NEW ECONOMICS FOUNDATION

THE LOCAL BANKING TOOLKIT

A PRACTICAL GUIDE TO STARTING A REGIONAL COMMUNITY BANK

CONTENTS

INTRODUCTION **2**

1. STAKEHOLDER BANKING AND REGIONAL COMMUNITY BANKS **4**
- 2.1 WHAT ARE STAKEHOLDER BANKS? 4
- 2.2 REGIONAL COMMUNITY BANKS AND THE CSBA MODEL 4

2. HOW TO BUILD A REGIONAL COMMUNITY BANK **8**
- 2.1 MAPPING EXISTING PROVISION 8
- 2.2 SCALING UP VERSUS BUILDING ANEW 11
- 2.3 GOVERNANCE MODELS – CHOOSING A MODEL TO SERVE LOCAL NEEDS 12
- 2.4 DIFFERENT BANKS, DIFFERENT OUTCOMES 13
- 2.5 POTENTIAL STAKEHOLDERS AND THE VALUE OF A CSBA BANK 14
- 2.6 BUSINESS FORMATION AND BUILDING A BANK, STEP-BY-STEP 17
- 2.7 CAPITALISATION 22
- 2.8 LOCAL AUTHORITIES AND COUNCILS IN FOCUS 24

3. INVESTMENT PATHWAYS **26**
- 3.1 LOCAL AUTHORITIES 26
- 3.2 CATALYTIC INVESTMENTS AND DEVELOPMENT FUNDS 28
- 3.3 SOCIAL IMPACT FUNDERS AND CHARITABLE FOUNDATIONS 28
- 3.4 PUBLIC PENSION FUNDS 29
- 3.5 ANGEL INVESTORS AND HIGH NET WORTH INDIVIDUALS 29
- 3.6 VENTURE CAPITAL 30

4. FINAL THOUGHTS **31**

5. FREQUENTLY ASKED QUESTIONS **32**

ENDNOTES **36**

INTRODUCTION

Our economy is severely unbalanced, with too many people missing out on the opportunity for a decent, productive and rewarding livelihood just because of where they live. Underpinning these imbalances is an overly concentrated and profit oriented banking system that is not fit for purpose. The structure of our banking system fundamentally reinforces the UK's notoriously uneven economic landscape, and helps make it the least financially resilient of major advanced economies.[1]

Nearly 10 years after a global financial crisis that came at an incalculable human cost, many are asking what finance is ultimately for? Who does it serve? And who should it serve? We urgently need a resilient financial system that serves the economy; that helps people to realise the decent, productive and rewarding livelihoods they are entitled to.

As the New Economics Foundation (NEF) has argued[2] a key priority should therefore be to re-establish local sources of banking that aim to deliver a positive social impact as well as financial returns. By creating a network of local stakeholder banks that support investment opportunities and offer financial services to disenfranchised communities, we can start transforming our broken banking system into one that serves the UK economy.

With the potential to deliver an array of social and economic impacts to their local economies, a growing number of practitioners, local councils and research institutes are becoming increasingly interested in how to set up a regionally focused local bank. Responding to this interest, this toolkit aims to provide a practical guide to establishing a type of local stakeholder bank: a regional community bank.

The toolkit is structured as follows:

1. **Section 1 begins by explaining what we mean by a regional community bank and how it differs from other local stakeholder banks in the UK.**

2. **In Section 2, we highlight the practical steps to establishing a regional community bank.**

3. **As capitalisation and investment is a significant obstacle towards building regional community bank, Section 3 provides specific insight into some investment pathways.**

4. **Section 4 provides some concluding remarks.**

5. **Section 5 attempts to help with some frequently asked questions.**

1. STAKEHOLDER BANKING AND REGIONAL COMMUNITY BANKS

2.1 WHAT ARE STAKEHOLDER BANKS?

Previous work by NEF highlighted that stakeholder banks have a broader set of objectives than simply maximising profits, including customer value, financial inclusion, and local economic development. [3] The essence of stakeholder banks is that instead of maximising profits for shareholders, they explicitly aim to deliver a range of broader benefits to stakeholders while earning sufficient profits to ensure financial sustainability and security.

They fulfil a social mission and have a strong positive impact on local economic development. In general, they deliver more stable returns and lending than commercial banks and performed well during the financial crisis. Finally, in addition to creating social and economic value, they complement commercial banks by serving different markets.

2.2 REGIONAL COMMUNITY BANKS AND THE CSBA MODEL

In the UK, many of the existing alternative finance providers could be classified as stakeholder banks, including community finance development institutions (CDFIs) and credit unions. An alternative stakeholder banking model has been developed by the Community Savings Banking Association (CSBA), which has developed its model around delivering regional community banks across 18 different regions of the UK.

The CSBA has been building significant momentum and visibility over the last few years, and has identified several communities of practice with the potential to establish its banks. The most advanced of these groups is the Greater London Mutual (GLM), which has registered its corporate vehicle as a registered mutual society, has secured a full complement of board members, is currently seeking investment capital, and has begun its banking license application process.

The Royal Society of Arts (RSA) and NEF are supporting the CSBA's efforts to establish regional community banks, and the rest of this toolkit refers predominantly to the establishment of this model.

There are a number of reasons for this approach:

- The CSBA model exhibits all the characteristics and functionality that have made stakeholder banks in Europe and elsewhere successful. This includes: collaboration in networks to achieve economies of scale, an enshrined social impact mission alongside seeking a financial return, and a geographically bounded sphere of operations.
- There is significant momentum, support, and expertise behind this model, and thus a strategic and pragmatic opportunity has arisen with which to deliver the benefits of stakeholder banking in the UK.
- The CSBA model has been specifically designed to be fully scalable, financially sustainable, and to offer consistent, integrated, and impactful locally rooted financial services across the UK.
- As we continue to show throughout this toolkit, the CSBA model appears a likely and viable vehicle with which to deliver the significant social and economic impacts that stakeholder banking can offer, as well as an opportunity to do so in a way that could help to address social and economic inequality and imbalances across the UK. Table 1 outlines an overview of the CSBA model.

TABLE 1: THE CSBA MODEL AT A GLANCE

SCALE	SUSTAINABILITY
• Operates in a target market of 2.5-3m people in regions, and 7m in London • Fully financially sustainable at 46,750 personal and 12,750 business members • This represents 0.72% of personal current account market and 0.18% of small and medium enterprise (SME) loans banking market by value (figures for London) • Balance sheet of over £187 million by year four, and £550 million at maturity by year nine (figures for base financial model) • Regional operational focus at the bank level, with local tailoring and relationship based banking at the local level • Cost collaboration across the CSBA network enabling economies of scale	• Turning an operating profit by year four, and an overall profit by year six, reaching full financial sustainability • Income streams include interest rate arbitrage, account fees, payments fees (levied on card providers not customers), safestore deposit box rental, and foreign exchange services • Transparent monthly fees of £5 for personal members and £10 for business members, providing operating income for the bank • Prudent and responsible lending only to those who can afford to pay back, resulting in low bad debt ratios • Low overheads • Asset base diversified across personal unsecured, mortgage, and SME lending – mitigating risk and avoiding concentration

SOCIAL MISSION

- Constitutionally committed to pursuing inclusivity, responsibility, and social impact
- Socially inclusive, offering universal access to current accounts within operational territory, regardless of customers' potential profitability or credit history
- Jam jar accounts and budgeting tools
- No unauthorised overdraft charges
- Partnership and collaboration with community services, including charities, social enterprises, co-operatives, and other social financial service providers
- Redistributes surpluses to members through dividends, savings bonuses, passing on efficiencies to members, and lower interest rates
- Presence in localities and communities where mainstream banks are receding
- Controlled by membership: see Co-operative governance

21ST CENTURY BRANCH BASED BANKING

- Commitment to branches, facilitating access to financial system
- Two branch types: principal and satellite
- Principal branches will be staffed, and include autonomous loan managers empowered to make lending decisions based on their own expertise and local conditions, as well as safestore deposit boxes and counter services
- Satellite branches will be unmanned, and use smart ATMs to provide 24/7 access to cash, deposit and transaction services, including the ability for businesses to pay in and withdraw notes and coins, and office hours access to loan application and customer services via video link
- State of the art integrated online banking and mobile app
- Telephone banking and support services
- Helps serve the needs of gig economy workers and smaller SMEs through 24/7 cash-based services

CAPITAL AND INVESTMENT

- Initial capitalisation of £20 million required, achieved through share equity
- No further external investment rounds needed after initial investment as bank is forecast to be fully financially sustainable
- Shares available for purchase at £15 per share, tradable amongst members
- Every new customer/member must also buy at least one share, providing ongoing CET1 capital investment to the bank
- Dividend paid once bank is operating at full financial sustainably, forecast to be from year six
- CET1 capital ratio of over 15% at maturity – higher than incumbent big banks

FULL PRODUCT RANGE

- Current accounts
- Debit cards
- Savings
- Unsecured loans
- Mortgages, including guarantor-backed mortgages for first-time buyers
- Foreign exchange
- Safestore deposit boxes
- Business accounts
- SME lending, including smaller loans and longer-term loans than those offered by incumbent banking sector
- No credit cards – functionality instead provided at lower cost to customers and merchants through arranged overdrafts on debit cards
- Real time accounting, meaning payments will not be authorised if the account has insufficient funds, no unauthorised overdrafts will be levied, and balance inquiries will always accurate
- Ability to design bespoke and innovative products, such as savings accounts to finance community energy, local housing, or other strategic opportunities

