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To whom it may concern

Social Impact Investing Discussion Paper

As one of Australia's leading professional services firms, we believe we are well placed to share our perspectives on important problems impacting our country. We are committed to positively contributing to the Australian community to support and enable initiatives that will strengthen the future prosperity of our nation. Indeed, our global purpose to 'Build trust in society and solve important problems' drives our desire to play a part in contributing to the solution for Social Impact Investing (SII) in Australia.

Our submission sets out our belief that the SII market needs scale, trusted data and appropriate measurement to be successful in Australia. Our response shares insights from PwC subject matter experts to address a number of specific questions raised. However, of greater importance is the role of government in driving a process that involves investors and service providers to co-create innovative solutions.

Our detailed submission is attached. We would welcome the opportunity to discuss our views further. Please contact either of us or Rosalie Wilkie on (02) 8266 8381 or rosalie.wilkie@pwc.com.

Kind regards

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Foreword

Social impact investing (SII) provides a unique opportunity to address the most challenging social issues with innovation and collaboration, from all sectors of our community. The key benefits of SII is the focus on social outcomes, to achieve this the use of private capital is important, as is the sharing and transfer of risk. However, real difference is created when all sectors work together to provide real outcomes to areas of unmet social need, rather than the disparate and disconnected interventions defined by jurisdictions and areas of responsibility that have, until now, been used to address such problems. The question in our mind is, therefore, how best to design, structure and implement an innovative and collaborative approach, which in turn needs:

- The right commissioning.
- Assignment of value and measurement.
- Alignment of outcomes and incentivisation.
- Access to funding.

Above all, SII requires investors who are willing to invest and investable propositions they can invest in. There are many potential investors – financial institutions, super funds and Private Ancillary Funds (PAFs), for example – but at the moment they are not aligned on the investability of SII propositions. Government needs to help here by supporting and building such propositions in a way that appeals to investors with the appropriate and transparent assignment of value, sharing and transfer of risk, along with alignment of outcomes and incentives.

We believe the following areas could help make this shift:

- ***Scale is currently insufficient to attract many investors***. SII is costly for investors, intermediaries and providers to establish. Greater scale would improve economic and social returns as well as investor attractiveness. Scale would take SII beyond pilots and into the mainstream.
- ***Understanding in many parts of the investor community is limited.*** Traditional investments are based in the creation of assets that are tradeable and capable of being reliably and regularly valued. Investors need support to understand the sector and have confidence in how outcomes will be measured and rewarded such as minimum and maximum returns along with capital security.
- ***Impact measurement is a critical consideration in SII.*** It is a recognition of 'shifting the dial' (for the social issue) and also the trigger for payment. Measurement is complex and needs further nurturing and development. A pragmatic but imprecise approach may often be more beneficial than exact definitions and elimination of causal interdependencies.
- ***Many benefits are indirect or qualitative rather than cashable.*** The costs of intervention and financing of benefits are very tangible. It is therefore commonplace for there to be a cash deficit within the term of a SII.
- ***Social issues that SII is intended to address are agnostic*** to commissioner and government jurisdiction. There's a need for a holistic approach and the recognition of the benefit that comes to all from having a positive impact on our most challenging social issues.

Building on these points, if it is agreed that an 'imperfect market' exists for SII, and this slows progress, we believe that the role of government is to help address some of the issues that make the market imperfect and remove impediments to progress. We have expanded on this in the body of the document.

Larger scale SII would also require greater confidence in the investment market that could be supported, at least initially, by a level of capital guarantee or minimum assigned financial value to impact investing mechanisms.

Turning to the specific role of government, we suggest that this should include being a:

1. Market influencer.
2. Driver of data policy so there is high quality integrated data.
3. Supporter of better commissioning and more innovative procurement processes.
4. Shaper of the organisational and tax systems.

We have provided more details below.

1. Market influencer

In many states, Governments are piloting SII as an initial precursor to something bigger. This ‘staged’ approach to SII can help build confidence in the market. As already mentioned, scale is a major issue to overcome – for schemes, providers and the investment market. A greater contribution by government in the first stages, perhaps by adopting more of an underwriting approach with a gradual withdrawal once market forces come into play, could help build market confidence. Governments do, however, also need to consider how they ‘guarantee’ or underwrite some of the less cashable benefits on an ongoing basis.

SII can also act as a catalyst in the provider sector towards a more collaborative, citizen centric approach for a better outcomes culture. Our experience tells us that many grant regimes create competition within the sector for input, activity or, at best, outcomes based in terms of measurement and funding. The Government has already commenced a role as ‘market disruptor’ for such change through the introduction of the National Disability Insurance Scheme and this kind of role – market shaping – needs to continue.

