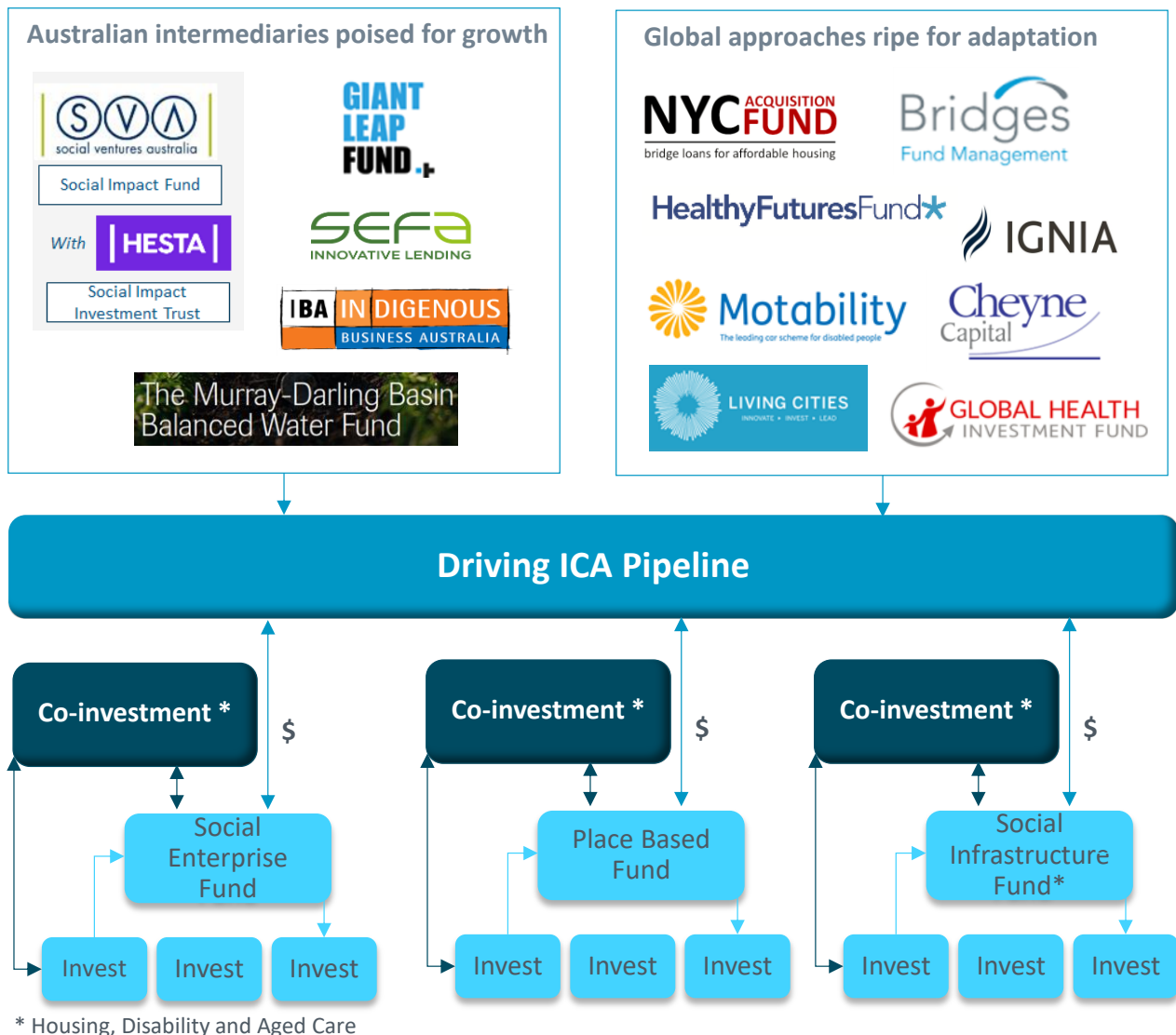
Figure 8: ICA's proposed initiatives for Pipeline Development



Source: Impact Investing Australia, 2017

Drawing on international experience, early opportunities for investment have been identified in: social and affordable housing as a complement to other initiatives; accommodation and services for people with disabilities to support transition to the National Disability Insurance Scheme; community investment to drive jobs and economic activity in priority areas and; the acceleration of outcomes based approaches to commissioning, (Figure 9).

Figure 9: Initial opportunities for ICA’s Pipeline



Examples of potential wholesale investments for ICA include:

- a fund to invest in aspirational small and medium enterprises in communities that have experienced a lack or withdrawal of investment to generate impact in jobs and local economic activity, (Case Study 1);
- a social impact bond fund focused on social service based investments across a range of outcome areas;
- a social housing investment fund to create purpose built accommodation for people with disabilities, (Case Study 2); and
- a fund that makes investments to: support new business models that enable new approaches to tough social issues or; enable social purpose organisations to expand successful initiatives.

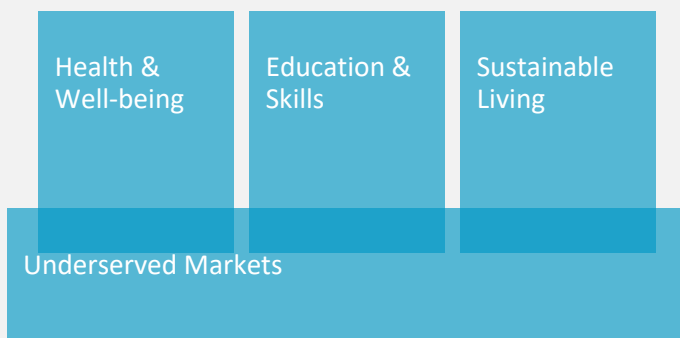
Case study 1: Drawing on the UK experience – an Australian place based investment fund



UK experience: Bridges sustainable growth fund:

- Bridges’ Sustainable Growth Funds invest in ambitious growth businesses that are helping to tackle some of society’s biggest challenges – in areas like healthcare, education and the environment.
- Bridges invest **£2m-£20m** in businesses pursuing organic growth, buy and build, and multi-site roll out strategies across any of their impact themes.
- Since its first fund was launched in 2002, Bridges have built a strong track record resulting in 10 successful exits generating multiples ranging from 1.6-22x.
- In 2013, the fund won best British private equity exit for the partial sale of its stake in the Gym Group at 3.7x generating an IRR of 50%.

Impact themes:

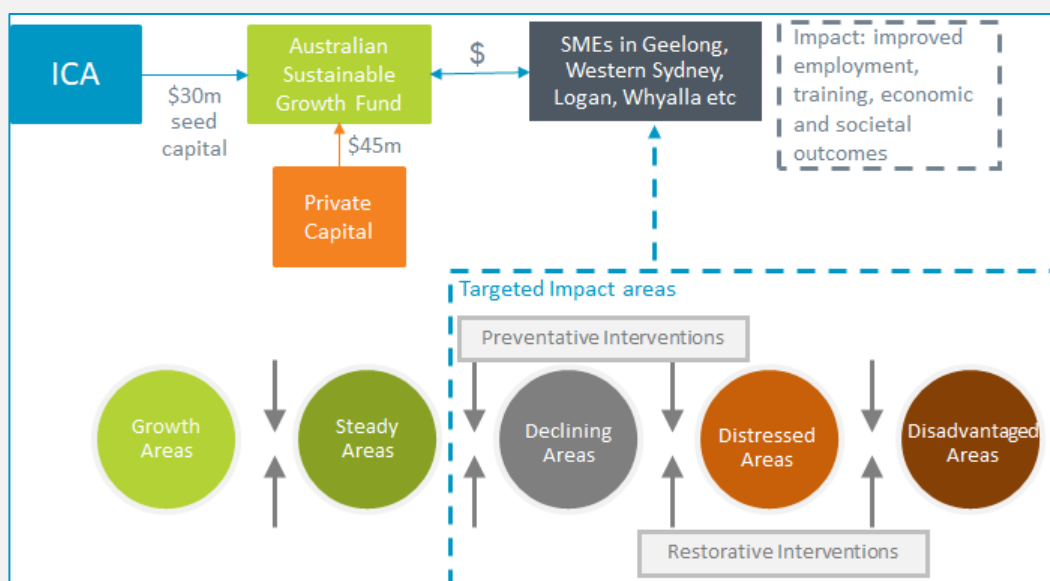


Examples of investments:



Australian concept for a sustainable growth fund:

- Building on work already done to adapt leading community investment models for the Australian context, ICA could cornerstone an Australian sustainable growth fund.
- Like the Bridges fund, it will seek to invest in SMEs in communities which have experienced sustained under investment.
- Impact will be targeted at economic development, employment and training opportunities and improved societal outcomes within the communities.
- Ultimately designed to shift long term dependency on public funds in these communities and create a demonstration effect to encourage further innovation and private investment.



Source: Impact Investing Australia, 2017 from information collected on Bridges Sustainable Growth Fund.

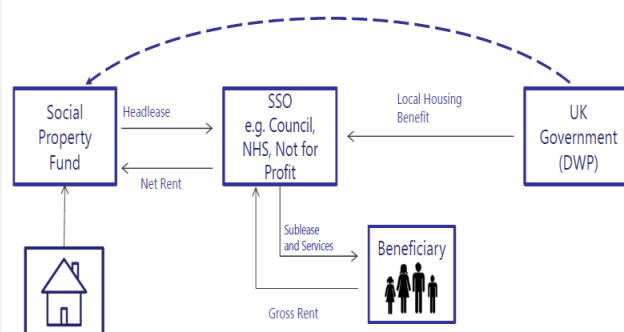
Case study 2: Drawing on its UK Experience – Cheyne Capital Australia disability housing impact fund



Cheyne social property impact fund, (SoPro):

- Cheyne Capital is one of the largest alternative asset managers in Europe with ~US\$14bn in assets under management of which over US\$2-3bn are in real estate funds [2017].
- In 2014, it established SoPro to address the chronic shortage of supply in UK social property. At 30 September 2017 the fund had £250m under management.
- The UK wholesaler, Big Society Capital was an important seed investor in the Fund.
- The fund's objective is to increase the capacity of social sector organisations, (SSOs) for the delivery of their front line services. Properties are bought or built for the needs of the SSO and their beneficiaries, and leased on attractive and extended terms (circa 20-40 years).
- New Philanthropy Capital (a social consultancy) ensures all investments are socially responsible.
- Overall targets for the fund are for an IRR of 10-12% with 5-6% expected in annual distributions.
- SoPro is a part of the New Communities Partnership, (with Kier Living, the HCA²⁷ and Lloyds Banking group), a unique £1bn housing delivery fund with ambitions to help the public sector to build 10,000 new homes across the UK.
- SoPro is delivering over 1,500 homes across disability, key worker, social and elderly housing without the need for any government grant.

