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The Promise of Impact Investing

Rarely has a field been so energized by a new idea. Impact investing in its various forms has opened the door to new forms of capital for new forms of social enterprise organizations that promise to deliver measurable social and environmental results through use of market mechanisms. Paradoxically it was the failure of the global financial system in 2008 and its repercussions on private and public spending that have sparked a new interest in harnessing private capital to solve society's biggest challenges, be it education, healthcare, or poverty alleviation.

There seems to be a discernible shift in the spectrum of financial flows for social change. While the bulk of investments are still in the form of grants and donations in the United States (and government expenditures in developing countries), impact investing is beginning to emerge as a significant new form of social capital, where investors seek to recoup their capital at, or below, market rates – clearly looking for financial returns in addition to social returns inherent in the activities of the invested organization. J.P. Morgan and Monitor Institute have each independently estimated the immediate size of the global market to be at least $500 billion in the next decade.

Innovative experiments in social investing are already emerging in countries around the world—from Mexico to India to the United Kingdom. And, all the while, this burgeoning movement is taking place in the midst of an intergenerational wealth transfer estimated at $41 trillion over the next 50 years, of which nearly $6 trillion is expected to be directed towards social problems.[1]

It is against this backdrop that we are gathered at the Harvard Business School to construct a role for a forum such as ours to influence the field and shape the future development of "social capital markets," much in the same manner that the School influenced the development of the field of venture capital. The aim is to gather a small group of "investor" organizations at the leading frontiers of this field to understand what would constitute success for the field. More specifically given Harvard Business School's historic focus on the "enterprise" as the unit of analysis, our aim is to understand the opportunities and challenges facing investors, intermediaries, and implementers, and to facilitate the development of solutions to the problems they face. Our ultimate goal is social change, but our immediate aim is to facilitate this through the social enterprise organizations that engage with the problems every day.

[1] John J. Havens and Paul G. Schervish, "Why the $41 Trillion Wealth Transfer Estimate Is Still Valid: A Review of Challenges and Questions," *The Journal of Gift Planning* 7, no. 1 (January 2003): pp. 11-15, 47-50. Also, Havens and Schervish, *Millionaires and the Millennium: New Estimates of the Forthcoming Wealth Transfer and the Prospects for a Golden Age of Philanthropy* (Social Welfare Research Institute at Boston College, October 19, 1999), http://www.bc.edu/content/dam/files/research_sites/cwp/pdf/m_m.pdf, accessed October 2011.

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While the impact investing hype is perhaps justified, a modest dose of skepticism should keep us honest as we press ahead with this "new space." As mentioned before, ultimately the goal of impact investing is to make a significant dent on many of the world's daunting social and environmental problems. Can private, profit-motivated investment deliver permanent social change? The optimists will cite the so-called success of microfinance, where today over $50 billion is loaned to over 100 million micro-entrepreneurs in countries such as Bangladesh, India, and Mexico. While microfinance initially started out predominantly as a nonprofit industry, today some of the world's largest microfinance organizations such as SKS Microfinance in India and Banco Compartamos in Mexico have a significant portion of their equity capital held by investors. The pessimists no doubt will point out the lack of any other industry, apart from microfinance, which can boast similar results at scale, the die-hards among them questioning whether even microfinance is the success it is touted to be, given the current state of the Indian microfinance industry.

In all fairness, impact investing should not be charged with carrying all the burden of addressing humanity's social and environmental problems. Consider the following facts: Two billion people on the planet do not have access to safe water, heath care, or financial services. A billion people do not have access to electricity. Two hundred and fifty million children do not have access to education or childhood immunization, with 2.5 million dying every year as a result. In our own country, 47 million Americans do not have health insurance, 25 million are below the poverty line, and 15 million are unemployed. Our senior citizens in 25 years could be without Social Security or Medicare. We are consuming the earth's natural resources at an alarming rate even while dangerously increasing the earth's temperature through damage to its protective stratosphere. In the next 25 years there is likely to be a severe shortage of water even in developed countries. And so on. . . . Obviously without public investment and leadership there cannot be lasting solutions to the huge challenges facing our society. The lessons from the last two decades of development, however, suggest that with private enterprise participation, it is possible to unleash the power of market mechanisms to break down these challenges into smaller more manageable parts and attack them in a sustainable manner, more efficiently and effectively than what government alone can do. Our aspiration therefore is to study and inform mechanisms that significantly expand the role for private enterprise in addressing the world's most pressing social problems. While impact investing is not the silver bullet, at least we should be able to say "we moved the needle." The aim of the forum is to advance knowledge that will enable investors, intermediaries and implementers to all perform at a level that will ensure success for the industry.