2. Public data policy for robust measurement

Given the vital importance of impact measurement to the success of SII, we believe there needs to be a more robust approach to data availability and connectedness. The Australian Digital Health Agency has started on this journey with health data and information. This approach needs to be extended to all areas of public policy data. As we comment in the paper, the issues SII is intended to address do not recognise organisational boundaries meaning that the underpinning data need to be better linked and connected.

The Australian Government needs to consider a public data policy to ensure the key stakeholders in social investment – government agencies, investors, service providers, and investment proponents – have access to high quality integrated data with sensible privacy safeguards.

3. Supporter of better commissioning and more innovative procurement processes

Commissioning of SII schemes needs improvement. Traditional public procurement methods don't work effectively in this space.

Commissioning needs to engage stakeholders and encourage new entrants through approaches like open innovation platforms (similar in some ways to 'early market engagement' or 'market sounding') to allow a broad range of views to contribute towards consensus while exploring possible solutions. We strongly believe that for collaboration and co-creation to be effective, the right stakeholders need to be engaged at the right time. A more innovative procurement process would allow for this to occur at the initial and supplementary stages.

Traditional 'transactional' procurement approaches need to be updated with thinking like that adopted in the European Competitive Dialogue process, where dialogue and co-creation are seen as positives rather than impediments to probity.

4. Shaping the organisational and tax systems

The discussion paper has a significant number of questions on the role of Private Ancillary Funds (PAFs) in SII. We consider that Federal and State reforms are required to support a range of funding vehicles and concessions, and that PAFs are just one of the things required for a successful social impact investment market.

We would also support a review that utilises State and Federal arrangements to meet funding and policy objectives, including pre-tax, post-tax and roll over relief mechanisms to support investment by companies, trusts, self-managed superannuation funds and individuals.

It's time to do different things, not just the same things differently

Australia should be optimistic about the future for SII: superannuation funds need to diversify asset classes; service providers are keen to impact agendas in different ways; intermediaries and private companies see a role where they can add value; and, above all, there is a need for solutions to issues that are not being addressed through traditional approaches.

In summary, we believe the foundation for effective use of SII lies in the quality of the process for collaboration between the State and Federal governments, traditional service providers and new groups from which initial thinking about potential solutions to complex social challenges will emerge.

Government can be a key enabler through better commissioning processes; giving more opportunities for players to work together; structuring and supporting potential deals in a way that recognises SII not as a traditional investment; encouraging new organisations to participate; promoting greater scale; and ultimately creating an environment that supports, not stifles, innovation.

PwC Submission - Social Impact Investing Discussion Paper

Our submission seeks to address the three key components for consultation in the discussion paper, namely:

1. The role that the Australian Government should play in the social impact investing market
2. The principles for social impact investing
3. How to address potential regulatory barriers to the growth of the social impact investment market

1. The role that the Australian Government should play in the social impact investing market

For this component of the paper we will articulate what we believe are the main barriers to growth of the social impact investing (SII) market in Australia and then outline the role that we believe the Australian Government can play to overcome these barriers.

Barriers and the role that government can play in overcoming them

We believe that the main barriers to growth are (Q1):

A. Traditional risk and return framework may not apply to SII.
B. Certainty of measurement.
C. Lack of track record.
D. Scaleability.

A. Traditional risk and return framework may not apply to SII

Barriers (Q1)

Traditional investments rely on an expected return profile relative to an expected level of risk. In the case of SII the return is measured in terms of social impact, which may not always be readily nor easily quantified. In addition, in many areas of unmet social need the effort and initiatives required do not create separately identifiable and tradeable assets. As such we have a divergence of needs and requirements of the parties in a SII environment. Conversely, the traditional risk and return model does not match the needs for social investment given the reliance on financial outcomes. For example, the need to deliver better services to a disadvantaged cohort does not create either a right to ownership of an asset or ongoing stream of cash flows to which a financial valuation can be readily or easily assigned.

Returns from SII differ again from traditional investment returns in that they have longer investment periods and illiquidity, which requires a different valuation framework. Such a framework would consider benefits that are in some part qualitative and non-cashable and may accrue to other parties than those by whom the costs are incurred.

Role of government as ***market influencer*** (Q4)

The potential role of government can be seen as one of reducing the 'imperfect market' conditions through firstly influencing (through active participation) the market to enable the needs of investors and social outcomes to be met.

