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PUBLIC POLICY

Social Lending:
A Tool for Grantmakers,
an Opportunity for Communities

Prepared by
Laura Benedict

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Ian Axford (New Zealand) Fellowships in Public Policy

Established by the New Zealand Government in 1995 to reinforce links between New Zealand and the US, Ian Axford (New Zealand) Fellowships in Public Policy provide the opportunity for outstanding mid-career professionals from the United States of America to gain firsthand knowledge of public policy in New Zealand, including economic, social and political reforms and management of the government sector.

The Ian Axford (New Zealand) Fellowships in Public Policy were named in honour of Sir Ian Axford, an eminent New Zealand astrophysicist and space scientist who was patron of the fellowship programme until his death in March 2010.

Educated in New Zealand and England, Sir Ian held Professorships at Cornell University and the University of California, and was Vice-Chancellor of Victoria University of Wellington for three years. For many years, Sir Ian was director of the Max Planck Institute for Aeronomy in Germany, where he was involved in the planning of several space missions, including those of the Voyager planetary explorers, the Giotto space probe and the Ulysses galaxy explorer.

Sir Ian was recognised as one of the great thinkers and communicators in the world of space science, and was a highly respected and influential administrator. A recipient of numerous science awards, he was knighted and named New Zealander of the Year in 1995.

Ian Axford (New Zealand) Fellowships in Public Policy have three goals:

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Fellows are based at a host institution and carefully partnered with a leading specialist who will act as a mentor. In addition, fellows spend a substantial part of their time in contact with relevant organisations outside their host institutions, to gain practical experience in their fields.

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We acknowledge and thank the following government and corporate sponsors that support the Ian Axford (New Zealand) Fellowships in Public Policy programme:

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- New Zealand Customs Service
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- State Services Commission
- Te Puni Kōkiri (Ministry of Māori Development)
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Many roads lead to Jennifer Gill, whose wisdom, guidance and support have played a critical role in the design and implementation this project. The foundation she leads, ASB Community Trust, along with the Tindall Foundation commissioned Glen Saunders' report, *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand,* which has been my bible.

Coincidentally – or in the wonderful Kiwi way, maybe not – Jenny had helped establish the Ian Axford Fellowship when she was CEO of Fulbright New Zealand. In her current role as ASB Community Trust's CEO, she is a member of the board of Philanthropy New Zealand and suggested that I seek a second host outside the government. She was right. I found having one foot in the government sector and one foot in the private sector significantly expedited my gaining an understanding of the Kiwi environment and opened many doors.

Without Jenny, I would not have met Glen Saunders whose work in New Zealand and around the world has been seminal in developing the field of social lending. From when we first met electronically, when I was scoping out project ideas back in the States, and throughout the entire fellowship, Glen has been my guide, mentor, and sounding board. Thank you, Glen, for your support and candour. I have learned tremendously from your vision, intelligence, and experience.

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In closing, I encourage interested readers to contact me if you have questions or comments about this paper. I will be in Aotearoa New Zealand until December and then will be only a few keystrokes away. My ongoing email address is benedictlaura1959@gmail.com.

Laura Benedict
Wellington, August 2010

EXECUTIVE SUMMARY

Social lending is a tool: a tool to empower communities, organisations, families and individuals. It is a way to fund projects, buildings, businesses, ideas and dreams.

While grants and donations are attractive and hold a definitive place in civil society, their supply is limited. Unlike grants and donations, social loans recycle. The funds from repaid loans can be re-lent. Furthermore, social lending allows endowed philanthropic organisations to use their assets for mission purposes, not only the revenue generated by those assets.

Similar to bank loans, social loans need to be paid back and they generally require interest payments, as well as collateral or security. Social loans differ from bank loans in that they promote social goals. The three main borrower categories are:

- social enterprises and non-profits, where the borrowing entity has explicit social goals as its purpose
- small businesses owned by and/or hiring the disadvantaged, where the purpose of the project is income generation and job creation which are the social goals
- low-income families and individuals borrowing to meet their routine expenses and/or to become homeowners and start building their net worth. Breaking the cycle of poverty is the social goal.

Lending is a hand up, not a hand out. The dignity of believing in someone enough to give a loan can be very empowering. The analysis needed to apply for a loan and the discipline needed to repay one can help borrowers hone their business skills.

Social lending can unlock millions of dollars. In the 1980s, the government wanted to remove its guarantee of New Zealand's Trustee Savings Banks. The resulting restructure created 12 community trusts dedicated to grantmaking and supporting their local communities with $2.8 billion in community-controlled assets.[1] These resources are mainly invested commercially. In general, the trusts' emphasis has been on getting the highest, safest return. If, however, 20 per cent of the trusts used just 5 per cent of their assets for social lending, $28 million new dollars could be available to promote social goals.[2] These numbers grow when you add New Zealand's other endowed foundations. Social lending is a tool for accessing these assets.

In summary, social lending is a powerful tool. It recycles. It can help borrowers develop business skills and promotes dignity. When utilised by endowed foundations it can unlock assets.

Social lending exists in New Zealand, but at far lesser levels than in the US, the UK or other parts of Europe.[3] New Zealand's existing organisations do good work, but

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[1] Slack, A., and J. Leung-Wai (2007) *Giving New Zealand: Philanthropic Funding 2006*, March 2007, Sections 6.3

[2] These percentages come from actual experience overseas. In the UK and the US, where the social lending marketplace is more developed, Glen Saunders estimated that about 20 per cent of endowed foundations do some social lending and, of those, they use about five per cent of their endowments for social lending. (Saunders, G., *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand*, (2009), p.16 paragraph 4.2.6).

[3] Saunders (2009), *A new funding paradigm: Prospects for social lending and investment by*

currently they are limited in their scope:

- some serve only one community, which leaves many communities without access
- some limit the size of their loans because their capital base is small
- some serve only non-profits and not small businesses
- some are dependent on annual fundraising because their operating model runs at a loss.

A table of New Zealand's social lenders is in Appendix 1.

A portion of New Zealand's social lending activity has been to promote Māori development. Over the last 30 years, there have been lessons learned and some enduring social lending models developed. Some of these lessons and models are described in chapter two. The lending implications of Māori historical disadvantage (the need for capacity building and flexible underwriting) and the challenges of Māori cultural preferences on accessing credit, especially for larger, collectively owned enterprises, are also discussed in that chapter.

Chapter three introduces the concept of an intermediary. At its simplest, an intermediary acts as a go-between for grantmakers and communities. In the US, I work for Self-Help, which is a large non-profit social-lending intermediary. The intermediary structure could be better utilised in New Zealand. I profile Self-Help and two successful New Zealand social lenders:

- Prometheus Finance is a $16.6 million lender that finances social and environmental projects throughout the country. In the last five years, they have made 500 loans, totalling $8 million with minimal losses.
- Awhi Credit Union is a Māori-led grassroots organisation. It has 1,900 members and puts a premium on developing financial literacy and helping its members better manage their household finances. In recognition of the need to begin savings regimes early, Awhi Credit Union is starting a credit union at Rotorua Girls College.

Chapter four pulls all these strands together into recommendations for a Kiwi social lending system that includes intermediaries to fill gaps in the current environment, a Māori-funded guarantee for loans secured by collectively owned land, and expansion of credit unions, like Awhi, serving low-income communities.

The final chapter describes ways the government might support these developments. Social lending should remain outside the government. Legislation, regulation, and tax policy, however, could be designed to remove barriers and support the growth of social lending.

I hope this paper can serve as a legacy document, recording some history and some of the current thinking in the fields of Māori development, philanthropy, and in the

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foundations in New Zealand, Retrieved 1 February 2010 from: http://www.tindall.org.nz/information-research/#Social, p.17

community and voluntary sector. Finally, I hope that the ideas and recommendations contained herein can aid in the continued development of social lending in Aotearoa New Zealand.

TABLE OF CONTENTS

INTRODUCTION

Social lending's time has come.

If the topic is new to you, social lending has many different names (community development lending, program related investing, impact investing) and purposes (social enterprise development, job creation and breaking the cycle of poverty), but at its simplest, it is a tool to fulfil a social purpose.

Background

Many factors and events have converged to make social lending timely. The following initiatives reflect this momentum:

- In late 2008, New Zealand's National Party came to power. Its platform features social lending: "Investigate whether a venture capital fund for the community and voluntary sector, like those that have been set up in the United Kingdom and Australia, has merit in New Zealand."[4]
- Hon Dr Pita Sharples, Minister of Māori Affairs and co-leader of the Māori Party, formed a Māori Economic Taskforce in 2009, which, among other tasks, is developing a plan to increase Māori access to credit. The taskforce intends to implement resulting recommendations by June 2011.[5]
- In 2009, ASB Community Trust and the Tindall Foundation commissioned Glen Saunders to write *A new funding paradigm: Prospects for social lending and investments by foundations in New Zealand*.[6] This report focuses on how foundations can use their assets or endowments to invest for both social and financial returns. Since the publication of *A new funding paradigm: Prospects for social lending and investments by foundations in New Zealand*, ASB Community Trust and the Tindall Foundation have sponsored two day-long social lending workshops for approximately 50 executives and trustees of private foundations and trusts from throughout New Zealand. I have had the opportunity to participate in these and use Self-Help, where I work in the US, as an example of a social lender.
- At the end of 2009, the Poutama Trust announced a lending partnership with Kiwibank for Māori small businesses needing credit enhancement.
- In February 2010, 300 people attended a Community Economic Development Conference in Waitakere City. The theme of the conference was financing community initiatives in more sustainable ways. There was consensus at the conference that the time is right to develop social enterprises and social lending in New Zealand.
- Also in February 2010, I started this fellowship. The Ministry of Social Development's (MSD) Office for the Community and Voluntary Sector

[4] Bennett, Hon P. (13 April 2008). 'Turbo-charging community groups'. Retrieved 20 July 2010 from : http://www.national.org.nz/Article.aspx?ArticleID=12095
[5] McCabe (1 June 2010) pers. comm.
[6] Saunders (2009), *A new funding paradigm: Prospects for social lending and investments by foundations in New Zealand,* Retrieved 1 February 2010 from: http://www.tindall.org.nz/information-research/#Social

(OCVS) and Philanthropy New Zealand have been my co-hosts.

- For the last few years, Philanthropy New Zealand and OCVS have sponsored a series of seminars around the country, called Funders Forum. One of this year's seminar topics was social lending. About 150 private and government grantmakers attended the seminars.
- Prometheus Finance lends to community projects throughout New Zealand. A social enterprise itself, Prometheus is developing new programmes in response to the increasing interest in social lending.
- In June 2010, Hon Tariana Turia, Minister for the Community and Voluntary Sector and co-leader of the Māori Party, convened a meeting to explore what roles the government might play in the social enterprise and social lending space. Actions from the meeting include: OCVS to advise Minister Turia on ways to keep the work ongoing after my fellowship is over, to reconvene the group in the near future, and to follow-up on several initiatives that the minister learned about at the meeting.[7]

While working on this paper, I have watched the development of a social lending movement in New Zealand. It has been an honour to be at the right place at the right time. I suspect that my 20 years of practical experience as a social lender have helped give me the credibility to capitalise on this timing. I must acknowledge, though, that as a practitioner, this paper is more of an opinion piece based on my practical experience than a well-researched, balanced policy analysis. Drawing on this experience, I have included a number of anecdotes from Self-Help in this paper to illustrate how social lending might work in New Zealand.

Terminology

While the language of this report is English, I will use Māori when it is useful to describe this work in the Māori context. Learning about Māori history, culture, and vision has been one of the richest parts of my fellowship experience. To reflect the history and shared ownership of this nation, I will use Aotearoa[8] New Zealand when referring to my host country.

There are a surprising number of differences between American English and Kiwi English. These differences are particularly apparent when using technical language, especially given the dynamic state of social lending both in Aotearoa New Zealand and abroad.

My primary fellowship advisor is Glen Saunders, an international expert in social finance. He strongly believes in the importance of clarifying social lending terminology. He says, "It's an important aspect of getting people aligned and genuinely talking about the same things rather than using the same words but meaning different things... Getting clarity in the vocabulary in New Zealand will help the development of social lending in my view. *Failing* to get clarity could lead to tears as

[7] The background paper prepared for the meeting and a summary of key points from the meeting are posted on OCVS's website at http://www.goodpracticefunding.govt.nz/funding-options/other-funding-options/index.html

[8] Aotearoa is a Māori name for New Zealand meaning "land of the long white cloud".

people mix and match social lending in an uncritical way. One of the big risks New Zealand faces is people mixing up social finance approaches. This could lead to lenders losing money and concluding that social lending does not work. A string of failures will leave folks shy of social lending for a decade."[9]

For the purposes of this report, I have developed a social finance glossary. I hope that this glossary will also assist in the broader discussion in Aotearoa New Zealand.

- **Credit union**: A credit union is a financial co-operative that encourages savings, thrift and education to enhance the social and economic well-being of its customers. Once overhead and other expenses are paid, any income from loans is returned to customers in the form of dividends on savings, reserves, and improved or additional services. Credit unions are registered under the Friendly Societies and Credit Unions Act of 1982. Credit unions are locally owned by their customers and not-for-profit. Under the Securities Act, credit unions are subject to a regulatory regime, where an independent trustee company acts as prudential supervisor.
- **Grantmakers**: This broad category includes any organisation or individual that makes grants or donations. It includes private foundations, iwi,[10] government agencies and the semi-private statutory trusts.[11]
- **Microloans**: Microloans are under $50,000 and made to support small enterprise activities. In some sectors, it also refers to small loans to help low-income families meet their weekly bills. I refer to these types of loans as consumer or personal loans and not microloans.
- **Risk capital**: Funds available to absorb losses. It can be restricted to special purposes (e.g. childcare loans) or unrestricted, for any type of loss. It generally shows as equity on an intermediary's books.
- **Social enterprises**: Mission driven organisations that apply market-based strategies to achieve a social purpose. Sometimes referred to as triple bottom line organisations, they include both non-profits that use business models to pursue their mission and for-profits whose primary purposes are social.[12] They aim to accomplish targets that are social and/or environmental as well as financial. Many commercial businesses would consider themselves to have social objectives, but social enterprises are distinctive because their social or environmental purpose remains central to their operation. Some non-profit organisations see social enterprise as a way to reduce their dependence on charitable donations and grants while others view the business itself as the vehicle for social change.
- **Social enterprises and non-profits**: One of the three social-lending markets as described in chapter one, it is when the borrower has explicit social goals.

[9] Saunders (30 June 2010) pers. comm.
[10] Iwi is Māori for tribe.
[11] In the late 1980s, Aotearoa New Zealand sold many of its banks and energy companies to the private sector. The proceeds of these sales capitalised grantmaking trusts. In addition, the government runs a lottery and allows controlled, private gambling with the proceeds returned to the community through grants.
[12] Aotearoa New Zealand does not have a special corporate category for social enterprises. The UK has created a new legal form to accommodate their special nature, called Community Interest Companies. See www.cicregulator.gov.uk and chapter five for more information on this.

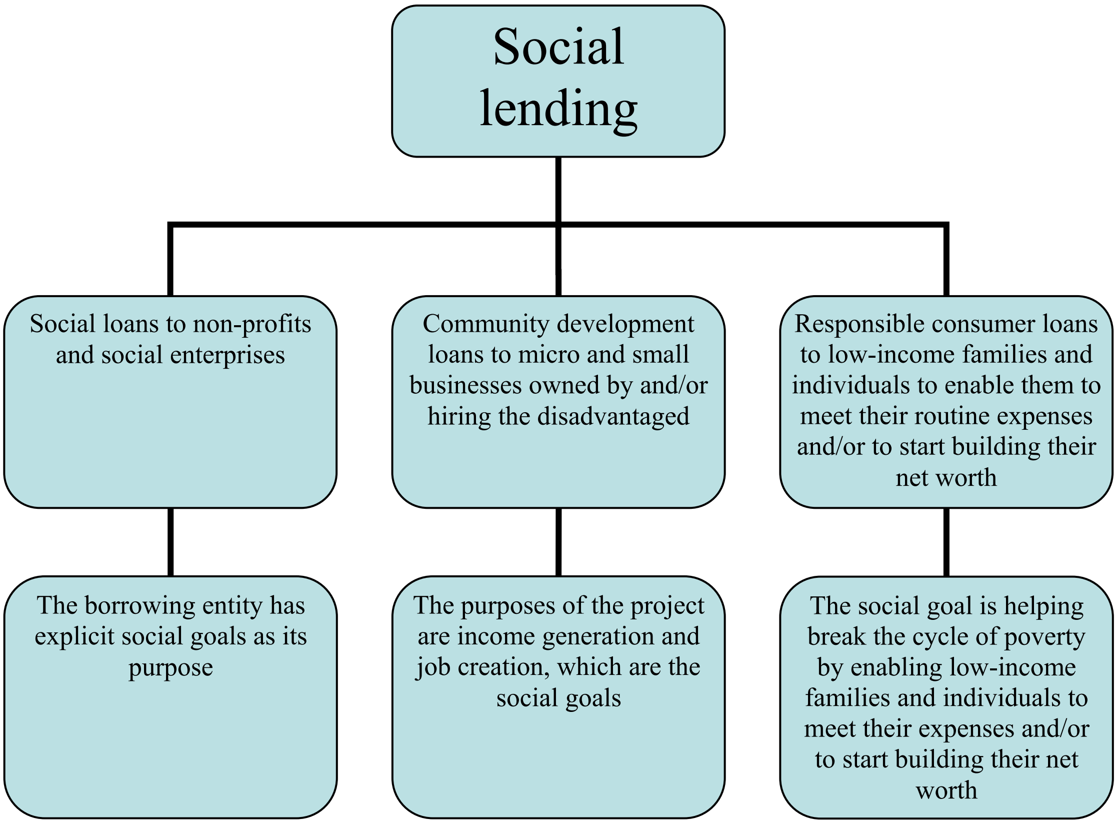
Called the third sector in the United Kingdom, it includes the community and voluntary sector as well as for-profits that are social enterprises.

- **Social finance**: A set of financial instruments that is broader than social lending. It includes, for example, equity investments. Like social lending, all aspects of social finance have social aims.
- **Social lending**: I was unfamiliar with the term before coming to Aotearoa New Zealand. The term with which I am more familiar is "community development lending". My ignorance is likely the result of the different paths that the field has taken in Europe and in the US. I have come to embrace the term "social lending" because it succinctly captures the various components of the field. A field unified by the shared aim to accomplish goals that are good for society, hence social loans. I note that "impact lending" and "impact investing" are gaining favour around the world, but it is unclear if this favour will endure. Since "social lending" is better known here, I will use it in this report. The term is particularly useful when talking about the overall field or about lending to social enterprises and non-profits – a group that immediately gravitates to the term. With other borrowers, especially individuals and small businesses, the term might be offensive or counterproductive. In these cases, the lender will likely refer to their service in generic terms like "business loan" or "consumer loan" or "personal loan".
- **Technical assistance**: A broad category of activity designed to support the learning and skill development of borrowers. Lenders sometimes provide technical assistance. At other times, third parties that specialise in this service may provide the technical assistance. Technical assistance is not to be confused with borrowers using consultants to do work for them. Put simply, technical assistance is teaching people to fish, not fishing for them. Sometimes technical assistance is referred to as capacity building or facilitation services as it facilitates learning and skill development and builds capacity. Good technical assistance providers offer general information, and ask good questions so that the beneficiary does their own thinking and owns the knowledge. For example, helping start-up entrepreneurs, a good technical assistance provider shows the client a business plan format, explains what goes into it, and then sends the entrepreneur away to write their own plan. The technical assistance provider then reviews the plan, points out concerns, and asks questions to help the entrepreneur improve the plan.

  Technical assistance providers that are also lenders need to ensure that they are not too leading with their suggestions or that they lend to borrowers who provide weak business plans. In many countries, including Aotearoa New Zealand, there is a specific legal risk, called lender liability. Entrepreneurs can sue lenders that they believe have made recommendations that have caused the entrepreneur harm. In addition, if lenders lend when they realise an entrepreneur's plan is weak, then the lender can be liable for not alerting the applicant. In all its years of providing technical assistance to borrowers, Self-Help has never been sued for either of these issues. Still, lender liability merits caution and can be a good argument for separating the lending and technical assistance functions.

1 THE SOCIAL LENDING LANDSCAPE

Social loans are like bank loans in that they need to be paid back and they generally require interest payments and collateral or security. They differ from bank loans in that they promote social goals. The three categories of social lending are shown in the following chart.



Unlike grants and donations, social loans recycle. The funds from repaid loans can be re-lent, or recycled to other borrowers. In these leaner economic times, this is an especially attractive feature.

Social lending is a hand up, not a hand out. This aspect of social lending was compelling to one of the participants in the Funders Forum talks I gave. In an evaluation of the session, the participant had this to say about the community development type of social lending:

> I've worked in that sector in major MED [Ministry of Economic Development] environments therefore, for me, it [social lending] is very important as i [sic] know how it changes lives FAR MORE than grants primarily as it looks to the Dignity of the Borrower which in return adds to the dignity of the lender. YES, we will do more social lending.[13]

It can also help borrowers hone their business skills by virtue of the analysis needed to apply for a loan and the discipline needed to repay one.