CO-OPERATIVE GOVERNANCE

- Mutual governance structure, creating the UK's first genuinely co-operative bank
- Bank is owned by, works for, and is accountable to its membership
- One member one vote system for annual general meeting voting, meaning influence is equal amongst membership rather than commensurate to size of their investment and shareholding
- Bank run by professional executives, with oversight provided by professional, non-executive Trustee Directors
- Provisions in the bank's constitution enable membership to exert influence over the board, including on pay and executive appointments, enabling financial participation and local control
- Commitment to Rochdale Principles, including collaboration amongst co-operatives including other CSBA banks
- Simple, transparent structure – no holding companies or parent charities
- Regional banks are members of the CSBA, exerting control over the Association and facilitating collaboration

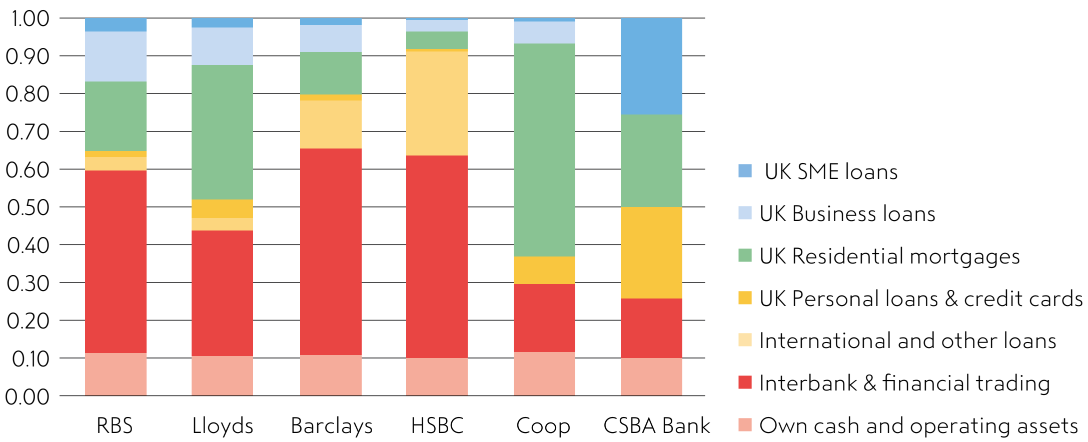
MUTUAL TRUST

- Honest and transparent fee structure, including removal of free-if-in-credit accounts which penalise low-income customers
- Constitutional commitment to act in members' best interests
- Geographically bounded, so works only for local and regional membership
- Prudent and sustainable lending at the heart of the bank's ethos and operations – will only provide credit to those who can afford to pay back
- Branch staff empowered to make their own decisions, enabling trust through genuine relationship banking
- No bankers' bonuses – instead, surpluses distributed to all members through bonuses, dividends, and enhanced interest rates
- Value-added services designed around members needs and best interests
- Accountability and control enabled through co-operative governance

*All figures are based on the latest financial projections of the base financial model developed by the CSBA, except where indicated that figures apply to London only. Full financial model and business plan available under signature of a Non-Disclosure Agreement – contact James Moore of the CSBA for more details at info@csba.co.uk

As well as these features, the CSBA financial model outlines how the bank intends to allocate its asset resources. Comparing this with the actual asset allocation of the UK's existing high street banks demonstrates the extent to which the CSBA model is designed to finance the real economy, with a far higher proportion of its asset base allocated to small and medium enterprises (SMEs) and unsecured personal lending, and a far lower proportion allocated to interbank and financial trading. Figure 1 shows what one pound deposited in the CSBA model would fund.

FIGURE 1: COMPARISON OF ASSET ALLOCATION OF UK BANKS.



Source: Tony Greenham/Bank Annual Reports and CSBA Financial Model

2. HOW TO BUILD A REGIONAL COMMUNITY BANK

2.1 MAPPING EXISTING PROVISION

The first step in establishing a regional community bank is to map the existing financial provision landscape in the local target region, to assess the market gaps in existing provision and to identify the tapestry of stakeholders that could advance or oppose its realisation. This is a necessary initial step to be relevant and deliver impact:, regional community banks need to be designed to cater to the specific opportunities, obstacles, and risks of the local economy. Moreover, by mapping existing provision practitioners will be better placed to decide whether to scale-up existing provision, or to build a new regional community bank.

As a general guide, we set out the products and services offered by alternative types of regional finance providers in Table 2. Table 2 is based on forthcoming NEF research that reviews alternative banking provision in the UK. The findings of the research suggest that whilst existing financial provision has had some notable social impact and serves a broad and diverse set of needs, in certain places there may be significant and widespread gaps in financial services provision for the underserved in both the SME and personal markets. It is in such areas where a regional community bank might be worth setting up.

At a glance, each type of institution offers something different. However, this high-level overview does not show the particular market and customer segments in which each institution operates. For example, althougw h CDFIs and community banks both offer SME loans, the former is more likely to offer loans to start-up businesses, as the higher default rate associated with start-ups would exceed regulatory tolerances for a licensed bank. The more detailed mapping of existing financial provision would

TABLE 2: ALTERNATIVE MODELS OF FINANCIAL SERVICE PROVISION

INSTITUTION	SCALE	KEY FACTORS IN DETERMINING SCALE	ROLE	PAYMENTS	DEPOSITS	INVESTMENTS	PERSONAL LOANS	SME LOANS	INFRA-STRUCTURE
Community bank (CSBA)	Regional	3 million population to provide viable scale for licensed bank, but still tailored to and accountable to region (eg: Greater London, West England – Bristol, Bath and North East Somerset, Wiltshire, Gloucestershire)	• Payments and banking services • Savings covered by deposit insurance protection • SME and personal loans, including secured and unsecured • Can be tailored to offer longer term investment products.						
Community Investment Fund	Metro/county	Strong common identity among public investors, and proximity to infrastructure projects funded (eg: Hackney or East London, Bristol and Bath)	• Longer term retail savings • Investment in social and economic infrastructure • Ambition to offer longer term retail investment products						
CDFIs	Various, from national to regional and some city, regional, or even local level	Market knowledge - there does not seem to be consistency, with some choosing sector specialism and some choosing have geographic specialism (eg: Key Fund, Sheffield covers the North of England)	• SME lending to businesses turned down by banks • Personal lending to people excluded from bank credit						
Credit union	Regional/metro/ county/ district/ neighbourhood – highly dependent on individual credit union (notes 1 & 2)	Common bond of up to 2 million adults, and proximity to financially excluded communities. (eg: City of Plymouth Credit Union - but they are increasingly merging to cover larger territories in an attempt to become more cost efficient)	• Specialised lending, often to people excluded from bank credit, or in financial distress • Savings covered by deposit protection insurance • SME loans permitted but rare • Some current account provision						
Local currencies	Town or city	Strong sense of place, presence of local supply chains, and operational and organisational capacity of currency operator	• Payments • Can act as a proxy for deposits if operated by a credit union, as in Bristol • Nascent development of business credit schemes						

Notes:

1. Credit unions can also have a common bond based on occupation, such as the fire service credit union, and these are national.
2. Liberalisation around credit union regulation allows them to provide transactional accounts and SME loans, however in practice there are very few instances of them doing so as described above.
3. As the national scale is not included, we have not shown social banks, such as Triodos, which may have a positive impact on local sustainability and prosperity.
4. Regional grant making foundations, equity investors and community share issues are also excluded as we are focusing primarily on credit institution.

aim to identify the areas of overlap and complementarities between the different types of provider. Together, existing alternative bank providers can co-operate, and function as an ecosystem of local financial providers. Under the right conditions, this ecosystem can help gain economies of scale and achieve many of the same goals as those of a regional community bank.

There is no hard-and-fast way to complete such a mapping exercise, and the process to achieve it should be dictated by the participants and stakeholders who are interested in delivering socially impactful finance in their own area. That said, there are a number of key questions that the mapping exercise should seek to answer that are outlined in Table 3.

TABLE 3: KEY QUESTIONS FOR MAPPING EXISTING FINANCIAL SERVICE PROVISION

ALTERNATIVE PROVIDERS • What alternative providers already serve this area? Are there credit unions, CDFIs, and other practitioners serving this region? • What is the scale and level of development of these providers? Where are the gaps? • How collaborative are these providers? Are there forums or institutions that facilitate and convene their collaboration and engagement, such as Local Enterprise Partnerships? • Who are the people involved in these institutions? What are their opinions on local conditions, and what are their attitudes to local banking or new institutions?	**MARKET DYNAMICS** • What are the demographics and market characteristics of this region? • What are the competitive advantages and sectoral strengths of this area? • What is the business landscape of the region? What sectors are experiencing or likely to experience growth? • What other economic initiatives influence this area, whether driven by national, regional, or local policy?
MARKET SEGMENTATION • What is the shape and scale of underserved markets in this area – both for SMEs and individuals? • What is the lending profile in the region, and what are the areas that receive the least adequate provision? • What activity have the biggest banks exhibited in this region, and where have they fallen short? • What is the complexion of physical financial service provision, including bank branches and ATMs?	**LOCAL STAKEHOLDERS** • What is the position and attitude of local and regional government to financial provision in this area? • Whose value chains and service propositions could be enhanced by improved financial service provision? • Who are the local and regional actors that could be allies or opponents of a new regional community bank? • What other initiatives have happened in this area, and who has driven them?

There is a multitude of sources that can help answer the questions above and to assist with mapping existing provision. However, by far the most important success factor is to include the right local stakeholders in the discussion. We advise that before initiating any stakeholder banking project, local banking practitioners seek out and consult existing financial service providers in their targeted area of operations.