This can first and foremost be achieved by providing a level of capital guarantee or minimum assigned financial value to impact investing mechanisms. Without this, the market will continue to be unable to meet the needs of the broader owners of private capital and those responsible for managing it.

The government could also consider creating a central funding body. Such a body could participate directly in opportunities - perhaps with different financial conditions that effectively provide the guarantee. One key role might be the underwriting or 'making cashable' qualitative and broader benefits that would not accrue to commissioners. The UK Big Lottery has agreed to provide a similar role.

B. Certainty of measurement

Barriers (Q1)

From the service provider perspective, current proposed measurement systems place too much burden of evidence and proof on the service, which limits innovation and builds conservatism (financial and otherwise) into proposals. Once the programs are in place the measurement systems are inflexible, preventing them from being changed to meet the needs of the stakeholders.

From the investor perspective, in order for investors to be informed on the performance of their investment they need information on what returns will be earned based on different levels of performance and outcomes.

In addition, there is the challenge of interdependency or interlinking of outcomes. Within the SII arena it is rare, and will continue to be rare, to find examples and circumstances in which a highly defined controllable intervention solely leads to the intended social outcome. Rather, there will be interdependencies between existing programs by both the public sector and not for profit (NFP) sector, and new innovative programs which together will lead to positive social outcomes.

The current construct of requiring a separation and attribution of impact from different programs and organisations creates a barrier to the effective implementation of SII initiatives. An example of how this manifests is that state-based SII initiatives are reluctant to support programs that require cooperation with other ministries within the state or federally funded services (for example, in the health sector, the role of GPs) as it impacts on the ability to measure outcomes to defined inputs. To date, this interdependency has created complexity which is not being effectively managed and results in a lack of innovation in approach.

Few (if any) social issues that SII might be applied to can be solved by single services or interventions. It's a many-to-one rather than one-to-one relationship. SII starts with the outcomes required and works backwards - this is irrespective of government, organisational or funding regime. Inevitably, therefore, it's impossible to fully attribute outcomes to the action of one party. SII is rightly about bringing players together around joint interventions to secure outcomes.

By its very nature there are long time lags for payment triggers, which means investors can become nervous about the likelihood of returns and the public sector pays more given the cash flow implications. There's a similar issue in the outcomes-based commissioning that the Primary Health Network (PHN) is pursuing.

We have provided additional insights on measurement under the Principles of SII component.

Role of Government in ***measurement*** (Q4)

We believe that Government needs to develop the principles of measurement for impact investing that provide appropriate allowances for innovation and adaption in program design and delivery. Certainty of measurement with the appropriate balance of rigour and adaptability for the benefit of both the social outcomes sought and investors' knowledge will also be key.

A potential solution to long time lags for payment triggers is to consider more interim outcomes or outputs that could trigger payments. The UK SII market is deploying this thinking, as are some PHNs in Australia.

C. Lack of track record

Barriers (Q1)

Some of these barriers could be overcome should service providers and/or intermediaries have a proven track record; however, as the market is nascent, this is not the current circumstance. The whole focus of SII is often about incentivising new solutions or interventions that will usually not have historical evidence. Investors need to be confident in operators or service providers as otherwise they will not secure returns. These operators and providers will often struggle to demonstrate evidence of efficacy. To counter this situation, governments may need to do more to underwrite SII.

Role of government as ***evidence provider*** (Q4)

The role that government can play here is to provide the evidence base through the better gathering of data, and transparent publication of experience to demonstrate what works and what doesn't.

D. Scalability

Barriers (Q1)

Most SII initiatives to date have been delivered by non-government organisations (NGOs) and NFPs, neither of which typically have significant scale, operating certainty to commit to programs of scale, nor in many cases, sufficient experience to manage risk effectively or apply rigorous project and program management. Many SII pilots have therefore been relatively small in scale and limited to investment sums of approximately $10 million or less.

Some commentators, in discussing SII, only reference NFPs and NGOs as potential service providers, with private organisations generally assigned a role as an intermediary or the providers of private capital. It is our view there is no real rationale for such a mind-set.