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[13] Anonymous response to an evaluation survey conducted by Philanthropy New Zealand after the 2010 Funders Forums.

Trevor Gray of the Tindall Foundation suggested at a recent meeting that Aotearoa New Zealand might have more community-owned resources, per capita, than any other nation.[14] This is a result of the 1980s restructure of New Zealand's Trustee Savings Banks and some utilities, as well as the establishment of lotteries and gaming trusts – the various trusts set up by legislative mandates. The founding legislation for the community trusts, for example, states:

> Purposes of community trusts
> (1) Property vested in, or belonging to, a community trust must be—
> > (a) held on trust to be applied for charitable, cultural, philanthropic, recreational, and other purposes; and
> > (b) applied for purposes that are beneficial to the community principally in the area or region of the trust.[15]

Investment of capital outside the region concerned, as is often the case, could be seen as contrary to the above purpose. Social lending can help the trusts invest locally.

The liquid, or investable, assets of the community trusts are roughly $2.8 billion.[16] If 20 per cent of the trusts used just 5 per cent of their assets for social lending, $28 million new dollars could be available to promote social goals. Social lending is a tool for unlocking these community assets and investing them in the local communities.

These percentages are derived from actual experience overseas. In the UK and the US, where the social lending marketplace is more developed, Glen Saunders estimated that about 20 per cent of endowed foundations do some social lending and, of those, they use about five per cent of their endowments for social lending.[17] I believe these numbers are conservative in that they only include assets of the community trusts, not other grantmakers' assets.

Social loans generally come from a philanthropic institution's endowment and, therefore, offer the philanthropic institution a new and significant set of funds with which to fulfil its mission. Recognising that in most cases, the return is lower from social loans as opposed to conventional endowment investments, some institutions use their grantmaking budgets to make up the difference. Some funders also agree to reimburse the investment budget for any losses.

While social loans are generally made from endowments, some foundations and trusts elect to use their grants budgets instead. This can be a course of action when a foundation or trust is just starting a social lending programme and it is administratively easier than amending investment policies. In addition, non-endowed philanthropists can and do use the loan-making tool, but without the added benefit of being able to tap a new source of funds in accessing their endowments.

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[14] Gray (17 June 2010) pers. comm.
[15] Retrieved 21 July 2010 from:
http://www.legislation.govt.nz/act/public/1999/0054/latest/DLM25611.html
[16] Slack, A. and J. Leung-Wai, (2007),*Giving New Zealand: Philanthropic Funding 2006*, March 2007, Sections 6.3
[17] Saunders (2009) *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand*, p.16, paragraph 4.2.6

Social lending sometimes comes with technical assistance or facilitation services on such areas as budget planning, financial management, project feasibility and marketing for enterprise borrowers or, for low-income individuals seeking consumer loans, the loan might come with credit and budget counselling to help the borrower get out of the debt trap. Some lenders provide the technical assistance themselves and others refer prospective borrowers to third parties.

Technical assistance is often hard to take. Social lenders find that when they have the carrot of a loan at the end of the assistance process, the motivation to listen can be much higher. Likewise, when a borrower is in trouble, the "stick" of foreclosure is also motivating. While effective, it is a slippery slope. It is critical that borrowers "own" decisions related to their plans, which if handed to them by a third party, they may not. Another risk is that the borrowers take advice because they see it as a condition of the loan. If the project does not go well, the borrower may sue the lender. These concerns argue for lenders to refer borrowers to third parties. Both approaches are used in social lending and, when needed, the technical assistance with social loans, whether by the lender or by a third party, can significantly enhance the benefit of the loan to the borrower.

In summary, social lending is a tool that recycles. It can help borrowers develop business skills and it promotes dignity. When utilised by endowed foundations it can unlock assets.

Lending to social enterprises and non-profits

As I have spoken with leaders of Kiwi foundations, trusts, and non-profits, I have quickly learned that the best way to explain what social lending is, is to explain first what it is not. This is to dispel people's anxieties: anxieties that social lending will "let government off the hook" as a retired MP and community trust trustee voiced, or that it will undermine philanthropy and core Kiwi values of generosity and compassion for those less fortunate.

Social lending is *not* an answer to most charitable needs and it is *not* generally a replacement for operating grants. Most non-profits need donations, grants and contracts. Food banks, for example, exist because the people that use them do not have enough money to put healthy meals on their families' tables. There is not much opportunity for food bank operators to charge their customers for their services, thus they are dependent on grants and donations. A food bank would likely be unable to afford to repay a loan.

It is possible, however, that a food bank might add a programme to generate revenue. For example, the food bank staff or volunteers might invite the low-income people that eat meals with them to stay and make crafts that could then be sold. Such a social enterprise would generate revenue for the food bank, while helping the craftspeople to develop skills.

The food bank's social enterprise might be an appropriate borrower if it needed money to expand its building for the new service or to buy inventory for making the crafts. The theory being that the revenue from the enterprise would be enough to repay the loan and, ideally, provide additional revenue to the core programme.

Traditional non-profits can also benefit from loans when they have some form of predictable revenue and, depending on the lender, some collateral or security in the event that the revenue predictions fall short. It makes sense for non-profits to borrow when they want to:

- replace an existing expense and obtain an asset, such as buying a facility instead of renting, or buying a vehicle that is leased
- improve an asset to save money, e.g. by better insulating their building or putting on solar panels
- bridge to future income in the following scenarios:
    - building expansion
    - start-up phase of new government contract
    - while waiting for pledges to come in on capital campaign
    - working capital for an income generating social enterprise.

One more *not* about social lending: it must *not* be disguised grants. Social lenders of all sorts, from all over the world, have learned that they must be willing to foreclose if the borrower fails to repay the loan. If not, the stick mentioned before loses its might and the borrowers feel that they can walk away from their loans. When that happens, the investors into the loan fund cannot be repaid and the social lending programme is undermined.

While not for all non-profits and community organisations, and not a replacement for operating grants, social lending *is* another tool in a grantmaker's toolbox. Social lending to social enterprises and non-profits is not new in New Zealand, just underdeveloped, according to *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand,* commissioned by two of New Zealand's most influential foundations: ASB Community Trust and the Tindall Foundation.[18]

When asked why the Tindall Foundation cared about social lending, Trevor Gray, its manager said, "The Tindall Foundation has been making social loans over 10 years, but at a very low level. The last 12 months has seen an increase in appetite for this sort of lending, influenced by colleagues overseas. We are seeing that social enterprise in New Zealand is beginning to take off and needing to go to a scale, which donations will not serve adequately. We are now doing it on a more considered and rigorous basis and are committed to developing this as a well-structured programme in the decade to come."[19]

Another Kiwi social lending pioneer, John Prendergast of the Community Trust of Southland, often combines loans and grants allowing the trust to provide significantly more funding to community groups, especially for facilities. While they might make a

[18] Saunders (2009), *A new funding paradigm: Prospects for Social Lending and investment by foundations in New Zealand*, pp.17-20 Retrieved from: http://www.tindall.org.nz/information-research/#Social

[19] Gray (12 May 2010) pers. comm.

$100,000 grant for a community sports facility, by tapping their endowment, they might also make $1 million loan.

When Warren Jack, Executive Director of Habitat for Humanity Greater Auckland, learned I was here to look at how social lending might be expanded, he shared that Habitat affiliates here could easily utilize $10 million over five years and as much as $5 million over one to two years if they could borrow it. They have a strong asset base, but have difficulty borrowing against it because banks fear the repercussions of foreclosing on social enterprises and non-profits.[20]

I have created a snapshot of many of the Kiwi social lenders in Appendix 1. The largest and strongest of these (i.e. most financially self-sufficient), is Prometheus Finance. Established in 1983, over the past five years Prometheus Finance has made around 500 loans totalling some $8 million, with minimal losses. These loans are for amounts between $3,000 to $500,000 to individuals and organisations that are engaged in activities that benefit people and the planet. This includes working with Energy Efficiency and Conservation Authority (EECA) to provide energy efficiency products for Kiwi homes and loans to develop community resource recovery and recycling organisations such as Community Business and Environment Centre (CBEC) in Kaitaia. Another project Prometheus has been involved in is securing property for Forestry for Life, an organisation that is working with MSD's Work and Income programme and Massey University to provide transitional employment for ex–prisoners in Palmerston North.[21] Prometheus is profiled in chapter three.

To help increase social lending in Aotearoa New Zealand, ASB Community Trust and the Tindall Foundation have broadly disseminated *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand.* The two organisations launched the report at a meeting attended by approximately 40 grantmakers in December 2009. They also held day-long meetings in Auckland and Wellington which were attended by approximately 50 grantmakers. I was invited to participate in the two meetings to discuss my fellowship research and describe Self-Help's model of social lending. At the end of the first of these, Jenny Gill, ASB Community Trust's Chief Executive Officer, said that she thought it was the best discussion she had ever heard among philanthropists in New Zealand.

Glen Saunders, author of *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand*, and I had the ear of approximately 50 community trust leaders at their biennial conference in Napier in March 2010. In addition, Philanthropy New Zealand, one of my two hosts, included an article on social lending in the autumn 2010 issue of their magazine, *Philanthropy News*.

For the last few years, Philanthropy New Zealand and OCVS have convened a series of Funders Forums around the country. This year about 150 grantmakers attended the forums, which were held in six cities. As part of this year's forum, I presented "Social Lending: putting your assets directly to work for your community".

These efforts have been on the lender side, but interest is mounting on the borrower side as well. As I was starting my fellowship in February 2010, 300 community

[20] Jack (15 February 2010) pers. comm.
[21] Saunders (11 May 2010), Prometheus board of directors chair, pers. comm.

development advocates convened a successful Community Economic Development Conference in Waitakere City. The conference looked at ways to develop and finance community initiatives in more sustainable ways. There was consensus at the conference that the time is right to develop social enterprises and social lending here.

Word is also getting out about social lending through the following means:

- The March 2010 OCVS newsletter described my fellowship project.[22]
- Access Radio's Collaborative Voices show interviewed me in April.
- I spoke at two Association of Non-Governmental Organisations of Aotearoa (ANGOA) Community and Voluntary Sector Roundtable meetings (March and August).
- I wrote an article entitled "Social Lending in New Zealand"[23] for the New Zealand Federation of Voluntary Welfare Organizations (NZFVWO) online and in print newsletters.
- NZFVWO, independent of my work, is hiring a Community Enterprise and Project Development Manager to help its members develop social enterprises.
- The New Zealand Centre for Social Innovation is hoping to bring a model for developing social entrepreneurs to Aotearoa New Zealand from the UK known as Schools for Social Entrepreneurs (SSEs).
- I am scheduled to present at a ComVoices Parliamentary breakfast in August 2010. These periodic gatherings attract both MPs and people from the community sector. This breakfast will be hosted by Hon Peter Dunne, Minister of Revenue.
- The New Zealand Council of Social Services is featuring social entrepreneurship at its annual conference in Dunedin in November.

Lending to disadvantaged small businesses

One of the first social loans I made for Self-Help was to help a Native American purchase and install a concrete batch plant in a rural part of North Carolina. I will never forget seeing "First American Concrete" emblazoned on the side of the plant towering over the town with a population of 2,400. The personal and community pride in this small business, combined with the eight or so jobs created for other Native Americans, was why it was a social loan.

Turned down by conventional banks, the borrower came to social lender Self-Help. The borrower's credit history was messy and he needed help strengthening his business plan. As the loan officer, I made three five-hour return trips to visit him and his site over a three-month period before we closed the $150,000 loan. This amount of time per loan is one reason commercial bankers are not inclined to serve this market: it costs too much. Self-Help was only able to afford to do this because our time was subsidised

[22] Retrieved on 31 May 2010 from: http://www.ocvs.govt.nz/publications/newsletter/issue-31-march-2010.html#02nbspUScommunitydevelopmentexecutiveexploressociallendingopportunitiesinNZ3
[23] NZFVWO's newsletter. Retrieved on 1 June 2010 from: http://nzfvwo.org.nz/new-dialogue-blog/social-lending-in-new-zealand/#more-552

Small business social lending includes loans like the one described in the box to First America Concrete and microloans, made famous by 2006 Nobel Peace Prize recipient, Muhammad Yunus, founder of the Grameen Bank in Bangladesh. In developing countries, microloans are generally very small (a few hundred to a few thousand dollars) and mostly to women sole-proprietors. In the US and other more developed countries, the loan sizes are larger, $1,000 to $50,000, and are to men and women sole-proprietors.

When I met Kevin Robinson, Chief Executive of Te Rūnanga o Te Rarawa, and told him about my work, his first thought was that microloans could enhance his iwi's new initiative to train beekeepers. A small loan could help the trainees set up or grow their own beekeeping or honey-related businesses.[24]

It is important to note that in this context, the term "social lending" is not usually applied. In fact, in talking with Jacqui Te Kani, on the board of the Māori Womens Development Inc, and telling her about my work in social lending, she said that if she called her loan programme "social lending," her repayment rate would decline. The Māori Womens Development Inc has been making small business loans for over 20 years. She elaborated, "If we were to apply the term 'social lending' this would automatically be seen as a social dependant opportunity as opposed to a commercial activity whereby women are creating business opportunities for themselves. The word 'social' is often associated with dependency or being reliant on handouts, where this fund is to put women into business."[25]

As with lending to social enterprises and non-profits, it is my impression that there is only a small amount of social lending to disadvantaged small businesses occurring in Aotearoa New Zealand at present. Based on my conversations with Māori and Pacific leaders, there is, however, a significant amount of interest in growing it. I will discuss this momentum in chapter two in the context of Māori development. With my limited time, I was unable to take as deep a look at the small business needs and opportunities for Pacific people and other ethnic minority communities. I suggest that taking that deeper look would be an important next step in developing social lending here.

For a list of social lenders making small business loans here, some past and some present, see the table in Appendix 1.

Lending to low-income individuals and families

The types of social lending already described focus on organisations: businesses, social enterprises and non-profits. The third, and final, category addresses the needs of low-income individuals and families. First it provides a responsible (i.e. reasonably priced and socially motivated) alternative to fringe lenders, also known as loan sharks. Second, it promotes homeownership through savings schemes, counselling and flexible, yet appropriate loans. Successful results with the first type of consumer lending is generally a prerequisite to attaining the second type, with the combined result of making it possible for families to begin building net worth.

[24] Robinson (9 April 2010) pers. comm.
[25] Te Kani (26 March 2010 and 27 July 2010) pers. comm.

The first of these consumer loans (cash flow or payday loans) provides a less burdensome temporary fix to a bigger economic problem of incomes at the lower end of the spectrum being inadequate to sustain a family. This challenging economic reality is increased when the family members are imprudent in their spending behaviour and do not know how to, or choose not to use budgeting.

As Don Gray, Deputy Chief Executive of MSD,[26] and Dr Colin Tukuitonga, Chief Executive of the Ministry of Pacific Island Affairs (MPIA),[27] independently shared with me, too much and inappropriate use of personal debt is a big problem here. For that reason, MSD and MPIA are both involved in financial literacy efforts.

Whereas the first of these types of loans is based on a temporary fix to a larger economic challenge, the second type of consumer social lending, homeownership, is an asset-building model, where the asset is real estate.

Self-Help became an active homeownership lender after realising, in the mid-1980s, that most small businesses are started by entrepreneurs who take out a loan against their homes as collateral. At that time, there was a dramatic differential in homeownership rates between white and black households in the North Carolina. Just as financial literacy and the appropriate use of consumer debt is a precursor to homeownership, homeownership is a common path to small business development.

Some credit unions are already meeting the first of these consumer finance needs: small relatively short-term loans for household expenses. Aotearoa New Zealand has three such examples in Awhi Credit Union serving 1,900 mostly Māori members in the Bay of Plenty; Aotearoa Credit Union serving 15,000 mostly Māori and Pacific members, with offices from Auckland to Porirua; and Westforce Credit Union with 6,600 members, also mostly Māori and Pacific members, with offices in Auckland and Northland. Each of these institutions puts a premium on developing financial literacy and provides countless hours helping their members manage their household finances. Awhi, for example, is so committed to this mission, that it is planning a credit union at the Rotorua Girls College in recognition of the need to start financial training early.

Awhi's size has, to date, prevented it from getting involved in responsible mortgage finance.[28] Aotearoa and Westforce credit unions have made a few home loans, but they find that their borrowers generally lack the financial strength to buy a home. If the right product and subsidies are developed, credit unions could help increase homeownership rates by taking up the second type of responsible consumer lending; home loans.

Churches and religious programmes are the other major player in the cash flow loan market. As illustrated in the table of social lenders in Appendix 1, some of the main

[26] Gray (24 March 2010) pers. comm.
[27] Tukuitonga (26 March 2010) pers. comm.
[28] The key word for this category of social lending is "responsible". The loans need to be fairly and transparently priced, based on the verified income of the borrower, based on accurate real estate assessments, and, often, combined with homeownership counselling. The mortgages that contributed to the global credit crunch were not responsible in this way.

Christian denominations, as well as non-denominational and other religious programmes, offer financial literacy training, credit counselling and, in some cases, no or low-interest loans to help low-income people get out of the debt trap. The largest of these is Kingdom Resources in Christchurch that, in 2009, served over 2,600 adults with the assistance of 140 volunteers and a small staff.[29]

[29] Retrieved 2 July 2010 from: http://www.kingdomresources.org.nz/1/index.php

2 MĀORI DEVELOPMENT

This chapter explores opportunities that social lending might offer Māori. I have worked for the last 20 years as part of an organisation with a core mission of promoting the economic development of lower socio-economic communities, I am eager to see social lending in Aotearoa New Zealand do the same.

While all three types of social lending have appeal to all ethnic groups here, in Māoridom, I heard a lot about small business opportunities that are thwarted by lack of capital and the need for technical assistance in business skills.

I was very fortunate to meet with the leaders of four iwi (Kevin Robinson of Te Rarawa, Mark Solomon of Ngāi Tahu, Teresa Tepania-Ashton of Ngāpuhi, and Tiwana Tibble of Ngāti Whātua o Orakei). I also met with several prominent Pākehā[30] who are widely regarded as advocates for Māori rights (Sir Douglas Graham, Patrick Snedden, and Stephen Tindall) and other Māori leaders listed in the acknowledgements section of this paper. In all of these conversations, I received universal interest in exploring ways to make social lending available for Māori communities.

History of Māori loan programmes

Over the last 20 years, Māori-Pākehā relations have changed significantly because of Treaty settlements.[31] There is a new and evolving power balance and a partial reversal of economic fortunes. The Treaty settlement process has moved some Māori from a grievance mindset to a development mindset, especially for those iwi that have regained assets from the Crown.

What better way for an iwi to invest a portion of its settlement dollars than into a social lender that can recycle and leverage those dollars on behalf of its community – its iwi, hapū (sub-tribe) and whanau (families). Just as philanthropy was exploring using their assets for social lending, thanks to the advocacy efforts of the ASB Community Trust-Tindall team, the same tool could be brought to iwi asset managers.

As *A new funding paradigm: Prospects for social lending and investment by foundations in New Zealand* was being researched, Hon Dr Pita Sharples, the Minister of Māori Affairs was convening a Māori Economic Taskforce. Its reference groups are in their research phases. The chair of the Investment, Capital and Enterprise workstream, June McCabe, shared their work plan.[32] She said that they are currently doing a discussion document on the concept of a Māori development or investment fund to accelerate Māori economic development, including innovation, project financing and microlending.