The structure of the rental arrangement:



Cheyne Australian disability housing impact fund, (CADIF)

- Cheyne is exploring investor appetite for its CADIF which would be launched in partnership with Ability First Australia (AFA), a large strategic alliance in the specialist disability service sector.
- The fund will be dedicated to investing in Specialist Disability Accommodation (SDA), helping to support the estimated 110,000 person increase in housing support requirements identified under the roll out of the National Disability Insurance Scheme (NDIS).
- The fund will purchase or develop property for long term SDA use, with tenant rent paid from the NDIS program, with leases on a triple net basis²⁸ and over a 20 year period.
- Social impact will be independently audited annually including an assessment of care provision by SDA Providers.
- The fund will assist governments in the roll out of the NDIS by helping to support supply and privatisation of stock into a growing rapid demand for SDA properties. The value of these properties is estimated to be \$11.5bn of which 43% will be stock new to the sector.
- Indicative return expectations, [IRR basis net of fees], for the assets within the portfolio over the funds 20 year horizon are: 6-7% for existing stock [unlevered], and 9-10% on new stock [levered].
- Should the Cheyne fund be launched, a capitalised ICA would be well positioned to provide investment to catalyse the fund and its impacts.



Source: Impact Investing Australia, 2017, from discussions with Cheyne Capital

²⁷ Homes and Communities Agency

²⁸ This means the fund would have a rental claim on the AFA, the Disability Service provider and the tenants

Conclusion

Like any new market, impact investing in Australia will grow faster with an effective catalyst. A go to place to help co-ordinate fragmented efforts, and support intermediation and demonstration of new approaches to solving our societal issues. International experience has shown the effectiveness of a national impact investment wholesaler in catalysing the market.

The Australian Government has taken some good first steps in support of impact investing both in initial policy moves in the 2017 budget and through supportive speeches and commentary from Ministers and Senators. There is now a significant choice to be made and that choice is in the hands of the Australian Government. The Government can continue to take incremental steps and not realise the impact investing markets potential, or it can enable a game-changing institution and unlock the opportunity to drive positive societal outcomes at scale. Australian communities need the Government to make the right choice.

Recommendation:

Create a step change in Australia's impact investing market by committing \$150m in 2018/19 to be matched by Australian financial institutions and other societally focused investors to establish Impact Capital Australia (ICA). ICA will be a game changing \$300m wholesale institution with the capital, mission and mandate to improve people's lives by driving the impact investment market in Australia to scale.

This year's pre-Budget submission focuses in on the highest priority action to achieve a breakthrough in enabling and supporting the market for impact investment, ICA.

ICA is the measure that will enable demonstration of more innovative approaches to tackling issues that matter for communities rather than letting the market cherry pick opportunities. ICA is the measure with the greatest potential to pump prime the intermediaries and build the capacity needed to reach scale.

Implementing ICA will help sustain Australia's leadership position globally in the field of impact investing. Building on our competitive position, it could help unlock new sources of foreign investment into both our own country and across the region.

ICA complements the 2017 Budget measures and could be supplemented over time with other measures that ground a whole of government approach that encourages impact investment.

ICA is not the only constructive step the Australian Government could take, or the only one that will be needed, (**Appendix 5** includes details of other initiatives). However, ICA is the one that will make the biggest difference and is the measure most likely to put the market on a path to scale. ICA will change the game because it is unique. It exists not to make a surplus profit or compete against others in the market but to act as an independent, designated market champion with the capital and mission to grow the market.

The AAB and Impact Investing Australia welcome the opportunity to have input into this pre-Budget process. We urge the Australian Government to take up the opportunity for targeted action to fuel development of impact investment. Members of the AAB and Impact Investing Australia Executive will be happy to meet to discuss any aspect of this Submission.

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APPENDICES

Appendix 1: Update on the views of the Australian impact investing market

The next wave of Australian strategy

Since 2014 the AAB have been bringing together people, ideas and resources to help tackle big issues affecting Australia and our region. The AAB's work has consistently been informed by practitioner and participant experience and voices from across the impact investing ecosystem.

A further round of market soundings was conducted in October and November 2017 to assess what has changed over the last three years, what is happening and what is needed next. This will inform the next wave of AAB strategy development in 2018.

This field scan involved interviews, worked case studies and a broad-based survey supplemented by research and literature on the current state of the field and emerging trends locally and overseas. On behalf of the AAB, the team spoke one on one with more than 45 people active in impact investing and conducted a survey which received over 40 full responses, including a significant number from people working in and with governments.

The views from the impact investing playing field have been documented and a sketch video and brief report that play back what was heard will be available prior to the end of the year and released more formally in early 2018.

Key insights

Some clear messages came through from the field. A strong sense that:

- The Australian impact investing ecosystem (**Figure 10**) has shown positive development over the past 3 years, more people are getting involved and early investments are building track record.
- Things have matured from relatively ad hoc, uncoordinated initiatives into early stages of market and practice building.
- There is more potential, and people would like to see impact investment grow.

Views on how much potential and the prospects for it to be realised depended on where people sit in the ecosystem and their perspective on some key factors. Significantly, that includes whether governments take up a more proactive role.

Almost everyone spoke or commented on the need for scale. Their comments reflected that scale means different things to different people. For some it was about transactions of larger dollar amount. For others scale meant activities that benefit people and communities being replicated, packaged and/or designed for reach and growth.

A strong sense came through that developments so far have been led from finance - investors, financial intermediaries and government. People spoke about a need for more balance with focus on design and capability to push impactful activity into the system.

People recognised and welcomed the growing government interest and activity, at Commonwealth, State and even local level. And they would like to see even more proactive signalling and engagement, particularly to provide catalytic capital, build the market builders and infrastructure and to engage on data and outcomes based commissioning.

Some were positive about interest from corporates and investors, including superannuation funds, in the UN SDGs and ideas like shared value and saw real potential for growth if this can be developed effectively.

Some identified concrete opportunities in 'sweet spots' where there is alignment of policy priority and interest, unmet need and demand and conditions for investor interest. This included in areas such as housing, changes in the system for people with disabilities and regional infrastructure and jobs.

Some themes came through clearly about challenges still to be addressed, in particular:

- growing and deepening the pool of skilled intermediaries;
- developing packaging and aggregation investment opportunities for investment that can attract more mainstream actors including superannuation funds;
- mobilising more catalytic capital that can provide flexibility to demonstrate new models and unlock additional investment;
- accessing and developing data that supports good design, impact management and measurement.

The market sounding points to levers that can accelerate and enable impact investing to grow and develop as an enabler of innovation, enterprise and impact:

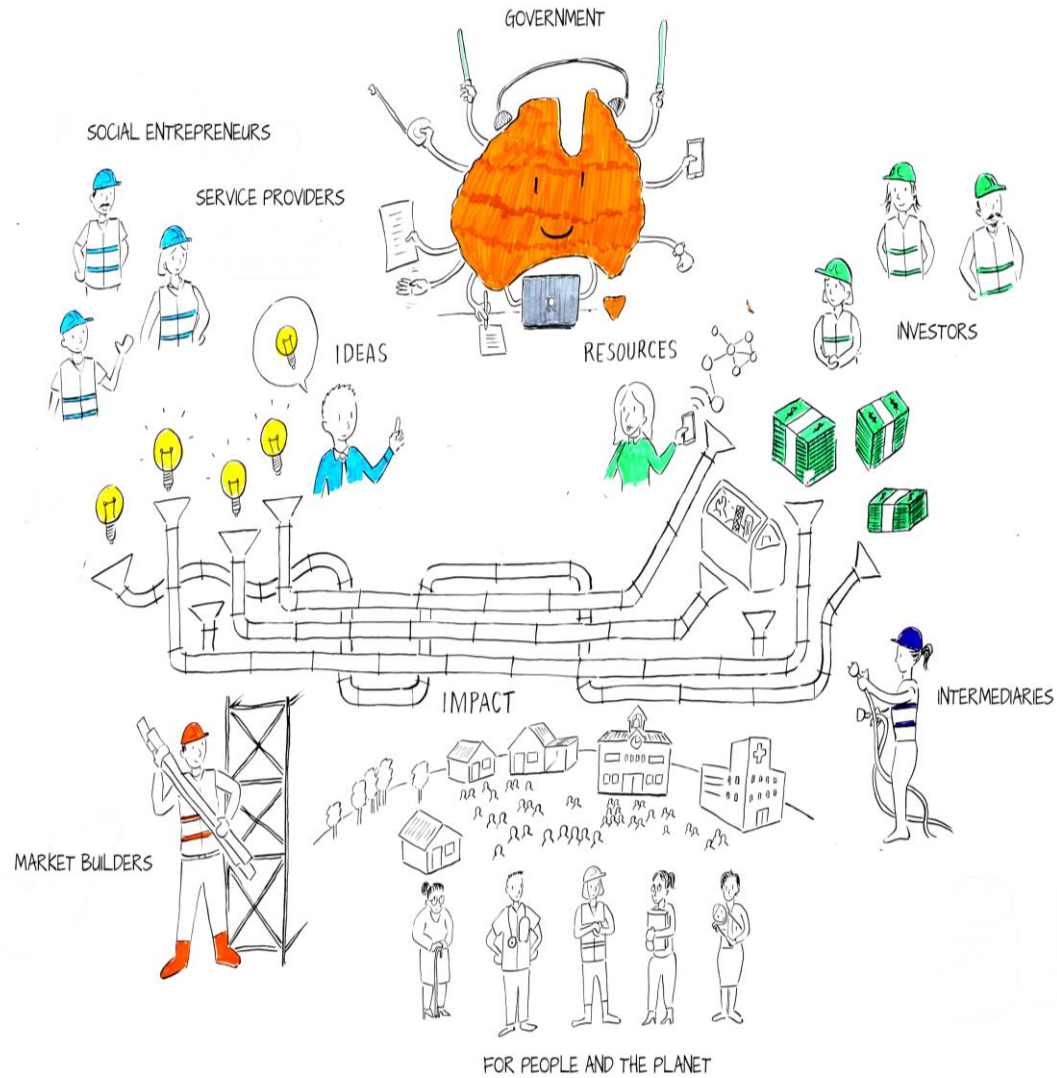
- designing for scale and to replicate good ideas;
- deepening and skilling up the intermediary market in a sustainable way;
- packaging opportunities differently to make them more attractive to investors, including pooling and aggregation options;
- attracting sources of (catalytic) capital that can unlock both activity and capital;
- encouraging governments to broaden and deepen their engagement and be more proactive in helping to guide and support market growth;
- strengthening impact management and measurement;
- discouraging impact washing;
- building on growing interest in the UN SDGs to engage and mobilise institutional investors, superannuation funds and corporates;
- marketing impact investing more broadly and activating consumer demand to incentivise action;
- taking up global opportunities and harnessing impact investment to support development in our region; and
- Investing time, resources, effort and money in market building.