*Role of Government in **exploring delivery structures*** (Q4)

For the Australian Government to secure greater scale in its SII ambitions it could look beyond NFPs and NGOs. These kinds of bodies inevitably have a role to play in delivery as their aims and objectives tend to be very much aligned with the kinds of change SII is intended to secure. To really secure scale, new and different skills and capacity are required, including:

- **Program and project management -** this will be required to drive the programs and coordinate what will inevitably be a disparate group of providers. These programs need significant coordination and control and it is unlikely that such large and complex programs will have been managed before by NGO and NFP providers working together as a group. These programs will need one party without a vested interest to act as the overall coordinator and project manager.
- **Taking risks -** SII involves significant risk taking. Delivery (as well as investment) providers need to be able to take and manage this risk.
- **Financial resilience -** few NGOs and NFPs have significant balance sheet strength. When the UK let contracts in this area they were often led by large scale private providers with a number of NGO and NFP sub-contractors.
- **Analytical capabilities -** we consider that SII needs deep analytical capabilities to identify:
    - intervention areas
    - the starting point or baseline, and
    - the impact and its attribution

  This kind of capability may be more appropriately provided by larger, specialist private providers.
- **The capacity to operate at scale -** this is perhaps one of the biggest impediments to scaling itself - NGOs and NFPs are unlikely to have this if operating alone.
- **Governance strength to lead beyond authority -** leading outside the organisation by influencing and guiding other stakeholders to support objectives. As an example, the whole question of well-being might be in the remit of one part of government but it needs involvement and support from many others, in government and beyond. This needs a set of new and very different skills.

This kind of scale can only come from engaging with others, including the private sector. Involving private entities will deliver greater scale and fundamentally a greater impact, all of which can be assessed in value-for-money terms, whilst also building and strengthening the capabilities of the NFP and NGO sector.

Opportunities and the role that government can play to leverage them

We believe that the following opportunities could play a critical role in the enablement of a thriving SII market in Australia:

A. Access to data.
B. Better collaboration between Australian and State Governments.
C. Innovative procurement processes.
D. Building trust between critical parties in the SII process.

A. Access to data (Q4 and 9)

We share the Australian Government's vision of harnessing the value of public data to grow the economy, improve service delivery and transform policy outcomes for the nation.

In the context of SII, an important part of the Australian Government's public data policy will be to ensure that the key stakeholders in social investment – government agencies, investors, service providers and investment proponents – have access to high-quality integrated data. This access is necessary so that the expected costs and benefits of a proposed investment can be assessed and the performance of current and past investments evaluated. Such assessments are critical to a well-functioning SII market.

The challenges of achieving this goal are well known to agencies, researchers and service providers engaged in the analysis of the Australian Government's social sector data. We think that these challenges are best solved by creating a legislative framework and supporting data management infrastructure that encourages data sharing and integration while protecting the privacy of Australian citizens. The draft findings of the Productivity Commission's report into data availability and use make some important points in this area and we look forward to seeing the final recommendations.
From our perspective, Australia needs a legislative framework and associated data management infrastructure that:

- **Streamlines data sharing across government agencies -** Although progress has been made in this area, much public data remains siloed within agencies. We have seen a real desire in government departments involved in social sector policy and service delivery to make effective use of cross-agency government data. However, the current processes for obtaining cross-agency information can be slow with protracted negotiations and ethics approval procedures. We have also seen that some agencies have a culture of risk aversion which further adds to the difficulty in sharing data.
- **Addresses concerns about data privacy -** We think that the culture of risk aversion is driven by real concerns about data privacy. Data privacy breaches can have significant impacts on individuals and business including discrimination, reputational damage and identity fraud. An appropriate data governance framework can mitigate the risks of privacy breaches and will be essential to freeing up the sharing of data across agencies.
- **Provides high quality datasets that are easily integrated and provide a citizen-centred view -** The Government's historical administrative and survey data contains a wealth of detail that, through appropriate analysis, will provide important inputs into the design and evaluation of social impact investments. This public data is most valuable when it is available at the level of the individual and enables a transactional view of an individual's interactions with the government across a full range of agencies over their lifetime. New Zealand's Integrated Data Infrastructure (IDI) is a successful example of a database that provides such data. The IDI is an infrastructure that maintains and updates the integrated datasets. It also has data access and governance structures which provide access to the data for approved research projects while mitigating the risks of data privacy breaches.
- **Provides regular updates of the integrated datasets -** A key principle of SII is the ability to make robust measurements of outcomes in a timely manner. In many cases outcomes will be assessed by examining government administrative data across a range of government agencies. Integrated citizen-centred datasets that are robust and regularly updated will increase the efficiency of outcome assessment for SII.

Opportunities for the Australian Government to form data sharing partnerships with State and Territory Governments, intermediaries and/or service providers. (Q10)

It is well understood that the benefits from social impact investments can cross government jurisdictions. For example, an initiative leading to more resilient families and less youth homelessness may lead to reduced health and justice costs at the state level and reduced welfare and greater tax revenue for the Australian Government. As such, a full appreciation of the benefits of many social impact investments can only be revealed if different government jurisdictions and agencies share their data. We understand that many state agencies have revealed a strong desire to enter into such partnerships.