Other potential sources of information include:

- Office for National Statistics
  - Local Statistics services[4]
  - Official Labour Market Statistics (Nomis)[5]
  - Business Statistics, particularly the 'Activity, size and location' data sets[6]
- The British Business Bank, particularly the 'Small business finance markets' data sets[7]
- Local government sources of constituency, borough, and ward level data, including local authorities, councils, and combined authorities demographic statistics
- Market research and repeated surveys, such as:
- The SME Finance Monitor[8]
- Regional equivalents such as the Greater Manchester Business Survey[9]
- The British Bankers' Association statistics, particularly their postcode lending data (now absorbed into the UK Finance trade body)[10]
- Industry bodies and trade associations, including
  - Responsible Finance lending statistics[11]
  - The Federation of Small Businesses' Resource Hub[12]
- Local and regional business partnerships, including
  - Local Enterprise Partnerships, particularly the regional EU Structural and Investment Fund Strategy research series, which is also referred to as the Investment Strategy for Financial Instruments research series[13]
  - British Chambers of Commerce policy work[14]
- Financial exclusion and social impact research, particularly from
  - Personal Finance Research Centre, University of Bristol[15]
  - School of Social Policy, University of Birmingham[16]
  - Joseph Rowntree Foundation[17]

As well as demographic and business statistics, relevant initiatives and strategies that feed in to the financial provision and inclusion agendas should be examined. For example, Bristol City Council has approved a 50 year resilience strategy as part of the 100 Resilient Cities initiative,[18] which was recognised by research participants to have the potential to feed in to and increase leverage for council involvement in delivering a regional community bank. Similarly, local councils' economic regeneration and financial inclusion strategies will often carry significant relevance for any stakeholder banking project, and can give a steer as to the warmth of local government to any potential initiative.

2.2 SCALING UP VERSUS BUILDING ANEW

Mapping existing provision and identifying market gaps should help practitioners better understand the local economic context. The results of these exercises will help determine the next key strategic question: whether to scale up existing provision, or whether there is ample demand and enough committed local stakeholders to deliver a new regional community bank. Local stakeholders should consider whether investment would be most impactful by being directed towards existing providers, either within the area or as new entrants to it, or whether a new bank institution would create better value and impact for the investors' strategic priorities.

During our consultation process for this research we found that different areas had different answers to this question. In Birmingham, stakeholders felt that existing provision was serving their region well, and there was limited appetite to build a new regional community bank. Initiatives to scale up existing financial provision were welcomed, as well as a desire collaborate more in networks to gain economies of scale. In Manchester, Bristol, and Greater London, local stakeholders were keener to see a new type of financial institution serve their region and fill the gaps in existing provision.

Areas that experience expansive and impactful existing provision could consider facilitating and supporting those institutions to scale up. As well as financial support and direct investment, creating forums and institutions through which existing providers can collaborate and align can be a cost-effective and impactful way to scale up social finance. For example, Responsible Finance has published a detailed guide for how to tackle financial exclusion through local financial partnerships, and includes several real-world examples of collaboration between alternative providers to achieve this.[19]

Manchester is a great example of how existing financial institutions can collaborate to achieve enhanced service provision and greater social impact. But it is also an interesting case study of how local provision mapping can demonstrate that a regional community bank may still be desirable, despite the positive impact of existing providers.

In a recent paper from the Inclusive Growth Analysis Unit of the University of Manchester, the authors noted that bank lending to SMEs had fallen more in Manchester over the last three years than in comparative cities, whilst one in five local businesses report difficulty in accessing growth finance.[20] The report concludes that there is "a need for additional finance in Greater Manchester to support the growth of SMEs and social enterprises", and recommends that the Greater Manchester Mayor undertakes an impact assessment and feasibility study with a view to establishing a regional community bank there.[21] The roundtable focus group held in Manchester with local stakeholders, as well as follow–up deep dive interviews, supports the findings of the Inclusive Growth Analysis Unit.

2.3 GOVERNANCE MODELS – CHOOSING A MODEL TO SERVE LOCAL NEEDS

If the mapping exercise identifies unmet financial needs, consideration should be given to the best governance model for new institutions, or expanding existing institutions and partnerships. As described in in previous work by NEF, different models create different outcomes.[22]

We recommend considering three key criteria:

1. **Mission:** does the institution have a mission that is aligned with public objectives? This might include, for example, a commitment to serve the economy of a specific region, or to offer transactional banking services to those who cannot obtain a current account with high street banks. Is there a 'mission-lock' that prevents the mission being diluted or ignored in favour of other objectives?

2. **Risk and return:** would investment in the institution generate a sufficient combination of direct financial returns and broader economic benefits, including uplift to business rates revenue, to justify the risks associated with making the investment? Are the economic returns incidental to the institution's strategy or integral to its mission? How are financial surpluses distributed among different stakeholders, and how is that decision taken?

3. **Accountability separation of powers:** would investment by local authorities or other local anchor institutions create potential conflicts of interest and if so how will such conflicts be handled? Can the institution operate independently of control by major investors, thereby protecting them from being held accountable for particular lending decisions? It is particularly important in the case of investment by local authorities, where strict divisions between political objectives and lending decisions must be maintained and seen to be maintained.

The answers to these questions will influence the types of local financial institution that are appropriate for the local area and the investors' strategic priorities, and should help to determine where their investment is targeted in pursuit of local need and strategic priorities.

2.4 DIFFERENT BANKS, DIFFERENT OUTCOMES

Just as there are different types of financial institutions that deliver different types of functions and roles within a regional financial system, so too are there different types of banks. Whilst the impacts of shareholder-owned banking models have been previously highlighted by NEF, it is also important to note that different designs of stakeholder banks that have been attempted so far in the UK have had different results.[23]

One of the most widely cited has been Cambridge & Counties Bank, which has seen impressive rates of growth in developing a portfolio of £588 million worth of loans and deposits of £685 million in only three years of operation, turning an £18.1 million profit in 2016.[24] Cambridge & Counties Bank is often cited as a stakeholder bank because its owners that capitalised the bank are the Cambridge Local Government Pension Fund and Trinity College of the University of Cambridge. Yet, despite its name and being owned by two local stakeholder institutions, the Cambridge & Counties Bank is a shareholder-owned, private limited company. As a result, its loan and asset base is focused across the UK, delivering no specific local economic or social impact other than shareholder returns generated for its two shareholder institutions. Research participants also highlighted that Cambridge & Counties has largely sought to finance SMEs that have collateral to lend against, suggesting that they are not addressing a particular market failure, or serving the underserved.

Similarly, it has been widely reported that Warrington Council has invested £30 million in a new challenger bank, Redwood, "aimed at boosting investment in small and medium sized businesses in the town and beyond".[25] Like Cambridge & Counties Bank, Redwood has no specific local remit or social impact imperative baked into its structure and governance model. As a result, it's difficult to see how the bank will create and deliver geographically targeted social impact, or why it would serve the underserved. It is also targeting lending to businesses secured against property.

By contrast, there are some banking models that are designed with stakeholder impact in mind. One example is the Hampshire Community Bank (HCB), which aims to be a regional community bank – albeit with a slightly different banking model to that one put forwards by the CSBA, one designed by Local First CIC. This model includes specific provision to serve its local region, as well as the imperative to pursue social impact, and to include profit redistribution to local beneficiaries. In 2014, the bank secured £5 million worth of investment from Portsmouth City Council specifically on the basis that the bank would "help to create a strong, sustainable economy in Hampshire" including through increased SME provision, serving the financially underserved, distributing of surpluses "to support charitable and other deserving causes in Hampshire", and to act as a strategic partner for the council in delivering its economic and regenerative agenda.[26] Although the HCB has yet to launch to the public, the bank has initiated its banking license application and expects to be granted permission to operate with restrictions in 2018.[27] If it is successful in doing so, the HCB's specific social remit and locally-focused governance structure make it a promising proposition as a socially impactful stakeholder bank.

2.5 POTENTIAL STAKEHOLDERS AND THE VALUE OF A CSBA BANK

Based on the three roundtables, extensive interviews, and practitioner experience that informed this research, Table 4 summarises the potential stakeholders that could benefit from a regional community bank, and the value proposition that such a bank could offer.

Practitioners interested in setting up a CSBA bank should consider such stakeholders as potential allies and contributors. In addition, a case for investment can be made where the bank's value proposition improves service delivery and impact outcomes for the stakeholder to a significant degree. As a result, understanding the value chains and the way that a community bank could influence and support their service and operational delivery could help in recruiting these stakeholders' support, and the table below can be used as a starting point for generating buy-in and potential investment from each potential stakeholder.