Defining the Field

***Impact investing**: Actively placing capital in businesses and funds that generate social and/or environmental good and at least return nominal principal to the investor.*[2]

The commonly accepted definition for impact investing is investment that creates social or environmental benefits while also providing a return of principal, with returns ranging from zero to market rate. Investor intent to create a social or environmental impact is also necessary; accidental

[2] Monitor Institute, *Investing for Social and Environmental Impact: A Design for Catalyzing and Emerging Industry* (Monitor Institute, January 2009), p. 11, http://www.monitorinstitute.com/impactinvesting/documents/InvestingforSocialandEnvImpact_FullReport_004.pdf, accessed October 2011.

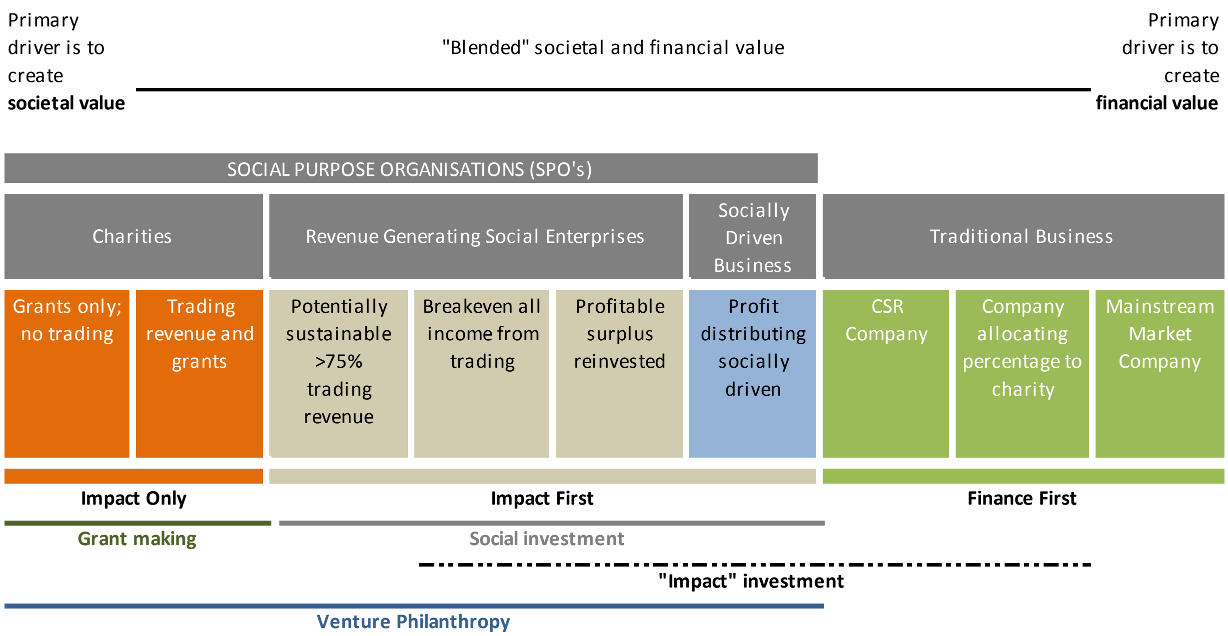
positive impact is not sufficient.[3] This does not include socially responsible investing (SRI), which only screens for harm rather than explicitly seeking a positive impact.

Monitor Institute segments impact investors into two categories: Impact First investors and Financial First investors. Impact First investors' primary goal is to achieve a social or environmental impact, with a secondary goal of financial return. They are more likely to be able to accept concessionary returns ranging from repayment of principal to market rate. Financial First investors' primary goal is to achieve a financial return, with a secondary goal of social or environmental impact. Financial First investors are more likely to be institutions such as pension fund managers, which are obligated to seek market rate returns. They operate primarily in mature sectors such as microfinance and low-income housing, and may enter a market once Impact First investors have launched the market and proven its viability. "Yin-yang" or blended value deals, as Monitor Institute calls it, combine a variety of capital with different return requirements to support an opportunity. Because Impact First investors may be willing to accept a lower or potentially nominal return on their investment or are willing to take on greater risk, Financial First investors can meet their financial return requirements. By partnering with Financial First investors, Impact First investors have the potential to significantly increase the total amount of funding available to an enterprise seeking capital.