The benefits of data sharing across government jurisdictions was discussed in detail in the Productivity Commission draft report on data availability and use. That report (still in draft form) outlines a legislative and regulatory framework to encourage data sharing and we agree with the general direction of the recommendations in that report.

B. Better collaboration between Australian and State Governments (Q4 and 8)

Development of criteria

We strongly believe there are opportunities for the Australian Government and states to work better together on these agendas. Ideally, criteria for identifying such cases might include:

- where the social challenge pervades all aspects of government - as most do
- where both State and Australian Governments currently fund interventions
- where these are getting limited traction, and
- where working together could secure more innovative solutions

Collaboration on funding approaches (Q5 and 6)

We know that the kinds of social challenges that SII sets out to address do not recognise governmental or organisational boundaries. Our view is that SII should ideally be commissioned on a joint basis.

One of the biggest challenges in SII is the evaluation and hypothecation of broader, often non-monetary and indirect benefits. For example, reducing recidivism will have an impact on employability and, therefore, potentially wellbeing and tax generation. These are 'knock on benefits' that would not directly accrue to the states pursuing recidivism-based SII. There is therefore a question about whether the Australian Government might underwrite these sometimes qualitative, often indirect, benefits. In the UK, the Big Lottery plays a similar role, often rendering SII deliverables where it otherwise would not have been possible. Another example is the UK Cabinet Office's £20 million Social Outcomes Fund to contribute to social impact bonds where government savings accrue over a number of departments.

Another example of where Australian and state governments could play joint roles is where citizens are impacted by the actions of both federal and state funding and activity. Health is an example of where the continuum of care stretches from Australian Government funded primary care through community provision and into largely state-funded acute care. Most commentators would say that to achieve truly integrated care requires joint commissioning, pooling of budgets and a single approach. SII could support such an approach. This would also overcome challenges where costs of one sector, say, investment in primary prevention, result in benefits to another, such as fewer admissions in the acute sector. SII could be used to incentivise the best overall system outcomes.

Our view is that Australia suffers from many fragmented and directly funded initiatives that impact on some parts of social problems but not the whole system. Because of the hypothecated funding, sometimes from different government tiers, it's very difficult to take a holistic approach to the problem. Those problems that require multi-faceted interventions - and many do - might benefit from a more 'joined up' approach that could be facilitated by SII. The other benefit of the SII approach is its outcomes-based focus. Our experience tells us that many grant regimes are input, activity - or at best outcome-based in terms of measurement and funding. These approaches often incentivise the wrong things. Adopting outcomes-based approaches incentivises the achievement of outcomes.

The previous opportunities were identified in the discussion paper; however, we believe that the following two opportunities should be considered by government as additional significant contributors to SII in Australia.

C. Innovative procurement processes (Q2 and 3)

Our contention is that current public procurement processes are too 'transactional' and that this does not support collaboration, co-creation or dialogue – all of which, we consider, would result in better solutions. Government could explore procedures such as Competitive Dialogue used in Europe.

An additional approach for government to consider is to utilise challenge-based processes in order to identify and engage talented stakeholders who can contribute to solutions that will deliver impact and explore new business models. This 'open innovation' approach is designed to connect with new talent to challenge traditional thinking.

Many of the SII challenges are complex in nature with many interconnected challenges, stakeholders and human behaviours influencing the issues. The probity-compliant procurement process of open innovation (similar to 'early market engagement' or 'market sounding') allows groups to identify consensus while exploring for possible solutions and preserving future procurement options.

Lastly, we would welcome more use of unsolicited proposals, but where the threshold test for progression to a 'co-creation' stage is an innovative idea that solves a defined problem, rather than 'uniqueness' in idea or ability to deliver. Government could encourage the unsolicited submission of ideas rather than only issuing Requests for Tenders – it could establish overarching SII focus areas and criteria to then invite more proposals.

D. Building trust between critical parties in the SII process (Q4)

We believe the foundation for effective use of SII lies in the quality of the process of collaboration from which initial thinking about potential solutions to complex social challenges emerges.

We believe there is a need to bake the investing perspective into the collaborative problem-solving process of collective thinking, designing and prototyping earlier and more systematically. This will be an essential part of educating the investment community so they are a more integral part of the larger problem-solving community, rather than waiting on the sidelines until solutions (possibly poorly designed for want of earlier expert input) are brought to them for funding.