TABLE 4: POTENTIAL STAKEHOLDERS AND CSBA VALUE PROPOSITION

TYPE	POTENTIAL STAKEHOLDER	CSBA BANK RELEVANT SERVICE PROPOSITION	VALUE PROPOSITION
Individual	Underserved or previously financially excluded	• Access to a full service current account • Budgeting tools and Jam Jar functionality • No unauthorised overdrafts • No debt products • Referrals to support service partners, eg: debt advice charities or financial education partners • Access to ATMs and branches in underserved areas • Transparent and predictable charging structure of £5 per month with no other fees or charges of any kind. • Ability to use broader range of evidence for 'know your customer' rules, and no credit checks unless credit is applied for, can allow full current account provision to those currently excluded.	Full service current account enables the individual to enjoy full access to the financial system, enabling them to cut costs through potentially significant mitigation of the poverty premium, as well as assistance with budgeting and prioritising payments. This helps to build the individual's financial health and confidence, whilst also offering a touchpoint for referrals and further service assistance. No unauthorised overdrafts or in-appropriate marketing and cross-selling of credit cards helps prevent the individual from falling into problem debt, whilst the bank's onboarding service orientates the beneficiary with knowledge of the bank's servic-es, the value they can derive from these services, and a route towards improved financial health outcomes
	'Everyday' customer	• High quality, low cost, full function banking services, including online & mobile banking and full product suite • Ownership & control of the bank through membership • Local & regional focus • Profit distribution through better interest rates, dividends, and bonuses	All customers receive a high quality banking experience with the full range of services and channels expected from a modern bank. Financial participation, ownership, and control exerted through the membership structure, engendering belonging and mutual trust, as well as being part of a community of mutual benefit that reinvests in the local economy. As a shareholding member, each customer also enjoys better interest rates and the opportunity to enjoy dividends and bonuses – the everyday customer both contributes to the success of the bank, and enjoys the fruits of that success
Business	SMEs	• Business current accounts with simple, transparent charging structure • SME-focused lending, including for non-standard and unorthodox businesses rejected by mainstream banks • 24/7 cash and deposit services via satellite branches • Genuine relationship banking • Ownership and control of the bank through membership • Profit distribution through better interest rates, dividends, and bonuses	Similarly to the service proposition for individuals, the bank provides a current account as its anchor product for SMEs. Unlike many high street banks, almost all transaction fees are included in the monthly charge for the account, thus increasing simplicity and potentially saving money for the business. The bank's ability to empower local branch managers to assess loan decisions is likely to enhance lending outcomes for non-standard businesses rejected by incumbent banks, whilst branch provision benefits cash-reliant businesses. As with individuals, business members also benefit from ownership and control of the bank, profit distribution mechanisms, and the economic and social regeneration effects that result from a locally and regionally focused financial institution
Government	Local authorities, councils, and combined authorities	• Local and regional economic regeneration, creating, capturing and recycling value in the local economy • Inclusive and sustainable growth, driven by a locally focused and accountable institution • Increased revenue from business rates as business outcomes improve • Direct revenue from investments in the bank • Enhanced job outcomes due to SME support • Reduced demand on support services, especially those related to financial exclusion • Can support and help to deliver resilience, regeneration, and inclusion strategies • Satellite branch site locations can co-locate with existing local authority services	The bank's model offers both social and economic benefits to local government directly through its service provision and indirectly through improvements to the local economy. Enhanced outcomes for underserved individuals reduces the demand burden on stretched local government services, as well as through enhanced job prospects. Likewise, improved business outcomes not only increase economic activity in the local economy, creating a local multiplier effect, but also can enhance business rates through improved business outcomes. As locally focused, geographically limited and accountable institutions, these banks can help to drive and deliver economic regeneration, resilience, and financial inclusion strategies for local government. At the same time, direct investment from local government enables a direct financial return through dividends and profit redistribution. Given the high concentration of potential customers, as well as the often extensive amount of land and community resources such as libraries, town halls, and council houses at their disposal, local government may also be attractive target locations for satellite branches, which the local government body could potentially subsidise or provide free of charge. This could have the added benefit for local authorities of increased use of their own services. Given their vested interest in local economic and financial health outcomes, local government bodies should be key targets for investment (see Section 2.8 below).

	National government	• Rebalancing the economy away from London • Investment in the real and productive economies • Improving financial inclusion outcomes • Improving the resilience of the financial system as a whole	Regional investment, enhanced business conditions and improved financial inclusion outcomes help to rebalance the economy away from London and the South East. The bank's focus on providing services to SMEs helps to rebalance the economy away from the financial services industry, while a more diversified financial services system that includes a broader array of different types of banks will help to make the system safer and more resilient as a whole. Given their vested interest in economic and financial health outcomes, national government bodies should be key targets for investment (see Section 2.8 below).
NGO and third sector	Debt charities and other service providers	• Specific provision and bespoke products for the underserved • Service referrals in both directions	Provision of products and services for those at risk of financial exclusion and vulnerability will help to mitigate and reverse negative outcomes for target beneficiaries of these NGOs and service providers. In turn, this gives those service providers a bank to whom they can refer their clients for such provision. Vice versa, the bank can refer its members and potential customers who are identified as at risk or in poor financial health to those other service providers.
	Housing associations	• Specific provision and bespoke products for the underserved • Service referrals in both directions • Satellite branch site locations	Housing associations host a high proportion of low income residents, and their rent revenue is directly affected by those residents' financial health. As a result, Housing Associations have a vested interest in promoting positive financial outcomes for their residents, and in promoting financial capability. The bank's financial health services offer the opportunity to encourage better outcomes, whilst Housing Associations themselves can be powerful referral agents of potential customers for the bank. Given the high concentration of potential customers, Housing Association developments may also be attractive target locations for satellite branches, which the Housing Association could potentially subsidise or provide free of charge
Financial Service Providers	Credit unions	• Transactional accounts • Referrals	The Rochdale Principles and the constitutional commitment to delivering social impact enables the bank to collaborate with credit unions that want a partner institution to refer their members to for transactional accounts. Equally, the bank may want to refer members to a partner credit union that are seeking financial education, or who are seeking loans but that don't fit the bank's risk profile
	CDFIs	• Transactional accounts • Referrals • Joint investments	Similarly, the bank has the opportunity to collaborate with CDFIs by becoming a referrals partner, particularly for those businesses seeking transactional accounts from the CDFI, or higher risk lending from the bank. In addition, there is opportunity for co-investment in projects where finance is sought from more than one institution
	Other banks	• Referrals • Investment returns	Although close partnership is less likely than with CDFIs and credit unions, incumbent banks may still want to enter into referral partnerships with a CSBA bank in a similar way as some do with credit unions and CDFIs and in Local Enterprise Partnerships. This is particularly the case where the CSBA bank could offer referrals in the other direction for bigger and/or more complex businesses. In addition, incumbent banks may become potential investors in the bank for the financial returns, particularly through their CSR funds or social impact subsidiaries, such as RBS' Social and Community Capital

Investors	Traditional investors, high net worth individuals, institutional investors	• Investment returns • Portfolio diversification • Social impact (dependent on investor interests)	The attractiveness of a CSBA bank to traditional investors will depend on their investment area interests, sought risk profile, and investment portfolio composition. The pitch to traditional investors essentially rests on the financial returns available through the bank's dividends and profit redistribution, as well as the opportunity for steady, long term returns, and the diversification of an investor's portfolio. The social impact profile of the bank may be of interest to some angel or individual investors, but is unlikely to appeal to traditional institutional investors. In addition, because of the limited geographic operations, acceptance of lower profitability customers, and refusal to offer higher return products such as unauthorised overdrafts, a CSBA bank has intentionally limited its growth and profitability prospects to be both organically grown and socially and economically prudent and sustainable. As a result, CSBA banks are not an attractive proposition for venture capital funds, who look for explosive growth and opportunities for quick exits at high profit.
	Social impact investors	• Opportunity to advance social impact outcomes and priorities of the social investor • Generate a financial as well as social return • Design, deliver, and evidence the provision of sustainable and socially impactful finance	Several social impact investors pursue priorities surrounding economic resilience, financial inclusion, and local regeneration. Depending on the nature and focus of the funder and their priority impact streams, a CSBA bank could add significant benefit to the advancement of the funders' goals. Through equity investment the funder would be in line to receive financial returns carried by the bank's shares and profit distribution mechanisms, the same as any investor or shareholding member would be. In addition, the direct provision of socially impactful financial services to the underserved could create the opportunity for a CSBA bank that is funded by a social impact investor to evidence the impact that its banking services are having, and to publicise that evidence. This could create significant additional value for funders engaged in financial exclusion, economic resilience, and regeneration, particularly those who fund research and advocacy programmes.

2.6 BUSINESS FORMATION AND BUILDING A BANK, STEP-BY-STEP

As well as the specifics of the banking model, the local economic and business climate, and the milieu of stakeholders, it is essential for anyone interested in establishing a regional community bank to appreciate that it is a business, first and foremost. That means that there are significant practical, organisational, and cultural aspects that need to be consciously built and designed, as there would be with any other business. The first and most important of these is assembling a team who have the skills, abilities, and perseverance to deliver such a complex and challenging project.

2.6.1 Assembling a team

Finding a lead – the bank's Chief Executive Officer (CEO)

The first of these is the regional bank's future CEO. This person will drive the project forward and will provide the main impetus for the bank's establishment, growth, and success or failure. The role of the CEO will vary and change throughout the lifespan of the project, particularly between the formation of the bank as an idea, and the realisation of the bank as an operational and ongoing concern. As a result, the CEO role would ideally be filled by a dynamic organiser who has the ability to understand the changing needs of the bank at the various stages of its development and lifecycle, as well as the ability and aptitude to be able to adapt to and deliver on those diverse needs. Given the CEO's overall responsibility for all of the bank's operations, it is essential that they have an extremely strong knowledge of the financial sector, preferably with a large network to call upon and experience within financial institutions to bring to bear for the benefit of the project.

Core Staff – Chief Financial Officer (CFO), Chief Compliance Officer (CCO), Chief Risk Officer (CRO), Chief Operating Officer (COO)
As with any complex business, there is a need for highly specialised and skilled individuals within the bank that can lead on the core functions that will enable the business to operate. Whilst diverse and highly differentiated, the roles of the CFO, CRO, COO, and CCO are essential for the effective management of the bank, and are highly specific roles. Ideally, each role would be filled by someone with previous experience in that role within the financial sector. However, given that the CSBA model is a regional socially impactful bank, the wages on offer for these roles are significantly lower than they would attract from a commercial bank. As a result, the CEO will need to find collaborators who are willing and able to fill these roles who are motivated at least as much by social and economic impact as they are with personal financial gain. These roles and job descriptions, as well as that of the CEO, are explained in detail in the CSBA's Senior Management Structure Manual, available on request from the CSBA.

Non-Executive Trustee Directors
As well as the executive staff, the CEO will need to recruit Non-Executive Trustee Directors to the board who want to further the bank's ethos, mission, and aims, and who have the ability to hold the executive to account – including the CEO. According to the CSBA bank constitution, the board may have no more than 12 members, of which a simple majority must be Non-Executive Trustee Directors. Board members are also required to sit on the various committees and subcommittees of the bank, and to provide leadership and guidance on questions of strategy, execution, reporting, compliance, and the effective and prudent delivery of the bank's services. In recruiting such directors, a variety and diversity of participants should be sought, both in terms of professional experience and competencies, as well as in terms of demographics and lived experiences. This will help ensure the bank has the widest array of perspectives and voices from which to draw, which will help strengthen the bank's performance, as well as to exhibit and further the bank's fundamental values of inclusion, fairness, and competence.