While institutional investors may choose to focus on Financial First or Impact First or Blended Value, it is not inconceivable that the same investor take different positions with different intermediaries and implementers who are at different stages of their growth cycle. Or for that matter the same investor might support an impact only/grant fund in one part of the organization while simultaneously investing in a financial return fund of the same organization. **Figure A** illustrates one view of the range of investments from purely socially motivated to purely financially motivated. Investor goals are incorporated at the bottom, in the range of Impact Only, Impact First, and Finance First investments, illustrating the fluidity between boundaries and the definitional overlap as it relates to the emerging taxonomy in the field.

[3] The Parthenon Group, *Investing for Impact: Case Studies Across Asset Classes* (The Parthenon Group, March 1, 2010), p. 3, http://www.parthenon.com/ThoughtLeadership/InvestingforImpactCaseStudiesAcrossAssetClasses, accessed October 2011.

Figure A: The Investment Spectrum



Source: European Venture Philanthropy Association, *European Venture Philanthropy Association: An Introduction* (European Venture Philanthropy Association, October 2011), p. 5, http://evpa.eu.com/wp-content/uploads/2010/08/EVPA-Introduction-October-2011__2.pdf, accessed October 2011.

There are a variety of investors participating in the impact investing space: development finance institutions, private foundations, large-scale financial institutions, commercial banks, retirement fund managers, boutique investment funds, corporations, community development finance institutions, and high net worth individuals.[4] Although a return on capital excludes philanthropic gifts from the impact investing definition, foundations and other nonprofit organizations can participate in impact investing through mission-related or program-related investments. Mission-related investments are market-rate investments of endowment funds that align with the social or environmental mission of the foundation. Program-related investments accept below market returns and count toward endowment disbursement requirements in the U.S; more on PRI later in this primer. **Exhibit 1** provides a quick overview of foundation investment options.

It is fair to conclude that impact investing is not seen as a panacea or replacement for philanthropy but instead a potential source of net-new capital working in concert with philanthropy and market-based approaches to support social change. The most exciting players in this field are a new breed of intermediaries such as Acumen Fund, Grassroots Business Fund, IGNIA, Omidyar Network, and Root Capital (listed strictly in alphabetical order) who invest the funds aggregated on their behalf in for-profit and nonprofit social enterprise organizations through a variety of financial instruments. See **Exhibit 2** for a representative list of players and what they do. Each has a unique strategy, ranging from IGNIA, which looks for above market returns, to Acumen Fund, which looks for a blended return. A broad range of asset classes are involved in impact investing: cash, senior

[4] J. P. Morgan, *Impact Investments: An Emerging Asset Class* (J. P. Morgan, November 29, 2010), p. 16, http://www.jpmorgan.com/cm/BlobServer/impact_investments_nov2010.pdf?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1158611333228&blobheader=application%2Fpdf, accessed October 2011.

debt, mezzanine/quasi-equity, public equity, venture capital, private/growth equity, real estate, other real assets, and hedge funds.[5]

Size of the Market

In 2009, Monitor Institute estimated the size of the impact investing market to be $500 billion over the next decade, noting that innovation in certain areas, such as affordable housing in developing countries, could significantly grow the industry at a faster rate.[6] To place this in context, U.S. philanthropic giving approximates roughly $300 billion a year, of which foundation giving is about $45 billion (2009), and corporate giving $15 billion (2009).[7] Interestingly, since 1969, U.S. foundations have had the flexibility to make program-related investments (PRIs) at below market rates (mainly loans), which count towards their annual 5% distribution requirements. In a 2011 Foundation Center study of 1,200 foundations only 14% of those surveyed engage in mission investing, half of which have PRIs, and 28% of which hold a combination of PRIs and mission-related investments.[8] The question that jumps out is whether this low level of PRI deployment is because of conservative investment practices of foundations or whether it is a sign of a lack of enough high-quality investment options.