Convening the right stakeholders at the right time

The right stakeholders

The discussion paper highlights stakeholders such as potential investors, policy makers, NGOs and other social entrepreneurs interested in leveraging the impact investing mode, as core to SII in Australia and we agree. However, in our experience convening requires a mixture of deliberate design and some serendipity. That means the ability to uncover, and invite into the process, 'unusual suspects' whose views and experience might not initially have been thought to be either relevant or useful (which aligns to our earlier views on 'open innovation').

The right time

We believe that for SII to grow and make a greater contribution to solving some of Australia's most complex social problems, the right people need to be involved from the start: those with the skills and experience to understand where an investment model could play a significant part in the mix of capabilities needed to turn possible solutions into prototypes and scalable solutions.

An investor's eye adds considerable ballast to the mix of skills and approaches in the collaborative process. We think growing and spreading an SII ethic and capability in Australia will require those with impact investing skills to become part of the collaborative problem solving process as early as possible.

However, we are aware we need to get the balance right and make that expertise available at the right time in the development of ideas and prototypes. Too early, and good or promising ideas might get cut off before they have had a chance to be developed. If expertise is left out of the mix for too long, though, it might be harder to work out effective ways to make impact investing part of the solution.

Effective collaboration

If the art of convening is essentially about 'getting the right people in the room', then the practice of effective collaboration is about what happens once they are 'in that room'. Our experience suggests the best collaboration occurs when it is across unusual combinations of people and organisations who bring different perspectives to a shared passion for new ways to tackle persistent social challenges. By using good convening and effective collaboration tools to draw an SII perspective into the problem solving process from the start, trust between investors and service delivery providers can be built.

To complete our response to the role the Australian Government should play in SII, we will address two final questions.

What Australian Government policy or service delivery areas hold the most potential for social impact investing? (Q7)

PwC supported the Australian Government in exploring the Investment Approach to supporting those most likely to face a lifetime dependency on benefits. We consider that this would be a strong candidate for an SII approach: by inviting bidders to identify such individuals and then deliver a range of interventions to support them, future benefits dependency could be reduced. The outcome would be reduced benefits dependency compared to a control group over a set period of time. There may be intermediary outcomes like securing employment.

We think health is another example but only where it's done in partnership with states. This would incentivise integrated care. This could be used, for example, to augment the health care homes trials or explore alternatives to activity-based GP funding - the Medical Benefits Scheme.

A final example might be indigenous outcomes - working with PHNs to 'close the gap' on health outcomes.

What do you see as the future for social impact investing in Australia? (Q2)

We believe that Australia should be optimistic about the future given the current existing market forces of: superannuation funds needing diversified asset classes; the progress and interest to date shown by service providers, intermediaries and private corporations; and the sheer need for a solution requiring inventive and innovative approaches.

We think SII could evolve over three stages in the future:

- The first stage would require greater government involvement and steering to encourage: a) private capital to divert to this asset class; b) service providers to build a track record (that may be underwritten by government) without restrictions that are too onerous; and c) the involvement of other players (including the private sector) as providers.
- The second stage would bring second round investments with track records and outcomes in place and continuing innovation without the continued support and involvement of government.
- The third stage would involve the government withdrawing from the structural elements of impact investing as the asset class, service providers and intermediaries create an effective market place.

2. The principles for Social Impact Investing (Q11)

2.1. Value for money

We agree 'Value for money' must be included but it is challenging to assess. The acid test question is 'compared to what?'.

Many areas where SII might be applied have seen years of traditional public investment with limited impact. The efficiency and effectiveness of these interventions has therefore been limited. While the overall costs of the SII may seem expensive, if the investment secures better outcomes it may well be better value for money.

The second issue is value for whom. As already stated, benefits often accrue to multiple parties and therefore to truly consider value for money, governments need to consider all benefits to all parties.

2.2. Robust outcomes-based measurement and evaluation

Establishing robust outcomes that are both meaningful and measurable will be a challenge. The immediate challenge will be to establish a collective understanding of, and agreement on, a common set of goals and outcomes. This will require substantial investment in co-design processes to effectively engage and stimulate leadership across relevant agencies and providers. This will then need to be followed up by applying direct accountability and performance indicators, including the collection of robust data towards common goals at the agency and the population level.

The ability to develop a robust approach to measurement will rest on understanding, and clearly articulating, what is to be achieved, with whom and over what time frame. Part of this will be acknowledging that initiatives aren't delivered in isolation and accepting that there will be a certain element of 'noise' as part of the equation. It would be unrealistic to expect cause and effect to be demonstrated clearly for each initiative and it would be far more feasible to approach outcomes-based measurement as a pragmatic, collective approach to impact.