These findings reinforce the call for proactive, targeted government action, catalytic capital and a focus on developing qualified intermediaries.

The AAB welcomes engagement and collaboration from governments in the implementation of market infrastructure and development of the next wave of strategy to accelerate growth of impact investment in and from Australia.

For further background material on the field and developments in impact investing see the material on the [GSG](#), [AAB](#) and [Impact Investing Australia](#) websites.

Figure 10: Illustration of the impact investing Eco-system



Source: AAB Field Scan Report, to be released 2018

Appendix 2: Impact Capital Australia

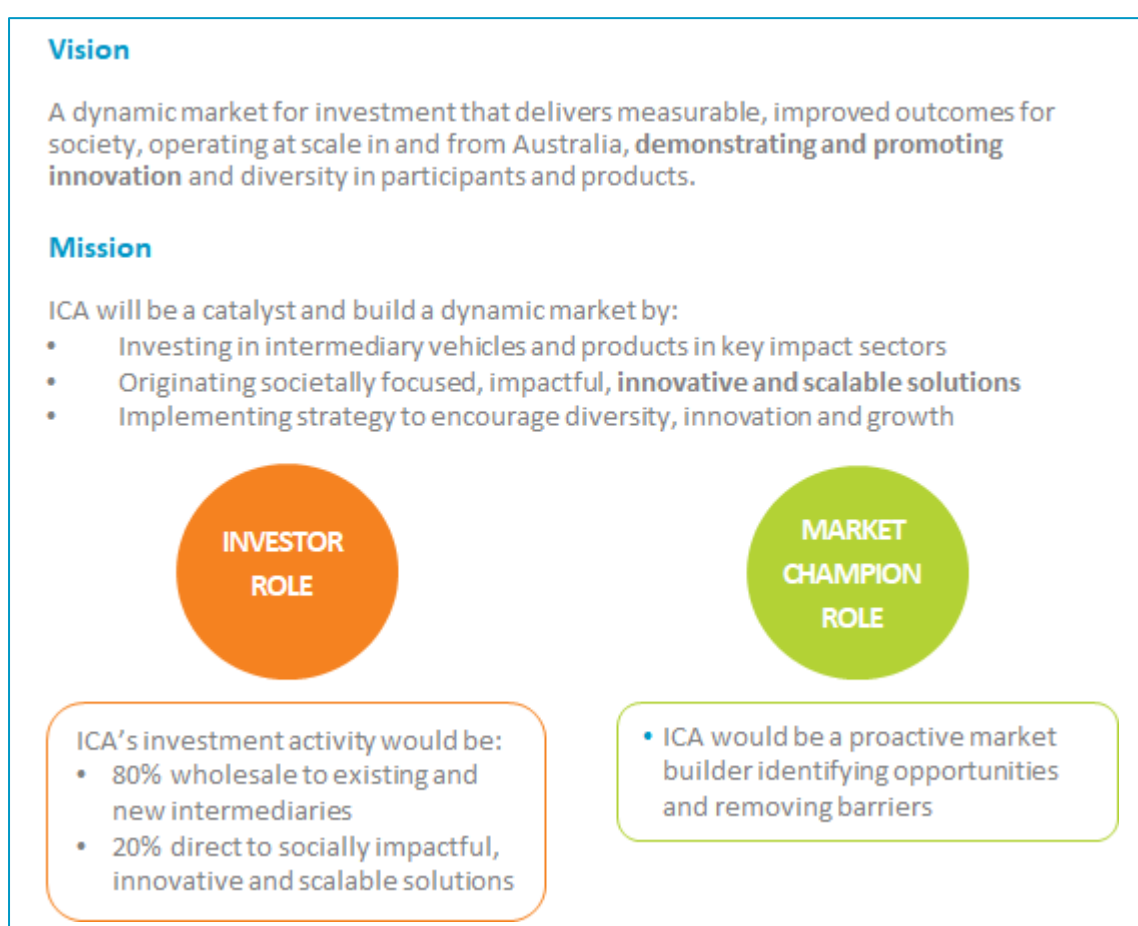
About ICA

A detailed Blueprint has been developed for how ICA can and should be brought to market. It is available at [Blueprint to Market](#).

The strategy and design has been developed with leaders from across sectors. The work to date on ICA has drawn on a broad evidence base and cross-sector skill set both locally and globally. It is grounded in a deep understanding of the local market and lessons learned internationally. There is a clear and accountable plan for implementation.

The vision and mission for ICA are set out in **Figure 11**.

Figure 11: Impact Capital Australia: vision, mission and mandate

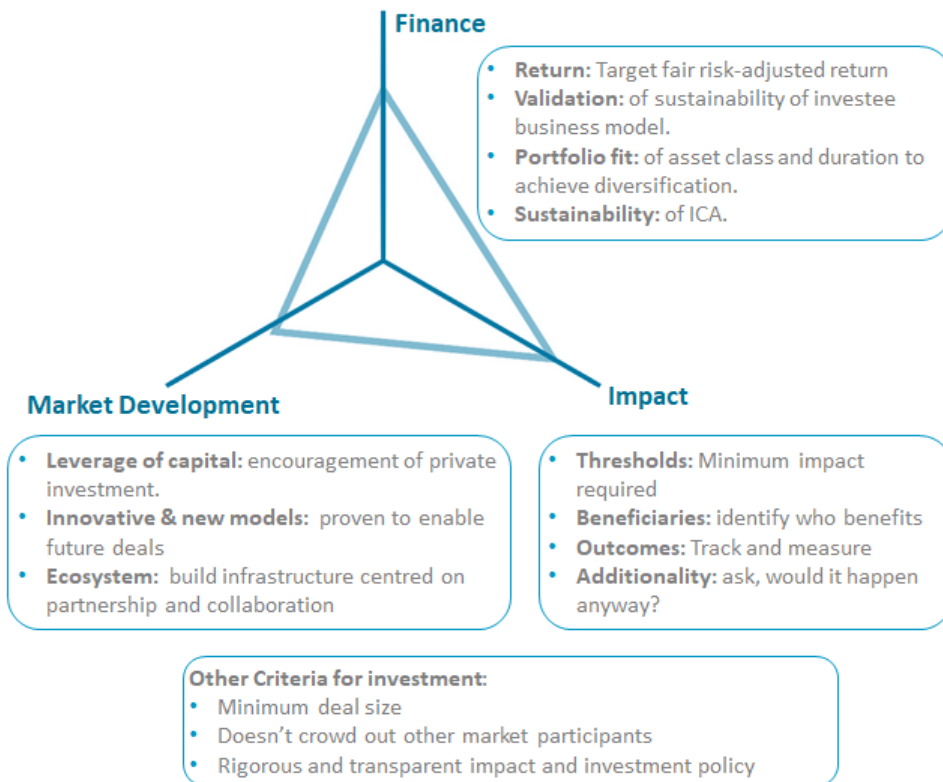


Source: Impact Investing Australia, 2016

ICA's investment mandate will have three central elements: clear impact, financial viability and contribution to market development (**Figure 12**). ICA's predominant investment focus will be wholesale (**Figure 13**), providing finance to existing market participants to grow their reach and impact, and encouraging more participants to enter the market because capital is more readily available to them.

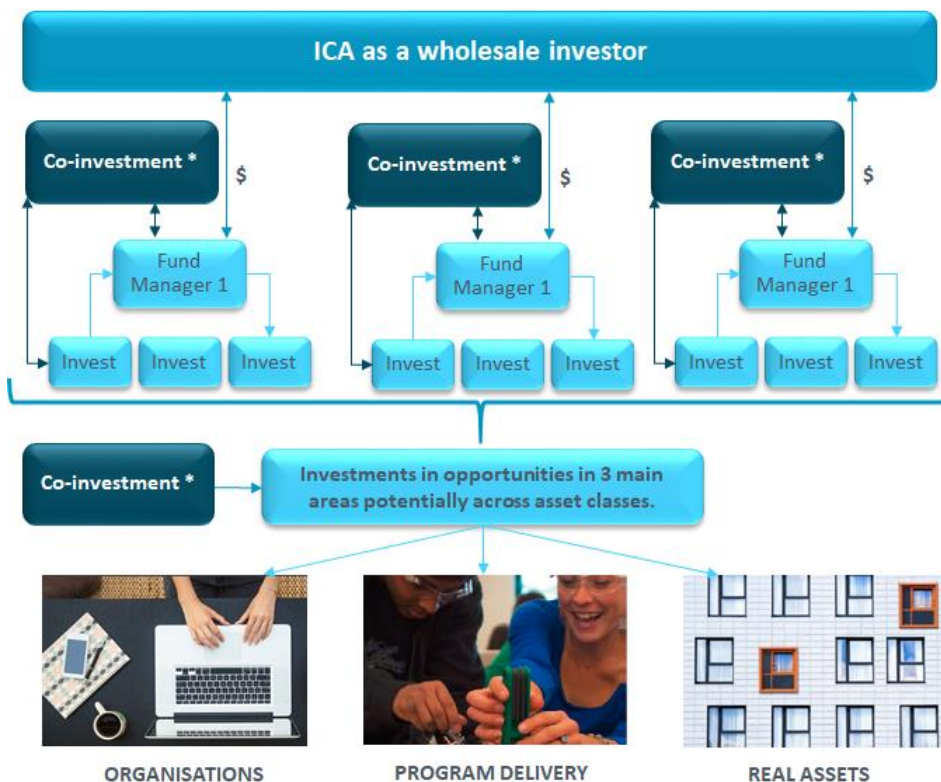
To be effective, ICA will also need capacity to be proactive to fill market gaps where deals will otherwise not happen, and where its participation will send a market signal that unlocks the potential for transformative approaches and for resources that will not otherwise be available.