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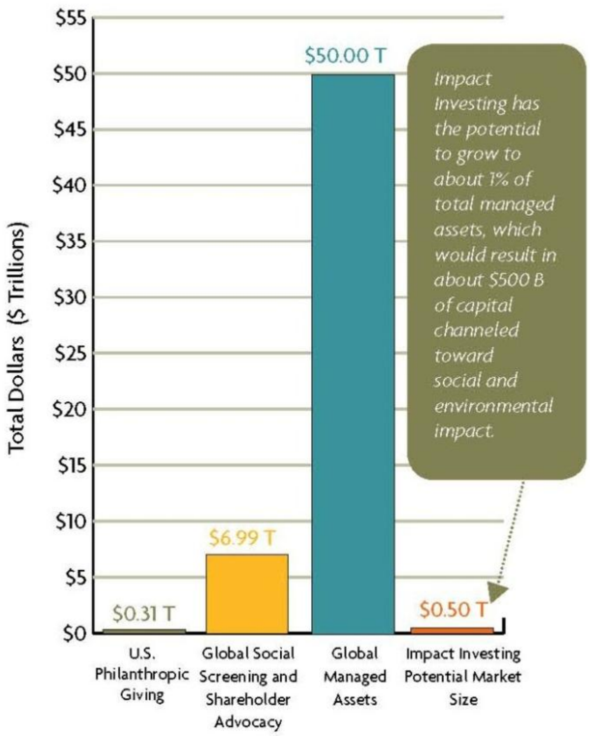
5 The Parthenon Group, *Investing for Impact*, p. 15.

6 Monitor Institute, *Investing for Social and Environmental Impact*, p. 9.

7 The Center on Philanthropy at Indiana University, *Giving USA 2010: The Annual Report on Philanthropy for the Year 2009* (Indianapolis: Indiana University, 2010), p. 11, http://www.cfbroward.org/cfbroward/media/Documents/Sidebar%20Documents/GivingUSA_2010_ExecSummary_Print.pdf, accessed October 2011.

8 Steven Lawrence and Reina Mukai, *Key Facts on Mission Investing* (The Foundation Center, 2011), p. 1, http://foundationcenter.org/gainknowledge/research/pdf/keyfacts_missioninvesting2011.pdf, accessed October 2011.

Figure B: Comparative Market Sizing



Source: Monitor Institute, *Investing for Social and Environmental Impact, p.* 9.

J.P. Morgan provided a more granular, yet broader range for the impact investing market over the next decade, from $400 billion to $1 trillion, from just five sub-sectors of the industry (urban housing, water for rural communities, maternal healthcare, primary education, and microfinance) concentrated at the Base of the Pyramid (BoP) market,[9] which is defined as the four billion people earning less than $3,000 a year.[10]

The J.P. Morgan estimate, encompassing only five sub-sectors, signals a potential market, when all possible asset classes and additional sectors are included, that is significantly larger than the Monitor Institute's estimate.

[9] J. P. Morgan, *Impact Investments: An Emerging Asset Class*, p. 11.

[10] Allen Hammond et al., *The Next 4 Billion: Market Size and Business Strategy at the Base of the Pyramid* (World Resources Institute, International Finance Corporation, March 2007), p. 3, http://pdf.wri.org/n4b_fulltext_hi.pdf, accessed October 2011.

Table A J.P. Morgan Estimate of Potential Capital in Five Impact Investing Sub-Sectors over the Next Ten Years

Sector	Potential Invested Capital Required (USD bn)	Potential Profit Opportunity (USD bn)
Housing: Affordable urban housing	$214–$786	$177–$648
Water: Clean water for rural communities	$5.4–$13	$2.9–$7
Health: Maternal health	$0.4–$2	$0.1–$1
Education: Primary education	$4.8–$10	$2.6–$11
Financial Services: Microfinance	$176	Not measured

Source: J. P. Morgan, *Impact Investments: An Emerging Asset Class*, p. 12.