The Senior Management and Certification Regime
As well as the CEO and the four core staff members (the CFO, CRO, COO and CCO), the chairs of the Audit and Compliance Committee, the Remuneration Committee, and the Risk & Credit Oversight Committee will be covered by the Senior Management and Certification Regime, administered by the Financial Conduct Authority. This means that each person will need to be approved by the Bank of England before being able to take on their role at the bank, where approval is based on the applicant being a 'fit and proper person' to fulfil their duties, and on the bank outlining particular responsibilities and functions that those roles are required to deliver. These requirements are laid out in detail in the FCA Handbook and the PRA Rulebook, whilst the CSBA has provided the documentation required as part of the regime for its regional community banks.

Founding Members
In addition to the board and executive team, the mutual structure of a CSBA bank requires that the institution register with founding members. Board and members of the executive team can of course be founding members themselves, and where these have been recruited at the outset it makes sense for them to be so. Given the specific

skill sets and level of experience that is required for these positions, however, it may make sense to register the mutual with a cohort of founding members who are not part of the executive team or Trustee Directors. The benefit of doing this is that the mutual can be founded before all staffing positions have been filled, and in addition means that additional expertise and capacity can be brought in to the team at an early stage who can share some of the heavy lifting of setting up the bank. In particular, broader and more holistic skill sets that are not demanded by the core staff roles but that would benefit the institution are valuable to seek in founding members, for example expertise in fundraising, policy, communications, marketing, facilitation, administration, and so on.

It's also valuable to recruit founding members who have the time and capacity to contribute to the development of the bank at an early stage. Both executive team members and Trustee Directors are afforded paid positions in the bank once it is at operational capacity, whereas founding members are not. As a result, Trustee Directors and executive team members may be less able or willing to work until their remuneration can begin. Such a dynamic does not exist with founding members, and so they can be valuable additions to the fledgling organisation.

Developing the team
The Non-Executive Trustee Directors are professional and so expected to be paid once the bank raises funding. However it is likely to be possible to attract good Non-Executive Trustee Directors on an unpaid basis in the early stages. The spread of skills is mandated by the Bank of England, who have the final say over whether individuals and the board collectively are suitable. This is a key requirement of the banking license application process, and the CSBA are able to advise on this area. With the executive team, it's not necessary to have them all in place immediately, but they will need to be recruited and paid during the application phase. It is quite possible that the initial founder directors may not be the ones that end up launching the bank once it has its licence. However, some paid executive time is need quite early on if the bank is going to make progress with any speed towards preparing a compelling banking licence application and raising funding. Finally, the founding members are important for delivering the bank and generating momentum, as well as providing a good opportunity to embed key stakeholders from the beginning.

Given these differences in roles, skills, and capabilities, one route is to put together a start-up/launch team, possibly paid through a mixture of grant funding or seconded from other local stakeholder organisations, which gives way to a final executive team at launch. The key point is that there must be a core of competent and experienced staff with sufficient time to devote to starting up the bank. If it is left to people doing it voluntarily in their spare time there is a danger that the bank will never come to fruition.

2.6.2 Registering as a Mutual

Once a minimum of three founding members (which can include members of the executive team and/or Non-Executive Trustee Directors, and which should also include the CEO) the bank can register as a Co-operative Society under the Co-operative and Community Benefit Societies Act of 2014. The CSBA model does not propose creating any holding companies or complex arrangements involving setting up any Trusts or charities in addition to the Co-operative Society, and in many cases doing so may complicate matters. Instead, the Co-operative Society is a simple, transparent, and robust structure that can provide the corporate vehicle for the bank from start up to maturity, and which can begin to seek investment and to issue shares immediately. Specific guidance and the registration forms for establishing a new Co-operative Society can be found on the FCA's website.[28]

2.6.3 Signing an Exclusivity Deal with the CSBA

Any group aiming to deliver the CSBA stakeholder banking model must first strike an agreement with the CSBA themselves, and to sign an exclusivity arrangement that precludes other groups from establishing a CSBA bank in the same territory, and which stipulates the relationship, rights, and responsibilities between the two parties. Upon signing the agreement, the new Co-operative Society gains full access to the CSBA's 'bank in a box' which includes all the necessary paperwork, business and financial models, and support and guidance to bring the bank to fruition.

2.6.4 Getting a bank account

Next, to facilitate payments to and from suppliers, workers and partners, and to facilitate and receive investment, the bank must open a business bank account. Given the nature of the business and the potential competitive element, some high street banks refused to offer the first registered CSBA bank, the Greater London Mutual (GLM), a bank account of its own. As a result, it may prove difficult to register a new account for a fledgling CSBA bank – though at the time of writing Lloyds Bank was willing to provide an account and currently banks the GLM. In the future, it may be that established CSBA banks are able to offer new and start-up CSBA banks a business account to help them off the ground.

Bank of England Approval

The final stage for a new CSBA bank is to complete the Bank of England Approval process, and to gain a banking license. This is also the most difficult and time consuming stage. The CSBA has a completed template banking license application for its banking model, and has also secured partnerships with Linklaters and KPMG to deliver legal support and auditing services respectively for these banks. However, each bank that submits a banking license application will be wholly responsible for its delivery, and beholden to its demands and responsibilities. Therefore, it is essential that new Co-operative Societies established to deliver the CSBA model are fully literate in the agreements they are entering into, and fully comfortable being beholden to them.

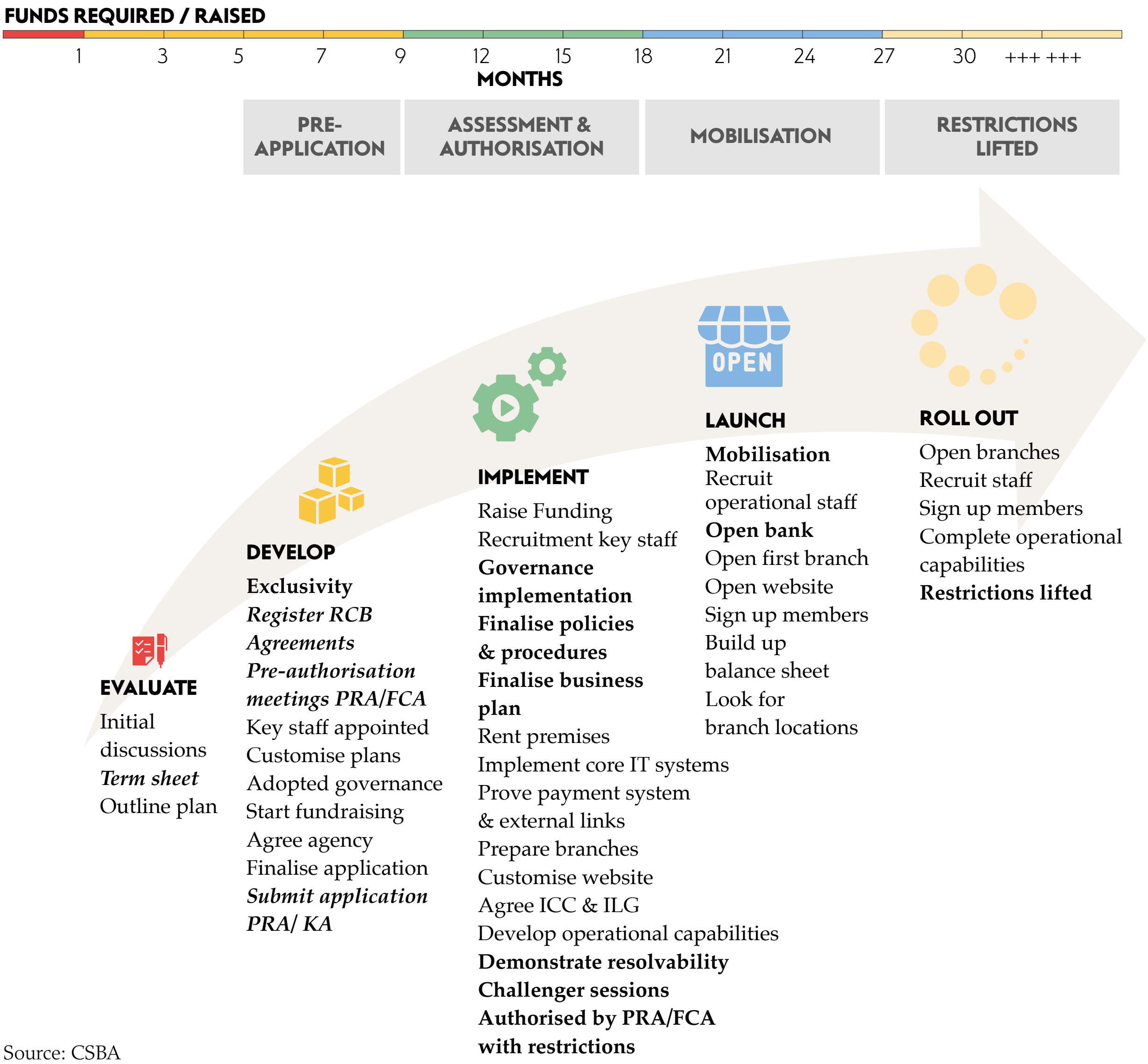
From submission, the banking license application takes 12 months to complete. In that time, the aspiring CSBA bank will need to meet stringent regulatory requirements around its systems, staffing, structure, and business plan, as well as demonstrating the resolvability of its balance sheet in the case of failure and to convince the Bank of England that it has a viable and realistic plan to scale to full operations. Most crucially, the bank will need to have raised the full £20 million equity by the end of the 12 month assessment period. If the aspiring bank fails in any of these regards, its application will be rejected and the Society will need to start the process from scratch. As a result, it is recommended that a significant proportion of the equity capitalisation is committed to or soft-circled before submitting the application and firing the 'starting gun' on the 12 month time frame. At the very least, the aspiring bank will want to have lined up an array of potential investors who can capitalise the bank, as well as to have raised enough start-up capital to employ the core staff for the 12 month authorisation period so that they can build the bank and satisfy the regulatory and capital requirements. The CSBA model estimates that this amounts to some £1.1 million of start-up capital, which is recommended to be raised before submitting the banking license application (see Section 2.8 below).