Figure 12: Portfolio dynamics for impact



Source: ICA Implementation presentation, 2017

Figure 13: ICA's role as a wholesaler

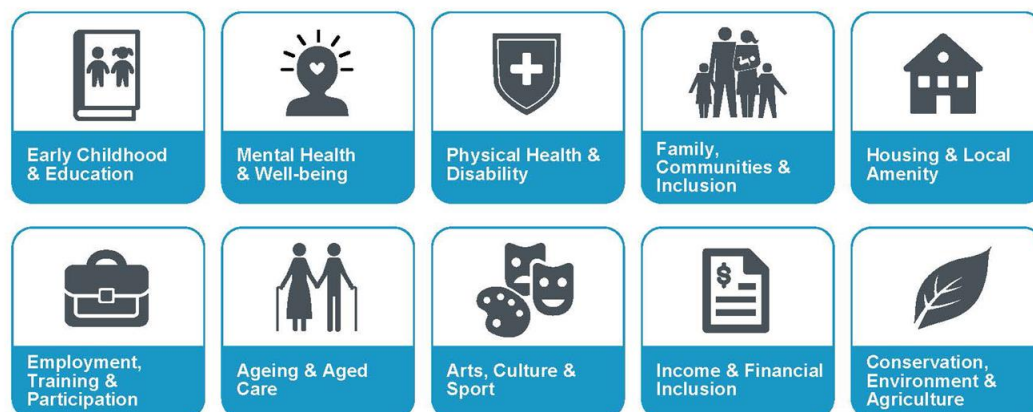


* Could be corporate, private or philanthropic

Source: ICA Implementation presentation, 2017

As a threshold requirement, all investments will need to demonstrate impact in one or more of the outcome areas that define the portfolio.(Figure 14).

Figure 14: ICA outcome areas



Source: Addis, R et al, 2015, Blueprint to Market: Impact Capital Australia.

Examples of potential wholesale investments for ICA could include:

- a fund to invest in aspirational small and medium enterprises in communities that have experienced lack of, or withdrawal of, investment to generate impact in jobs and local economic activity;
- a social impact bond fund focused on social service based investments across a range of outcome areas;
- a social housing investment fund to create purpose built accommodation for people with disabilities;
- a fund that makes investments, to support new business models that enables new approaches to tough social issues or enables social purpose organisations to do more of what works.

Beyond its investments, ICA will have a clear role as market champion, targeting barriers to growth, actively developing and openly sharing expertise, knowledge and tools. It will build meaningful engagement with communities, sector experts and with regulators and governments.

This role in combination with its investment mandate will position ICA to ‘grow the pie’, creating a multiplier effect, by delivering greater value from public investment and unlocking private capital and talent, and expanding the potential for impact.

Financial model for ICA

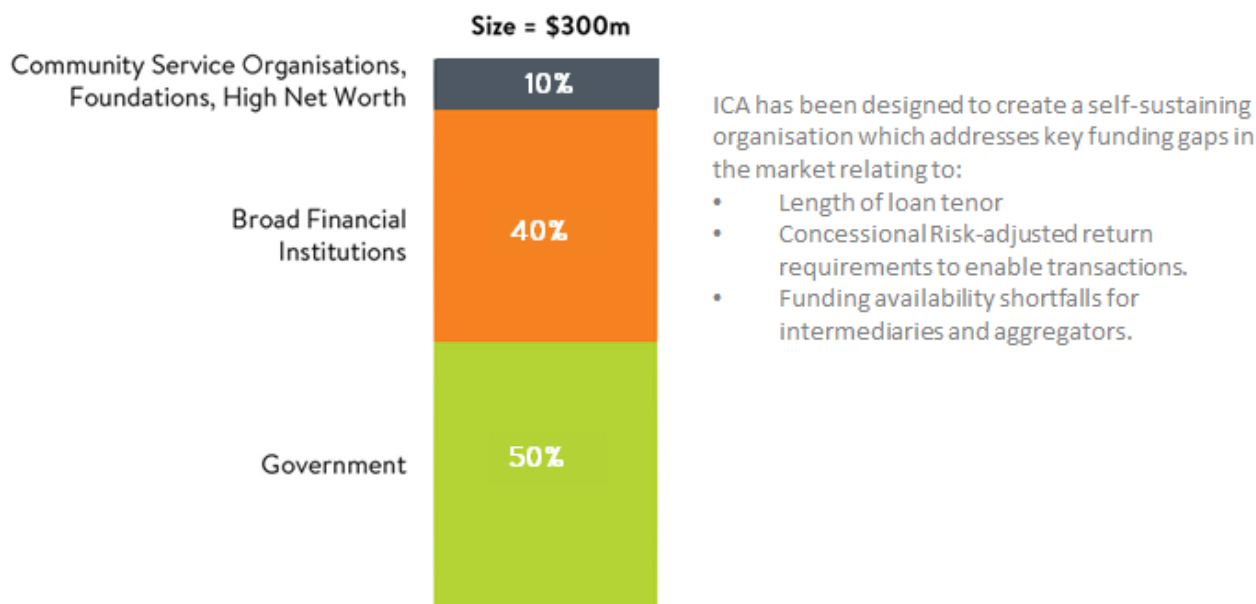
Modelling indicates ICA will need **initial capital of \$300m** to provide a signal to the market, invest in deals at scale, and to operate self-sufficiently. Initial capital contributions to ICA (Figure 15) have been modelled: Government 50%; mainstream financial institutions 40%; community, philanthropy and other investors 10%.

If the government’s contribution was a grant ICA’s income stream, including interest earned on seed funding, will support the origination function and fund market building activity and the establishment and operating costs.

The terms of funding are likely to be different for each of the categories of capital provider. Grant or investment funding from governments; debt from major financial institutions on terms that include

preservation of capital but with a return below full commercial rates; and debt on similar terms from the community sector and other investors providing it meets their fiduciary duties. Initial modelling anticipates ICA will have a self-sustaining cash flow profile within 7 years.

Figure 15: Initial capital structure for Impact Capital Australia



Source: Modified from Addis, R et al, Blueprint to Market, 2015

Initially conceived by the Australian Advisory Board as a \$350m fund, a rigorous process was put in place to validate the capital requirements for ICA thereby reducing this to \$300m. Underpinning this is a financial model developed by Impact Investing Australia together with a Working Group of senior leaders and A.T. Kearney, and predicated on ICA's proposed business operating model.

The first step in this process was the construction of an economic model to better understand the key financial levers of the business across the elements of revenue, capital and expenses. The economic model also considers the tangible and intangible drivers of value, such as brand and government policy changes, to enable appropriate risk recognition and assessment across these dimensions. The economic model was further broken down and tested for key sensitivities. These identified sensitivities form the basis of the most significant variables and assumptions around which the financial model is built.

Once the initial financial model was constructed, a sub-committee of the Working Group, with extensive experience in financial markets and analysis, rigorously examined assumptions and sensitivities. The financial model went through extensive and iterative revision as part of this process.

The modelling indicates that \$300m is the total capital required to ensure a sustainable business model for ICA. The first 5 years of cumulative net income will result in a deficit which will need to be supported by ICA's initial capital. Over a 10 year period, this deficit becomes a surplus as investments mature enabling ICA to self-sufficiency. It is anticipated ICA will reach net positive cash flow in 7 years with steady state cash flow in 10 years, based on an assumed life cycle of investments at 7 years. Capital contributions to ICA will need to be patient to correspond with the underlying investment profile.

A summary of the economic model, sensitivities and financial model are available in the full Blueprint document.

Drill down on the multiplier effect

It is anticipated that a government investment in ICA will have a significant multiplier effect on government capital. This is set out in **Table 5** below with a blended multiplier effect of 16x.

Table 5: ICA Multiplier effect explained

	ICA at Start up	Direct [D]	Wholesale [W]	Total ICA [D+W]
% of portfolio		20%	80%	100%
ICA Investment (\$M)		60	240	300
Maximum Investment %		40%	40%	n/a
ICA + Private Direct Investment		150	600	750
Maximum % of Investee Purchased			25%	n/a
Funds Investment (\$M)			2400	2400
Government Capital (\$M)	150	30	120	150
Total Private capital (\$M)	150	120	2280	2400
Multiplier on Government funds	1.0	4.0	19.0	16.0

Source: ICA Implementation presentation, 2017

ICA modelling assumes that the maximum direct or wholesale investment ICA makes in an entity is 40%. This is consistent with the ratio of comparable companies such as the Clean Energy Finance Corporation and Big Society Capital since inception.

Investments by funds in investee companies is capped at 25% which takes into account both a conservative approach to the multiplier effect and risk management at the fund level.

The result shows a multiplier effect on private capital of 16x on the government's capital at the final stage of investment. Implying a \$150m contribution by the government into ICA will unlock \$2.4bn of private capital.

Governance and leadership

Clear, transparent and accountable governance is a minimum requirement for ICA. Its governance principles are designed to enable it to execute its unique mission and mandate effectively and for impact, financial return and the benefit of the market as a whole (**Figure 16**).

ICA's mission and mandate for the public good will be embedded in its Constitution and in the policies that govern its operations. ICA also needs to be independent and not be reactive to, or inhibited by, shorter-term drivers, vested interests, or changes in the political environment.