There are several current examples of how collective approaches to impact are driving change. Male Champions of Change is one such example, where a group of influential male leaders across Australia were brought together and challenged to improve female leadership and gender equality across Australian workplaces as a common goal. Through their respective organisations they were able to implement a range of strategies and initiatives. The collective social impact of their work would be cumulative and would not have been applied in isolation of other more general workplace policies and initiatives. Measurable (quantifiable) impacts of their collective impact would include equity in remuneration, representation in leadership roles, representation on boards and implementation of workplace policies like flexible working schemes. Meaningful outcomes from this work would include female leadership in the workplace and the resultant shift in workplace culture.

2.3. Fair sharing of risk and return

We agree with this principle and recognise that 'fair' is hard to define. The Australian Government may need to adopt less 'aggressive' expectations of risk and reward initially to seed the market and encourage engagement. Many potential investors are wary of the SII 'new' market area. Government also needs to consider how SII-based interventions fit with the status quo. Are there ways in which current 'services' could be reigned in and therefore improve value for money?

2.4. A deliverable and relevant social outcome

We agree with this principle. As covered elsewhere the challenge is probably measurement.

3. How to address potential regulatory barriers to the growth of the social impact investment market

Before responding to some specific queries raised in this discussion paper on Private Ancillary Funds (PAFs), we believe it's important to first outline the sources of capital and funding for SII in Australia. We consider that federal and state reforms are required to support a range of funding vehicles and concessions, and that PAFs are just one aspect of this analysis for a successful social impact sector in the future.

We anticipate that a range of donors, investors and taxpayers have sources of capital to invest in this sector. These funds could be pre-tax, post-tax, held in concessionally taxed entities or currently invested into other assets. In order to create a dynamic investment approach to social impact, reforms should be made to accommodate a broad range of investors before any particular fund structure is analysed in detail.

Rather than thinking through the typical model of ancillary funds and deductible gifts in isolation, we would support a review that utilises state and federal arrangements to meet funding and policy objectives. These concepts include:

- Vetting by State and Federal Governments to approve a **national priority list of social impact projects** that receive funding based on the concessions outlined below.
- **Pre-tax capital in companies, trusts and SMSFs, and held by individuals -** concessions, deductions or offsets for amounts contributed to social impact investment, similar to the Government's recent innovation incentives directed at early stage innovation companies.
- **Post-tax capital in companies and SMSFs, and held by individuals -** exempt earnings from the returns generated from priority social impact investments (i.e. not included in assessable income for income tax purposes).
- **Roll-over relief for assets sold in order to invest in social impact -** where investors have sold pre-existing investments in order to make cash available for impact investing, any gains should benefit from roll-over relief in order to defer gains on sale.

The benefit from adopting a range of reforms to attract capital investment into social impact is that the source of funding is not limited to one type of investor or entity type.

This review provides an opportunity for the Departments of Treasury across the country to collaborate and co-create solutions for this sector and to meet the demand for investors that want to contribute to the community in ways that have not been available in the past. Without an approach such as this we have a concern that access to funding will be restricted unnecessarily to categories like Deductible Gift Recipient donors and/or funds held in PAFs.

We believe that there is a natural fit for PAFs to be a key investor group in SII and hence a review of current regulation is important to identify potential barriers to their ability to invest. With respect to the questions posed in the submission, we make the following comments:

- It is important to recognise that donations may be made to a PAF by the founder of the fund, associates of the founder (which includes companies that they control), employees of the founder or a deceased estate of any of those entities. Therefore, when considering who the largest financial donor is for the purposes of the sophisticated investor test, this should not be limited to the director of the trustee in their personal capacity but should also take into account donations that are made by entities that they control.
- We continue to see PAFs as a vehicle through which multiple generations of the one family engage in philanthropic activities, and which allow the younger generations to play an active role in the family strategy. However, it may be the case that the wealth of the family has not transferred down to the younger generations and therefore they may not meet the sophisticated investor test in their own capacity.
- To provide a robust framework to ensure that the PAF is adequately advised prior to making an investment, we agree that it would be reasonable for an independent and qualified accountant to provide a certificate, rather than rely on self-certification by the trustees.

In conclusion, PwC believes that SII has the ability to transform the current social and investment sector, and that the key to this is collaboration across State and Federal Governments, traditional service providers and new groups such as those from the private sector.