One of the reference group's consultants, Jason Mika, shared a thick binder of

[30] Pākehā is the Māori term for people of European heritage in Aotearoa New Zealand.
[31] In 1840, the British government and many Māori leaders signed the Treaty of Waitangi. Ever since, its interpretation has been disputed. Starting in the later part of the 20th century, these disputes started being settled with large amounts of cash, other assets, and privileges transferring to iwi. The process continues.
[32] McCabe (1 June 2010) pers. comm.

materials gathered as background to their work. In it and from my interviews, I learned the history of Māori loan aspirations and schemes. A summary follows:

- Mana Enterprises: In the mid-1980s, the Crown gave $12.5 million to iwi to on-lend to their members to promote small business development.[33] Little guidance or training was given along with the funds and, not surprisingly, much of the funding was lost.[34] Where the social lending skills were already present at the iwi, the programme was more effective, helping set up some good businesses as well as establishing some of the Māori Authorities and iwi organisations that are here now.[35] The scheme folded in 1993-94. A couple of the Mana Enterprise legacy organisations, Aotearoa Credit Union and Ngāi Tahu Finance, are described on the next page.
- Māori Development Corporation: This development fund was established in 1987 to complement Mana Enterprises. It made larger investments (generally over $100,000) to medium or large businesses. By 1993, it was mostly making equity investments and seemed more focused on fund growth and profitability than Māori business development. By 1996, the government withdrew its 49.9 per cent ownership and was bought out by Tainui Māori Trust Board for almost $21 million. This sum represented a nearly $8 million profit which, at the time, the government agreed to use to help set up a proposed development finance vehicle at Poutama Trust.[36] Poutama Trust's online newsletter states that they may finally be fulfilling this commitment in the form of a partnership with Kiwibank.[37]
- Māori Womens Development Inc: The Māori Women's Welfare League launched this lending programme in 1987 with government capital and operating funds. It continues to make loans and provide technical assistance to Māori small business owners (men and women). Current data on impact is not available.[38]

Among the successes of the Mana Enterprises programme were these two strong offshoots:

- Aotearoa Credit Union: This 15,000-member credit union with over $15 million in assets[39] started out in 1989 as MUMA Credit Union. Funds repaid from the relatively successful Mana Enterprises loans made by the Manukau Urban Māori Authority (MUMA) supported the credit union through its formative years.[40] The credit union has 10 offices: seven in Auckland, and one each in Hamilton, Whanganui, and Porirua. While it does not offer small business loans, it has become a vital resource to many of its mostly Māori and Pacific low-income members who rely on their savings accounts and personal

[33] *Mana Enterprises Programme: A baseline report*, p.15
[34] Anonymous (26 April 2010) pers. comm.
[35] Mika (10 July 2010) pers. comm.
[36] Groves (2000) p.16
[37] Poutama newsletter October 2009, Poutama Trust. Retrieved 9 July 2010 from: http://www.poutama.co.nz/newsletter/zeronine/oct09.htm#3
[38] Groves (2000) p.17 reports that as of 31 July 1999 they had made 120 loans for $693,200 creating 255 jobs and providing technical assistance to 349 other businesses. I have been unable to find any more up to date information.
[39] Financial Statements (30/9/09) Retrieved 9 July 2010 from: http://www.business.govt.nz/companies/app/ui/pages/companies/otherSearch
[40] Osborne (28 April 2010) pers. comm.

loans to meet their monthly living expenses.[41] They have a small portfolio of home loans, but it is rare that their borrowers can afford to become homeowners as the majority of their members are either low-income earners or unemployed. Of note, their membership falls along the following ethnic lines: approximately 40 per cent Māori, 40 per cent Pacific, and the remainder are from other ethnic backgrounds.

- Ngāi Tahu Finance: Like Aotearoa Credit Union, Ngāi Tahu Finance was created with the repaid Mana Enterprises loans. In its first five years, it lent to 166 businesses that employed 304 people. Their average loan size was $55,000 to $60,000 with interest rates between eight and 14 per cent. The repayment rate was 95 per cent, with no significant losses. Only one in 20 of the businesses failed in those first five years. Notably, despite providing extensive technical assistance to their borrowers, Ngāi Tahu was both self-sufficient and profitable.[42] My understanding from conversations with Mark Solomon, Te Rūnanga o Ngāi Tahu Kaiwhakahaere, and his runanga development chief, John Reid, is that the programme was absorbed into the broader, more commercial Ngāi Tahu Holdings. It is currently under review and likely to be restarted in a new and enhanced form.[43]

This history, combined with the current work of the Māori Economic Taskforce illustrates the depth of interest around credit access and social lending for Māori entrepreneurs. The following Māori Party policy statement underscores this interest. It says that the Māori Party aims to:

> Streamline the funding distributed by the Ministry of Economic Development to create a Community Development Bank. The Bank will make small loans to whanau and family businesses to incubate and rollout new products and services.[44]

The rest of this chapter explores how Māori credit access differs from credit access for other Kiwi entrepreneurs. I then make recommendations to overcome the challenges. The two reasons for the difference, in my opinion, are historical disadvantage as Māori and Pākehā have struggled to find a way to live cooperatively and equitably in Aotearoa New Zealand, and the Māori cultural preference for collective ownership and governance.

Historical disadvantage: current implications

Historical disadvantage means that the incomes[45] and educational achievement[46] of Māori are lower than national averages. These combine to make it harder for some Māori to start and grow businesses. It is harder in two ways:

- lower-income people lack the personal resources and credit histories to make lenders comfortable

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[41] Soutar (19 March 2010) pers. comm.
[42] Groves (2000) p. 25; Solomon (11 May 2010) pers. comm.
[43] Reid (21 June 2010) pers. comm.
[44] Māori Party Policies. Retrieved 8 July 2010 from:
http://maoriparty.org/index.php?pag=cms&id=130&p=election-policy.html
[45] The Social Report (2009) Ministry of Social Development, p.63
[46] Ibid. p. 41

- they are less likely to come from families with a succession of prosperous business people or have a bevy of friends with business experience to advise them. In addition, with less formal education, they may need more guidance and technical assistance to get their businesses off the ground.

While entrepreneurial spirit is independent of income and historical advantage, a lack of income and historical advantage can discourage its expression. An old, but invaluable study, entitled *Financing Māori Business*, prepared by Alan Groves for Te Puni Kōkiri (TPK) in 2000, states "Anecdotal evidence, supported by the primary data gathering aspect of this research, suggests that as many as four in five prospective Māori business participants are failing to secure start-up capital".[47]

Some small businesses get their first capital as investments from friends and family – that is harder to do when one is poor. Other entrepreneurs take second mortgages on their homes to start or grow their businesses. Unfortunately Māori homeownership rates are dropping,[48] making that indirect access of capital harder to obtain. Hence, unconventional capital or social finance comes into play. A social lender focusing on this market needs to bring flexibility to their underwriting[49] and provide or collaborate with a provider of strong, practical technical assistance.

> Self-Help, for example, rarely makes unsecured loans. We regularly lend, however, with impartially secured loans where we rely on the psychological value of the collateral. In one instance, we took a lien on an auntie's home with only minimal equity in it. We knew that the watchful eye of the auntie would be a strong surrogate for tangible collateral.

Entrepreneurs are people with an idea and a drive. They also need a host of skills to turn their ideas and drive into successful enterprises. Most entrepreneurs rely on formal and informal advisers. Finding these advisors is a lot harder to do on a low income when the entrepreneurs do not have the funds to hire the advice or the network to ask for it for free from family and friends. The result is that they need technical assistance.

While there are a number of strong and effective small business technical assistance and facilitation services for Māori, my experience has shown that incorporating the technical assistance into the lending process is effective. According to Community Development Finance Association (CDFA), the UK trade association for community development financial institutions (CDFIs), their data suggests that default rates can be affected by the provision of advisory services. Some CDFIs provide finance only, while others provide finance and advisory services. A CDFA study showed that those providing advice have an average default rate three per cent lower than those who do

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[47] Groves (2000) p.12

[48] According to Housing New Zealand, "Since 1991 the proportion of Maori who own their home has fallen from 61.4 percent to 45.2 percent in 2006 (Figure 2). Between 1991 and 2006, the Maori home ownership rate fell disproportionately faster than that of European households. The Maori home ownership rate fell approximately 16 percent, and the European home ownership rate fell approximately 11 percent." *Maori Housing Trends Report*, (September 2008) Housing New Zealand, Retrieved 10 July 2010 from: http://www.hnzc.co.nz/hnzc/web/research-&-policy/housing-research-&-evaluation/summaries-of-reports/maori-housing-trends-report-2008.htm

[49] By "underwriting", I mean figuring out how to make a loan work for both the borrower and the lender. Social lenders need to tread a fine line between flexibility and making sure they are repaid.

not – despite the fact that many CDFI customers will receive advice elsewhere. This helps establish the value of delivering finance alongside technical assistance.[50]

The incentive of a loan can motivate entrepreneurs to do the hard work and step back to learn and adapt. For example, many of Self-Help's small business borrowers find the process of putting together their loan application, a business plan and cash flow projections, immensely helpful. Self-Help staff members never do the work for the applicant. Rather, Self-Help staff give applicants the tools they need and then provide constructive feedback to the applicant's submission.

Self-Help's experience is mirrored on the South Island. One of the keys to Ngāi Tahu Finance's success has been "introducing one-on-one training, mentoring and support services for clients".[51] While still profitable, they were willing, because of their social lending mission, to lower their return in order to enhance their services. They "lowered the hurdle (rate of return) and put a little more weighting on the person in the overall assessment".[52]

Ngāi Tahu's experience shows that it is important that lenders are creative, open minded, and culturally competent. Some of the cultural issues are Māori while others relate to norms that get established when people have been on the dole for a long time. As June McCabe said so succinctly, a "grant mentality is an absolute problem".[53] The dignity of believing in someone enough to give a loan can be very empowering. Understanding these softer attributes is a critical part of social lending. In my many years of hiring commercial loan officers, I have found that it is easier to make a social activist into a banker than a banker into a social lender.

Collective ownership

Cultural competency has fundamental ramifications in the Māori context that go beyond understanding history and cultural identity. It directly affects loan underwriting. Collective ownership and governance, which are deeply rooted cultural preferences, conflict with non-Māori approaches to loan making where real estate is a primary form of collateral to secure loans and where personal guarantees by the owners are expected. Both of these approaches are virtually impossible with collective ownership.

The reason that lenders take collateral and personal guarantees is to have a secondary source of repayment. It is a core principle of lending and an effective method of minimising risk of losses to the lender. Real estate, which generally appreciates over time and cannot easily be moved or hidden, is a good fallback to a lender. Another fallback is a personal guarantee by an owner, especially if that owner has net worth or can get another job outside the borrowing business if that business should fail.

A major interest of Māori leadership is around supporting and growing collective enterprises, often at the iwi or hapū level, that have multiple owners on collectively

[50] *Inside Out* (2009), Community Development Finance Association, Retrieved 20 July 2010 from: http://www.cdfa.org.uk/about-cdfis/state-of-cdfis-research/ pp.16-17
[51] Groves (2000) p.26
[52] Ibid.
[53] McCabe (28 June 2010) pers. comm.

owned land. Often these more complex enterprises are larger and have more sophisticated management that might not need the technical assistance typically required by disadvantaged borrowers. What they need, however, is alternative ways to provide that secondary source of repayment.

The United States Department of the Interior, Office of Indian Energy and Economic Development, Division of Capital Investment has successfully used a federal guarantee to stimulate and support small business development in Native American communities. It might serve as a model for Aotearoa New Zealand. A description of the guarantee and its eligibility criteria is in Appendix 2.[54]

Since 1974, this agency has provided nearly $1 billion in loan guarantees. In their fiscal year 2009 alone, they guaranteed $71 million of loans. Interested in exploring this model, I emailed the programme's director, Phil Viles, about his programmes' performance and learned:

> 'Default' is a term of art and defaults can be cured and the loan can lurch forward to full term, so we use the term 'loss' and we pay off after a Claim for Loss has been filed and we have examined it. When I took over the program three years ago, our loss rate was about 1.5% and since that is one of our assessment measures, my boss got our 'allowable target' raised to 4%. He not only saw hard times coming, but also wanted us to take more risk. I checked last week and the loss rate we are experiencing now, since 1992, is 2.67%. If I remember correctly, that is losses paid out less recoveries divided by total amount of guaranteed loans actually funded. Businesses benefited have run the gamut from fishing boats in Alaska and along the northwest coast of the US to convenience stores in South Dakota, and many others.

He goes on to add:

> Keep in mind I am quoting guaranteed loans only; from 1975 for twenty plus years, we did direct loans, but we were not any good at it, it became politicized, etc.[55]

I find two points especially compelling in Vile's comments: the programme performed so well that they chose to take on more risk, and that their experience led them to conclude that government should not be a direct lender. I also find the programme's slogan, "Helping Guarantee the Economic Future of Indian Country",[56] very relevant to Māori development because of its emphasis on the important Māori value of preservation of the land.

I gravitate to loan guarantees because I have seen them work in the US. Self-Help was the first credit union and social lender in the US to use the federal government's Small Business Administration (SBA) guarantee programme and the first to use another federal department's guarantee programme, the US Department of Agriculture's Rural Development guarantee.

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[54] Retrieved from: http://www.bia.gov/WhoWeAre/AS-IA/IEED/DCI/index.htm
[55] Viles, P. (16 June 2010), , Chief, Division of Capital Investment, Office of Indian Energy & Economic Development, US Department of the Interior, email
[56] Retrieved from: http://www.bia.gov/WhoWeAre/AS-IA/IEED/DCI/index.htm

We saw enough promise in loan guarantee programmes that we designed one to use to help minority-led charter schools.[57] Self-Help's proposal and pro-formas are included in Appendix 3.[58] Our modest initial efforts to secure grant funding for the risk capital were unsuccessful and then the US economy fell apart which led Self-Help to table the proposal.

I recommend the creation of a Māori guarantee programme to help lending institutions, whether they be a social or conventional lenders, overcome the challenges of lending to collectively owned enterprises on collectively owned land. I am not alone in making this recommendation. Poutama Trust is currently looking into creating a guarantee programme, which is mentioned in several of the papers I have referenced, and the Grove's paper for TPK has some useful information about Canadian, Australian and the US programmes.[59]

I spoke with staff at Treasury and Ministry of Economic Development (MED) to better understand the Kiwi experience with loan guarantees. I learned of the existence of a set of guarantees offered by the New Zealand Export Credit Office. I recommend exploring its performance, strengths, weaknesses and applicability as a model for Māori collectively owned enterprises. Chapter five captures other insights about loan guarantees.

If the guarantee programme and Māori social lending ideas are not new, why then, have they not developed? What can be learned from the previous Māori social lending experiences and previous recommendations?

- As Phil Viles, who manages the Native American guarantee programme, said about government as a direct lender, "we weren't any good at it, it became politicized, etc." My experience in the US, my understanding from international experience and the experience of the Māori Development Corporation all support Viles contention. The previous recommendations have tended to want to place the ownership of the social lending within the government: with TPK, Poutama Trust, or the Māori Trustee. I recommend that they set up or use a private intermediary lender as described more fully in chapters three and four.
- Mana Enterprises shows us that social lending is a specialised skill even for the small loans. Granting capital to be on-lent, without proper training and/or experience is likely to produce poor results. The flip side of this is that, as Ngāi Tahu and MUMA show, the right people with the right guidelines can make for an effective programme. Social lending should be done by skilled, experienced professionals.
- Some of the recommendations for a Māori finance facility have been that it be run on a commercial basis.[60] While loans to larger, stronger enterprises could be commercially viable, Self-Help's experience is that the level of technical assistance needed and the often smaller loan sizes need the support of either

[57] Charter schools are publicly funded private non-profit schools that are free and open to all students.
[58] Ozlem Tanik, Senior Analyst, Self-Help, did the conceptual and analytical heavy lifting for this model.
[59] Groves (2000), pp.20-23
[60] Groves (2000), p.37

> operating grants to cover losses or subsidised capital to minimise expenses (see discussion in chapter four). None of the Māori banking models that I have seen includes a non-profit arm to attract such subsidy from philanthropy and government. I recommend that the lender be non-profit or have a non-profit affiliate.

Much of the Māori Economic Taskforce's work and this chapter are about business development, but it is important to recognise that all three types of social lending have the potential to benefit Māori. It feels fitting to close this section with the following quote from Alan Grove's report:

> In considering the financing options for Māori, this report concludes that the money is available – much of it in Māori hands. What is missing is a user-friendly interface between the entrepreneur and the investor, and a means for the growing band of potential Māori equity investors to be actively involved. It concludes that Māori themselves could be instrumental in resolving the issues around access to finance for prospective Māori business people.[61]

[61] Groves (2000), p.7

3 INTERMEDIARIES

This chapter describes the concept of an intermediary, profiles three successful examples, and concludes with ways grantmakers can support them.

The concept

An intermediary "intermediates" or acts as a go-between for grantmakers and communities.

Grantmakers: Governmental, tribal, religious and philanthropic grantmakers want to accomplish social goals (expanding childcare options, improving education, and reducing poverty in Māori and Pacific communities are examples). By investing in a social lending intermediary, they can:

- leverage their dollars and thus broaden their impact
- outsource the work to an institution with social lending professionals on staff
- insulate themselves from the risks of turning down compelling but unviable projects and of foreclosure.

Grantmaker investments can come in the form of grants or loans to the intermediary for technical assistance, risk capital or loan capital with the latter two recycling as long as the lending programme is successful.

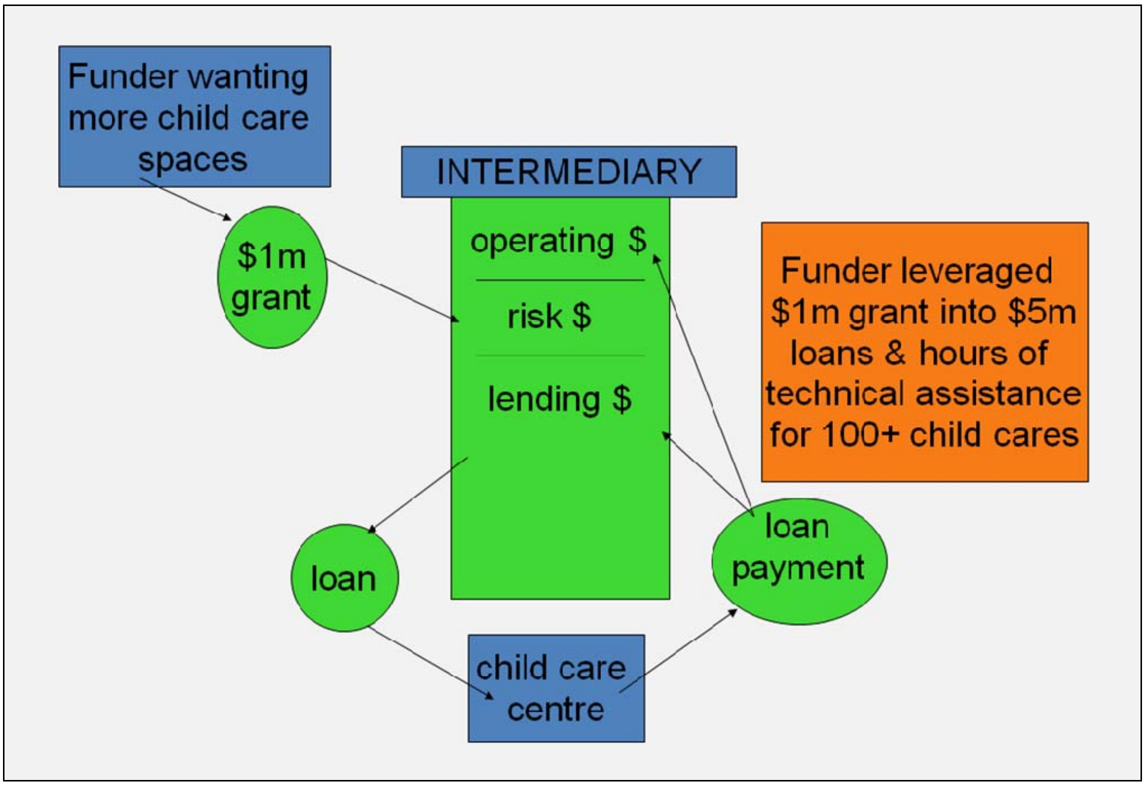
Communities: Social and business entrepreneurs, traditional non-profits and families often have compelling capital needs deemed too small, too risky or too unknown by conventional lenders and yet are beyond the scope of grantmakers. They often also need guidance and support in articulating and realising their needs and projects.

An **intermediary** brings skill in:

- lending
- providing technical assistance to help community members realise their ambitions
- managing a complex mixture of funders – each with its own accountability.

As a social enterprise that is not trying to maximise profits, an intermediary can afford to make small loans, spend time on both the front end of advising potential borrowers and on the back end of helping troubled borrowers find solutions.

When the North Carolina Division of Child Development wanted to expand the quantity and improve the quality of childcare, it gave Self-Help $1 million to use as credit enhancement. Since the partnership began, Self-Help has helped childcare providers get started, expand, purchase safe vans to transport children on enrichment trips or to pick them up from rural locations, purchase playground equipment, remediate lead paint, and add insulation to cut down on energy costs. Along the way, they have leveraged the grantmaker's investment five times and provided thousands of hours of business support. See the following diagram:



Profiles of intermediaries

Three intermediaries are profiled in this section. I start with Self-Help, an example of what a mature intermediary can become. As a US example, its relevance to Aotearoa New Zealand is somewhat limited, but I feel it is important to include so that the reader appreciates what my biases might be. I started working at Self-Help in 1989, when I became the 16th staff person. I have worn many hats, including fundraiser, general manager of the non-profit parent, early-stage developer of the secondary market programme, and finally, the role I have held for the last nine years: head of the commercial lending department. That department comprises 30 staff members making loans ranging from $5,000 to $40 million to non-profits, social enterprises and disadvantaged small businesses.

Next is Prometheus Finance, the largest and financially strongest Kiwi social lender. The final profile is of Awhi Credit Union, a smaller, but very effective intermediary.

Self-Help

Mission: Creating and protecting ownership and economic opportunity for people of colour, women, rural residents and low-wealth families and communities.

History: Founded in 1980 by a couple who wanted to translate the successes of the civil and women's rights movements into the economic arena. Self-Help's initial strategy was to help workers whose manufacturing jobs were moving to less developed nations to start their own businesses. Self-Help became a financial institution in 1984 to support its technical assistance work, initially to the cooperatives and worker-owned enterprises with which it was already working.