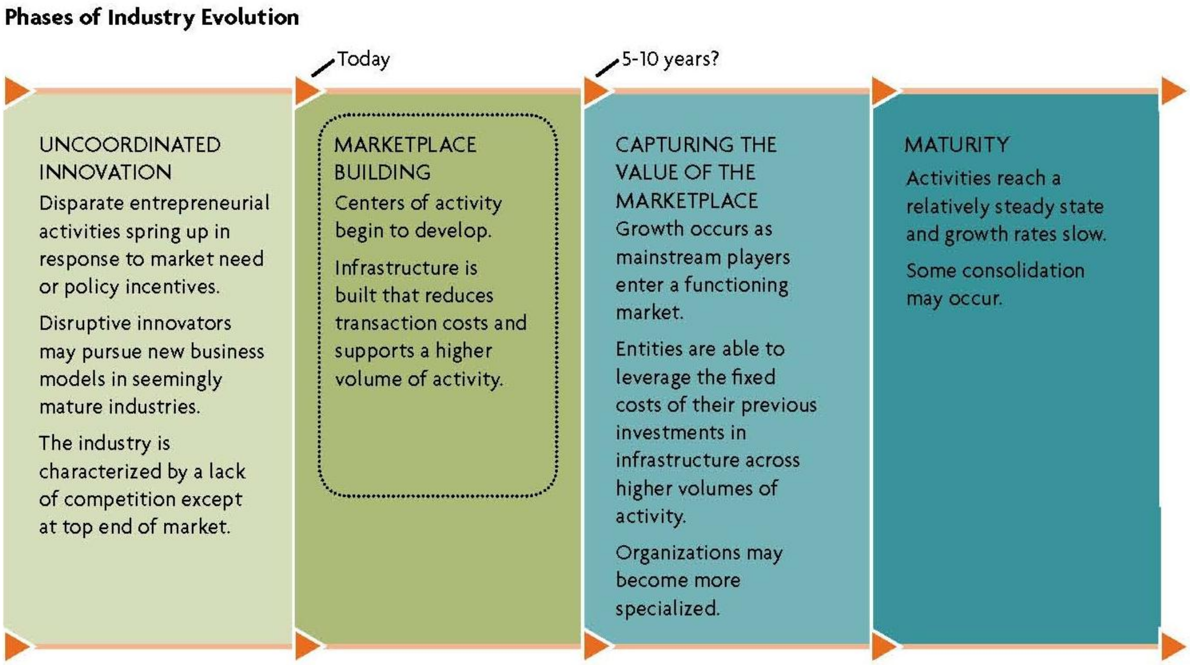
It can be seen from **Table A** that the two largest segments are housing and microfinance, which have a natural business model entailing repayment of principal and interest as part of the terms of the loan. The other sectors mentioned in **Table A**, for example, Clean Water and Primary Education, have traditionally found it hard to build a revenue model that recovers the cost of capital. While the targeted individuals and families gain from the social intervention, the larger gain rests at a collective level for society in the long term. The benefit revenue streams are both short term and long term and both at the level of the individual and society. It therefore becomes hard to monetize and aggregate the revenue streams and match them against program costs. In fact there may be large tracts of the social sector where earned revenue with profit surplus is pretty close to impossible to achieve.

Developing the Field

Going by Monitor Institute's assessment (see **Figure C**), at this point, there are significant challenges ahead for the Industry which is still in a nascent stage of formation. The Social Investment Task Force in the U.K. identified the need for a range of suppliers, well-functioning intermediaries, a social investment trading platform, and the recognition of social investment as an asset class to further the development of the industry.[11] In addition there are several more challenges that must be overcome for social investing to grow beyond the stages of early development into a robust industry: regulatory reform to allow and encourage participation in the social investing market and a clear and standardized measurement of what is social impact. But even as these industry building activities are being undertaken, the early movers in the field, such as the organizations represented in **Exhibit 2**, have to demonstrate market success. Collectively those organizations are in a position to invest nearly a billion dollars in this space. Their success is the surest way to spur the next stage of development in the field as implied in **Figure C**.

[11] Social Investment Task Force, *Social Investment Ten Years On* (Social Investment Task Force, April 2010), p. 8, http://www.socialinvestmenttaskforce.org/downloads/SITF_10_year_review.pdf, accessed October 2011.

Figure C Building a Marketplace for Impact Investing



Source: Monitor Institute, *Investing for Social and Environmental Impact, p.* 12.

Some of the infrastructure needed to support a growing marketplace is already underway. Networks like ANDE (Aspen Network of Development Entrepreneurs) and GIIN (Global Impact Investing Network) facilitate industry dialogue and collaboration by connecting investors with opportunities and with each other to promote the development of the industry. See **Exhibit 3** for a brief overview. Under the auspices of GIIN, IRIS (Impact Reporting and Investment Standards), a measurement system, is being developed, which will be discussed more later in this primer.

Government as Insurers of Social Impact (Bond)

The social impact bond or "Pay for Success" contract connects private investment with nonprofit service providers and governments to produce improved social outcomes that generate government savings. Government contracts with a social impact bond-issuing organization (SIBIO) to obtain social services. The SIBIO in turn issues the bonds to private investors who will receive both a repayment of principal and an ROI from performance-based payments if the benchmarks are achieved. The investors provide the working capital to the SIBIO, who in turn funds the service providers. The government only pays its return if and when performance targets have been met.[12] The social impact bond is designed to address specific types of social or environmental projects. See **Exhibit 4** for a brief explanation of how the bond works. Social Finance, a Boston-based intermediary modeled after its U.K counterpart, has identified a set of criteria that must be met for a social bond to be successful: there must be high net benefits, measurable outcomes, a well-defined treatment

[12] Jeffrey B. Liebman, *Social Impact Bonds* (Center for American Progress, February 2011), p. 2, http://www.americanprogress.org/issues/2011/02/pdf/social_impact_bonds.pdf, accessed October 2011.