Legal advice has been obtained from Ashurst on regulatory and compliance considerations and structuring

and governance. Policies and processes will be put in place to embed the requirements and ensure it is compliant with relevant licensing and regulatory requirements. It will be transparent and accountable to the public and market. It will operate collaboratively, including with its founding partners.

Figure 16: Structure and governance will ensure conformity to the agreed mission and mandate



Source: Adapted from Blueprint to Market, 2015

ICA will be constituted as a public company with a Constitution that embeds and safeguards its mission and mandate. The Board of the organisation will have responsibility under the Corporations Act for its stewardship. A majority of the Board will be non-executive directors to safeguard the independence of the organisation.

A committee structure will be put into place to oversee key aspects of governance and operations. Additional expertise may be sought, in particular to ensure that expertise and evidence on social impact, on investment and on markets are brought together in appropriate combinations.

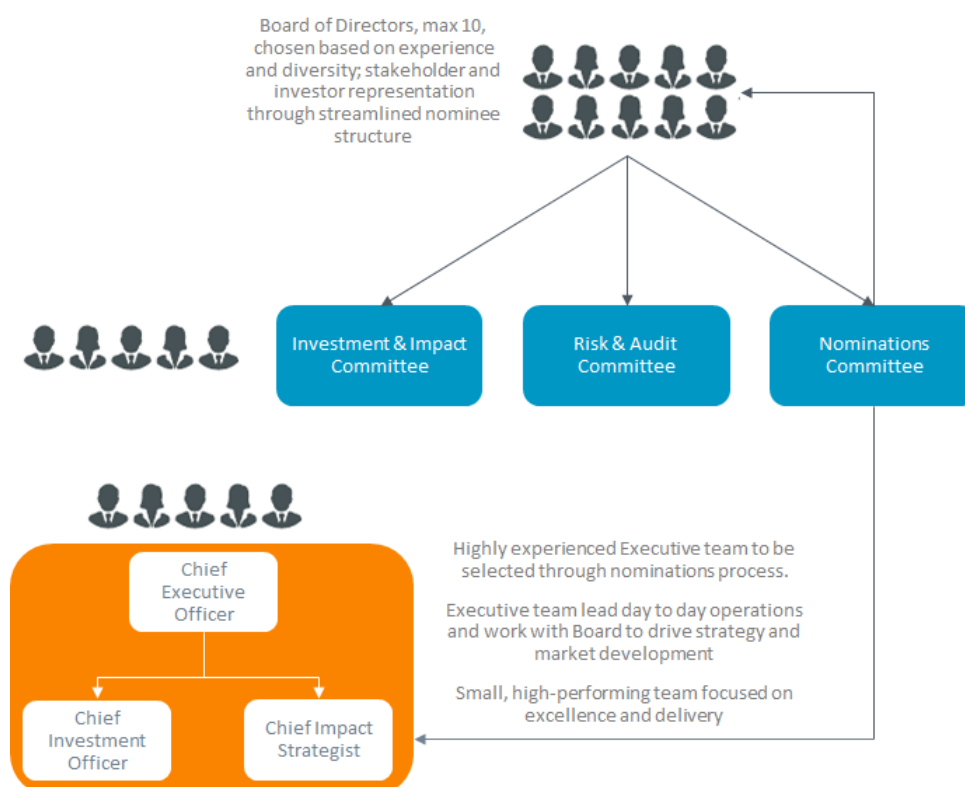
ICA will also be accountable for performance as an organisation, investor and market champion. It will have structured and rigorous processes for measurement and reporting. Those processes will embed accountability for impact achieved, financial performance and market development effects.

In addition, ICA will proactively seek to establish a reputation in the market for excellence, integrity and transparency; and operate on a basis where transactions with which it is involved reach the market with effective execution and monitoring of impact.

ICA will have a first rate Board of committed Australian leaders that combines diversity of experience and perspectives with individual credentials, providing ICA with stewardship to operate with excellence, integrity and impact (**Figure 17**).

A highly effective team led by a first rate executive will be critical. Based on the lessons from other impact funds, the team will be constructed to integrate investment professionals, impact strategists and systems expertise for maximum capacity to deliver across the three core elements of impact, financial viability and market development. Over time, ICA will become an important training ground for talent.

Figure 17: ICA will have a leadership structure to support effective execution & accountability



Source: Revised from Blueprint to Market 2015

ICA will recruit people with clear values-alignment with its mission, excellent track record, skills, experience and reputation to satisfy expectations of government, regulators, and other investors and to build confidence with the social and impact investment sectors. Across the team, there will need to be capacity to deliver against all dimensions of the mission and mandate.

For the purposes of establishing ICA, leadership from the Australian Advisory Board on Impact Investing will work with key stakeholders including government and other founding capital providers to establish an appropriately credentialed Board to make initial appointments.

Once operations are established, an Appointments Committee of the Board will be responsible for nomination of future Board members and key executive positions including Chief Executive Officer, Chief Investment Officer and Chief Impact Strategist. Board Committees will comprise members of the Board and appropriately qualified external parties that bring particular expertise.

Implementation and accountability

ICA can be delivered in line with all requirements of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) and the *Commonwealth Grants Rules and Guidelines* (CGRGs). The design for ICA and the proposed founding partnership for Government specifically meets all of the seven key principles under the CGRG, including integrated governance arrangements to mitigate risk. Performance monitoring is built into the design and will be reflected in contracting arrangements, including for impact reporting to be made publicly available.

The implementation plan is already in advanced stages of development. Work to refine this is on-going through process of securing founding partnerships with Government and financial institutions to enable ICA to be operational as quickly as possible once the initial capital is secured. The plan recognises that an establishment phase during which key personnel are engaged and proper accountabilities and governance are established will be essential before funding can be deployed in the market. An outline of the proposed approach to implementation is set out in **Figure 18** and the implementation tasks are further detailed in **Table 6**.

Ensuring that the robust policy logic and design and the governance and accountability mechanisms are mapped and reflected in contract arrangements with Government will be an essential step. Initial delivery of value for money will include securing partnerships with financial institutions and other private and community sector partners.

An independent Board of highly qualified and experienced leaders will be appointed as a first step as stewards for the implementation. Appointment of a CEO and other key executive roles including the Chief Investment Officer and the Chief Impact Strategist is a priority.

Operationalising the Governance architecture (as outlined) will also be a priority. This includes finalising a Board charter, establishing investment and operating policies and putting in place a framework for measuring and reporting on ICA's operating and financial performance, including impact. In addition, a risk and compliance framework together with related policies will be adopted. Effective risk management will be critical in ensuring the ultimate integrity and sustainability of ICA as an organisation and no investment will be made before this is in place.

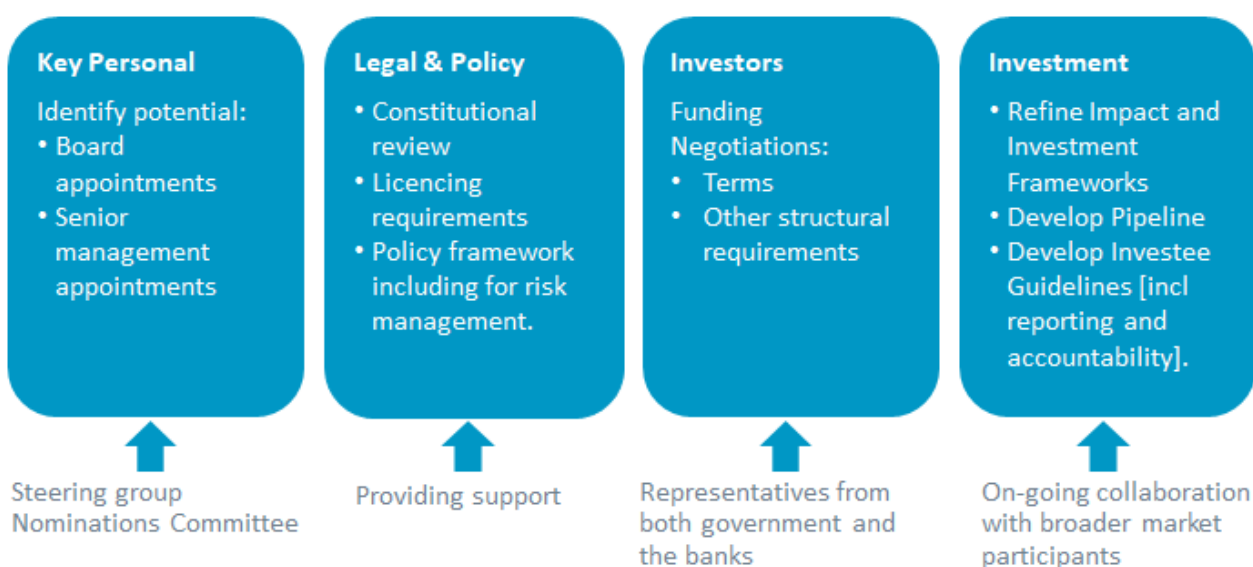
Figure 18: Key implementation milestones will ensure a strong basis for ongoing governance



Steering Group

Governance and oversight will be provided by a highly experienced steering group with a strong track record and skills set across finance, business, government and the NFP sector. The steering group will be accountable to capital providers and work with major stakeholders.

Clear workstreams, milestones and timeline



Source: Impact Investing Australia, 2016

This implementation stage for ICA will be relatively fast and its organisational structure will evolve from the core as it builds capacity. It may be necessary to retain specialist advisors to provide advice to the Board during this initial phase to ensure that all of the compliance obligations are met and processes established in a manner that meets the intention of best practice governance, risk management and delivery.