In response to the desires of our African-American customer base, we began offering small business loans to sole proprietorships, but quickly learned that few potential borrowers were able to offer their homes as collateral for the loans because they did not own a home. This led Self-Help to start homeownership lending. We subsequently initiated a community facilities programme to finance schools, childcare centres and health care providers in low-income neighbourhoods. The most recent addition to Self-Help's loan products is consumer lending to help low-income people avoid loans sharks.

To increase our scale and impact, we started a secondary market programme to purchase, package, and generally resell responsible home loans made to low-income families by commercial banks. In 2002, we started a dedicated advocacy arm, the Center for Responsible Lending, to change banking laws and regulations on behalf of low-income communities.

Programmes: Self-Help provides financing, technical support, consumer financial services, and advocacy for those left out of the economic mainstream. As of 31 December 2009, Self-Help had invested $5.66 billion in financing to 64,140 families, individuals, and organisations. These beneficiaries include:

- low-income borrowers – 84 per cent
- people of colour – 46 per cent
- women – 42 per cent
- people in distressed areas – 33 per cent
- people in rural areas – 17 per cent.

The following programmes assisted them:

Direct Home Lending
- $318 million
- 4,293 homeowners

Secondary Market Home Lending
- $4.57 billion
- 50,869 homeowners

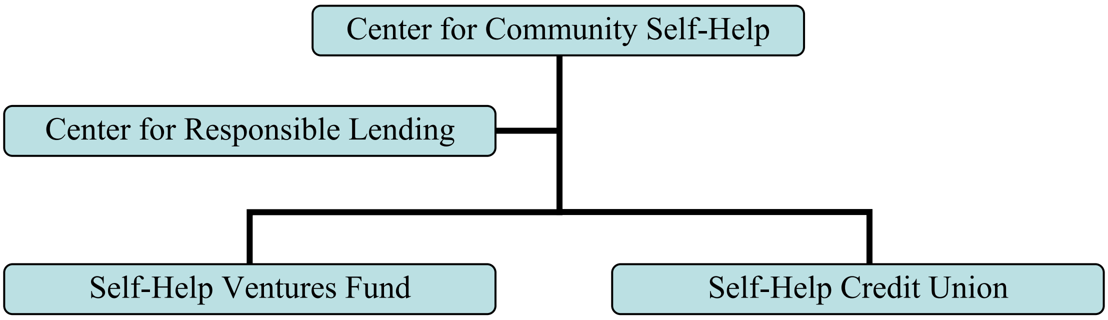
Community Facilities Lending
- $213 million
- 807 projects
- 9,017 jobs created/maintained
- 50,054 childcare, charter school, and housing spaces created or maintained

Real Estate Development
- $107 million invested
- 132 homes completed
- 21 commercial properties owned and managed

Consumer Financial Services
- $304 million in savings accounts
- $27 million consumer loans
- 4,646 consumer loans

Small Business Lending
- $419 million
- 3,201 entrepreneurs
- 24,142 jobs created/maintained

Corporate structure: Self-Help comprises approximately 25 different corporations to accommodate different strategic and tax needs. This is a simplified rendition of Self-Help's structure:



Financial highlights (as of 31 December 2009):

- assets – $1.35 billion
- deposits – $307 million
- net worth – $341 million
- annual revenue – $97 million.

Funders/investors: Operating income for our lending and real estate activities is primarily earned income. Our advocacy work receives grants from private foundations. Risk capital comes from retained earnings and governmental and private grants. Lending capital comes from depositors in our credit union, the New Markets Tax Credits programme, and low-interest loans from government and foundations.

Challenges:

- helping current borrowers survive the economic crisis while minimising Self-Help's losses
- managing liquidity
- managing growth in employees, programmes and geographic spread
- avoiding and responding to attacks by foes of our Center for Responsible Lending.

Contact information: www.self-help.org

Prometheus Finance[62]

Mission: To mobilise savings and investment to provide capital for social and environmental projects in Aotearoa New Zealand.

History: Founded in 1983, Prometheus' mission is to provide a way for savers to invest their money in people and projects that are socially or environmentally responsible. Prometheus began as a charitable trust and then, due to limitations this structure placed on its growth, it changed to a credit union. In 2003, Prometheus became a regulated non-bank deposit taker.

Prometheus has enjoyed steady growth and has weathered the recent financial crisis well. It has expertise in social lending as well as in the management of savings and of a quasi-banking organisation. It can and has offered this knowledge, expertise, networks and shared values to others.

Prometheus is based in Hawke's Bay but the majority of its clients, both savers and borrowers, are based elsewhere, particularly in Auckland, Wellington and Christchurch. Its approach rests on four pillars:

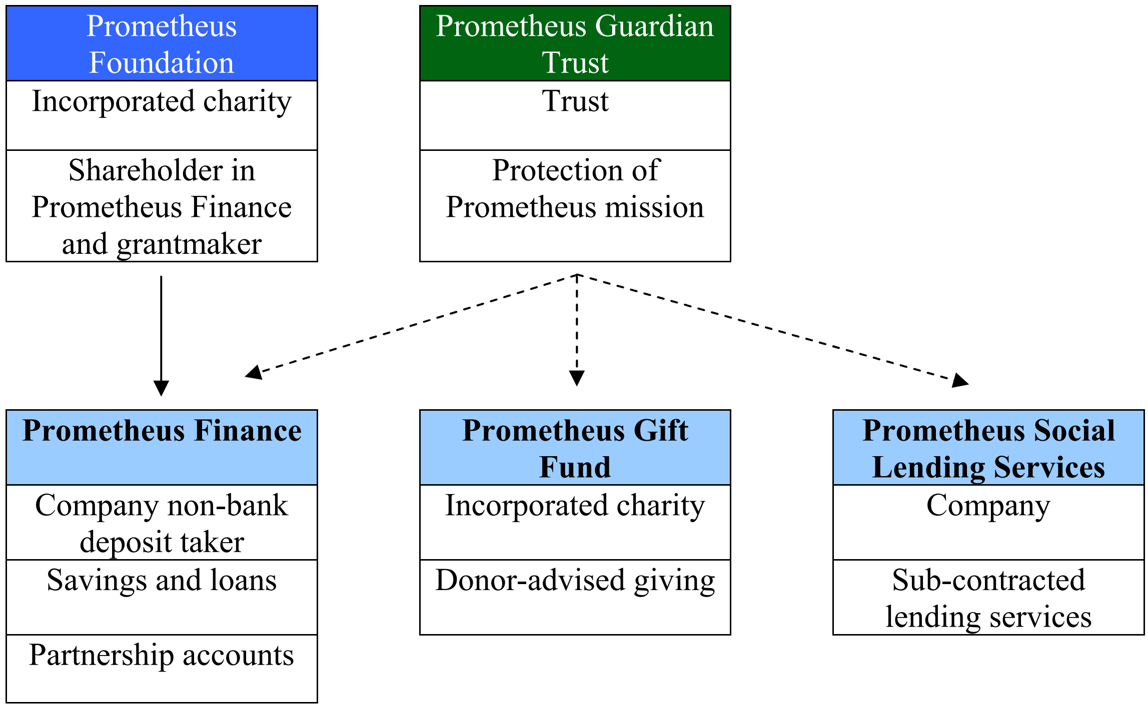
- *Commitment to social and environmental finance*: Every borrower has to show positive social and environmental purpose. This gives them integrity and solidity and strengthens Prometheus' lending.
- *Considered and prudent in who is lent to*: It lends responsibly to individuals and organisations that have good ideas and can demonstrate good management and the ability to take on a loan.
- *Considered and prudent in how it manages itself*: Prometheus maintains a prudent ratio of capital to the amount of money managed.
- *Not only for profit*: Prometheus aims to make a profit to maintain its stability and provide a prudent level of reserve but it does not pursue profit for its own sake or seek to maximise it.

Programmes: Prometheus helped establish some of Aotearoa New Zealand's leading social and environmental businesses such as Living Nature cosmetics, CBEC, Piko Wholefoods, and Artemis Herbal Medicine. Prometheus works with some of the local leaders in organic agriculture, eco-housing, and resource recovery and recycling. In the past five years, Prometheus has made approximately 500 loans totalling some $8 million with minimal losses. Loans are for amounts between $3,000 and $500,000.

It piloted the first financing of consumer eco-products with Greenpeace, Solahart and the Energy Efficiency and Conservation Authority (EECA). Prometheus is developing a number of new partnership arrangements. For example, 2010 saw the launch of the 'Organic Saver' term deposit account, a partnership with the Soil and Health Association to raise funds targeted for lending to organic projects. This benefits Soil and Health and their work promoting the development of organics through the donation to Soil and Health of a percentage of the interest earned on these accounts.

[62] Sue Cooper of Prometheus Finance provided information for this profile on 7 July 2010.

Corporate structure: Prometheus Finance is a regulated non-bank deposit taker. It has a special governance structure to protect its social mission with a separate guardian trust with veto powers over appointments of directors and changes to Prometheus Finance's constitution. The guardian trust scrutinises changes to ensure that Prometheus' mission is upheld.



Financial highlights (as of 30 June 2010):

- assets – $16.6 million
- deposits – $14.5 million
- net worth – $2.1 million
- annual revenue – $1.1 million.

Funders/investors: The majority of depositors are private individuals. There are a smaller number of institutional clients, mainly from the third sector, which generally provide larger deposits. There are three shareholders, all with a minority stake: The Prometheus Foundation, a grant giving charitable foundation, and two of Europe's leading socially responsible banks, Triodos Bank and GLS Gemeinschaftsbank.

Challenges:

- increasing Prometheus' profile to grow its assets
- developing new products and services for the growing number of people and organisations wanting to use socially responsible finance
- meeting the increasing burden of compliance while maintaining its core mission and continuing to grow.

Contact information: www.prometheus.co.nz

Awhi Credit Union[63]

Mission: Promoting financial and social well-being within its communities.

History: Founded in 1993 by a group of Māori women wanting to better their rural coastal community in the Bay of Plenty. Originally called Torere and Districts Credit Union, its name was changed to Awhi, which has two meanings: in Māori, “awhi” means to nurture and the letters stand for “Altogether We Have Independence”.

Programmes: Budget counselling, deposit services, consumer loans, and community building activities to give back at the local, national and international levels. In 2000, Awhi Credit Union collaborated with Habitat for Humanity and Housing New Zealand to build and finance 21 homes primarily for first-time homebuyers on special assistance. This year’s giving back activity at the local level is to create a youth credit union at Rotorua Girls College.

Corporate structure: It is a single entity, governed by a board of directors elected from the membership of Awhi Credit Union.

Financial highlights as of 31 March 2010**:**

- assets – $3.8 million
- deposits – $3.2 million
- net worth – $570,502
- annual revenue – $999,468.

Funders/investors: Credit unions are cooperatives. The members are the owners, investors (or depositors) and borrowers. The investment cycle starts with members saving together, then, as needed, receiving loans which they pay back with interest to cover the credit union’s expenses. Any profit left after covering expenses is used to build the credit union’s institutional reserves and to pay dividends back to the members.

Challenges:

- legislation about capital adequacy and related parties
- increasing compliance costs.

Contact information: www.awhicu.co.nz

[63] Rachell Mio, CEO of Awhi Credit Union on 6 July 2010, provided information for this profile. Alan Groves report includes an in-depth case study of Awhi (it was still called by its former name: Torere & Districts Credit Union) on pp.61-66.

Ways grantmakers can support intermediaries

Grantmakers, whichever type, can support social-lending intermediaries in a variety of ways. There is a strong history of such support in the US. Kiwi grantmakers might consider providing:

- operating grants to help an intermediary get started or for an existing intermediary to start new initiatives
- operating grants to subsidise the cost of technical assistance if it exceeds the revenue earned from the loan, i.e. because the assistance needs are great or because the loan is small or at a low interest rate
- loans for the intermediary to re-lend – this is especially helpful if the intermediary is not a depository
- if it is a depository, then deposits into social banks/finance companies/credit unions for loan capital
- capital grants or forgivable loans to absorb risk in areas that are of particular interest to the grantmaker, like for childcare in the diagram earlier in this chapter
- loan guarantees – using their balance sheets to back social or conventional bank loans.

The following chapter describes how these various supports will further social lending. The final chapter discusses a variety of ways that government can support intermediaries.

4 TAKING SOCIAL LENDING TO NEW LEVELS IN AOTEAROA NEW ZEALAND

Social lending already exists here but at far lesser levels than in the US, the UK or other parts of Europe. I have been fortunate to meet some of this country's social lending leaders and am impressed by their commitment, creativity, and endurance. Their organisations do good work, but they are limited in their scope. Some serve only one community leaving many communities without service; or the size of their loans is limited because their capital base is small; or they serve only non-profits and not small businesses; or because their operating model runs at a loss, they are dependent on annual fundraising to keep their doors open.

Through the convergence of events described in the introduction to this paper, the opportunity seems ripe to fill some of these gaps and take social lending to a new level.

This chapter offers a vision of a robust Kiwi social lending system. The system would combine three elements described in detail below. The first is an intermediary or set of intermediaries to help fill some of the gaps in the current Kiwi social lending environment. Said intermediary would also actively collaborate with and serve other social lenders. The second is a guarantee, open to all qualified lenders, for Māori enterprises on collectively owned land. The third is an expansion of the low-income serving credit unions.

A Collaborative Aotearoa New Zealand Intermediary (CANZI)

To bring this vision into reality, I recommend that grantmakers and community stakeholders assess the interests and capacities of the existing social lenders and create one or more social lending intermediaries to complement and support the existing services. For the purpose of this paper, I will create a fictitious organisation and call it CANZI for Collaborative Aotearoa New Zealand Intermediary. CANZI is simply a construct: a means to share ideas about how to grow social lending in Aotearoa New Zealand.

I use the term "create" loosely in that CANZI need not be new. It might well evolve from a reformulation of existing social lending players: it could grow out of one of the stronger intermediaries or emerge from a joint venture between organisations.

While CANZI could serve all types of social borrowers, the organisational structure to deliver all three types of services weighs against this. I recommend that it focus on lending to enterprises: initially to social enterprises and non-profits (the first category of social lending), then, as its systems and relationships develop, to add service to disadvantaged small businesses (the second category). CANZI would not provide consumer finance as that service is best done locally.

CANZI should make loans directly to borrowers and, as a collaborative intermediary; it should support, incubate and provide services to other lenders. Its collaborative lenders might include foundations, trusts, government units, banks and other social loan funds.

This vision of a CANZI will take time to develop but, eventually, it will need to be:

- a resource for other social lenders
- broadly available through partnerships
- diverse
- a private, non-governmental organisation
- a model social enterprise
- large enough to achieve economies of scale and offer leverage.

After exploring each of these characteristics and the opportunities they offer, I will discuss the risks and disadvantages of CANZI. The chapter ends with recommended implementation steps for CANZI, the Māori guarantee, and expansion of low-income credit unions.

A resource for other social lenders

The goal of this proposal is to take social lending to a new level: to grow the movement seeded and ploughed for years by the various social lenders profiled in the summary table in Appendix 1. CANZI should not monopolise the market. Rather, it should be a resource to existing and new social lenders by offering the following services:

- loan servicing (i.e. collecting loan payments)
- staff and board training on lending
- development of templates for applications, agreements and borrower technical assistance materials
- due diligence for loans beyond the social lender's comfort zone (for example, a small foundation might want to make a loan out of its endowment and seek advice from CANZI, or one of the existing angel funds might wish to grow and want guidance as it masters making more complex loans)
- advocacy – CANZI could coordinate a coalition of Kiwi social lenders and, as appropriate, give voice to the movement (more specific priorities might be to advocate for the creation of something like US New Markets Tax Credits[64] that has pumped millions of dollars into low-income neighbourhoods in the US, often as loan capital for social lenders).

Broadly available through partnerships

CANZI, through its direct and indirect lending roles, should eventually help make social lending available to any enterprise with a creditworthy plan and a social goal. The most efficient and effective way to accomplish this is for CANZI to have one office, centrally located, and then a dynamic network of relationships with other social lenders and local community groups. Key to making this work would be relationship managers who would be "circuit riders" to actively cultivate, nurture and

[64] See chapter five's discussion of Tax Policy and http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5

manage these relationships. The savings from having only one office would help offset the circuit riders' travel budgets.

Self-Help has had regional offices in North Carolina for approximately 20 years. Compared to Aotearoa New Zealand, which has almost 4.4 million people and is a little over 1,900 km by car from end to end, North Carolina has 12 million people and is 870 km. While certainly adding value, the Self-Help regional offices did not break even financially and were frequent drains on management time. A 2009 cost-benefit analysis has caused us to phase them out.

CANZI would identify and cultivate local or sectoral[65] partners from among the following types of organisations (the types of organisations are here for illustrative purposes and are not an exhaustive list):

- social loan funds[66]
- philanthropic trusts
- councils of social services
- early childhood associations
- local Māori development organisations
- Māori business facilitation services
- Pacific peoples' development organisations
- local government councils
- recycling networks.

CANZI would fully staff the larger loans that would be primarily to social enterprises and non-profits. The smaller social enterprise and non-profit loans, as well as the microloans and small business loans would likely be done in conjunction with a partner organisation with local knowledge, local presence and, in some instances, locally generated risk capital.[67]

What each organisation will do will vary depending on the loan size and if the partner has risk capital at stake. Before rolling out its partnership-lending component, CANZI would need to determine specific loan levels and underwriting criteria. Striving to be financially viable, CANZI would be unable to provide significant amounts of technical assistance for small enterprises all over the country.

Where there is no partner organisation, CANZI could use a streamlined automated underwriting process. Automated underwriting allows a borrower to provide

[65] By "sectoral" partner, I mean an umbrella, advocacy or support group for a particular sector, such as health care or recycling.
[66] CANZI would need to identify where there are effective social lenders covering an area or sector. In those cases, CANZI would not do any outreach and, if a borrower from that area or field were to come to CANZI, it would refer the borrower to the other social lender. This stance may surprise, but I posit that when social lending matures here, there will be more than enough borrowers to go around.
[67] A partner organisation, wanting to tap the expertise of CANZI without wanting to lend itself, could raise funds to serve as risk capital that would function just like the childcare example in chapter three. For Māori, this could be settlement funds.

information and then the lender can match the borrower data with a predictive model for repayment. For borrowers that meet the standard, the lender will verify the borrower's information and approve a loan. Although automated underwriting loses the personal touch and narrows the band of potential borrowers, it is a way of opening up credit access to some degree.

Respective roles of the intermediary and its partner

Local or sectoral partner	CANZI
Refer loans	Manage risk
Provide local information	Create underwriting guidelines for smaller loans
Provide technical assistance	Make loan decisions on bigger loans
Provide capital (community trusts, iwi, churches, local council)	Fund accounting and reporting
Process smaller loans	Bear the burden in foreclosure and denial of loans

In Appendix 4, I have included a more detailed breakdown of roles for different types of loans and partner relationships. Individualised partnership agreements would need to spell out these roles, a distribution of revenue streams (earnings on the risk capital, borrower interest payments, and establishment, processing and closing fees), and an accounting for losses between CANZI and the partner's risk capital.

Diverse

Māori, Pākehā, Pacific peoples, and other ethnic minorities would all need to feel ownership in the organisation. They would need to be treated with equal respect and consideration by CANZI staff and policies. A recurrent theme in the literature about Māori capital access is the need for self-determination and for a Māori lending institution. While understanding this preference, I also recognise that Aotearoa New Zealand's population may not support multiple social lending institutions of scale. I posit that CANZI, with strong partnerships and a diverse staff and board, is worthy of consideration by those advocating for a Māori bank.

Marketing materials, applications and closing documents would need to be available in some Pacific languages and Māori. All staff, regardless of their heritage would need to understand and honour the values of the various Kiwi cultures.

In support of a diverse approach, leading Māori businesspeople have noted their preference for hiring the best people, regardless of heritage, provided they understand and honour Māori culture and are willing and able to share their knowledge and skills with Māori.

A 2003 report on Māori economic development had this to say on cross-cultural institutions, "There is a sense that economic development using Pākehā institutions creates a risk of people losing their "Māoriness", when it is this Māoriness that is at the core of development. In some cases, genuine trade-offs may exist. However, in most instances, an apparent trade-off between Māoriness and economic success is in reality a failure of the existing institutions to reconcile the two better."[68]

With my outsider's eyes and ears, I believe that now is the perfect time to launch a diverse development organisation. As the injustices against Māori are being worked through, CANZI could be a place for collaboration in developing Aotearoa New Zealand's lower-income communities where there could be cross-sectoral, cross-regional, and cross-cultural learning.

A private, non-governmental organisation

The intermediary should be a private organisation. International experience has shown that governments are not good social lenders, except when they are lending to intermediaries. They are great at making grants and providing contracts to community organisations. According to Glen Saunders who is actively involved in social lending internationally, "when government does it [social lending] directly itself the process becomes politicised, prevents others getting involved, disrupts the arrangements already there and tends to be something here today and gone tomorrow".[69]

Government loan funds, even when run by seasoned, non-partisan public servants, have a way of becoming political. Phil Viles from the US government's Native American Capital Investment programme described in chapter two concurred when he said, "we did direct loans, but we weren't any good at it, it became politicized, etc".[70]

As public institutions, these same political pressures can make it hard for a government lender to foreclose on a delinquent borrower and the surest way to undermine a lending programme is for the borrowers to learn they do not really have to repay their loans. I suspect that one of the reasons that a Māori bank does not currently exist is that most of the schemes for it have been placed within government.