Building a business
Underpinning and throughout each of these stages, participants, members, stakeholders and staff will be building a new organisation. As a result, the building of a new bank includes the same dynamics and challenges that the founding of any new business entails. Systems and ways of working will need to be built from the ground up, including project management processes, communication channels, forums for collaboration, and the delineation and distribution of roles and responsibilities. As with any

"INERTIA IS THE BIGGEST OBSTACLE. PEOPLE NEED TO BELIEVE THAT IT CAN BE DONE"

CSBA LEAD

FIGURE 2: REGIONAL BANK DEVELOPMENT STAGES SMALL SPECIALISED BANK.



Source: CSBA

start up, these can often be messy, not clearly defined from the outset, and frequently overlapping, with the need for many contributors to 'muck in' as and when they can, often on voluntary time and at antisocial hours. This can create strategic as well as operational tensions within the start-up organisation, and it is incumbent on all participants to display collaborative leadership in building an institution that delivers on its values whilst harnessing the skills, experience, and commitment of those willing to build a bank from the ground up. The culture of an organisation emerges either by design or default, and can become a strategic asset to the institution or a drag on its productivity. As a result, it is important that the CEO, the executive team, and the Trustee Directors make regular time to focus on institutional development, and to nurture a productive and collaborative culture that builds a flourishing, values-led institution.

2.7 CAPITALISATION

The most challenging aspect of building a new bank, and of being awarded a banking license, is achieving capitalisation of £20 million. Despite being a relatively small figure in the context of the banking industry, it is still a sizeable capitalisation target for a new community organisation to achieve.

At the time of writing, there are currently no CSBA banks that have yet achieved the £20 million capitalisation target. Accordingly, we naturally recommend that practitioners and aspiring CSBA bank Co-operative Societies pursue capitalisation strategies and targets that make sense to them, and which leverage the networks, knowledge, and expertise of the contributors in the Society. Table 5 outlines a proposed example strategy for approaching the capitalisation target, and includes suggestions of where, who and what to target for the different phases of capitalisation, as well as what their money would be put towards.

2.7.1 Phases of capitalisation

Given the high capitalisation target, it is unrealistic to expect to raise the full £20 million in one lump sum. Furthermore, investors will want to be reassured that the project is developing adequately, and that initial funds are being spent in a way that makes full capitalisation most likely. There are also different risks associated with investing in the business at different times, and so different potential funders will be more or less appropriate at different stages of the fundraising drive. As a result, a phased approach to capitalisation that enables different investors to come on board at different times is most likely to yield the best results. This approach is summarised in Table 5, and then outlined in greater detail below.

Stage 1 – Start-up

This phase of funding enables the model to be tailored to local circumstances, to conduct feasibility and impact assessments, and to pay for contributors' time to continue raising funds and developing the business. Given the higher risks associated with earlier stage investment, targets for the first investment phase should be patient investors that place a high value on the potential social impact of the project. Convincing potential investors to become the first mover can often be the hardest phase of capitalisation, so it may also be the case that such investors should be offered improved terms to reflect and reward the higher risk that their investment carries. The rules and regulations around such rewards are complex for Co-operative Societies, though there may be ways of navigating them through the awarding of bonus shares, for example.

TABLE 5: CAPITAL INVESTMENT PHASING FOR A CSBA BANK

STAGE	TARGET	WHAT WILL THE FUNDING BE USED FOR	KEY TARGET INVESTORS
Stage 1 – Start-up	£150k - £300k	Market research and tailoring of model to local circumstances. Recruit board. Start application process to gain feedback from regulators.	• Social investors • Charitable foundations • Social impact funds
Stage 2 - Authorisation	£1 million - £2 million	Recruit executive team. Conclude supplier contracts, build back office, IT and operational infrastructure. Obtain provisional banking licence.	• Social investors • Charitable foundations • Social impact funds
Stage 3 - Mobilisation	£4 million - £5 million	Open branches and online channels, recruit branch managers and staff, training, as well as designing policies, procedures, and products.	• Social investors • Charitable foundations • Social impact funds • Local authorities • Pension funds • Investment funds • CSR funds • Angel investors
Stage 4 - Launch	£13 million - £14 million	Full capitalisation can take place once an unrestricted banking licence is obtained, but investor commitments must already be in place to achieve the licence. This provides regulatory capital requirements for the bank to begin to build its balance sheet.	• Social investors • Charitable foundations • Social impact funds • Local authorities • Pension funds • Investment funds • CSR funds • Angel investors
Stage 5 - Crowdfund	£1 million	To take place at the same time as the launch fund raise, the crowdfund helps to build a customer base whilst also providing a marketing opportunity for the new bank.	• Members • The public

Stage 2 – Authorisation
Completing the Bank of England's authorisation process is a long and complex undertaking, which also requires significant recruitment, partnerships, and the building of significant infrastructure such as the head office and first principal branch. By this stage, the bank will have secured some initial investment, which should make attracting investors who will go 'bravely second' somewhat easier. In addition, the authorisation funding enables the bank's core staff to make tangible progress towards the building of the institution and the achievement of a banking license, generating momentum and visibility which can be leveraged for further fundraising. Given the clear sequencing of expenditure outlined in the CSBA corporate and business plan, investment can also be raised against specific deliverables and milestones during this phase, such as the location and acquisition of principal and satellite branches.

Stage 3 – Mobilisation
At this stage, the bank's scale and operations increase significantly. The CSBA regional banking model requires three principal branches at launch, as well as the recruitment and development of a fully staffed customer support centre and greater compliment of head office and backroom staff. Policies, products, and procedures will need to be in place before launch, and marketing and promotions can begin in earnest at this point.

Stage 4 - Launch
This is when the lion's share of capital will need to be raised through completing the purchases of share

capital equity. This enables the bank to satisfy regulatory requirements on capital reserves and to allow the bank to begin to build its balance sheet through operations. To obtain a banking license the aspirant bank will need to prove that it has the ability to raise this amount of capital, but the investments won't have to actually be subscribed until the Bank of England approves the bank's license application, which provides a degree of risk mitigation for the bank's investors.

Stage 5 – Crowdfunding
A significant part of the launch capital can be sought from crowdfunding, which as well as being a capital raising exercise also provides an opportunity to market the bank and to provide visibility and consumer demand for the bank's services. There are some prominent examples of start-up banks raising and surpassing £1 million fundraising targets through crowdfunding campaigns,[29] which has the added benefit of creating a database of retail investors and potential customers for the bank to launch with. Crowdfunding can also help to increase the bank's transparency and connection with its investors and future members, through things like investor events and other rewards for crowdfund investors.

Equally, there are also prominent examples of crowdfunding campaigns that have generated significant capital and goodwill, only for the product or service never to come to fruition, eroding trust and losing investors' money. As a result, a crowdfunding campaign for a bank fundamentally predicated on mutual trust should only be attempted once the chance of successful launch is already very high, and the majority of capital has already been raised.

2.8 LOCAL AUTHORITIES AND COUNCILS IN FOCUS

Due to their strategic interest in inclusive growth, economic regeneration, and financial inclusion, and their opportunity to benefit from improved business outcomes through retained business rates, local authorities and councils are a key target for investment in these regional community banks.

There are a number of different pathways through which local authorities and councils can invest in these banks, but critical to all of them will be convincing the authority that the bank will help them deliver on their strategic priorities for their area of operation. Most authorities publish their strategic and operational plans on their websites, so taking the time to understand how a regional bank could intersect with and advance these agendas will be crucial in generating mutual understanding, interest, and engagement with the bank. The support of both councillors and finance officers (Section 151 Officers) will be critical to securing investment from authorities, and aspiring stakeholder banking practitioners should seek to engage both elected councillors and Section 151 Officers for this purpose. Other roles within local authorities may also come to be useful allies and advocates for investment, such as resilience officers, financial inclusion teams, business support and economic regeneration departments, or even the leaders of the council or authority. In each case, it's essential to understand the bureaucratic and political dynamics that exist within each authority and each region, and to gain the support of the most influential stakeholders, which will vary from place to place.

The primary piece of legislation that enables council investment into these types of banks is the Localism Act of 2011, which confers a general power of competence on authorities and enables them to "do anything that individuals generally may do" including the power to act "for a commercial purpose" and to act for "the benefit of the authority, its area or persons resident or present in its area."[30] Some research participants cited using this legislation successfully to persuade their authority to invest in credit unions, and the same argument can be used to invest in a regional community bank. Similarly, Portsmouth City Council, Tees Valley Borough Council, and Winchester City Council all reference this power in their decisions to recommend investment into the Hampshire Community Bank,[31] whilst the Portsmouth decision includes reference that:

> *"Creation of the Hampshire Community Bank would be in line with the following strategies: the LEP Strategy for Growth, Portsmouth City Council's Regeneration Strategy and the Medium-Term Financial Strategy that aims to drive regeneration, reduce the demand for council services and reduce the council's reliance on central government grant."*

These minutes demonstrate the potential leverage points that may convince councils and authorities to take the decision to invest in a regional community bank, so understanding these frameworks and strategies is crucial.