Table 6: Key implementation tasks will involve rigorous framework, policy and systems development

	Stage 3 (~6 months)	Stage 4 (~6 months)
Legal and Governance	<ul style="list-style-type: none"> Finalise ICA Board Obtain required licences e.g. Australian Financial Services Licence Put in place financial delegations from Board to Executive Define Board Charter clarifying role and risk/control Framework Formalise Board operating structure including role of sub-committees Finalise Risk Management and Compliance Framework Formalise organisational structure & employment plan Develop impact and investment performance frameworks Develop corporate plan and reporting frameworks 	<ul style="list-style-type: none"> Adopt and publish Board charter and operating, investment and performance policies Establish Board sub-committees Implement performance and reporting systems Publish corporate plan Embed risk management & compliance systems Adoption of investment and valuation policy and investee reporting guidelines.
Personnel	Finalise key executive appointments	Recruit other key personnel
Finance and Operations	<ul style="list-style-type: none"> Establishment tasks including: office accommodation & set up, insurance, auditors, tax registration, software and systems, communication and IT contracts, service contracts etc. Develop a more detailed forward budget Refine initially identified areas of potential investment 	<ul style="list-style-type: none"> Document and adopt policies and procedures relating to: financial operations, HR and Finance delegations, procurement, accounts management, stakeholder and media communications Engage market, in particular financial intermediaries Formal launch
Communications	Initial development of stakeholder and media communications strategy	<ul style="list-style-type: none"> Design and establish ICA website Ongoing communication materials

Source: Updated from Impact Investing Australia, 2017

Risk management

International experience and an understanding of the Australian market for impact investment has informed a preliminary assessment of the potential risks and associated mitigation strategies for ICA. Some of these are outlined in **Table 7**.

Table 7: Early Identification of some potential risks and associated mitigation strategies.

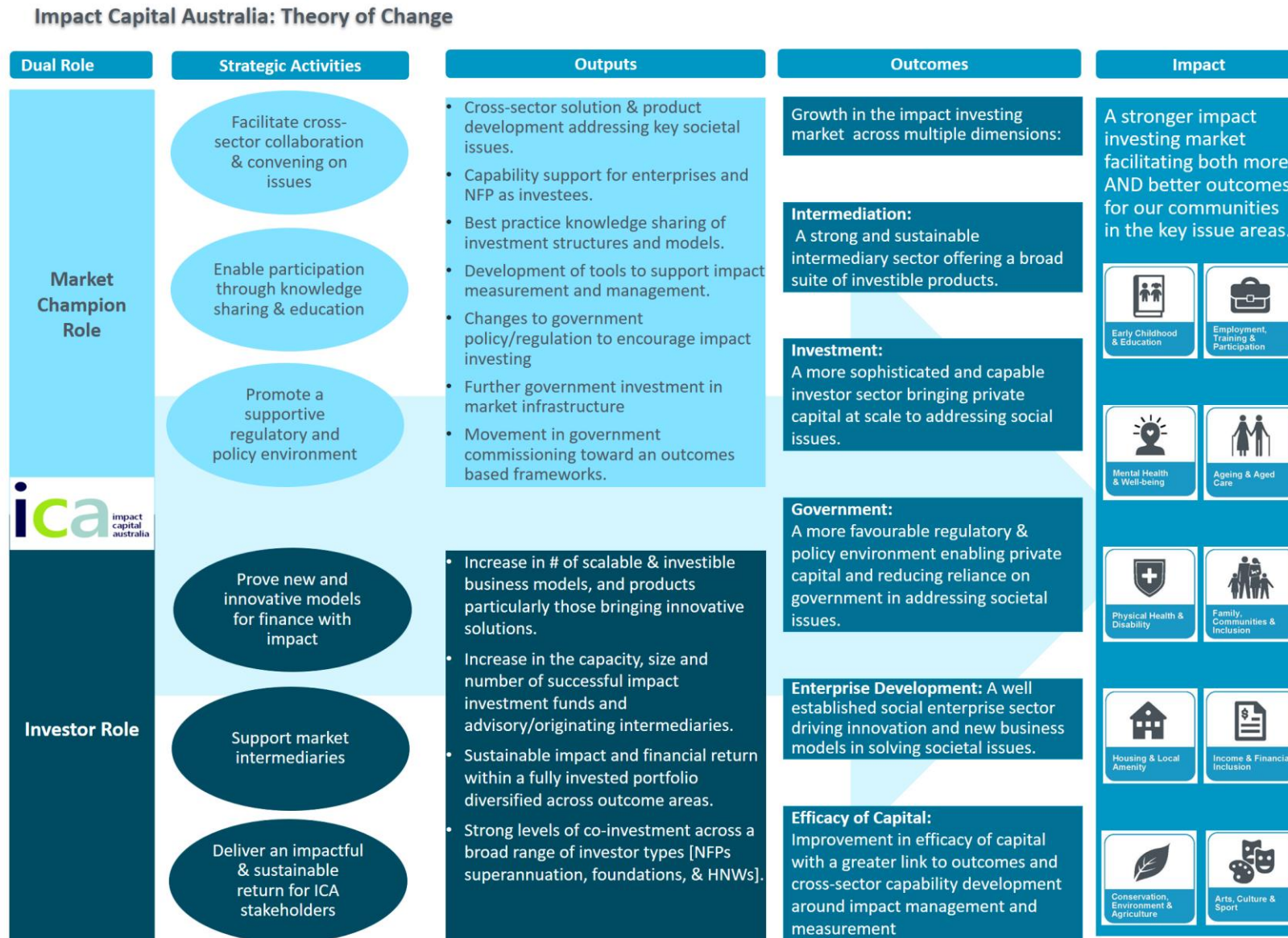
Risk	Mitigation strategy
Capital deployment slower than forecast	Provision for ICA to undertake origination and design and co-create strategies with the market; capacity development for intermediaries
Failure to capture impact	Development of practical, useful impact framework including employing best practice impact management in design, strategy, management and measurement
Lack of Innovation	Foster partnerships and collaboration; convene stakeholders to co-design in areas of priority for need and demand
Lack of scale	Understand mainstream investor needs and combine focus on services with asset backed transactions while scalable enterprise models build
Underperformance of financial return	Balance portfolio across finance, impact and market development dimensions and design for financial sustainability over medium term (7-10 years); manage investor expectations on term requirements to achieve impact and financial outcomes.

Source: ICA Working Group discussion and analysis

ICA Theory of change

Figure 19 sets out ICA's Theory of Change for a stronger impact investing market facilitating more and better outcomes for our Australian communities.

Figure 19: ICA’s Theory of change



Source: Impact Investing Australia, 2017

Appendix 3: Alignment with Social impact investment principles

Principle	Relevant features of Impact Capital Australia
<p>Government as market enabler and developer</p>	<p>ICA is specifically designed to execute on the Government's role as a market enabler and developer.</p> <p>Impact driven organisations and initiatives need access to appropriate capital as well as increasing the pool of capital. This comes through clearly in feedback from the Australian market and evidence from other fields of market activity and development of impact investment elsewhere.</p> <p>It is central to ICA's mission to encourage diversity, innovation and growth of the market as fit for purpose. ICA will 'grow the pie' as its purpose is to drive toward a dynamic market operating at scale and demonstrating and promoting innovation and diversity in participants and products.</p> <p>Experience from other markets shows that this kind of central market champion with catalytic funding is needed to drive market transition and can drive growth.</p> <p>The G8 Social Impact Investment Taskforce, which included government representatives from each of the G7 countries and the EU, identified a wholesale institution to support and grow intermediaries and act as market champion as a key piece of market infrastructure to ground and accelerate development of impact investment required in all local markets. Other jurisdictions already have institutions in place or work underway.</p> <p>Without this type of capital, initiatives in the market are likely to remain sub-critical mass for some time, limiting self-sufficiency and inhibiting capacity for innovative models to scale.</p> <p>Providing catalytic capital and facilitating development of key market infrastructure is central to governments' established market building role.</p>
<p>▪ Address (regulatory) barriers that impede development or sustainability of the market</p>	<p>ICA addresses barriers to market development and market failures. These include availability of cornerstone capital, length of loan tenure, lack of origination capacity, shortfalls in funding availability for intermediaries and aggregators, misalignment of funding terms and incentives, mispriced risk and information asymmetries.</p> <p>While not regulatory, there are real barriers to entry and a recent field scan confirms they are inhibiting and slowing development.</p>

Principle	Relevant features of Impact Capital Australia
<ul style="list-style-type: none"> ▪ <i>Ready to leverage additional private capital or other investment opportunities, as appropriate, and help to grow the social investment market in Australia</i> 	<p>ICA will provide immediate and ongoing leverage for the Government commitment.</p> <p>ICA will trigger a multiplier effect. That starts with 1:1 investment of Government contribution in ICA itself. Each investment ICA makes into an intermediary will unlock additional private capital in co-investment. Each investment each intermediary makes will leverage still more private capital in co-investment.</p> <p>Modelling can be provided that illustrates and quantifies the expected leverage of capital.</p> <p>The multiplier effect will also apply to activity, talent attraction and impact.</p> <p>ICA will create additional investment opportunities through new investment vehicles and models and will have capacity to design new models in areas of need if they are not forthcoming from the market.</p>
<p>Value for Money</p>	<p>A Government commitment will incentivise and accelerate commitments from others.</p> <p>Without an institution like ICA in the Australian market, it is unlikely that transaction based activity will reach critical mass or that impactful models will scale in the short to medium term.</p>
<ul style="list-style-type: none"> ▪ <i>Reasonably expected to offer a net benefit, and represent a cost-effective delivery mechanism</i> 	<p>The Government commitment to ICA will be a one-off contribution of \$150m. That includes all operating costs.</p> <p>There are options for how the Government contribution comes into ICA, including investment options where the funds could be repayable within a defined period. However, more flexible funding will enable more innovative models to be developed and trialled in the short term.</p> <p>The multiplier effect is outlined above.</p> <p>ICA is designed to become self -sustaining within 7-10 years. It is scalable from this base, but requires critical mass to fulfil its mandate and become independent.</p>
<p>Robust outcomes based measurement and evaluation</p>	<p>Transparency and accountability for results are critical and designed into every level of ICA. It will be measured and evaluated with the lessons identified and communicated against identified market outcomes and the impact generated as a result of its activities.</p> <p>Building the evidence base and improving outcomes is central to ICA's focus on delivering innovative and collaborative approaches that increase effectiveness of services and reduce demand and costs over time.</p> <p>Together with the focus on innovative investment, this will direct capital and innovation toward tackling issues where better outcomes are needed.</p> <p>The scope outcome areas recognises that the needs of impact driven organisations for finance are various and that the ideas and structures capable of delivering better outcomes will come from different parts of the market.</p>