Furthermore, given the small size of this country and its dynamic political system, government programmes can come and go quite quickly. Elected governments often have short-term goals focused on the next election. Lending, on the other hand, is a long-term commitment (with some loan terms in excess of 20 years) and it takes a while to build a strong lending programme: to cultivate the staff, policies and systems to become an effective social lender. This level of commitment can be hard to sustain in government.

Strong intermediaries need not only to be private, but they also need to be operationally independent of government because, if the organisation is dependent on government support either for its capital or covering its operating expenses, the same political pressures can come into play.

Self-Help, which has governmental investors, is, however, operationally independent (i.e. Self-Help's employees' salaries are covered by net earnings from operations and periodic private grants). The benefits of this position were brought home when Self-Help's founder, Martin Eakes, was on the floor of the North Carolina legislature. A prominent politician pulled Eakes aside and said that if Self-Help did not make a loan

[68] NZ Institute of Economic Research (Inc.) (2003), p. 45
[69] Saunders (25 February 2010) pers. comm.
[70] Viles (16 June 2010) pers. comm.

to one of his constituents who had significant political influence, the politician would see that Self-Help's operational funding was cut. The loan applicant/constituent's business plan was too weak to merit a loan at that time, so Eakes confidently replied that he would hold a press conference the next day explaining what pressure he had received. He was able to take this high moral ground and turn down an inappropriate loan because of Self-Help's operating independence.

There are many valuable roles that government can play in social lending. These roles include outsourcing lending to an intermediary and ensuring that regulations assist the market to develop social lending. For a fuller discussion of ways that governments can support social lending, see chapter five.

Self-Help and Prometheus both utilise charitable affiliates, as the diagrams in chapter three illustrate. In Self-Help's case the founding parent organisation, the unregulated revolving loan fund and the advocacy arm are all charitable. We favour having the non-profit parent to hold us true to our mission and to provide investors' favourable tax treatment for their investments.

For Prometheus, its foundation is a significant but minority shareholder that receives dividends along with the other shareholders. It uses these dividends to make charitable donations within this country. The foundation is not, however, a significant activity within Prometheus' scheme. In addition, there is the Prometheus Guardian Trust, which has as its task to protect Prometheus' mission. It does this by holding a single special share, which necessitates that any new director or any change in the Prometheus constitution must first get the guardian trust trustees' agreement – they have a right of veto. Guardian trust trustees are people who have had a long involvement with Prometheus or have a clear connection to its task. They are generally people with a more cultural orientation to protect its social mission.

A model social enterprise

CANZI needs to be run like a business and a non-profit. This duality of purpose is what defines a social enterprise. Because it will be taking on more risk in its lending than a conventional bank, it needs extra risk capital, which is most likely obtained from philanthropic and government sources, especially at the early stages of the intermediary's existence. To protect their investment, funders generally want to invest in a non-profit because of its inherent mission alignment. Over time and with success, CANZI will accumulate retained earnings that can also be used to absorb losses.

An intermediary covers its operating expenses primarily[71] out of the net income from the loans it makes. In essence, the components of the net income are the revenue from the loan (interest and fees) minus the sum of all of the costs. Costs include 1) what it pays to its investors and 2) what it costs to make the loans, namely a) transactional costs, like processing the loan application and disbursing and collecting back the loan funds; b) technical assistance; and c) losses if the loan runs into trouble. In other words:

[71] It can also earn income on the idle funds and can take on other services, like consulting to community trusts on due diligence, servicing loans for existing social lenders that want help or administering a Māori guarantee programme.

(interest + fees)
– (payments to investors + transactional costs + technical assistance costs)
– loan losses
= net income from lending

If the loan capital is from grants and low-interest loans to the intermediary, then the interest rate the intermediary needs to charge the borrower can be lower, or the amount of technical assistance it can afford to offer the borrowers can be higher. If the intermediary can only attract market rate investments, then, philanthropy and government can elect to make operating grants to help cover the technical assistance costs or it can eliminate direct technical assistance from its model as some intermediaries do.

Subsidy is an important part of this model, but so is running the intermediary like a business. A well-run intermediary can be profitable, just as was the Ngāi Tahu Finance example in chapter two. What it does with those profits, however, is what determines its overall status.

In a conventional bank, the profits go to the shareholders and employees. If a product or service is not profitable, it generally is dropped. In the proposed intermediary, profits from one aspect could subsidise other areas. It is okay and even good to make a profit, so that an enterprise can offer services that are valuable, but that are not profitable.

Self-Help, for example, makes commercial loans ranging from a few thousand to a few million dollars. We do not make a profit on the smaller loans, but, when done well, the larger loans subsidise the smaller loans for an overall breakeven operation.

As a provider of technical assistance on running efficient organisations, CANZI itself must be well run. Cliff Colquhoun of CBEC, one of Aotearoa New Zealand's foremost social enterprises and an early and repeat borrower of Prometheus, has said, "Borrowing made me think like a business".[72]

Large enough to achieve economies of scale and offer leverage

As it is now, there are about 20 different Kiwi social lenders serving enterprises (i.e. not including the consumer finance social lenders) shown on the summary table in Appendix 1, each with administrative and overhead costs, plus their own loan underwriting and servicing costs.

In his 2006 report, *Microfinance funds in New Zealand*, Glen Saunders concluded "All but one, Prometheus Foundation, are not operationally sustainable – the income they generate does not cover their operating costs, although several of the smaller funds make extensive use of volunteers to run themselves which allows them to break even. They are also not capital sustainable. For both, they rely on grants and donations, or soft loans, to remain solvent or increase their size."[73]

[72] Colquhoun (24 May 2010) pers. comm.
[73] Saunders (2006), *Microfinance funds in New Zealand*, p. 2 paragraph 1.1.3

Some of these funds might choose to outsource some of their operations to CANZI, or to use their loan capital as risk capital with which to collaborate with CANZI (see the discussion in "Broadly available through partnerships" above), or to merge with the new intermediary. Others will and should prefer to remain independent and, as stated earlier, CANZI's policy would be to make referrals when and where a strong alternative exists.

As a larger lender working throughout the country and across sectors, CANZI offers its investors the benefit of risk diversification. For example, should organic farming be deemed unhealthy, and that borrower market experiences challenging times, CANZI's overall portfolio would suffer less because of its diversity. Likewise, should Ruapehu erupt, a Taupo-area specific lender could be devastated because so many of its borrowers would be hurt. CANZI, with a geographically diverse portfolio, would have performing loans to balance against struggling loans from the impacted region.

A strong fund manager

While some investors into CANZI will have particular communities they want served, others will have broader goals in investing. For example, an iwi may elect to make a restricted grant to the intermediary to promote small business lending for its iwi members. Understandably, the leaders would want to know that "their" money was helping "their" iwi members. While that iwi's funds would be restricted in use, their iwi members would have access to less restricted funds, say from an investor who is interested in promoting women in business, regardless of the women's heritage.

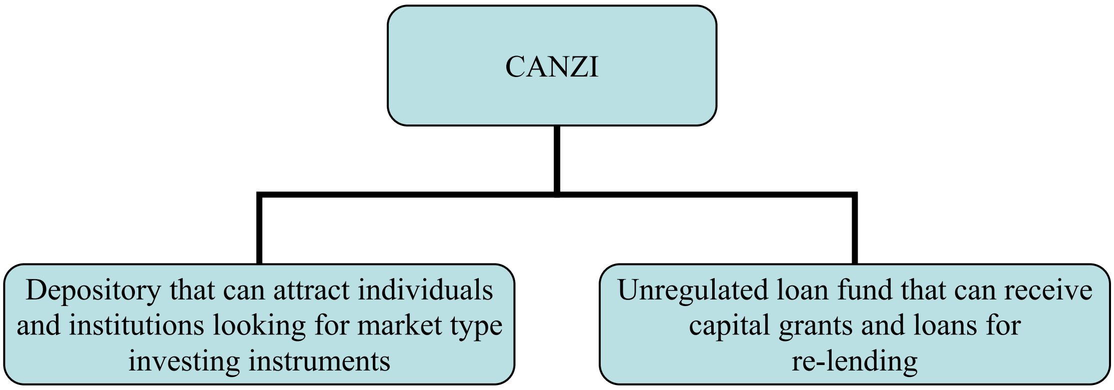
Self-Help's experience shows that most depositors support the overall social lending mission and so do not need to restrict their funds to, say environmental causes, in order to invest, thus adding more unrestricted funds to be leveraged by restricted dollars, as described in the iwi investor example immediately above.

An intermediary with a broad mission can leverage restricted funds with more general funds. It is essential, however, that the intermediary have strong accounting and reporting systems in order to guarantee all funders that their monies are being used as intended, and to meet multiple funders' reporting needs that will document the effectiveness of the funders' investments.

A depository

An important path to both scale and leverage is the incorporation of a bank or a non-bank deposit taker (NBDT) into the intermediary. A general definition of a depository is that it is a financial institution (such as a commercial bank, finance company or credit union) that is legally allowed to accept monetary deposits from consumers and comes under some level of regulation and accreditation. Regulation promotes discipline and accountability in the overall institution because it requires regular reporting and periodic audits. It also brings in new money because of the legitimacy of being a bank or NBDT.

In order to undertake the more innovative and, arguably, risky lending, CANZI will need a companion lending entity that is not regulated. That entity might hold the risk capital from local partner groups or grantmakers interested in supporting social goals, like the childcare funder example in chapter three. Risk capital is equity or funds available to absorb losses. It can be restricted to special purposes (e.g. childcare loans or loans made to members of an investor iwi) or unrestricted, for any type of loss. It generally shows as equity on the intermediary's books.



Funding

It is not possible to design a thorough capitalisation and funding plan without knowing more about the form CANZI will take. Will it start from scratch or emerge from a partnership between existing organisations and/or a reformulation of existing social lending players? These decisions are outside the scope of this paper. What I can do, though, is to suggest some funding ideas. I have organised my suggestions according to the different types of funding that it takes to run an intermediary.

Operating capital: Once established and at scale, it should be largely self-sufficient, but during its start-up, it should seek funding from grantmakers interested in social enterprises, economic development, poverty alleviation, Māori development and innovative philanthropic tools.

Risk capital:

- funds raised by local groups wanting to partner with CANZI, the funders might be statutory trusts, foundations, councils, wealthy individuals, religious groups or iwi
- the assets of existing loan funds that want to collaborate
- central government departments and their affiliates with sectoral interests such as Arts and Culture, Education, Environment, Social Development's various departments, Health, Housing, Labour, Pacific Island Affairs, Poutama Trust, and TPK
- lotteries and other Crown-funded grants schemes administered by the Department of Internal Affairs (DIA)
- other grantmakers currently lending or providing capital grants for facilities.

Loan capital:

- each of the funders listed above might want to make a loan, or they might elect to make a deposit, or both
- socially motivated individuals and institutions, like non-profits and religious institutions,[74] wanting a social return from their depository
- if the recommendation to create something analogous to New Markets Tax Credits is acted upon, then this instrument could attract significant capital for lending (see chapter five tax policy section).

Risks and disadvantages of CANZI

CANZI is a construct: a means to share ideas about how to grow social lending in Aotearoa New Zealand. I hope that the preceding sections show its advantages and the opportunities it offers. It is important, too, to state its risks and disadvantages.

Too big and complex: The potential scope of CANZI might not work. It might collapse from the weight of its ambition to:

- serve different markets (small businesses, social enterprises, non-profits, endowed trusts and foundations)
- be national in a country of multiple islands and remote places
- develop complex and variable partnerships to accomplish the lending, technical assistance, referral and advocacy
- combine smaller and larger loans and the different underwriting orientations they necessitate.
- be diverse – will differences between Māori and Pākehā business values prove too challenging to combine, will Pacific peoples and other ethnic minorities be marginalised, are two social lending markets (social enterprises and non-profits, and disadvantaged small businesses) so different that the needed lending cultures are incompatible
- both lend and build the social lending movement

Additionally, the evolving Kiwi financial markets and securities regulations might present insurmountable barriers.

Stifle competition and innovation: Would CANZI dominate other social lenders or would it empower them? It might well be a threat to the existing social lenders. It could be a competitor for grants, deposits and occasionally borrowers. In recommending a market-based strategy, however, I would be disingenuous, to not admit to supporting competition, which, I believe, would be healthy for the movement.

There are approximately 1,250 social lenders in the US[75] with a population of 310 million. This ratio of social lenders per capita would suggest that Aotearoa New

[74] 25 per cent of Self-Help's early depositors were religious institutions.
[75] Retrieved 1 June 2010 from http://www.opportunityfinance.net/industry/industry_main.aspx?id=234

Zealand could support 17 to 18 independent social lenders. The state of North Carolina, with a population of 12 million is closer in size. North Carolina is Self-Help's home state and it has a number of other active and innovative independent social lenders.

Lose the momentum: There is significant, palpable momentum to grow social lending here, with a number of initiatives already underway (e.g. community trusts ramping up their lending, Prometheus offering new services, the Māori Economic Taskforce plans, social enterprise advocates wanting to create a credit facility). Could the promise of CANZI delay or squelch these plans? Is an organic approach better and should funders support a variety of next steps that are already in the works, instead of supporting CANZI?

This momentum is precious and must not be wasted.

Guarantee for Māori enterprises on collectively owned land

I refer the reader to chapter two for a fuller discussion of the guarantee aspect of the proposed social lending system. A guarantee programme designed to attract loan capital to Māori enterprises on collectively owned land could use existing Māori assets to fund a loan loss reserve. The loans backed by the guarantee could be made by both conventional and social lenders.

This instrument would likely best fit the financing needs of smaller iwi- or hapū-level enterprises. Larger commercial endeavours' capital needs would likely exceed the capacity of a tool like this. Figuring out how to solve these larger capital needs is a primary focus of the Māori Economic Taskforce.

Smaller businesses are more likely to be sole-proprietorships or privately held corporations that would not qualify for the guarantee because they would not be on collectively owned land. For those that cannot access conventional financing CANZI could be a strong alternative.

Expansion of grassroots credit unions

My research revealed two Kiwi models for responsibly serving the low-income consumer finance market: faith-based programmes and credit unions. While I believe that CANZI could eventually serve this market, too, I do not recommend this path because the type of lending is quite different from the enterprise analysis needed for first two types of social lending and this third type of lending really benefits from the local presence of the provider.

I appreciate the quality offerings of the faith-based programmes. Their loans tend to be less expensive than the credit unions' loans because they are working with a largely volunteer workforce and their loan capital comes from church donations. In addition, depending on your perspective, the faith connection can be another value-add. The faith connection, for others, can also be a deterrent. In addition, the faith-based model usually lacks the integrated savings scheme that credits unions offer. Hence, my recommendation for best serving this market is to expand the number of local grassroots credit unions.

Credit unions like Awhi, profiled in chapter three and Aotearoa Credit Union, described in chapter two, are an inspiration and an under-utilised model here. A brief history of Kiwi credit unions shows a massive institutional consolidation. Their customer base has been relatively steady, though. From a peak of over 300 credit unions, there are now 30.[76]

A reason for this move to consolidate is the same reason I am recommending a relatively large centralised CANZI: economies of scale. Nevertheless, for this market, a local, distributed presence is important and, as Awhi, Aotearoa and a third low-income credit union, Westforce, show, it can work. It is, however, a struggle and is likely why there are so few. In the section on financial markets regulations in chapter five, I share some thoughts about how to lessen the regulatory burden.

Beyond the regulations, I recommend an advocacy and organising project to expand the availability of grassroots, low-income serving credit unions. The existing low-income credit unions could be strengthened and grow, new credit unions could be started, existing mixed income credit unions could be encouraged to grow the lower end of their market or to mentor smaller emerging credit unions. Two US organisations: the National Federation of Community Development Credit Unions and the North Carolina Minority Support Center model these types of initiatives. The former has just released a study, entitled *Low-Income Communities and the Great Recession: Financial Trends in CDCUs, 2009*. It paints an impressive picture.[77]

The New Zealand Association of Credit Unions (NZACU) could alternatively provide these services. They would certainly have the technical expertise. For example, they already have a booklet, available on their website, about how to start a credit union. Among its recommendations are the following capitalisation levels for a start up credit union:

- For standalone community credit union approximately
  - $3 million in savings (minimum to be viable)
  - Equity: at least 10 per cent of total assets
  - recommended: $3.5 million in assets.

- Supported industrial/special group credit union approximately
  - $1 million in savings (minimum to be viable)
  - equity: at least 10 per cent of total assets
  - recommended: $1.15 million in assets.[78]

One of the existing model low-income credit unions could also take on this organising role.

Credit union philosophy finds favour all over the world. Canadian and Australian indigenous communities, in particular, use credit unions effectively. In fact, Canada brought over the leadership of Awhi Credit Union to learn from its success. Awhi's and the other low-income credit unions' lessons need to be shared back home. Credit

[76] Retrieved 8 July 2010 from: http://www.nzacu.org.nz/Credit_Union_history.html

[77] National Federation of Community Development Credit Unions (2010), *Low-Income Communities and the Great Recession: Financial Trends in CDCUs, 2009*

[78] 'Setting up a Credit Union' p. 2, New Zealand Association of Credit Unions. Retrieved 12 June 2010 from: http://www.nzacu.org.nz/setting_up_a_credit_union.pdf

unions' collective, cooperative, self-help, structure should be particularly attractive with Māori cultural values. I encourage iwi leadership to consider this community development tool for their members.

Minister Turia opened her remarks at the meeting she convened on social enterprise and social lending in June 2010 by recalling her early days in Whanganui. She has long held the belief that the best way for communities to advance, is for them to invest in their own local solutions. She believes in restoring people to the essence of who they are – reinvigorating a spirit of self-determination and self-management.

The story she recalled was how, when the community saw a need for business development, they decided to do it themselves, the grassroots way, by each family taking one to two dollars per week from their pay cheques to provide the start-up capital for lending to small businesses. This story impressed me because of its embrace of grassroots collective action and the ethic of credit unions, which encourage their members to put aside a little regularly so that, down the road, they can improve their lives.[79]

Implementation

The ideas in this chapter suggest structures, relationships and systems that *might* evolve in Aotearoa New Zealand. Without doubt, as social lending grows here it will find unique Kiwi paths that suit unique Kiwi situations.

Wanting to capitalise on the current momentum, I end this chapter with some practical actions to help move along the path of a more robust Kiwi social lending environment:

- Create an Aotearoa New Zealand Coalition of Social Lenders.
    - Affiliate with Responsible Investment Association Australasia.
    - Set up caucuses within the coalition to cover each of the three types of social lending:
        - social enterprises and non-profits
        - disadvantaged small businesses
        - low-income consumers.
    - Identify opportunities to collaborate.
    - Develop an advocacy agenda.
- Reconvene the group that met with the Minister for the Community and Voluntary Sector to review this report and consider next steps that government might take to support the expansion of social lending.
- Assess government and private grantmakers' interest in investing in intermediaries and understand what their goals are.
    - Do some trusts want support for their lending (i.e., help establishing a programme, conducting due diligence on possible loans, and/or servicing loans)?

[79] Turia (17 June 2010) pers. comm.

  - Are there government-lending initiatives that might be better served by an intermediary?
  - Are there grant programmes that might be better served by social lending?

- Conduct a series of facilitated open-ended dialogues between those already active in social lending to identify gaps and find out where cooperation is possible with a view towards building CANZI or some enhanced social lending capacity.
- Share this report with the Māori Economic Taskforce, iwi, and other Māori leaders.
  - Listen to the taskforce's needs and ideas and identify opportunities to collaborate.
  - If there is interest, tailor the guarantee models described in chapter two and appendices 2 and 3 to suit Māori needs.
  - Explore collaboration with Poutama Trust on its loan guarantee scheme.
- Explore capital access needs for Pacific and other low-income entrepreneurs.
  - Share this report with Pacific and other low-income community leaders.
- Convene a summit on responsible lending.
  - The staff of the Ministry of Consumer Affairs are interested in facilitating this summit.[80]
- Assess credit union interest in expansion of service to low-income communities.
  - Promote the idea at the upcoming New Zealand Association of Credit Unions forum.
- Develop a government reform agenda starting with consideration of the ideas in the next chapter.

[80] Cole and Bidlake (6 July 2010) pers. comm.

5 WAYS THE GOVERNMENT CAN HELP

This chapter describes ways that government can support the growth of social lending in Aotearoa New Zealand. It is important to state, up front, that the initiative and operations of social lending should remain outside the government. As Robyn Scott, the head of Philanthropy New Zealand and one of my fellowship hosts articulated, “I've seen 'parachuted schemes’ which don’t go anywhere much (and lose money). I think it’s more about creating the context within which those with inherent entrepreneurial skills will act.”[81] As another advisor, Glen Saunders, expressed it, “Government is at its best when creating structures that allow the market to run better – clearing the road”.[82]

Following are a number of low-cost approaches for government to undertake and, in some cases, join with the private sector to catalyse and support social enterprises and social lending. Many of the recommendations have been tested overseas.