In addition to these authority specific strategies, a general framework for authority investments is laid out by the Chartered Institute of Public Finance and Accountancy in their Prudential Code of Practice for Capital Finance in Local Authorities, which stipulates that authorities must take due regard to the following aspects when weighing up an investment decision:

- **Affordability,** ie: implications for Council Tax
- **Prudence and sustainability,** ie: implications for capital receipts or external borrowing
- **Value for money,** ie: appraisal of options
- **Stewardship of assets,** ie: Treasury Management policy
- **Service objectives,** ie: implications for the strategic plan
- **Practicality,** ie: achievability of capital programme[32]

Each council has specified how it has interpreted these guidelines, and has published Treasury Management Strategies that outline investment and borrowing policy at the local authority level.[33] Being able to reference these Treasury Management Strategies and to outline how the regional community bank aligns with them will help to reassure and encourage a potential investor authority, and may help facilitate their investment.

3. INVESTMENT PATHWAYS

3.1 LOCAL AUTHORITIES

Local authorities are key targets for investment in a regional community bank, and there are a number of ways that they can structure such investment. The simplest and most attractive for the aspiring bank is through an equity investment where the authority buys a number of shares commensurate with their level of support, at £15 per share. This would make the authority a member of the bank, conferring the rights and responsibilities that come with it. An equity investment would enable the bank to spend funds in an unrestricted way in accordance with the business and financial plan developed by the CSBA, or could provide Core Equity Tier 1 Capital for the bank depending at what stage of capitalisation the investment was made at. A successful pitch for equity investment from local authorities and councils would leverage the value propositions outlined in Table 4 above, whilst also aligning with the authority's strategic priorities and Treasury Management Strategy as outlined in the previous section. Such investment would be subject to due diligence procedures and approval by the finance and scrutiny committees of the authority.

Another way for local authorities to structure their investments that research participants highlighted was the potential for authorities to invest through debt financing, providing loans to the bank that would later be paid back. This investment pathway is much less attractive than equity investment for the aspirant bank, because the interest rate charged on the loan would create a drag on operational and developmental spending, and may discourage equity investors whose capital would be at greater risk than the subordinated loan of the authority. Technically speaking, deposits made into the bank would also constitute debt financing that would require interest to be paid on top, so an aspirant CSBA bank should not be short of debt finance. Consequently, such an investment type would not be attractive for a CSBA bank under most circumstances, even when blended with equity investment.

There are also a number of ways that authorities can finance these investments. The first and most simple is through investing their reserves, which remain significant at some local authorities. In 2015, the sector held around £22.5 billion in cash reserves.[34] With interest rates so low and inflation creeping up, the value of these reserves is essentially being eroded whilst it sits in transactional or short-term deposit accounts. Although many councils will have structural or political impediments to releasing these funds, and although many will be averse to investing reserves at risk, the size of the sectors reserves and the opportunity to make significant long-term returns through investment in a CSBA bank makes this a viable investment pathway to explore.

Another way for local authorities to finance their investment would be to utilise the Public Works Loans Board (PWLB), and to make use of the historically low interest rates that this central government financing facility offers. Authorities are well used to utilising the PWLB to make commercial investments and to generate additional revenue streams, with councils spending £1.2 billion in 2016 on commercial real estate that was primarily financed through the PWLB.[35]

Councils usually utilise this facility to generate additional revenue streams, predominantly by making arbitrage gains on the interest rates that they apply to their on-lending (known as a 'carry trade'), or by investing in projects that carry rental or other commercial revenue streams. However, utilising the PWLB to invest in a regional community bank could instead be done at cost, given the social and economic benefits that such an investment would facilitate. Under such an arrangement, the council would borrow the required funding from the Public Loans Work Board, and charge the same interest rate (currently 1.2%) plus a small additional rate to cover the costs of providing the loan (around 0.25%). A deal structured in this way would not be appropriate for the early stages of capitalisation due to the higher risks involved and the longer timeframe that the bank would require to become profitable. Instead, a deal structured in this way would be more appropriate for the latter stages of capitalisation once the bank has received its authorisation and needs to build its capital base.

"COMMERCIAL REAL ESTATE IS EASY TO PROJECT AND IS SAFE, BUT THE RETURN ISN'T GREAT. IF YOU CAN GIVE A HIGHER RETURN THAN THE PWLB THEN THERE WILL BE INTEREST."

COMBINED AUTHORITY LEAD

One research participant described how this deal structure could be useful in growing a finance institution's loan book, whereby the subordinated loan is drawn down on only as and when additional capital is needed to cover the capital requirements of making additional loans. If the CSBA financial model is delivered upon, however, there will be no need for additional capital support for growing the loan book, as this will be provided by deposits and by members joining the bank and investing capital through their mandatory purchase of at least one share. As a result, subordinated loans may be more appropriate for the financing of other socially impactful financial service providers such as credit unions, particularly where it is used to provide the capital reserves that weight leveraged lending.

3.2 CATALYTIC INVESTMENTS AND DEVELOPMENT FUNDS

As described above, the first investment can often be the most challenging to secure. As a result, catalytic investments and development funds can often be a good target to help overcome the first mover hurdle, and can help to attract in further investors who would be reassured by earlier investment from public-backed sources. There are several of these types of investments on offer, and they differ across the country. Often they will be funded and/or administered by local or regional government, and are often targeted at economic regeneration or improving business conditions in a specified area. Examples of such funds include the Good Growth Fund in London, the Northern Powerhouse Investment Fund, and the various live programmes that are backed by the Regional Growth Fund.[36]

3.3 SOCIAL IMPACT FUNDERS AND CHARITABLE FOUNDATIONS

Another key investment pathway is through the support of social impact funders and charitable foundations, which frequently offer investments, loans, and grants. Whilst loans are unattractive for the reasons outlined above, equity investments and grants remain attractive for an aspiring bank. In both cases, applicants to the social impact funder will need to appeal to their strategic impact priorities, and to demonstrate how investments or grants will help to further their aims.

Regarding grants, it is highly unlikely that social impact funders and charitable foundations would provide grants as unrestricted CET1 capital. Grants are primarily provided on a restricted basis, and as such are required to be spent in a specific and prescribed way. As a result, grants can be useful in developing specific aspects of the business or the

"WE WERE PREPARED TO INVEST UP TO £1M AS CORE TIER 1 CAPITAL. WE CAN BORROW AT AROUND 1.2% PER ANNUM FROM THE PWLB, AND THAT DOESN'T COUNT AGAINST OUR BUDGET EXPENDITURE. IF WE BORROW AND LEND IT WOULD REMAIN AS A CAPITAL ASSET ON THE BALANCE SHEET AND WOULD NOT REFLECT OUR REVENUE POSITION. IT WOULDN'T BE THAT WE WOULD JUST DUMP THE MONEY IN THEIR ACCOUNT, WHAT WE WOULD SAY IS THAT AS YOU EXPAND YOUR BUSINESS, WE WILL PROVIDE THE CAPITAL NECESSARY TO MEET THE REGULATORY REQUIREMENTS AND YOU CAN DRAW DOWN AS AND WHEN NECESSARY."

LOCAL COUNCILLOR

investment proposition that buttress and support the capitalisation and development of the bank. For example, a social impact funder might be more inclined to provide grants to enable the bank to design its social impact framework, to fund a feasibility and impact assessment, or to develop a bespoke financial product that would serve the funder's impact priorities. In London, the aspirant CSBA bank the Greater London Mutual secured a £120,000 grant from the Big Potential Advanced fund to develop its service model for reaching and supporting the financially underserved and excluded.[37] Most social impact funders display their impact priorities publicly on their websites, and have formal processes for applying including funding rounds and deadlines throughout the year.

As well as grants, social impact funders and charitable foundations may see an equity investment as a good route to achieving their targeted blend of social and financial returns. Normally this is a different process than applying for grant funding, and can be pursued through close consultation with interested funding bodies. The social impact investment sector in the UK is highly collaborative and integrated, and so many funding bodies have the power to convene other funders and to make joint- or match-investments in step with each other. Equally, if influential social impact funders reject the case for regional community banks, or are otherwise unconvinced by the proposition on offer for whatever reason, their reluctance may influence other social impact funders.

3.4 PUBLIC PENSION FUNDS

Another potential investment pathway that was mentioned prominently by research participants was public pension funds. Unlike mainstream and incumbent funds, pensions managed on behalf of public sector workers often include greater consideration of social, economic and sustainability principles. In addition, the structure of the public pension fund sector is undergoing dramatic and wholesale change, which provides a strategic opportunity to pitch for investment from these funds.

Following a shake-up of Local Government Pension Schemes (LGPS), 89 pension funds connected to local authorities that were previously distinct are being pooled into eight larger regional pension funds.[38] As part of this process, each LGPS is required to review and update their risk management and investment strategy documents that control them, obtaining professional advice and consulting fund members on proposed changes. The output of this process is an Investment Strategy Statement (ISS), which as well as outlining the general direction of travel for the fund, specifies target asset allocations that the fund wants to allocate its resources to. Often these asset allocations include stipulations for private equities in the UK, as well as infrastructure investments – both of which a regional community bank could arguably qualify for.

This creates a strategic opportunity for investment where LGPS and pooled pension funds have yet to achieve their target asset allocations for infrastructure or UK private equities. In addition, these ISS documents are often still being consulted on and designed, and are required to be published no later than April 2018. Following this, ISS frameworks are required to be reviewed and updated every three years. Consequently, both during their current initial formation and their periodic reviews, there is opportunity to engage with and influence LGPS members and the fund managers who serve them towards investing in aspirant CSBA banks. The time and capacity demands likely to conduct a campaign that could successfully influence the design and structure of an Investment Strategy Statement should not be underestimated, but engaging with LPGS and pooled funds on their asset allocations and how to interpret and implement them could still be a valid investment pathway for aspirant CSBA banks.