Principle	Relevant features of Impact Capital Australia
<ul style="list-style-type: none"> ▪ <i>Agreement between co-investors and their service delivery partners on the social or environmental outcomes to be achieved</i> 	<p>Ten clear outcome areas have been identified as the foundation of the mandate for ICA. These were arrived at through collaboration with practitioners and experts from across community sector, service delivery, banking and impact investment.</p> <p>ICA's role includes being proactive to develop and encourage impactful, innovative and scalable solutions that can attract finance. In executing this role, ICA will convene and promote multi-disciplinary collaboration.</p> <p>Each investment proposal will need to embed such agreement and accountability in their proposals and operations in order to be approved for investment by ICA.</p>
<ul style="list-style-type: none"> ▪ <i>Ongoing outcomes-based measurement will be used to monitor the progress, risk and returns of the investment, allowing for the investment to be refined as appropriate</i> 	<p>ICA will practice leading impact measurement and embed in a world class impact management framework that runs through planning, policies, investment selection, management and measurement.</p> <p>Part of ICA's mission will be to promote effectiveness, efficiency and learning through targeted measurement.</p> <p>ICA will have the opportunity to work with the architects of the leading global conventions on impact management to customise and embed this framework and related systems.</p> <p>At a market level ICA will track indicators such as growth and leverage achieved by existing intermediaries, the number and diversity of new intermediaries, and the variety of investment vehicles and products and sources of capital.</p> <p>Measures will include the impact achieved, number and range of beneficiaries and outcome areas to which investment is directed.</p> <p>Investee fund managers will be required to employ accountable impact management and measurement strategies, systems and reporting as part of conditions of finance from ICA.</p>
<ul style="list-style-type: none"> ▪ <i>Ongoing outcomes-based measurement will be used to inform a robust and transparent evaluation to determine the investment's impact and efficacy in delivering on outcomes</i> 	<p>ICA will have a measurement, learning and evaluation framework. The measurement, learning and evaluation will be against the market outcomes ICA is designed to achieve and the impact generated as a result.</p> <p>Overall evaluations will be undertaken at the end of 5 years and 10 years. This will include evaluation of ICA's performance as an organisation; as an investor; and by the market development it creates.</p> <p>Success factors will include the multiplier effect achieved, impact delivered, resources unlocked and the demonstration effect of new types of transactions and capacity for impactful transactions at scale. Also, whether benchmarks for informed and appropriate risk adjusted return for particular types of impact investment are adopted more broadly by the market to reduce the need for credit enhancement over time.</p> <p>For particular outcome areas, new models and their impacts will be included in the evaluation. Appropriate distinctions will be required between areas where ICA makes a contribution and where results can be directly attributed.</p>

Principle	Relevant features of Impact Capital Australia
Fair sharing of risk and return	A core part of ICA's mission is to send clear market signals about fair risk adjusted return and impact for investments with social, environmental and/or cultural benefit.
<ul style="list-style-type: none"> <i>Opportunities to invest in social impact investments, and the risks and returns of those investments, should be fairly shared between parties to the investment (including, the Australian Government, investors and service providers).</i> 	<p>ICA's intended portfolio design encompasses impact, financial sustainability and market development benefits.</p> <p>The co-mingling of funds from the Australian Government and other investors in ICA facilitates this. Investors will receive a return on their investment but will not have any upside participation in financial value accrued through ICA. The terms being negotiated with investors are concessional to risk adjusted market return.</p> <p>The public benefits include market development, unlocking private capital and impacts across the outcome areas will accrue social, environmental, cultural and economic public benefit and value.</p> <p>A risk identification and management framework has been developed and mitigation strategies will be embedded in the operations of ICA.</p> <p>Capital providers will have representation on equivalent terms in the governance structure for ICA to enable their interests to be represented without compromising ICA's independence.</p>
Outcomes that align with Australian Government Policy Priorities	ICA aligns with a number of areas of government policy priority, including policies to enable and develop the impact investment market and Australia's innovation systems.
<ul style="list-style-type: none"> <i>Well-developed case for being able to successfully address social and/or environmental issues which are priorities for the Government</i> 	<p>Fairness, Security and Opportunity. The development of a robust for purpose and social enterprise sector enabled by greater access to capital will support inclusive economic and jobs growth. This will be further enhanced by increased investment availability in social services infrastructure.</p> <p>Delivery of essential services in healthcare, housing, disability support and employment. Enablement of:</p> <ul style="list-style-type: none"> greater efficacy of government capital in service delivery by targeting outcomes with each dollar invested; private co-investment delivering both more \$ and better results through measurement; Innovation in service delivery through collaboration of cross-sector actors. <p>Measures to encourage market-based approaches can also encourage competition and facilitate access to quality services for all parts of the community.</p> <p>Tackling cost of living pressures - housing affordability, childcare and power prices. Focus on scaling innovation around new structures and models including private co-investment and cross-subsidisation to deliver more affordable options at scale. ICA will provide significant stimulus to unlock private capital for housing and social infrastructure. This will encourage a range of intermediaries and approaches to meet growing demand for affordable stock and in key areas of reform where demand is growing such as aged care and disability support.</p>

Principle	Relevant features of Impact Capital Australia
	<p>Government lives within its means. Growing budgetary pressure around social issues which the government and philanthropy alone cannot continue to meet. Through unlocking private capital, ICA is intended to create a multiplier effect for government capital estimated at over 16x on fully invested capital.</p> <p>While ICA will operate domestically, it will send a strong market signals supportive of foreign policy priorities to encourage private sector partnerships, innovation and enterprise development in the Indo-Pacific and improve outcomes for women and girls. It is complementary to the recently announced Emerging Markets Impact Investment Fund and the Investing in Women and Pacific Rise initiatives.</p>
Co-design	<p>ICA has been developed through a process of consultation and collaboration over more than three years.</p>
<ul style="list-style-type: none"> ▪ <i>To encourage better outcomes in social service delivery and provide for innovation, social impact investments made by the Australian Government should be designed in collaboration with a broad range of stakeholders, including subject matter experts, and the communities and stakeholders who will implement them</i> 	<p>There has been extensive co-design in the development of ICA, including:</p> <ul style="list-style-type: none"> ▪ Market consultations led by the AAB in Australia in 2014 and 2017; ▪ A global process of consultation and collaboration through the G8 Taskforce; ▪ A multi-sector working group 2014-15 that designed the blueprint for ICA; ▪ Formal collaborations with Big Society Capital, Ashurst, AT Kearney; ▪ Involvement of Australia’s leading experts and practitioners in impact investment and in the role of governments and policy; ▪ Consultation with the OECD; ▪ Ongoing work to share lessons across countries for implementation of impact investment wholesale funds; and ▪ Extensive engagement with the sector, financial institutions and stakeholder groups in and connected to the field in Australia 2015-17. <p>ICA builds in co-design in its strategy and operations, including dedicated capacity for design and origination and to convene and promote multi-disciplinary collaboration.</p>

Appendix 4: Case studies

Examples of impact created by Big Society Capital in key outcome areas.

Case Study 3: Nesta Impact Investments and GetMyFirstJob – Education, training and employment



GetMyFirstJob (GMFJ) launched in 2012 as a one-stop-shop through an innovative web-based platform connecting young people, training providers, colleges and employers. This platform provides more effective and efficient connections across what had become a fragmented and difficult to navigate market.

In 2015, Nesta Impact Investments (NII) invested £500,000 into sales, marketing and other resources to enable GetMyFirstJob (GMFJ) to scale-up their reach and impact. At the time of launching in 2015, when unemployment amongst 16 to 24 years old's had risen by 30,000 to 764,000, over 160,000 young people were registered with GMFJ who hoped to place 10,000 young people into apprenticeships in that year.

Increasing the number of young people entering suitable apprenticeships creates measurable social impacts by improving their skills, employment readiness and rates of employment.

Impact:

The platform grew to 250,000+ candidates in 2016, processing 30,000+ applicants monthly and working with 150+ colleges, employers and providers across the UK. In December 2017, nearly 12,000 vacancies were listed, 28,000 candidates shortlisted and 500 recruiters were working on filling apprenticeship opportunities.

Improving the rate and quality of apprenticeship placements aims to encourage more apprenticeship opportunities for young people.

Catalytic Capital:

NII's lead investment saw a rapid growth of 500% of GMFJ's business. Following on from this success Nesta jointly invested £1m with City & Guilds Group in 2016. In 2017, NII provided an additional £320,000.

Source: Impact Investing Australia, 2017, adapted from information on Nesta Impact Investments and City and Guild websites.

Case Study 4: Bridges Funds Management and Babington Group – Education and training



A skills shortage continues to hamper the UK's economic recovery, with one in five job vacancies remaining unfilled; while employment among 16-24 year-olds continues to lag behind pre-crisis levels, with almost a million classified as NEET (not in education, employment or training). Bridges believed that Babington's high-quality apprenticeships and trainee programs in areas like accounting and insurance could help to address this skills gap, by allowing businesses to harness fresh talent and enabling staff to develop specialist skills through on-the-job training.

Bridges, a specialist sustainable and impact investor, invested in Babington in line with its focus on backing companies that have a clear growth opportunity by tackling major societal challenges or responding to long-term macro trends. Babington has continued to diversify its product offering, by expanding its Traineeship provision and increasing the breadth and depth of courses available

Impact:

Babington has supported over 32,000 learners, and helped over 3700 formerly unemployed people to find jobs. In 2015, it trained 1600 16-17 year-olds at risk of becoming NEET with about two-thirds of its students coming from underserved areas of the UK. It now works with over 2,100 employers to source and support talent.

Catalytic Capital:

A capital injection from Bridges Fund Management, a specialist sustainable and impact investor, catalysed Babington's growth. This investment from Bridges Sustainable Growth Fund II in 2009 helped scale Babington Group. Revenues increased from under £2m to more than £15m over the 7 year period. Exiting in April 2016, Bridges achieved an IRR of 33%.

Source: Impact Investing Australia, 2017 adapted from information on Babington Group and Bridges Funds Management websites.

Case Study 5: Golden Lane Housing and Retail Charity Bonds – Disability accommodation



Golden Lane Housing (GLH) was established in 1998 by Mencap, advocacy and service providers for people with learning disabilities. GLH is a charitable company providing quality homes to more than 2000 people with learning disabilities in the UK. One of the biggest challenges facing people with a learning disability is lack of access to suitable supported accommodation. Only 16% of people with learning disabilities in the UK live in supported housing in their community. Most live far away from their friends and family.