Financial markets regulations

I and other advocates for social lending believe in the benefits of a strong regulatory system. I applaud the current New Zealand Reserve Bank work around non-bank deposit takers (NBDT). I further applaud that it acknowledges the diversity of the deposit-taking sector. The Reserve Bank states that:

> The NBDT sector is an important component of the broader financial system because it provides funding to sectors of the economy that the mainstream banks often avoid, and provides alternative investment options for individuals and organisations.[83]

Note that the Reserve Bank FAQ on NBDTs includes an ability for them to:

> exempt entities or classes of entity from some or all of the NBDT requirements in circumstances where it would be unduly onerous or burdensome to apply the requirements. Exemptions may be granted on the basis of any terms and conditions that the Reserve Bank thinks fit.[84]

It would be helpful, nevertheless, for regulators to understand and recognise the differences between social lenders and other deposit takers.

For credit unions, there are currently a number of opportunities.

- Create a low-income credit union designation that would recognise the marginal revenue earning potential and public benefit from serving a predominately low-income customer base. Such a designation might reduce fees for required expenses and/or allow low-income credit unions to access funds otherwise not available to traditional credit unions. All Kiwi credit unions serve lower socio-economic groups. Most, however, have a mix of members, which makes them less financially constrained than those that focus on low-income communities. In the US, only low-income credit unions can

[81] Scott (10 February 2010) pers. comm.
[82] Saunders (20 February 2010) pers. comm.
[83] Retrieved 4 July 2010 from: www.rbnz.govt.nz/finstab/nbdt/3964224.pdf, p. 3
[84] Ibid, p. 4

accept non-member deposits and secondary capital. Low-income designation is an official action by a governmental supervisory authority. A US-based credit union qualifies if over 50 per cent of its members are "low income".

- Allow credit unions to accept deposits over $250,000. Regulators are considering a proposal to alter the cap and make it a percentage of assets, but I understand that the regulators have deferred an agreement on this and the issue has moved down their priority list.[85]
- Allow credit unions to undertake commercial social lending. Historically, credit unions have been providers of consumer finance. In 2007, the Friendly Societies and Credit Unions Act (1982) that governs credit unions was amended to allow them to add non-profits as members. In a March 2010 conversation with staff of the New Zealand Association of Credit Unions, it appeared that no credit unions were lending to non-profits.[86] More recently, one credit union is in the process of underwriting a loan to a non-profit.[87]

In addition, given last year's findings by the Inland Revenue Department (IRD) around overseas bank tax avoidance,[88] an opportunity exists to place a levy on foreign banks' profit taking from Aotearoa New Zealand. The proceeds of that levy could then support social lending. This might be a Kiwi version of the US Community Reinvestment Act (CRA). CRA encourages US banks to re-invest funds where they have depositors. It was created to stop the practice of redlining where banks would tell their loan officers not to lend in low-income minority communities. A result of this legislative mandate is that many banks fulfil their CRA requirements by funding social lenders.

Tax policy

Tax credits represent a powerful means of encouraging private investment in low-income communities. Many countries utilise this approach. In the US, for example, individuals and entities owing taxes are encouraged to invest in low-income communities through the New Markets Tax Credit programme.[89] These investments are generally made into social lending intermediaries, like CANZI, to re-lend to eligible borrowers operating in or on behalf of low-income communities.

The UK has a similar scheme, called Community Investment Tax Relief.[90] The tax relief is worth up to 39 per cent for the US programme and 25 per cent for the UK programme and is spread over seven and five years, respectively, starting with the year in which the investment is made.

In the Netherlands, the government created the *groenfund* tax regime whereby investment funds undertaking direct investment (i.e. not stock market investment) into 'green projects' incurred no tax. All the major banks as well as specialist social and environmental investors participated in raising substantial funding for such projects.

[85] Osborne (8 July 2010) pers. comm.
[86] Gavin (18 March 2010) pers. comm.
[87] Osborne (8 July 2010) pers. comm.
[88] Retrieved from: http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=10585008
[89] http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5
[90] http://www.hmrc.gov.uk/specialist/citc_guidance.htm

The government act extended *groenfund* to cover social projects, including projects with ethnic groups. This was beneficial in that mainstream financial institutions developed expertise in investing in new areas and raising funds for social projects. It also gave the Dutch government substantial leverage on the funding effectively used and allowed them to withdraw the scheme once a successful market had been established.[91]

Another approach for the government to consider is to provide a tax credit or deduction to lenders for interest foregone when they lend below market to charitable endeavours.

In the short run, there is a cost to the government in the foregone tax receipts, but, in the long run, if low-income communities get revitalised and social entrepreneurs develop innovative solutions to societal problems, then the additional taxes received and reduced social services costs, down the road, will offset the initial lost taxes.

Guarantees

I was surprised when I moved here to find so little use of loan guarantees. When well run, guarantee programmes are fiscally neutral and effective at leveraging private capital. They allow conventional and social lenders to stretch their underwriting criteria because they can request a guarantee, for a fee. If the borrower defaults, the guaranteeing agency will reimburse the lender for a portion of their loss. It is a risk sharing strategy. The guarantee levels in the US vary from 50 to 90 per cent.

Meeting with Joanna Gordon and Jeremy Corban at Treasury,[92] I learned that the use of government guarantees is rare and that there are only two central government guarantees at present and one of these is temporary.[93] They are the temporary retail deposit guarantee scheme and a set of guarantees offered by the New Zealand Export Credit Office (NZECO). According to NZECO's website, they "provide export credit guarantees to protect New Zealand exporters against uncontrollable events, and to enable them to offer extended finance terms to their international buyers. The NZECO aims to develop New Zealand's export trade".[94]

Wanting to understand why the use of guarantees was limited to export trade, I spoke with Jo Doyle, Manager of Industry and Regional Development at the Ministry of Economic Development (MED).[95] She helped put this paucity into context by sharing that Aotearoa New Zealand is ranked second by the World Bank, behind Singapore, for its overall ease of doing business and fourth on "getting credit." This is the same ranking, by the way, as the US.[96] She added, though, that Aotearoa New Zealand and Australia are the only two OECD countries that do not have some form of guarantee scheme for non-exporting firms.

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[91] Saunders, (15 May 2010) pers. comm.
[92] Gordon and Corban (8 June 2010) pers. comm.
[93] A third temporary guarantee was created to bolster the economy for wholesale funding but it is no longer in place.
[94] Retrieved from: http://www.nzeco.govt.nz/products/index.htm#nzeconot
[95] Doyle (8 July 2010) pers. comm.
[96] Retrieved from: http://www.doingbusiness.org/features/Highlights2010.aspx

Doyle also shared that one of the recommendations from an Employment Summit convened by Prime Minister Key at the end of February 2009 was to create a more general small business guarantee. The recommendation was considered and, at this point, no further action is planned.

The reason given for utilising a guarantee for export trade is that 97 per cent of Kiwi businesses have 19 or fewer employees. The small size of the country is viewed to contribute to the disproportionate number of small businesses and to be an instance of market failure. Since exporting opens growth opportunities for businesses, facilitating export opportunities is deemed more worthy of government intervention. The World Bank rankings offer support to this approach.

While I focus on central government roles in social lending in this report, I note that local governments use guarantees to back agencies doing work that meets their goals. I do not know the frequency and success of this strategy. Anecdotally, I have mostly heard of successful uses of the local government guarantee tool, but I have heard of losses.[97]

Despite this discussion of government guarantees, I do not recommend that government create a new loan guarantee at this point. When social enterprises gain momentum, however, I can imagine that compelling arguments may emerge in favour of creating a social enterprise guarantee scheme.

As discussed in chapter two, I recommend that Māori use some of their assets (such as Māori Trust funds or pooled settlement dollars) to back a loan guarantee programme for loans to Māori enterprises (for profit and non-profit) on collectively owned land. Poutama Trust is experimenting with a type of guarantee in partnership with Kiwibank: an exciting initiative to monitor. Depending on what happens with the Poutama Trust initiative, CANZI or the possible Māori Bank could be appropriate administrators of a guarantee. I would encourage whoever is the administrator to tap the expertise and experience of NZECO, the US Native American loan guarantee programme, also described in chapter two, and to peruse Self-Help's model in Appendix 3.

Charitable status and other legal matters

Consideration should also be given to whether social lenders would be able to successfully register as donee organisations so that donors could claim the associated tax benefits, and/or within the narrower category of being registered charities in order that the social lenders can benefit from the associated income and gift duty tax exemptions.

The legislation regulating charitable status in Aotearoa New Zealand is relatively new and under rapid growth. A systematic look at charities' laws, or the absence of them, culminated in the Charities Act of 2005 and the establishment of the Charities Commission. The law is largely based on UK models where the definition of charities accepted for most purposes goes back to Elizabethan times.

[97] Anonymous (29 June 2010) pers. comm.

Some models of social lending operate on a commercial basis, while others rely on charitable funding to subsidise the costs to borrowers, the risk, and the technical assistance. Although technical amendments to the Charities Act are currently being considered, a thorough review will be conducted by 2015. It will be important for the social lending movement to clarify whether changes would benefit the field or whether the distinctions between donee and charitable status are adequate.[98]

If changes are unnecessary, there might be a need for some information sharing. For example, although grantmakers are not limited to giving donations to registered charities, there is a misconception by many organisations that they must be registered with the Commission to get funding. It is actually up to each grantmaker to decide which organisations they fund. Very few limit themselves to registered charities. Even those who choose to only fund charitable purposes can still fund non-registered organisations as long as the *activity* they fund fits within the definition of charitable purpose.[99]

The charitability of economic development activities has proven challenging for the Charities Commission. It appears that such lending could be considered charitable if the borrower is poor. This would allow it to fit within the eligible category called "Relief of poverty" which states:

> In order to be charitable under this category, a purpose must:
>
> - be directed at people who are poor, in need, aged, or suffering genuine hardship, and
> - provide relief.
>
> A purpose is likely to be charitable under this category if it directs economic assistance toward the disadvantaged members of the community, or if the community as a whole is considered disadvantaged.[100]

These matters are in active discussion by the courts and the Commission, with important decisions pending as I write this paper.

It will also be important to consider what impediments there might be to private foundations and statutory trusts investing in small business development. It is my understanding that so long as the loan is from the trust or foundation's investment assets that the nature of the borrower is not an issue, but if the grant budget is involved, charitable or donee status may be an issue. I am aware of one statutory trust that intends to make small business loans to disadvantaged borrowers to promote economic development. I encourage others to offer these types of loans, either directly out of their assets, or by supporting an intermediary.

In addition to considering alternative legal forms and clarifying uses of the existing forms, the social lending movement would benefit from the following changes or considerations:

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[98] For a discussion of some aspects of this issue, please see attorney Mark von Dadelszen's thoughts in Appendix 5.
[99] Paton (2 August 2010) pers. comm.
[100] October 2009 guidance from the Charities Commission, 'Charitable purpose and community and economic development', p.2

- a review of trustee liability (i.e., when a non-profit borrows, do the trustees take on personal risks that go beyond their current scope of responsibilities)
- changes to Māori Trust and Poutama Trust legislation that might prevent the use of some of their assets to back a guarantee programme and/or for other social lending purposes
- allowing the grant funds managed and regulated by the DIA to be able to fund debt payments.

Unclaimed money

Unclaimed monies left in bank and non-bank deposit accounts could be a source of capital for social lending. Currently, the IRD receives the unclaimed money.[101] Ireland enacted legislation in 2001 and 2005 to use these funds for social purposes.[102] In July 2010 the new coalition government in the UK announced that they are creating a wholesale bank for social lending intermediaries using unclaimed monies. Their

> Big Society Bank will start with £60 to £100m in unclaimed assets... The money is to come from dormant accounts in banks and building societies, which have been estimated by the British Banking Association to contain £400m. Some third sector finance specialists estimate the sum could be ten times that... The bank is intended to provide wholesale finance to intermediaries that lend to non-profits, social enterprises and community groups.[103]

Funding

As I have tried to state clearly throughout this paper, the predominant view among Kiwi interested in developing the social lending sector is that the lending should be based outside of the government and not be dependent on government funding. There are, however, a number of ways that the government can help catalyze, support and grow the sector. While this section is called "funding", it primarily describes a redeployment of existing resources, and, by virtue of the recycling nature of loan funds, might save government money in some instances.

If the proposed social lending system is effective, I believe, like in the US and elsewhere, that government will want to provide some direct funding in order to help the private social lending system accomplish some of the government's goals. Once the social lending system was in place, a number of US federal and state-level departments started providing intermediaries with loan and risk capital because they saw how effective social lenders can be at helping the federal departments accomplish their own goals.

Recall the US childcare-funding example used in chapter two when I was describing an intermediary. In a like manner to that example, the following federal agencies

[101] Unclaimed Money Act 1971, Public Act, retrieved 10 July 2010 from: http://www.legislation.govt.nz/act/public/1971/0028/latest/DLM398423.html
[102] Retrieved from: http://www.pobail.ie/en/DormantAccounts/
[103] Ainsworth, D. (19 July 2010), *Third Sector Online*

partner with social lenders in the US by providing capital: the Small Business Administration and the US Departments of Agriculture, Education, Energy, Health and Human Services, Housing and Urban Development, and Treasury. Other levels of government (state and local) have also followed suit.

The following ministries and departments seem ripe to consider partnering with and possibly capitalising lending through CANZI and other intermediaries:

- **Ministry of Social Development** – Perhaps leveraging some of MSD's new Community Response Model's $90.5 million Quality Services and Innovation Fund.
- **Department of Internal Affairs** – Could a portion of the Crown and lotteries funds that they administer be used to make loans through an intermediary?
- **Ministry of Pacific Island Affairs** – This ministry might want to support the development of low-income serving credit unions in Pacific communities. They have already capitalised an intermediary, the Pacific Business Trust, to administer a small business loan programme. It served businesses run by Pacific people who could not otherwise access credit. When the default rate became too high, the trust halted the lending. The ministry continues to be interested in working with an effective small business-lending vehicle.[104]
- **Te Puni Kōkiri** – As chapter two illustrates, TPK appreciates the benefits of social lending. They, too, might want to support the development of low-income serving credit unions or other intermediaries.
- **Ministry of Agriculture and Forestry** – Looking at Prometheus Finances' successful track record lending to organic farms makes this ministry seem a possible partner.
- **Ministry for the Environment** – A member of the Community Recycling Network[105] suggested that the Waste Minimisation Fund Levy programme might leverage its impact by considering social lending.
- **Housing New Zealand** – The capital-intensive nature of housing suggests that this agency might be a good candidate to explore social lending.

It would also be worth looking at what governmental lending and facility-granting programmes already exist, and assessing whether the programmes could be delivered more effectively and economically by social lenders.

The Australian central and regional governments are actively supporting the development of private social lending intermediaries. As of this writing, they are seeking applications for a competitive process to provide seed capital to existing and emerging groups serving all three types of social lending.[106]

In the US, there is a department within the US Treasury devoted to the field, called the Community Development Financial Institutions (CDFI) Fund. It certifies CDFIs, provides loan and risk capital as grants, and makes grants for start-up and smaller

[104] Tukuitonga (26 March 2010) pers. comm.
[105] Colquhoun (9 April 2010) pers. comm.
[106] Saunders (21 July 2010) pers. comm.

CDFIs to acquire technical assistance. It also administers the New Markets Tax Credit programme mentioned in the section in this chapter on tax policy.

There are approximately 1,250 CDFIs in the US (not all are certified). Given the different scales of the US and Aotearoa New Zealand, it is unlikely that such a governmental infrastructure makes sense here, but I mention it as a testament to the degree to which the US government supports the field.

In the UK, the government has an extensive history of supporting social lending. Early, it participated in the creation of the "Local Investment Fund", a public-private partnership run by an independent group that provided high-risk loans and guarantees for loans to allow local community groups to raise capital to acquire assets for community purposes. Government representatives were involved as some of the directors of a non-executive governance board, but this was run independently of government and the majority of funding came from the private sector.[107]

A timely and compelling example of government support for social lending is the July 2010 announcement that the UK is creating a "Big Society Bank" using unclaimed assets. When he announced it, the UK Prime Minister David Cameron said, "that the bank will eventually make 'hundreds of millions' available to the sector.[108]

It is interesting to note that "Mr Cameron championed the bank concept as an 'incredibly ambitious' element of his manifesto during the election campaign. He said the institutions would 'strengthen and support social enterprises to help deliver our public service reforms' and 'provide new finance for neighbourhood groups, non-profits, social enterprises and other non-governmental bodies'. He added: 'This will provide social enterprises with the start-up funding and support they need to bid for government contracts or work towards delivering services under a payment-by-results model.'"[109]

Mr Cameron's public service reforms and ideas about "delivering services under a payment-by-results model" are similar to many of the approaches currently in favour in Aotearoa New Zealand. It is worth exploring whether or not this similarity might transfer to an eagerness to "strengthen and support social enterprises" through capitalising social lending intermediaries.

Social enterprises

Because most social lenders are social enterprises and because social enterprises are a primary borrower market for social lending, it is important to consider ways to improve the country's social enterprise environment.

Government support for social enterprise

Government does not have a position or policy around social enterprises. To facilitate the expansion of this model it would make sense for the government to develop such a policy.

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[107] Saunders (5 May 2010) pers. comm.
[108] Ainsworth, D. (19 July 2010), *Third Sector Online*
[109] Retrieved from: http://www.independent.co.uk/news/uk/politics/unclaimed-savings-to-fund-tories-big-society-bank-plan-2029414.html

Not surprisingly, social entrepreneurs are not clear where to look for central government support and guidance. Some have recommended the establishment of a minister or cabinet member who has specific responsibility for social enterprises.[110]

A current agency might be asked to broaden its coverage. That agency might be OCVS, which has been one of my two Axford fellowship hosts. It is based at the MSD, with a cross-agency relationship with the DIA's Local Government and Community Branch. DIA's Local Government and Community Branch or a department at the MED might also be appropriate homes for social enterprises. Regardless of which agency becomes its home, the staff would need expertise and background in social enterprise.

The UK government refers to voluntary and community organisations, charities and social enterprises as the "third sector". Their Office of the Third Sector falls under the Cabinet Office, which "sits at the centre of government and, with the Treasury, provides the government's co-ordination function. The Cabinet Office has an overarching purpose of making government work better and more efficiently."[111]

The following UK central government officials have social enterprises in their portfolios (given the new government after the 2010 general election, this may change, but it shows the central role that social enterprises play in the UK):

- Parliamentary Under-Secretary of State (Employment Relations, Consumer and Postal Affairs)
- Minister of State (Care Services).[112]

The walls between businesses and non-profits have not been as high overseas as they have in Aotearoa New Zealand where the majority of non-profits are volunteer run and have a strong donation/grant/government contract mentality. To help Kiwi non-profits that might aspire to think differently, the government might want to feature successful social enterprises and fund training for potential social entrepreneurs.

The training may not be a new government expense as capacity building and technical training of non-profits and the community sector occurs across the central government already. It could simply be a reprogramming of existing resources. These trainings might also support the replication of successful social enterprises in other communities.

A final suggestion for how government could help strengthen the social enterprise movement is to develop tools, as in the UK,[113] to measure the economic impact of social enterprises in the national and local economy. Such tools would need to measure employment, social, environmental and cultural impacts. This might be an excellent opportunity for a public-private partnership, with private funders supporting

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[110] Jeffs (10 May 2010) pers. comm.

[111] Retrieved: 9 July 2010 from: http://www.cabinetoffice.gov.uk/government-business/government-ministers-responsibilities.aspx

[112] Ibid.

[113] The Crown has sponsored a project called Social Return on Investment UK (SROI UK) that is working on ways to measure the impact of these entities and the funds invested in them.

the tool development and the government collecting and managing the data, as it already does in so many other areas. Similarly, OCVS and the community trusts jointly funded the Committee for the Study of the Non-profit Sector.[114]

Corporate structures

The current corporate structures and the laws that govern them may need to be revised in order to facilitate the work of social lenders and other social enterprises that cross the traditional bounds between business and charity**.** In the US, states and municipalities are starting to pass legislation to allow for "B Corporations" or social enterprises – the B stands for benefit. The UK is even more advanced and has a nationally authorised corporate form called a Community Interest Corporation (CIC).[115]

Procurement

Thoughtful procurement policies and practices can undergird the social enterprise[116] movement, especially in Aotearoa New Zealand where upwards of 40 per cent of the economy is government spending.[117] As Gary Kelk, a social enterprise expert who works with, among others, CBEC, pointed out in sharing this statistic, the government could multiply the impact of its dollars by working with social enterprises. First, it gets whatever service or product it is procuring, secondly, by procuring from a social enterprise, the government is supporting a mission-driven organisation, and thirdly, social enterprises are generally local, thus creating value in their communities due to their more localised spending patterns – especially on local wages and local services.