population, and credible impact assessments. In addition, failure of the program must not cause harm to treatment populations (i.e. a core service cannot be allowed to fail).[13]

In 2010, the U.K. government launched the first ever social impact bond (£5 million[14]), aimed at lowering recidivism rates at Peterborough Prison. If rehabilitation services are successful in lowering the recidivism rate, investors will receive a repayment of principal and a return of 7.5% to 13%.[15] This is the only use of a social impact bond thus far, but interest in the instrument in the U.S. and U.K. is significant. President Obama's 2012 budget proposes $100 million to be invested in social bond pilot programs in seven areas, including job training, education, and juvenile justice.[16] Massachusetts and Minnesota are also pursuing this instrument at the state level; Social Finance U.S. has proposed that housing for the chronically homeless, a service that can lead to significantly improved health outcomes for participants, would be a potential service to finance through social impact bonds.[17]

In spite of the early government support in the U.K. and U.S. for the instrument, it remains to be seen whether governments (federal and local) are willing to commit guaranteed funds in anticipation of future societal benefits. As mentioned before, the acid test lies in how they will be measured, validated, and compensated. Further one has to see how the intermediaries in this space, such as Social Finance, structure their tasks. Would they be purely financial matchmakers or would they and their investors play an active role in advising and engaging in the work of their invested social enterprise organizations? If social impact bonds are successful, it opens a new way for the private sector to provide the upfront capital, which will be recouped with down-the-road savings in government expenditure.

For Profit, Nonprofit, or Hybrid?

Current corporate structures for organizations with a social mission are nonprofit, for-profit, or a hybrid of either nonprofit with for-profit subsidiary, or for-profit with nonprofit subsidiary. Each structure has inherent advantages and problems. For-profit enterprises must attempt to provide a commercial return to shareholders and may therefore find themselves constantly balancing the pursuit of growth and profits with that of gaining deeper social impact. Nonprofit organizations, on the other hand, attempt to maximize social benefit but may not have ready access to large pools of capital to support and expand their work. Interesting hybrid models are emerging which attempt to blend for-profit and non-profit sources of funds in implementing the organization's mission, but without significant regulatory changes it is not clear how this organizational form will ultimately evolve.

New corporate structures are being tested and developed that blend profit seeking with a social mission. The Benefit or B Corporation is a new corporate class that is obligated to create a positive

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[13] Ibid., pp. 3–4, 18.

[14] "Private Backers Fund Scheme to Cut Prisoner Reoffending," *BBC News UK*, September 10, 2010, http://www.bbc.co.uk/news/uk-11254308, accessed October 2011.

[15] "Let's Hear Those Ideas: In America and Britain Governments Hope that a Partnership with 'Social Entrepreneurs'' Can Solve Some of Society's Most Intractable Problems," *The Economist*, August 12, 2010, http://www.economist.com/node/16789766, accessed October 2011.

[16] David Leonhardt, "For Federal Programs, a Bit of Market Discipline" *New York Times*, February 8, 2011, http://www.nytimes.com/2011/02/09/business/economy/09leonhardt.html, accessed October 2011.

[17] Social Finance, Inc., *Bringing Social Impact Bonds to Massachusetts: Response to Request for Information about Social Impact Bonds by the Commonwealth of Massachusetts* (Boston: Social Finance, Inc., June 10, 2011), p. 14, http://www.socialfinanceus.org/sites/default/files/Social%20Finance%20RFI%20Response.pdf, accessed October 2011.

social impact, and became a recognized legal form in Maryland and Vermont in 2010.[18] The Community Interest Company (CIC) is a corporate structure in the U.K. in which the company's activities must fulfill a community purpose and company assets are locked to use for a community purpose; since its creation in 2005, over 5,400 CICs have formed.[19] Legally recognized in nine U.S. states, the L3C (low-profit limited liability company) has as its main objective to provide a social good.[20] The business structure is designed to more easily qualify to receive PRI from foundations. However, because regulation concerning PRI is complex, it is yet to be determined to what extent enterprises and investors will be able to utilize it. The flexible-purpose corporation is a new form in California that would allow the company to pursue broader objectives than maximizing shareholder wealth, such as social impact. It would also be able to convert into a nonprofit corporation, a for-profit corporation, or other domestic business entity.[21] It still remains to be seen what innovations will enable organizations with a dual mission to succeed. A brief description of these various organizational forms is provided in **Exhibit 5,** from which it can be seen that none of the new forms of social enterprises have a tax exempt status, but what they get is the certification of being mission-driven, which then may enable them to attract capital at below market rates.