3.5 ANGEL INVESTORS AND HIGH NET WORTH INDIVIDUALS

Of course, there is also the opportunity to attract investment from individuals and philanthropists, particularly where they are minded towards social and economic impact. Such investors are often difficult to find and inundated with requests for investment, so building and leveraging personal connections and networks is crucial. There also exist private investor networks, public investor forums, and bridging organisations that match investors with opportunities such as

ClearlySo. Although these can often be hard to find and to be approved by, individual investors can be highly impactful for start-up businesses seeking capital, and should also be considered as a valuable and viable investment pathway.

3.6 VENTURE CAPITAL

Generally speaking, venture capital (VC) is not a viable route for investment for an aspirant CSBA bank. The CSBA model has been specifically designed to grow organically, prudently, and within geographical boundaries. As well as this, the bank is able and committed to serving lower profitability customers as part of its social mission which limits the rate of profit growth at the bank. Finally, due to its cooperative governance structure, large shareholders gain no more control over the institution than members with only one share – which all members are required to buy when they join the bank. As a result, a CSBA bank does not fit standard VC requirements of having significant control, a clear short term exit route and a high multiple capital gain on the initial investment. There may be some more blended forms of social or impact venture capital willing to take longer term equity stakes with lower financial, but higher social returns, however in general VC investment should not be treated as a priority by aspirant CSBA banking practitioners.

4. FINAL THOUGHTS

10 years after the financial crisis and significant shortfalls remain in banking provision in the UK, despite regulatory reform and various new challenger banks emerging. Stakeholder banking models have long been suggested as promising alternatives ready to fill the gaps left behind by incumbent banks, as well as to buttress, support, and collaborate with existing alternative financial provision. The weight of evidence supporting these models has grown, and so has the cohort of practitioners that are attempting to establish such banks.

The stakeholder banking model designed by the CSBA has demonstrated that fully co-operative, locally focused, and socially impactful banks are possible within the existing legal and regulatory framework. Their 'bank in a box' framework has overcome several significant barriers that previously existed in setting up a bank, including securing economies of scale, operational partnerships, approval for the banks constitution from the Bank of England, the creation of a viable business and financial model, and the extensive banking license application itself.

We hope that this Local Banking Toolkit also contributes to the ability of practitioners to get these banks off the ground, by summarising the evidence base around stakeholder banks, by providing a practical and pragmatic guide on how to set one up, and by sharing and amplifying existing knowledge and experience from across communities of practice in this area.

Stakeholder banks are both desirable and achievable in the UK. All that is needed now for their fruition is for people with sufficient motivation and ability to rise to the challenge by recruiting their team, raising the capital, and building a better bank.

We wish you the best of luck in these endeavours, and look forward to seeing the development of locally-rooted, socially impactful financial institutions up and down the country.

5. FREQUENTLY ASKED QUESTIONS

1. **Why a bank?**

   Banks can provide a full suite of financial services, allowing them to be a customer's primary financial institution whilst also enabling full financial sustainability for the institution. Banks are less inhibited by regulation or scale requirements than other forms of alternative financial provision, and are also uniquely able to expand the money supply at scale. This means that their impact can be much larger in terms of their reach and scale of support for the economy, as well as becoming an anchor institution for the local economy. For more information see Section 2.2.

2. **Why 3 million people?**

   The Bank of England has indicated that this is the scale at which the risk of having too concentrated a balance sheet is sufficiently minimised for them to approve a banking license application. In addition, a target market of 3 million people enables the bank to become sustainable at only a very small proportion of market share by volume, and an even smaller proportion by value.

3. **Isn't that too big for a local bank? Won't the bank lose its local focus and recognisable identity at that scale?**

   The CSBA model is delivered through principal branches that function as autonomous bank branches, with local Branch Directors empowered to make lending and other decisions themselves. This distributed authority enables the tailoring of services and operations at the local level, whilst the 'umbrella' of the regional bank enables economies of scale and requisite size to provide financial sustainability. In other words, the principal branches can act like local banks whilst the larger CSBA bank entity serves its region.

4. **How can a regional bank deliver social returns for locally mandated investors?**

   Through its locally focused principal branches. This has the additional benefit of being able to disaggregate lending and impact metrics across localities as well as regions, which is also enabled through the CSBA model's co-operative structure and commitment to transparency.

5. **What is the target market of the bank?**

   The CSBA regional banks aim to be fully inclusive, serving anyone and everyone living or working within their defined territory of operations. For financial sustainability, these banks will need a thorough mix of individuals from across the socio-economic brackets, as well as local businesses and SME members. The CSBA banking model is not a bank specifically for the underserved. It is a bank that is able to serve the underserved due to its sustainability profile and commitment to full inclusivity in its region.

6. **Why would the bank expect to lend to SMEs when they are so inherently risky?**

   The autonomy afforded to local Branch Directors enables them to use a broader array of 'soft information' to make lending decisions based on their own expertise, local conditions, and the specifics of the business requesting the loan. Unlike existing incumbent banks, stakeholder banks like the CSBA model are more able to take a wider diversity of information into consideration, as well as having lower operating and capital costs which mean they do not have to make as high profits on these loans. For more information, see Section 2.1.

7. **How does the bank hope to be sustainable when it is targeting unprofitable customers and the underserved?**

   The bank will not target the underserved exclusively. Instead, the bank is able to serve previously excluded individuals and businesses through its unique governance model, low operating costs, commitment to inclusion, and lower profitability requirements. Significantly, the bank will be targeting all demographics and customer types to enable its sustainability and to cross-subsidise underserved customers. Finally, the financial model has been designed such that even underserved or previously excluded individuals will break even for the bank rather than create losses, due to the monthly account fee and revenue derived from usage of their debit card that is levied on other financial institutions rather than the customer.

8. **Why does the bank charge a monthly membership fee?**

   The bank charges a transparent fee that represents a fair valuation of the cost of running a customer's current account, set at £60 per year. The free-if-in-credit model widely provided by other banks is only made profitable through charges and fees that have historically disproportionately negatively affected those on the lowest incomes. In particular, mis-selling and unauthorised overdrafts have been particularly burdensome, and the CSBA model structurally and explicitly prohibits both. Instead, the bank charges a fair, transparent, and upfront cost for its services.

9. **How does the bank hope to reach the poorest when it is charging for its accounts?**

   The average costs associated with the poverty premium that are directly associated with lack of access to a full-service current account are on average £307 a year. This means that a CSBA account can still save £247 a year for the most financially vulnerable in society. In addition, partners that are focused on financial exclusion or that provide services to those at risk of financial exclusion may have a vested interest in subsidising or paying this membership cost on behalf of their beneficiaries.

10. **Why would someone switch their account when other banks don't charge monthly fees?**

    No other bank offers the same level of accountability, control, or local and social impact. The bank offers a number of added value services that are not common amongst other service providers, such as jam jar accounts and budgeting tools, whilst also providing services that are unencumbered with legacy issues or old technology. The bank is based on mutual trust, prudence, and inclusivity, and also enables participation in its strategy and direction through its co-operative governance. No other bank can offer this confluence of benefits, and we believe that there is a large enough cohort that is willing to subscribe to this offer.

11. **What do I get if I invest in the bank?**

    As well as helping to deliver a locally rooted, socially impactful bank for your region, investment in a CSBA bank carries a number of rights and responsibilities as a member of the co-operative. These include the right to attend and vote as well as to propose motions at the annual general meeting, and to receive savings bonuses and financial dividends on shares held.

12. **Why £20 million? That's a hell of a lot for a local bank.**

    £20 million is the amount of equity capital needed to build a sustainable bank at a regional scale. This includes enough capital for all start up and capital expenditure requirements, as well as providing the CET 1 capital to build a locally focused loan book. Whilst £20 million is certainly a lot of money, it is also a very small target for a bank. For example, Warrington Council's investment in Redwood Bank was £30 million for a 30% stake into a bank that is not designed for local or social impact. By contrast, a CSBA bank will apply that capital investment to deliver on local strategic need.

13. **Why build a new institution when we can scale up what we have?**

    Whether or not to found a new regional bank should be decided by the stakeholder living within the region and by the needs and gaps of the local market. In some places it may be the case that existing provision is sufficient and simply needs support to scale up; in other areas it may be the case that there are gaps that only a bank can fill. In either case as well as in a blend of the two, the most important factor is to create provision that is adequate for and responsive to local needs. For more information, see Section 4.2.

14. **Won't these banks compete with other socially impactful financial institutions for scarce funding, resources and market share?**

    We believe that regional banks can be complimentary to existing alternative financial provision, rather than in competition. This is particularly the case given that credit unions and CDFIs often seek to serve customers that are beyond the CSBA bank's desired risk profile, but equally that need transactional services that those institutions rarely offer. Collaboration and coordination between alternative financial providers is highly desirable and socially impactful. For more information, see Sections 2, 4.1, and 4.3.

15. **What is the social impact that these banks hope to achieve?**

    These banks hope to advance significant amounts of finance into local and regional economies, boosting business outcomes whilst rebalancing the economy away from London and strengthening the diversity and resilience of the financial sector as a whole. The CSBA model enables full inclusion, meaning they can be used to tackle financial exclusion and the poverty premium where they exist. The banks aim to create a diversity of provision that enhances competition and service provision across the sector, whilst also providing value-added services to all members. In addition, the CSBA banks enable financial participation, accountability and control to normal members of society in a way that no other bank can or will do. In short, the social impact that these banks hope to achieve is both widespread and significant.

16. **Can a bank be set up both to reduce financial exclusion, and to bolster SME lending, or should these two objectives be tackled separately?**

    Yes, in fact they are more able to tackle financial exclusion because of their SME lending, not less. SME lending, as well as provision to those in good financial health, provides the revenues needed to sustainably serve these cohorts.

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WWW.NEWECONOMICS.ORG
info@neweconomics.org
+44 (0)20 7820 6300 @NEF
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WRITTEN BY:
Fionn Travers-Smith

CO-AUTHOR:
Frank van Lerven

COVER IMAGE:
iStock.com/Joas

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