North Shore City Council has a model policy that incorporates social and environmental goals into its procurement practices. Their sustainable procurement toolkit measures a potential tenderer's environmental impact, as well as its social and economic activities, including engagement with staff, local communities and non-profits. The Auckland Regional Council and the Rugby World Cup 2011 have also adopted this policy and toolkit for their tenders. A few examples of goods and services procured this way include vehicles, electricity for the region ($14 million a year), and gas provision. To spread the practice even further, North Shore's team have worked with other local government agencies, including Environment Southland, Thames Coromandel, Hamilton and Rotorua.[118]

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[114] Lawrence (23 July 2010) pers. comm.

[115] Retrieved from: www.cicregulator.gov.uk

[116] Social enterprises are not a focus of this report, but this and the next policy suggestions are included because social enterprises are a primary market for social lending and because social lenders are social enterprises.

[117] Kelk (28 May 2010) pers. comm. The 40+ per cent figure comes from taking total crown expenses excluding losses retrieved from: http://www.treasury.govt.nz/budget/forecasts/hyefu2009/36.htm shows $83,821,000,000. The following link: http://www.treasury.govt.nz/budget/forecasts/hyefu2009/01.htm shows down the page that the nominal expenditure GDP half-yearly update 2009 shows $180,000,000,000. $83 billion divided by $180 billion = 46 per cent. For more on the economic benefits of supporting social enterprises see Gary Kelk's report, *Valuing recycle town measuring which bucket has the most leaks*. Retrieved February 2009 from: http://www.communityrecyclers.org.nz. See also: Sacks, Justin (2005), *Public Spending for Public Benefit: How the public sector can use its purchasing power to deliver local economic development*, London: New Economics Foundation

[118] Field (29 July 2010) pers. comm.

Dunedin South Labour MP Clare Curran introduced a Kiwi Jobs Bill in July 2010, which seeks to establish a government procurement policy that favours local industries. It also seeks to establish a commission of inquiry to compare government procurement policies with those in Australia and elsewhere and to determine whether the government can have such a preferential policy without breaking international trading obligations.[119] To the degree that social enterprises are local businesses, this might be an opportunity to support social enterprises. It will be important to monitor the work of any commission of inquiry that results.

There are other procurement and contracting initiatives in government that merit monitoring. OCVS is finalising a Code of Funding Practice that offers guidance in contracting to support the financial sustainability of social enterprises and non-profits.[120] MED is mid-way through a four-year Government Procurement Reform Initiative to:

- achieve cost savings
- build procurement capability and capacity
- enhance New Zealand business participation
- improve governance, oversight and accountability.[121]

Scotland's community benefit clause gives a preference in tendering to locally owned or social enterprises.[122] In Australia, government officials wanting to develop the social enterprise field have identified that social enterprises providing government services for fees are affected by the nature of the contracts. For example, the length of the contract makes a big difference to potential lenders: five years is borrowable against but 12 months is not. Another issue is whether the fee is an actual fee or instead a contribution to specific costs. Changes are expected.[123]

A review of procurement and contracting policies is a no-to-low cost approach for government to take in supporting social enterprises. In addition to encouraging procurement from local and social enterprises, the review should examine the lengths of contracts, prohibitions against non-profits accumulating reserves, how the funding flows (before or after delivery of the goods or services) and how the fees are derived. Where governments overseas have done so, it has had a transformative effect.[124]

[119] McEntee, C. (19 July 2010), *The Dominion Post*, p.C5
[120] Lawrence (29 July 2010) pers. comm.
[121] Retrieved 29 July 2010 from http://www.med.govt.nz/templates/Page____44092.aspx
[122] Pia (16 February 2010) pers. comm.
[123] For example, contracts only being for a year, not allowing non-profits to retain surpluses, or considering adding a preference for social enterprises in government procurement.
[124] Saunders (16 July 2010) pers. comm.

CONCLUSION

Kiwi social lending is developing as I write, which has made the research for this paper a dynamic experience. In the last two weeks of my writing this report, a Kiwi Jobs Bill was introduced into Parliament that could help social enterprises secure more government contracts. A credit union official mentioned that an iwi is considering starting a credit union to promote economic health for its whanau.[125] Minister Turia alerted her ministerial colleagues about the current developments in the field. And, David Cameron announced the creation of a Big Society Bank with monies from dormant or unclaimed deposit accounts.

As the social lending environment continues to develop, I hope this paper can serve as a legacy document, pulling together some of the history and current activity. I also hope that the perspective, history, ideas and recommendations contained herein can aid in the continued development of social lending in Aotearoa New Zealand.

I conclude with practical ideas drawn from the implementation steps at the end of the chapter about taking social lending to new levels, and a summary of the ways government could support that growth from the last chapter:

- Create an Aotearoa New Zealand Coalition of Social Lenders.
    - Affiliate with Responsible Investment Association Australasia.
    - Set up caucuses within the coalition to cover each of the three types of social lending:
        - social enterprises and non-profits
        - disadvantaged small businesses
        - low-income consumers.
    - Identify opportunities to collaborate.
    - Develop an advocacy agenda.
- Reconvene the group that met with the Minister for the Community and Voluntary Sector to review this report and consider next steps that government might take to support the expansion of social lending.
- Assess government and private grantmakers' interest in investing in intermediaries and understand what their goals are.
    - Do some trusts want support for their lending (i.e., help establishing a programme, conducting due diligence on possible loans, and/or servicing loans)?
    - Are there government-lending initiatives that might be better served by an intermediary?
    - Are there grant programmes that might be better served by social lending?
- Conduct a series of facilitated open-ended dialogues between those already active in social lending to identify gaps and find out where cooperation is

[125] Gavin (21 July 2010) pers.comm.

possible with a view towards building CANZI or some enhanced social lending capacity.

- Share this report with the Māori Economic Taskforce, iwi, and other Māori leaders.
    - Listen to the taskforce's needs and ideas and identify opportunities to collaborate.
    - If there is interest, tailor the guarantee models described in chapter two and in appendices 2 and 3 to suit Māori needs.
    - Explore collaboration with Poutama Trust on its loan guarantee scheme.
- Explore capital access needs for Pacific and other low-income entrepreneurs.
    - Share this report with Pacific and other low-income community leaders.
- Convene a summit on responsible lending.
    - The staff of Ministry of Consumer Affairs are interested in facilitating this summit.[126]
- Assess credit union interest in expansion of service to low-income communities.
    - Promote the idea at the upcoming New Zealand Association of Credit Unions forum.
- Develop a government reform agenda starting with consideration of the following ideas from chapter five.
    - Financial markets regulations:
        - inform Reserve Bank officials in charge of implementing NBDT reform about social lending
        - consider creation of low-income credit union designation
        - allow credit unions to accept deposits over $250,000
        - allow credit unions to make loans to small businesses and social enterprises
        - consider a Kiwi version of the US Community Reinvestment Act that might place a levy on foreign banks' profit taking from Aotearoa New Zealand.
    - Tax policy:
        - create a Kiwi version of the US New Markets Tax Credit programme or the UK Community Investment Tax Relief programme
        - offer a tax incentive to lenders for interest foregone when they lend below market to non-profit endeavours.

[126] Cole and Bidlake (6 July 2010) pers. comm.

- Charitable status and other legal matters:
    - build Charities Commission understanding of social lending and explore the charitability of altruistic lending and of social lending to promote economic development
    - review trustee liability around social lending (i.e., when a non-profit borrows, do the trustees take on personal risks that go beyond their current scope of responsibilities)
    - evaluate possible changes to the Māori Trust and Poutama Trust legislation that might prevent some of their assets from backing a loan guarantee scheme and/or for other social lending purposes
    - allow grant funds managed and regulated by the DIA to fund debt payments.
- Unclaimed money:
    - allow unclaimed money in bank and non-bank deposit accounts to be used for social lending.
- Funding:
    - identify which ministries and departments might capitalise lending through CANZI or other intermediaries. Possible agencies are:
        - Ministry of Social Development
        - Department of Internal Affairs
        - Ministry of Pacific Island Affairs
        - Te Puni Kōkiri
        - Ministry of Agriculture and Forestry
        - Ministry for the Environment
        - Housing New Zealand
- Social enterprises:
    - Government support for social enterprises:
        - develop a government policy around social enterprises
        - establish a social enterprise function within government
        - use non-profit training resources to support the development of social enterprise skills
        - measure the impact of social enterprises in the national and local economy.
    - Corporate structures:
        - review corporate structures and laws to eliminate barriers to social enterprise and consider a Kiwi version of the UK CICs.

- Procurement:
    - review government procurement and contracting policies to eliminate barriers to and facilitate growth of social enterprises and social lending
    - consider replication of North Shore City Council's or Scotland's policies
    - monitor the progress of the Kiwi Jobs Bill and the work of the proposed commission of inquiry, OCVS' Code of Funding Practice, MED's Government Procurement Reform Initiative and Australia's procurement policy redesign.
- Guarantee:
    - When social enterprises gain momentum, consider creating a social enterprise guarantee scheme.

Key to all of these steps is to increase the number of stakeholders. I hope this report can help.

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APPENDIX 1: SUMMARY OF AOTEAROA NEW ZEALAND'S SOCIAL LENDERS[127]

Social enterprises and non-profits/borrowing organisation has explicit social goals

Name	Status	Area Served	Description
Prometheus Finance	Active	National	New Zealand's oldest social lender (established 1983). In last five years, made 500 loans, totalling $8 million with minimal losses. Loans ($3,000 to $500,000) to individuals and organisations to develop recycling organisations such as CBEC in Kaitaia, and securing property for Forestry for Life that works with MSD's Work and Income and Massey University to provide transitional employment for ex-prisoners.
Community Trusts	Active	As indicated in the territories served by each trust	About half of the community trusts have made a loan or two, and interest in social lending is growing, as evidenced by attendance at workshops given on the topic in March, April, and June. Two trusts – Southland and Canterbury – have experience that is more extensive. Over the last 10 years, Southland Community Trust has made 20 loans, ranging from $9,000 to $3.4 million.[128] Canterbury Community Trust typically makes 12 loans per year in the $20,000 to $50,000 range, but their loans can go as high as $500,000.
Tindall Foundation	Active	National	Making loans for over 10 years at a very low level. The last 12 months has seen increased appetite, realising that social enterprise in New Zealand is beginning to take off and needing to go to a scale that donations will not serve adequately. They are now lending on a more considered and rigorous basis (e.g. for affordable housing) and are committed to developing this as a well-structured programme in the decade to come.
Christchurch Small Business Enterprise Centre	Active	Canterbury	This technical assistance group, founded in 1983, hosts two loan funds for small businesses and social enterprises (Just Dollars & an Angel Fund).

[127] Where not specifically cited, the data for this table comes from Glen Saunders' *Microfinance funds in New Zealand* (June 2006) or from the mentioned organisations' websites. Please note that this table does not include commercial banks' standalone efforts. I am aware, however, of a couple of banks that are exploring social lending, especially to social enterprises, but their plans are still in process and are not yet appropriate for inclusion here.

[128] Prendergast (27 April 2010) pers. comm.

Name	Status	Area Served	Description
Nelson Enterprise Loan Trust	Active	Nelson City/ Tasman District Council	Founded in 1997, the trust manages approximately $400,000 in assets and makes loans with an average size of $20,000. Loans are for job creation and social enterprise development.
Employment Generation Fund	Active	Auckland and Northland	Founded in 1992, the fund has assisted more than 150 ventures, made advances of more than $1.7 million and created 350 full-time equivalent jobs. The fund supports ventures that show prospects of employment generation that favour youth and some ventures not eligible for help from any other source. They manage $550,000 and loans average $15,000.[129]
Quaker Investment Ethical Trust (QIET)	Active	National	Established in 1989 by Quakers "to provide an ethical savings, investment and loan service in such a way as to reflect Quaker concerns". Total lending in 2009-2010, April 1 through 31 March, was approximately $288,000. They have $846,000 of loans outstanding and total assets are $1.9 million as of July 2010. Most loans go to people and organisations not able to secure commercial loans. Loans are for housing, businesses, clearing high interest bearing debt, environmental enhancement, and tertiary education.
Christchurch City Council's Community Organisation Loans Scheme	Active	Christchurch	Designed to help non-profit community, social, recreation, sports, arts, environment or heritage organisations improve or develop new or existing facilities and other major projects.
Sustainable Initiatives Fund Trust (SIFT)	Active	Canterbury	Since 2005, SIFT has helped develop new ways of reducing waste to landfill with grants, loans and equity investments to social enterprises. SIFT has also assisted businesses with loans to increase their scale and reach – all using recycled materials.

[129] Hickling (22 July 2010) pers. comm.

Name	Status	Area Served	Description
Ripple (NZ) Ltd	On hold	National	Ripple's initial strategy is to create social impact by providing affordable loans ($500,000 to $3 million) in two key impact sectors: affordable housing and community facilities. Established in 2008, Ripple Ltd was set up to raise funds to lend by issuing debt securities to private investors who seek a blended financial and social return. The financial crisis and loss of confidence in the financial investment market has put the project into recess until late 2010.

Small businesses owned by or hiring the disadvantaged/income generation and job creation are the social goals

Name	Status	Area Served	Description
Poutama Trust partnership with Kiwibank	In development	National	The purpose of such a partnership is for Poutama to be able to help businesses access Kiwbank's Business Banking services, by utilizing its investment services to provide funds as part of the businesses deposit to obtain the loans.[130]
Christchurch Small Business Enterprise Centre	Active	Canterbury	This technical assistance group, founded in 1983, hosts two loan funds for small businesses and social enterprises (Just Dollars & an Angel Fund).
Nelson Enterprise Loan Trust	Active	Nelson City/ Tasman District Council	Founded in 1997, they manage approximately $400,000 in assets and make loans with an average size of $20,000 for job creation and social enterprise development.
Employment Generation Fund	Active	Auckland and Northland	Founded in 1992, they have assisted more than 150 ventures, made advances of more than $1.7 million and created 350 full-time equivalent jobs. The fund supports ventures that show prospects of employment generation that favour youth and some ventures not eligible for help from any other source. They manage $550,000 and loans average $15,000.[131]

[130] Poutama newsletter October 2009, Poutama Trust. Retrieved 9 July 2010 from: http://www.poutama.co.nz/newsletter/zeronine/oct09.htm#3
[131] Hickling (22 July 2010) pers. comm.

Name	Status	Area Served	Description
Quaker Investment Ethical Trust (QIET)	Active	National	Established in 1989 by Quakers "to provide an ethical savings, investment and loan service in such a way as to reflect Quaker concerns". Total lending in 2009-2010, April 1 through 31 March, was approximately $288,000. They have $846,000 of loans outstanding and total assets are $1.9 million as of July 2010. Most loans go to people and organisations not able to secure commercial loans. Loans are for housing, businesses, clearing high interest bearing debt, environmental enhancement and tertiary education.
Mana Programme	Closed	Selected iwi	Over 20 years ago, Te Puni Kōkiri's predecessor granted funds to iwi authorities to make loans to small businesses. Without adequate guidance or training, most of the funds were poorly used, according to Māori leaders interviewed recently.[132] Where social lending skills were present, the programme was more effective, helping set up some good businesses and establishing some of the Māori Authorities and iwi organisations that exist today.[133]
Māori Womens Development Inc.	Active	National	The Māori Women's Welfare League launched this lending programme in 1987 with government capital and operating funds. It continues to make loans and provide technical assistance to Māori small business owners (men and women). Current data on their impact is not available.[134]
Ngāi Tahu Finance	Under re-evaluation	Areas where Ngāi Tahu do business	A small finance company, started in 1994 with proceeds from the Mana Programme, it focuses where small businesses will generate sustainable employment opportunities, not only for their Ngāi Tahu owners but also for Ngāi Tahu generally.
New Zealand's International Aid and Development Agency	Under re-evaluation	Outside Aotearoa New Zealand	This agency has a long history of supporting micro-enterprise development overseas and could be a useful model for government support of lending schemes within its country.

[132] Anonymous (26 April 2010) pers. comm.
[133] Mika (10 July 2010) pers. comm.
[134] Groves (2000) p.17 reports that as of 31 July 1999 they had made 120 loans for $693,200 creating 255 jobs and providing technical assistance to 349 other businesses. I have been unable verify any more up-to-date information.

Name	Status	Area Served	Description
Women's Loan & Angel Funds	Active	Various cities across the country	This national network of funds provides small zero-interest loans and technical assistance to women entrepreneurs. Volunteers often run the funds. More information is available at www.angelfund.org.nz/links.htm

Low-income individuals using loan sharks/social goal is to help break the cycle of poverty

Name	Status	Area Served	Description
Awhi Credit Union	Active	Bay of Plenty	Māori-led, it has 1,900 members. Awhi puts a premium on developing financial literacy and helping their members better manage their household finances. They are starting a credit union at the Rotorua Girls College in recognition of the need to start financial training early. See their profile in chapter three.
Aotearoa Credit Union	Active	Auckland area, Hamilton, Porirua, Wanganui	Māori-led, with 15,000 members, they serve both Māori and Pacific members with a common loan amount of $100, often to pay basic life expenses. See Chapter two for a fuller description of their operations.
Westforce Credit Union	Active	Auckland and Northland	Founded in 1981, with assets of $22 million and 6,600 adult members today. 85% are low-income, with 75% of those being on benefits. 50% are Māori and 35% Pacific peoples.[135]
Christian Budgeting Services	Active	Various places in NZ	Low- to no-interest loans provided in context of debt restructuring to low-income people in financial distress.
Quaker Investment Ethical Trust (QIET)	Active	National	Established in 1989 by Quakers "to provide an ethical savings, investment and loan service in such a way as to reflect Quaker concerns". Total lending in 2009-2010, April 1 through 31 March, was $288,000. They have $846,000 of loans outstanding and total assets are $1.9 million as of July 2010. Loans are for housing, businesses, clearing high interest bearing debt, environmental enhancement, and tertiary education.

[135] Punter (20 July 2010) pers. comm.

As yet unnamed	In development	South Auckland	A pilot project is scheduled to be launched in 2010.

APPENDIX 2: NATIVE AMERICAN LOAN GUARANTEE ELIGIBILITY CRITERIA[136]

- Project must have a positive economic impact to the tribal reservation or service area.
- The percentage of a loan that is guaranteed or insured is the minimum necessary to obtain financing, but may not exceed 90 per cent of the unpaid principal balance and interest.
- Borrower must contribute at least 20 per cent in equity to the proposed project.
- Loans may be used for a variety of purposes including operating capital, equipment purchases, business refinance, building construction, and lines of credit.
- The maximum loan that can be guaranteed for individuals is $500,000; however, the programme can guarantee loans of greater amounts for tribes, tribal enterprises, or business entities, subject to program and policy limitations.
- The maturity of a loan is determined by the lending institution, based upon the use of the loan proceeds and the repayment capacity of the borrower; however, the loan term cannot exceed 30 years.
- Interest rates are determined by the lending institution but are subject to reasonable limitations established by policy.
- The lending institution must pay a one-time premium payment of two per cent of the guaranteed portion of a loan; however, the lending institution may charge the premium to the borrower as a one-time fee, or add the premium to the loan amount.

[136] DCI Brochure (1 June 2010). Retrieved from: http://www.bia.gov/WhoWeAre/AS-IA/IEED/DCI/index.htm

APPENDIX 3: SELF-HELP'S 2008 LOAN GUARANTEE TERMS AND CONCEPT PAPER

Terms for Lenders

Purchase	
Guarantee %	60% of loan losses.
Guarantee Term	Through entire term of the loan
Guarantee Description	In case of foreclosure, Self-help will cover 60% of loan losses after the lender has liquidated the collateral and collected recoveries. Self-Help will reserve the right to liquidate the collateral, or approve a liquidation plan by the lender.
Guarantee Funding Source	Pooled guarantee backed by an \$8.5m grant to be raised. The maximum amount of total guarantees will not exceed \$52.2m at any time. The full guarantee is backed by Self-Help net worth.
Burn-down Provision	None. Exception: See Underwriting Standards-balloon term.
Program Fees	2% upfront, 1% annual fees on guarantee.
Technical Assistance	Self-Help will provide ongoing technical assistance to the borrowers; especially about financial management, (*this is contingent on securing grant funds for technical assistance).*
Eligibility	For-profit and non-profit lenders (Bank, CDFI, other)
Borrower Eligibility Requirements	Borrower: Minority-led, independent public schools or CMO/EMOs. Definition of minority-led school: Leadership and founder and/or majority of board members minority. Purpose: School facility purchase, construction, and renovation. Only conditional guarantee during construction period. Geography: National
Underwriting Standards	Min Guarantee Amount: \$300,000 Max Guarantee Amount: \$4,800,000 Collateral: Lender to have a 1st lien on the property Interest Only period: Up to 1 year Balloon: No balloon. If there is a balloon at the end of the loan term, the guarantee will burn off over the term of the loan. Equity requirement: 0-10%
Underwriting Process	Initially to be performed by the lender. Self-Help will review packages from the lender.
Monitoring Requirements	Lender to submit analysis of annual audits, quarterly budget reports, and annual site visit reports to Self-Help.