Organizational innovations have made the funding side more complex. Funding a nonprofit organization or 501(c)3 is tax exempt, but the same is not the case with the new forms of organization. Would individual donors be better off with a straight-out donation that provides them a guaranteed tax benefit as opposed to a risky investment which has no tax benefits with little chance of recouping the capital?

Measurement

There are a variety of definitions for impact within the context of social change work. Within international development and evaluation, impact can be referred to as "significant or lasting changes in people's lives, brought about by a given action or series of actions."[22] Alternatively, impact can be seen as outcomes, once what would have already happened is removed from the equation. Impact is often a component of a logic model in which organizational inputs and activities result in a set of outcomes and greater social impacts. It is also seen as targeting "root causes" of a social problem.[23]

There is not a great deal of clarity regarding how to measure social impact within impact investing. Historical social and environmental performance measurement has been fragmented, with investors using proprietary measurement systems or not conducting consistent measurement. According to a J.P. Morgan survey, the vast majority of investors rely on anecdotal evidence and

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[18] B Corporation, "B Corp Legislation," *B Corporation Web site*, n.d., http://www.bcorporation.net/publicpolicy, accessed October 2011.

[19] CIC Association, "What is a CIC?," *CIC Association Web site*, August 1, 2011, http://www.cicassociation.org.uk/about/what-is-a-cic, accessed October 2011.

[20] "New Companies Combine Profit and Charity," *New York Times*, October 12, 2011, http://www.nytimes.com/interactive/2011/10/13/business/new-companies-combine-profit-and-charity.html, accessed October 2011.

[21] California Senate, "Senate Bill No. 201: Flexible Purpose Corporations" (Official California Legislative Information, February 8, 2011), http://www.leginfo.ca.gov/pub/11-12/bill/sen/sb_0201-0250/sb_201_bill_20110208_introduced.pdf, accessed October 2011.

[22] Chris Roche, *Impact Assessment for Development Agencies: Learning to Value Change* (Oxford, UK: Oxfam GB, 1999), p. 21.

[23] Leslie R. Crutchfield and Heather McLeod Grant, *Forces for Good: The Six Practices of High-Impact Nonprofits* (San Francisco, CA: Jossey-Bass, 2008), p. 24.

proprietary systems to measure an investment's impact; only 2% currently utilize a third-party system.[24]

However, ratings systems are being created, although they are in the early stages of development. Founded by Acumen Fund, B Lab, and the Rockefeller Foundation in 2009, Impact Reporting and Investment Standards (IRIS) aims to provide and encourage adoption of a "universal language for social, environmental, and financial performance that can be adopted within proprietary reporting tools."[25] Although initial reporting has focused mainly on financial data by sub-sector, IRIS plans future improvements including tracking sector-specific performance data, trends over time, and demographic information for all elements of the supply chain. As the brief description in **Exhibit 3** shows, the IRIS framework attempts to measure along three dimensions of which financial performance is one, and impact assessment constitutes the other two components. The measure is more akin to a balanced scorecard rather than an integrated metric. **Exhibit 6** presents an illustrative report card issued for a foundation.

Measurement systems like IRIS will increase the likelihood that impact investing will become rigorous and commonly accepted. With some built-in feedback loop and modifications, there is more than a decent chance that industry standards will emerge. At the same time since the assessment is more akin to a snap shot of what the organization has accomplished rather than an analysis of what the prospects are, impact investors will still have to wade into the details before they become comfortable with their investments, and that is the role that intermediaries could perform.

A Call to Action

Some may argue that the space of impact investing is not entirely new and there have existed stellar implementers in the field who have blended financial and social returns while maintaining high rates of growth. Yet it is only in the last decade that we have seen the emergence of intermediaries and investors, such as the ones in **Exhibit 2**, with explicit goals of achieving a financial return that at least covers the nominal cost of capital. To most of us it appears that impact investing is a young and emerging industry with disparate players, some brand new to the field of social change, while others are seasoned veterans experimenting a new approach to investing and intermediation. Even in this young industry there are players who are young adults and relatively well funded and others who are teenagers and just starting. Surely these different players will have different approaches to social change and different preferences for what return they would like for their investments. It is in this spirit of openness to widely different models that we approach the forum. Most at this forum will be investors, intermediaries or academics. Many will have a deep knowledge of the work of implementers, either through direct knowledge or case research. Regardless of who you are, please be prepared to share your insights to the following questions or a subset that applies to your particular position. The purpose being to use our deliberations as way of focusing on a few key ideas that have the potential to advance the field, and if possible constructing an action agenda for how we might explore those ideas before the next forum session tentatively planned for April 30/May1st :

- What is your organization's theory of change? What social impact are you aiming to achieve?
- What are the sources of your funds? What are your investors expecting? What are the terms of your promise?