The role for government is to enable commissioning processes based on ongoing dialogue from a number of stakeholders, to underwrite and provide capital support at least in its initial stages, and to develop data and measurement protocols to enhance collaboration and encourage innovation.

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Question	Page reference
1. What do you see as the main barriers to the growth of the social impact investing market in Australia? How do these barriers differ from the perspective of investors, service providers and intermediaries?	4,5,6,7
2. What do you see as the future for social impact investing in Australia: for example, can you foresee the development of new structures for social impact investing?	12
3. Are there any Australian Government legislative or regulatory barriers constraining the growth of the social impact investing market?	10,14
4. What do you see as the role of the Australian Government in developing the social impact investing market?	5,6,7,8,9,10,11
5. Do you see different roles for different levels of government in the Australian social impact investing market? For example, the Australian Government as co-founder with State and Territory Governments continuing to take the lead in developing social impact investments?	7,8,9,10
6. Are there areas where funding through a social investment framework may generate more effective and efficient policy outcomes than direct grant funding?	9,10
7. What Australian Government policy or service delivery areas hold the most potential for social impact investing? Are there any specific opportunities you are aware of?	12
8. Are there opportunities for the Australian Government to collaborate with State and Territory Governments to develop or support joint social impact investments?	8,9,10
9. What are the biggest challenges for the implementing the Australian Government's public data policy in the social impact investing market? What can do the Australian Government do to address these challenges?	8,9
10. Are there opportunities for the Australian Government to form data sharing partnerships with State and Territory Governments, intermediaries and/or service providers?	9
11. We are seeking your feedback on the four proposed Principles for social impact investing outlined in this section. a. Provide value for money b. Demonstrate fair sharing of risk and return c. Focus on a deliverable and relevant social outcome d. Have a robust approach to outcomes-based measurement	13
12. Are there any issues other than those identified relating to control that would suggest the options presented will not be sufficient to solve the problem?	We have provided broad feedback

13. Are there examples of recent situations where a PAF has considered that it is sufficiently controlled, or not sufficiently controlled, that fall outside these situations?	on these PAF related questions on pages 14 and 15
14. Do the options canvassed provide sufficient certainty around when a PAF is controlled by a sophisticated investor? Are there better options that are not discussed?	
15. How could these options be best incorporated within the appropriate legislation?	
16. Is a written statement from the board of directors of the PAF sufficient evidence of the status of the trust as a sophisticated investor, or should a letter from an independent third-party be required?	
17. What qualifications should the independent third-party person be required to hold?	
18. Is it common for a natural person involved with a PAF to meet the professional investor test, but not the sophisticated investor test, or visa-versa?	
19. Does this lack of control provision restrict PAFs established by professional investors from investing in impact investment products?	
20. Are there any similar issues about the application of the sophisticated investor test and/or professional investor test for investment by PAFs in financial products other than securities that are structured as impact investment products?	
21. If the Government were to amend any of these definitions to provide clarity for PAFs, would there be any consequences for other activities regulated by the Corporations Act, or other Commonwealth legislation?	
22. Are there relevant parts of the Corporations law, or other Commonwealth legislation and guidelines, which represent a barrier to PAFs investing in impact investment products?	
23. What guidance in particular would provide a desired level of clarity on the fiduciary duty of superannuation trustees on impact investing?	No comment
24. To what extent are the current arrangements for program related investments appropriate? Should changes be made to: **24.1.** recognise the total loan, rather than only the discount rate between a commercial rate and the concessional loan rate, for the purposes of meeting the ancillary's funds minimum annual distribution; and **24.2.** allow ancillary funds to make program related investments to non-DGR organisations?	No comment
25. What is the level of demand from both DGR and non-DGR organisations who could be recipients of program related investments?	No comment

26. What are the costs of administration for organisations receiving program related investments compared with receiving irrevocable donations?	No comment
27. Given the recent changes to the ancillary fund guidelines regarding program related investments, and noting the issues associated with making further changes, are there alternative mechanisms for promoting program related investments outside of ancillary funds?	No comment
28. Have you faced a legal impediment as a director of a social enterprise from making a decision in accordance with the mission of the enterprise, rather than maximising financial returns, that only a change in the legal structure could resolve? If so, what amendment to Commonwealth legislation, regulation or ASIC guidance would you consider is needed to address this problem?	No comment
29. Would making a model constitution for a social enterprise assist in reducing the costs for individuals intending to establish a new entity? What other standard products or other industry led solutions would assist in reducing the costs for individuals intending to establish a social enterprise?	No comment