GLH works with more than 80 different support providers to ensure all tenants can access the personal support they need to maintain their tenancy.

In 2014, GLH raised the first listed retail charity bond to finance this work. Retail Charity Bonds are a new way to borrow for established charitable organisations that develop assets, generate revenue and create impact. The bond was raised through Retail Charity Bonds, an initiative of Alia Impact Finance.

Impact:

This Retail Charity Bond capital was used to buy and adapt 30 homes for 120 people supported by Mencap, service providers and advocates for people with learning disabilities.

Support includes providing people with learning disabilities with the opportunity to live in the right house, in the right place, with the right support, so that they can prosper, develop their independence and skills and contribute to their communities.

Catalytic Capital:

GLH raised £11 million from investors through the first charity bond listed on the London Stock Exchange's Order Book for Retail Bonds in 2014. The Bond offered 4.375% per annum due 2021.

GLH's 2nd Retail Charity Bond (£18 million) offering 3.9% due 2027 was fully subscribed, closing earlier than expected in November 2017.

Source: Impact Investing Australia, 2017, adapted from information on Golden Lane Housing and Retail Charity Bonds Website

Case Study 6: London Early Years – Early childhood learning



Research shows that nursery education best supports children's early development. Many parents, especially women, are locked out of the workplace because of the cost of childcare. As a result children, especially those from disadvantaged backgrounds, miss out on the high quality early education they need to set them up for life.

The London Early Years Foundation (LEYF), an award-winning group of 37 nurseries across London provides children from all backgrounds with an affordable nursery place. LEYF nurseries are located in some of London's most disadvantaged areas. Social investment has enabled LEYF to develop a cross-subsidy business model whereby profitable nurseries in affluent areas subsidise community nurseries in deprived parts of London.

Impact:

LEYF builds social cohesion by bringing children from all backgrounds together. It supports family wellbeing through education that increases the child's readiness for school while enabling parents to return to work.

In 2016, 43% of the children attending LEYF nurseries were provided free of charge places across 38 nurseries. LEYF grew 60% between 2013-2016, taking on 14 new nurseries and providing an additional 1500 nursery places for children.

Catalytic Capital:

In 2014, two leading social impact investors, Bridges Funds Management and Big Issue Invest invested £1.25m to support LEYF's growth strategy to reach 5,000 children and their families by 2017. National Westminster Bank, provided an overdraft facility to go alongside Bridges' and Big Issue's investments.

In 2015, LEYF successfully raised a second stage of investment worth £1.5 million, with the support of ClearlySo, an impact investing intermediary.

Source: Impact Investing Australia, 2017, adapted from information on London Early Years Foundation Website

Case Study 7: The potential interaction of Government policy in the investment life-cycle of a 'for purpose' enterprise

Hireup:

Hireup is an online platform for Australians with disability to find, hire and manage support workers who fit their needs and share their interests. Users are able to search, message and book through the platform. Hireup allows people to manage their own relationships with support workers, with Hireup taking care of the necessary tax and super payments, insurance, payroll and workplace health and safety requirements.

Hireup ran a minimum viable product in late 2014 and early 2015. After proving the need and applicability of the model, Hireup then raised \$2.5m via an impact investment in late 2015. As a two-sided marketplace, the funds raised are helping Hireup to scale quickly and in lockstep with the national rollout of the National Disability Insurance Scheme (NDIS).

An ICA seeded specialist disability fund could co-invest the capital to bring an investment such as Hireup to scale.



The Government initiative (Budget 2017/18) on Social Impact Investment Readiness could provide similar future support to 'for purpose' enterprises at this stage.

A Government partnership and commitment of \$150m into ICA.



Source: Impact Investing Australia, 2017

Appendix 5: Additional budget measures to build the ecosystem

Additional measures outlined below complement ICA. These are designed to build government capacity and leadership, remove regulatory barriers, grow enterprising activity to tackle social issues and develop capacity for commissioning of services that improves outcomes and reduces costs over time.

The Budget measures proposed draws upon extensive work already done to develop useful and actionable policy frameworks for impact investment. Together, these measures are intended to stimulate different parts of the market and set the conditions for unlocking private capital and incentivising solutions that deliver better outcomes. They include recognition that government has important contributions to make to leadership and data that are often overlooked.

Identified as actions that can have the greatest impact, these measures complement the Australian Advisory Board strategy for the local Australian market, which reflects key recommendations of the global G8 Social Impact Investment Taskforce.

Summary of proposed additional budget measures:

Additional Budget Measure	Description	Costs
<p>Remove regulatory barriers to facilitate growth</p>	<p>Low cost measures to remove regulatory barriers to market growth:</p> <ul style="list-style-type: none"> ▪ Clarification of the fiduciary duties of philanthropic and superannuation trustees to put beyond doubt that impact can be considered in addition to risk and return by fiduciary decision makers; ▪ Ensure program and mission related investment is enabled to provide greater flexibility for philanthropic trusts and foundations to direct capital toward achieving their social mission through mission related investment; ▪ Assess the extent to which regulatory issues, accounting and balance sheet treatment of social infrastructure assets, including housing, is limiting capacity to attract private capital to these assets. This could be linked with policy work underway through the Council on Federal Financial relations to explore innovative mechanisms to boost affordable housing; ▪ Extend provision for unsolicited proposals to be brought forward from current parameters to include a transparent framework for unique proposals to develop the impact investment market or leverage private capital for priority policy priorities at scale; ▪ Amend the Corporations law to enable a clear legal framework for Benefit Corporations in Australia and investigate the application and impact of other innovations for purpose organisational forms; and 	<p>No administrative funding</p>

	<ul style="list-style-type: none"> ▪ Leveraging procurement to shift the way in which services are purchased by requiring that a broader approach to value creation be taken into account. 	
Promoting outcomes focus, efficacy and innovation	<p>Promoting better outcomes, efficacy and innovation starting with design and feasibility for 2 initiatives with a view to moving quickly to a decision on implementation in the out years of the Budget. The focus is building capacity to use market based mechanisms to attract capital to achieve strong social and economic outcomes, including through collaboration between the Federal and State Governments.</p> <p>The development work relates to the following.</p> <ul style="list-style-type: none"> ▪ A dedicated Outcomes & Innovation Fund to support proof of concept and scaling what works through outcomes based commissioning, including social impact bonds; and ▪ Protocols for data sharing to inform efficacy and innovation and facilitate more efficient and effective allocation of existing resources to achieve social impact. 	
Government leadership and engagement	<p>A suite of opportunities to build Government capacity and leadership and connect the Australian Government at the forefront of developments.</p> <ul style="list-style-type: none"> ▪ Nominating senior observers to the Global Steering Group for Impact Investing and the Australian Advisory Board on Impact Investment. ▪ appointing a clear Ministerial lead on impact investment. ▪ Developing the whole of government advisory remit of Innovation and Science Australia by including social innovation expertise on the Board. 	No administered funding required in the short term pending feasibility

Appendix 6: About us

The Australian Advisory Board on Impact Investing

The Australian Advisory Board on Impact Investing (AAB) provides leadership and strategy for accelerating the growth of the impact investment market in Australia. It is Australia's national advisory board to the Global Steering Group for Impact Investment (successor to the G8 Social Impact Investment Taskforce)

The GSG has 16 member jurisdictions with plans to build to 30+ member countries by 2020. At the annual meeting in Chicago (July 2017) strategies were agreed to drive global market to a tipping point by 2020.

The AAB led strategy to catalyse the market in and from Australia, Delivering on Impact, has seen a program of leadership, action and policy delivered. Experienced leaders spanning the finance, business, not for profit, philanthropic and community sectors committed to growing the opportunities for impact investment contribute to the AAB and its work.

AUSTRALIAN ADVISORY BOARD ON IMPACT INVESTING

Members:

Rosemary Addis (Chair)	Impact Strategist; Global Steering Group for Impact Investment
Adrian Appo OAM	First Australians Capital
Christopher Thorn	Ernst & Young
David Crosbie	Community Council of Australia
David Bennet	SEFA and Macquarie Foundation
Fabienne Michaux	NED, previously CEO Standard & Poor's ANZ
Louise Sylvan (Vice-Chair)	University of Sydney
Peter Munro	A.T. Kearney
Richard Brandweiner (Vice-Chair)	Leapfrog Investments
Rob DiMonte	NED; The Australian Centre for Social Innovation
Sally McCutchan (ex-officio)	Impact Investing Australia
Sandy Blackburn-Wright	Social Outcomes
Sarah Davies	Philanthropy Australia
Steve Lambert	National Australia Bank

Ambassadors:

Carol Schwartz AM	Trawalla Foundation
Carolyn Hewson AO	Non-Executive Director
Peter Shergold AC	Western Sydney University

Additional ICA Ambassadors:

Greg Hutchinson AM	Paul Ramsay Foundation; Bain & Co
Jillian Segal AM	Non-executive Director
The Hon. John Brumby AO	Non-executive Director; Professorial Fellow
Peter Hunt AM	Greenhill Investments
Rob McLean AM	Philanthropy Australia; McKinsey & Co
Simon Longstaff AO	The Ethics Centre
Simon McKeon AO	Monash University; Macquarie

Impact Investing Australia

Impact Investing Australia was established in 2014 in response to an industry-identified need for dedicated leadership, facilitation and capacity building. Its primary role has been to provide strategy development and execution support for the Australian Advisory Board on Impact Investing.

Responsible for driving the implementation of the Australian Advisory Board on Impact Investing’s strategy to catalyse the market for impact investing, Impact Investing Australia provides a focal point for market development in Australia, as well as participating in international efforts to grow the market globally.

Partners and supporters

Impact Investing Australia’s work is made possible through generous support from our partners and supporters and contributions of time and experience of a dynamic group of skilled volunteers.



Market Building and impact is made possible with collective action and resources. We thank our partners and supporters and welcome others who would like to contribute to realising the potential of impact investing in and from Australia.



Impact Investing Australia and the Australian Advisory Board on Impact Investing are pleased to partner with the RIAA Impact Investment Forum