Leasehold Improvement	
Guarantee %	80% of loan losses.
Guarantee Term	Through entire term of the loan.
Guarantee Description	In case of default Self-help will cover 80% of loan losses.
Guarantee Funding Source	Pooled guarantee backed by a \$1.4m grant to be raised. The maximum amount of total guarantees will not exceed \$4.8m at any time. The full guarantee is backed by Self-Help net worth.
Burn-down	The guarantee will burn down with principal payments only.
Program Fees	2% upfront, 1% annual fees on guarantee.

Technical Assistance	Self-Help will provide ongoing technical assistance to the borrowers, especially about financial management.
Eligibility	For-profit and non-profit lenders (Bank, CDFI, other).
Borrower Eligibility Requirements	Borrower : Minority-led independent public schools or CMO/EMOs. Definition of minority-led school: Leadership and founder and/or majority of board members minority. Loan purpose: Leasehold Improvement Geography: National
Underwriting Standards	Min Guarantee Amount: $80,000 Max Guarantee Amount: $500,000 IO period: Up to 1 year. Balloon: No balloon. If there is a balloon at the end of the loan term, the guarantee will burn off over the term of the loan.
Underwriting Process	Initially to be performed by the lender. Self-Help will review packages from the lender.
Monitoring Requirements	Lender to submit analysis of annual audits, quarterly budget reports, and annual site visit reports to Self-Help.

Concept Paper: Charter School Opportunity Guarantee Program
Self-Help Ventures Fund

Executive Summary: Charter schools have over the past 15 years provided many high-quality educational opportunities for students of color, who make up over half of the students in charter schools nationwide. Yet only about one third of charter schools are minority-led, and many of those schools struggle to obtain the financial resources they need. Initiative, innovation, and educational expertise are not lacking in minority-led charter schools as much as adequate access to capital and financial expertise.

Self-Help stands ready to launch a pilot facility loan guarantee program which will leverage $93 million in nationwide lending to high-performing charter schools led by people of color.[137] Recognizing that a stable and affordable physical setting is a primary driver of long-term charter school success and sustainability, our goal is to stimulate lending by banks and community development financial institutions (CDFIs) that will enable approximately 50 schools to acquire, construct, or improve their facilities. We estimate that the program will impact more than 25,000 students, predominantly students of color.

The Charter School Opportunity Guarantee Program will leverage $87 million in financing by conventional banks and CDFIs for facility purchase, new construction, expansion, or renovation, as well as $6 million in financing for leasehold improvements for schools that are renting facilities. The program will provide 60% guarantees for loans used to purchase, construct, or renovate facilities, and 80% guarantees for leasehold improvements, for overall guarantees totaling $57 million.

A nongovernmental guarantee program of this scale for charter schools would be unprecedented, and will be possible only with substantial philanthropic support. We plan to pursue $10 million in grant dollars for the initial capital to fund the pool and

[137] Defined as leadership, founder, or a majority of board members being people of color.

$2 million to provide technical assistance to schools. Self-Help would put at risk $47 million of its own assets to cover potential additional losses under the guarantees. Self-Help believes that its net worth and experience make it unique among CDFIs in its ability to leverage grant funds for the benefit of students of color. The initial grant and Self-Help's capacity to cover additional losses will encourage a wider range of financial institutions to take additional credit risk and invest directly in high-quality schools led by people of color.

I. Self-Help's Leadership as a Charter School Lender

Self-Help is one of the founders of the community development finance industry. Since 1980, we have provided $5.5 billion in financing to more than 57,000 small businesses, nonprofits, and homebuyers. Our commitment to charter school lending grows out of our mission to create ownership and economic opportunities for minorities, women, rural residents, and low-wealth families. Self-Help recognizes that development of a community's human assets is as important as developing its financial assets. To that end, we have made 67 loans to charter schools that serve disadvantaged students and communities nationwide, providing more than $100 million in financing over the past 11 years. These loans have enabled schools to create or improve more than 22,000 student spaces. We make it a priority to serve emerging high-performing, independent schools that are in their early stages, the very schools that have the greatest difficulty in accessing traditional sources of capital. We have found that these borrowers represent the best aspects of the charter movement, with passionate leadership, an entrepreneurial spirit, and often the potential for future growth and replication.

From its very beginning, Self-Help's lending has been concentrated on promoting ownership and leadership among people of color. For example, 45% of Self-Help's home loans are made to people of color, as compared to 27% of home loans made by all lenders. People of color receive 45% of Self-Help's small business loans, although minority-led firms make up only 18% of businesses nationwide. Reflecting this mission orientation, we have taken a special interest in examining the challenges faced by minority-led schools--more than half of our borrower schools are led by people of color.

As our charter lending has grown, so has our commitment to leveling the playing field and giving schools in disadvantaged communities equal access to the resources that they need. We offer advantageous and flexible loan terms, and we provide more than 2,000 hours in technical assistance annually to help schools solidify their business plans, strengthen their governance and financial management, and navigate the difficulties of complex construction projects.

Furthermore, Self-Help works extensively at the state and national level to strengthen the charter school movement, with particular concern for the needs of low-income and minority students and communities. We are active participants in national charter school organizations and are members of charter school resource centers and charter school associations in our target states. Each year, we lead dozens of presentations and conduct workshops at state and national conferences regarding issues important to charter schools, including facility financing, construction planning, governance, diversity, and community involvement. Laura Benedict, our vice president in charge of overall commercial lending, is treasurer of the board of the National Alliance for Public Charter Schools.

Self-Help has a history of successful, large-scale relationships with conventional lenders, a factor that will be essential to the success of the Opportunity Guarantee Program. Since 1994, we have operated the Affordable Home Loan Secondary Market Program which has helped promote responsible lending for homeownership on a national scale. Partnering lenders sell us loans they have made to low-wealth borrowers and then use the liquidity to make financing available to additional qualified borrowers. We assume the credit risk on the loans and sell them to Fannie Mae. Through relationships with 35 lenders, we have purchased $4.5 billion in loans and enabled more than 50,000 families to become homeowners in 49 states. This initiative was made possible by a $50 million loss reserve grant from the Ford Foundation. In addition, Self-Help participates jointly with banks to make facility loans to businesses under the Small Business Administration's 504 Loan Program. We have worked with 50 banks to provide more than $190 million in financing and facilitate the creation of more than 5,000 jobs– another example of our successful partnering with other financing institutions.

II. Barriers Faced by Charter Schools Led by People of Color

The need for quality educational choices in communities of color has been a substantial driver of growth in the charter school movement. A full 56% of the more than one million charter school students nationwide are students of color. Yet, leadership demographics are not representative of charter school populations, with only 32% of charter school principals being persons of color.[138] This imbalance underlines the importance of developing minority school leadership and providing those leaders with the financial tools and knowledge to make their schools successful.

Facility acquisition is often the most difficult operational challenge faced by charter schools, particularly minority-led charter schools. Too often, facility problems force schools with excellent academic programs to close their doors or prevent high-potential schools from opening at all. Lack of financial expertise, inadequate start-up capital, and limited access to lending networks are all contributing factors to these difficulties. Facility challenges can also adversely affect the quality of a school's instructional program by siphoning off financial resources and the limited attention of school leaders and board members.

Charter school leaders must have both educational and business expertise, yet Self-Help's research into minority-led schools indicates significant imbalance between these capacities. Among a sample of 70 charter school loans made by Self-Help and other CDFIs, schools led by people of color were academically stronger, with 81% of schools meeting Adequate Yearly Progress (AYP) at year of loan approval, as opposed to 55% for white-led schools. Yet, in a sample of 50 Self-Help loans, 100% of the white-led schools had board or staff business expertise, as opposed to only 43% among minority-led schools.

[138] Source: Alliance 50-State Survey, April 2006 and 2003-2004 US Dept. of Education, National Center for Education Statistics, School and Staffing Survey

Survey and focus group results showed concerns among leaders of color that reflect imbalance on these factors between minority- and white-led schools. Many leaders identified a shortage of financial management experience, lack of knowledge of the facility financing process, and limited access to networks of conventional lenders, CDFIs, and foundations. These findings are hardly surprising, given that many minority-led schools operate in low-wealth communities that remain outside of the financial mainstream.

III. Improving Financial Capacity and Access to Capital

A. Technical Assistance

Improved access to technical assistance for financial planning, facility financing, and the construction process will be critical to the future success for schools led by people of color. Given the dramatic growth of charter schools in communities of color, the charter movement must work to increase the capacity of current leaders and build a pipeline of well-prepared African-American and Latino professionals.

Self-Help is committed to helping to meet this need for technical assistance, either with a new collaborative organization or with a network of consultants and other resources. The effort will focus on participants in the Opportunity Guarantee Program, but all schools led by people of color will be able to access the services. Our initial efforts on this front will focus on an assessment of the needs of school leaders, an understanding of the technical assistance services already available, and a plan for filling the necessary gaps. We will explore how the program can complement and/or collaborate with similar resources such as LaRaza, LISC, Charter School Growth Fund, New Schools Ventures Fund, and New Leaders for New Schools. We will draw lessons from NCB Capital Impact's successful technical assistance program, which aided schools in Florida and Minnesota. In addition, we will collaborate closely with Partners for Developing Futures, which is an affiliate of the Charter School Growth Fund designed to address the under-representation of people of color in leadership positions in charter schools and charter school networks.

The ultimate goal of the initiative will be to deliver one-on-one consulting for schools in the areas of capital markets, financing, financial management, governance, facility planning and development, and grant raising. The initiative has the potential to cast a wider net with regional trainings for school leaders, leadership trainees, Charter Support Organizations (CSOs), financial consultants, and back office vendors, focusing on financing options, loan packaging, and cultural competence. In addition, the initiative would provide charter lending training for financial institutions led by people of color, including CDFIs and minority banks.

B. Facility Loan Guarantee Program

Far too many charter schools struggle with the challenge of obtaining a permanent facility, and Self-Help's research shows that it is of particular concern for schools in communities of color. The key to clearing this hurdle is access to affordable financing from lenders that are comfortable with the specialized risk of charter lending. Compounding the challenge is the reality that minority-led schools are often located in disadvantaged communities where access to capital has long been limited.

Self-Help's proposed Charter School Opportunity Guarantee Program seeks to:

1. Bring new lenders to the table to finance schools led by people of color;
2. Build the confidence of current charter school lenders in reaching out to high-potential schools that do not meet their stricter underwriting standards for collateral and/or financial management experience; and
3. Increase the availability of capital for early stage and startup schools that need to make improvements on leased facilities but lack adequate collateral or operational track records.

Self-Help will offer two guarantee products:

1. Guarantee for Purchase, Construction and Renovation Loans: This product would leverage grant funds at more than 10:1, providing $87 million in targeted financing of facility purchases, expansions, and renovations for an estimated 29 schools. Self-Help will guarantee 60% of loan losses after the lender liquidates the collateral and collects recoveries. The program will be similar in structure to federal USDA and SBA programs that are already familiar to many lenders. The pooled guarantee would be backed by $8,456,400 in grant funds, with any additional losses backed by Self-Help's own net worth.
2. Guarantee for Leasehold Improvement Loans: This product would leverage grant funds at more than 4:1 to provide $6 million in financing for an estimated 24 schools making improvements to leased facilities. Self-Help would guarantee 80% of loan losses. The pooled guarantee would be backed by $1,440,000 in grant funds, with any additional losses backed by Self-Help's own net worth.

The amount of purchase and leasehold guarantees is an estimate, and the balance between the two may vary based on demand. The number of borrower schools may also vary due to loan sizes.

Strengths of the Program:

- Leverages grant funds 10:1 for purchase lending and 4:1 for leasehold lending;
- Reduces the likelihood of schools closing due to facility or financing problems;
- Combines with technical assistance to strengthen leadership by people of color, particularly in the area of financial management;
- Strengthens start-ups and smaller independent charter schools that can grow into Charter Management Organizations (CMOs) and/or provide replicable models;
- Allows very early stage schools to make leasehold improvements;
- Increases lender confidence due to backing by the full faith and credit of Self-Help;

- Increases the participation of conventional lenders in charter school financing and leverages their community networks, marketing, and underwriting capacity;
- Allows lenders already in the charter finance field to reach more minority-led schools, including lenders that are not awardees of Department of Education Credit Enhancement for Charter School Facilities grants;
- Offers a streamlined underwriting process which is informed by Self-Help's extensive charter lending experience;
- Fills a gap between 15% guarantees (based on loan amount) already offered in the charter finance field and 90% guarantees (based on losses) offered by the USDA, which are only available to rural schools; and
- Limits amount of legal fees charter schools will pay to participate in the program. Self-Help will not charge for its internal attorneys' time, and we will work to limit fees charged by outside counsel.

Program Goals:

	Purchase	Leasehold	Total
Grant Requested			
Guarantee Funds Grant	$ 8,456,400	$ 1,440,000	$ 9,896,400
Start-up Expenses Grant			103,600
Proposed total grant request			**$ 10,000,000**
Goals			
Target # of schools - total	29	24	53
Target average # of schools - per year	6	5	11
National market capture of minority-led schools with permanent facility needs	3.5%	7%	
Leverage ($ of loan per $1 of grant)	10:1	4:1	
Total loan volume target	$ 87,000,000	$ 6,000,000	$ 93,000,000
Total guarantee target	$ 52,200,000	$ 4,800,000	$ 57,000,000

Preliminary Timeline:

March 2009	Pilot program ready to be launched
CY 2009	7 loans guaranteed
CY 2010	11 loans guaranteed
CY 2011	11 loans guaranteed
CY 2012	11 loans guaranteed
CY 2013	13 loans guaranteed

Measures of Impact:

Self-Help has a 28-year history of achieving and measuring the large-scale impact of our lending activities. Our staff includes a full-time Impact and Research Associate with the sole focus of quantifying and analyzing Self-Help's benefit to the communities that we serve. We expect to measure the following impacts:

- Amount of lending leveraged and number of schools served;
- Number of startup and early stage schools served;
- Number of student spaces created and maintained by borrower schools;
- Percentage of students of color;
- Percentage of low-income students;
- Academic success and longevity of borrower schools;
- Number of new lenders brought into the charter school finance field through the program;
- Number of school leaders and schools that benefit from the program's technical assistance; and
- Hours of technical assistance delivered by Self-Help staff.

Risk Assessment:

Likelihood of Default: To assess default risk, Self-Help looked at industry-wide charter school closure data, analyzed its own lending experience and underwriting criteria, and adjusted for the special risks of the guarantee program. According to Center for Education Reform data, during the 15-year history of charter schools 560 have closed while 4,147 are currently operating. That raw statistic reflects substantial risk, but it shows only one factor in understanding the true likelihood of default and the reluctance of many lenders to make charter school facility loans in disadvantaged communities.

For this program, we have estimated an aggregate default rate of 27% over 20 years for facilities acquisition and construction loans. For leasehold improvements loans, we project an aggregate default rate of 30% over 20 years. Factors we considered in estimating risk include:

- Loan terms under the program will range up to 20 years, yet there is inadequate historic charter school lending data to estimate losses over that period.
- The program will consist largely of loans that lending institutions considered unfeasible without the guarantee.
- The program will target independent early stage and startup schools, schools with little initial capital and limited financial networks, schools with a deficit of financial management experience, and schools with facilities that have limited value as collateral. We will not exclude more mature schools or those that are part of Charter Management Organizations (CMOs), but it is our sense that their access to capital is less challenging.
- Leasehold improvement loans will target very early stage schools with little or no collateral.
- Risk assessment must take into account the potential for negative changes in the federal and state policy and regulatory environment for charter schools over the next 20 years. Such changes could reduce resources available to schools and/or result in a climbing rate of school closure.

- Severe and long-lasting economic recession could lead to significantly higher losses.
- The program provides up to $57 million in loss guarantees (60% of the $87 million in purchase lending, plus 80% of the $6 million in leasehold lending.) If we have under-estimated risk and losses exceed the $10 million grant, Self-Help will be liable for any additional losses up to $47 million.

Losses from Default: Charter schools typically purchase properties such as old school buildings that have limited alternative uses and thus a restricted resale market. As a result, we estimate the loss given default to be 60% of the loan amount for purchase, construction, and renovation loans. For leasehold improvements loans, we have assumed that the school has virtually no collateral, and thus estimated losses would be 100% of loan amount.

Loss Calculations for the Entire Guarantee Program: As an example, with a default on a $1 million loan used to purchase property, the lender would typically take a loss of $600,000, of which 60%, or $360,000, would be the responsibility of Self-Help under its guarantee. For the overall $87 million purchase guarantee program, using an aggregate default rate of 27% over 20 years, total loan defaults would equal $23.5 million. Lenders would likely experience an average 60% loss after liquidation and recoveries, or $14.1 million. Self-Help would pay out under its guarantee 60% of that amount, or $8,456,400. For the $6 million leasehold guarantee program, given a 30% aggregate default rate over 20 years, lenders would experience $1.8 million in losses, with Self-Help paying out under its guarantee 80%, or $1,440,000. Self-Help plans to request $9,896,400 in grant funds to cover the anticipated losses projected in this scenario under its guarantees, and will commit its own net worth to cover any additional losses if these assumptions prove inadequate.

Summary of Loss Calculations:

Purchase Program	
Total lending amount	$87,000,000
Projected defaults over 20 years (27%)	$23,460,000
Projected lender losses (60% of defaulted loan amount)	$14,094,000
Self-Help guarantee paid out (60% of lender losses)	**$8,456,400**
Leasehold Program	
Total lending amount	$6,000,000
Projected defaults over 20 years (30%)	$1,800,000
Projected lender losses (100% of defaulted loan amount)	$1,800,000
Self-Help guarantee paid out (80% of lender losses)	**$1,440,000**
Total projected guarantee paid out by Self-Help	**$9,896,400**

APPENDIX 4: INTERMEDIARY PARTNER ROLES

What follows shows the different roles for partners who are co-investors and those that are not. In the examples that follow, the partner organisation is assumed to be a technical assistance provider as a core part of its services.

Loan-making for smaller loan with partner organisation as co-investor

	Partner	CANZI
Outreach and marketing	✓	
Application processing	✓	
Visiting the applicant	✓	
Decision-making	✓	✓
Loan closing	✓	
Routine payment collection and processing		✓
Working with troubled borrowers	✓	✓

Loan-making for smaller loan with partner organisation without risk capital

	Partner	CANZI
Outreach and marketing	✓	
Application processing	✓	✓ automated
Visiting the applicant		
Decision-making		✓ semi-automated
Loan closing		✓
Routine payment collection and processing		✓
Working with troubled borrowers	✓	✓

It is important to note that in the second instance, which relies on more automation, there will be less customised analysis and it is, therefore, likely that some credit worthy entrepreneurs will slip through the cracks.

APPENDIX 5: MARK VON DADELSZEN'S[139] DISCUSSION OF THE CHARITABILITY OF ALTRUISTIC LENDING

The law relating to the approval of charitable status to trusts or societies, either at common law (the law established by Court decisions) or by statute (particularly, now, the Charities Act 2005), does not sit easily with the concept of "social lending" whereby an individual makes funds available for use for charitable purposes but with the expectation that the funds will be returned to that individual.

The common law on charities is derived from the preamble to the Statute of Elizabeth I, sometimes referred to as the Charitable Uses Act 1601 or the Poor Relief Act 1601. Almost 300 years later, in *Income Tax Special Purposes Commissioners v Pemsel* [1891] AC 531 Lord Macnaghten in the House of Lords (at 583) classified charitable purposes into "four principal divisions" which have been frequently referred to ever since, not just in the United Kingdom where the decision was made but in other common law jurisdictions such as New Zealand. Those "divisions" are:

a) Trusts for the relief of poverty;
b) Trusts for the advancement of education;
c) Trusts for the advancement of religion; and
d) Trusts for other purposes beneficial to the community, not falling under any of the preceding heads, but within the spirit and meaning of the Statute.

Section 5(1) of the Charities Act 2005 adopts those "divisions," but the section goes on to make special provision for some relaxation of the law for some Māori charities, but that does not appear relevant to the present discussion.

My understanding of "social lending" is that individuals wishing to make capital available for charitable purposes on a "social lending" basis would expect their funds to be returned (unless they decided to forgive the debt) and would commonly not expect interest (and foregoing interest income in itself would be deemed to constitute a gift of the foregone interest). While it may be possible to structure entities to facilitate such "social lending" (with such entities thereby probably being charitable) and to structure "social" loans so they would probably be regarded as being charitable in nature, the present legislative framework in New Zealand does not provide sufficient flexibility or certainty to provide either the entities concerned or the "social lenders" that their activities and benevolence will be regarded as being charitable.

Some of the Charities Commission's recent decisions on the charitable status of proposed and previously approved charities raise questions that may have implications about establishing or preserving the charitable status of "social lending" entities or the activities of "social lenders." Some legislative provision for "social lending" would therefore seem desirable to avoid doubt and to encourage a form of charitable assistance that is unfamiliar to New Zealand government institutions but

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appears to be well-understood and accepted at least in some overseas jurisdictions, notably the USA and UK.