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[24] J. P. Morgan, *Impact Investments: An Emerging Asset Class*, p. 36.

[25] IRIS, *Data Driven: A Performance Analysis for the Impact Investing Industry*, 2011 IRIS Data Report (GIIN and IRIS, September 2011), p. i, http://www.thegiin.org/binary-data/Data_Driven_IRIS_report_final.pdf, accessed October 2011.

- How do you achieve your promised social impact? What activities and investments do you engage in? How do you use the funds you have received?
- How do you know you are achieving social impact? How do you measure it? How do you trade off financial impact versus social impact?
- How do you (will you) measure your organization's success?
- What can we, as a group, do to plug the gaps or advance the field? What particular topics should we focus on for deeper exploration?
- Is there a different way of conceptualizing the field that will make it more productive as a vehicle for social change going forward?

We are looking forward to a stimulating day of discussions and ideas at the forum.

Exhibit 1 Foundation Investments

Mission-related investments (MRI) are market-rate investments of a foundation's endowment funds that align with the social or environmental mission of the foundation. Defining an investment as MRI is an internal process; many foundations that engage in MRI do not have a formal investment strategy or policy statement.[a] Program-related investments (PRI) must serve a charitable, religious, scientific, literary, educational, or other exempt purpose, cannot to any significant degree be aimed at creating income, and cannot serve a political purpose. PRIs can accept below market returns and count toward a foundation's endowment disbursement requirements. Foundations in the U.S. are required to distribute annually at least 5% of the value of their assets for the previous year. The Tax Reform Act of 1969 created the PRI category allowing foundations to count this type of investment towards their 5% required disbursement. All foundation types (independent, community, and corporate) are able to make grants, PRIs, MRIs, or standard investments.

	Part of 5% Distribution	Expected Return	Funding Provided	Organizations Funded
Grants	Yes	Range from none to recoverable grant, expecting full payment[b]	Funding startup, growth, ongoing operations, ongoing capital needs	Nonprofits[c]
PRI	Yes	Can accept below market rate, but is not necessarily below market	Debt, equity, business startup and growth, loan guarantees, lines of credit, linked deposits, charitable use assets, other[d]	Nonprofits, for-profit businesses, government[e]
MRI	No	Market rate	Any	Any
Standard investments	No	Market rate	Any	Any

Source: Compiled by authors.

In 2010, foundations in the U.S. distributed $46 billion in funds and held assets totaling over $600 billion.[f] Of funds dispersed, PRI represented only a fraction of this. In a 2011 Foundation Center study of 1,200 foundations only 14% of those surveyed engage in mission investing, half of which hold PRIs, and 28% of which hold a combination of PRIs and mission-related investments.[g]

[a] Lawrence and Mukai, *Key Facts on Mission Investing*, p. 2.

[b] Ibid., p. 3.

[c] Grant Space, "Knowledge Base: Business Funding," *Grant Space: A Service of the Foundation Center*, n.d., http://grantspace.org/Tools/Knowledge-Base/Individual-Grantseekers/For-Profit-Enterprises/Business-funding, accessed October 2011.

[d] Steven Lawrence, *Doing Good with Foundation Assets: An Updated Look at Program-related Investments*, The PRI Directory, 3rd Edition (Foundation Center, 2010), p. xvi, http://foundationcenter.org/gainknowledge/research/pdf/pri_directory_excerpt.pdf, accessed October 2011.

[e] Ibid.

[f] Lawrence and Mukai, *Key Facts on Mission Investing*, p. 1.

[g] Ibid.

Exhibit 2 Examples of Intermediary Organizations

There is a broad range of actors in the field of social investing, with a diverse array of motivations, investment requirements, and approaches to structuring investments. The chart below outlines an illustrative snapshot of some of the kinds of players that are emerging across the social investment spectrum.

Organization	Organizational Form	Primary Investment Approach	Description
Edna McConnell Clark Foundation	Private nonprofit foundation	Grants (unrestricted)	Provides unrestricted, multi-year, multimillion-dollar investments in low-income youth development organizations in the U.S. Growth Capital Aggregation Pilot provides growth capital to allow most promising grantees to scale up.[a]
Root Capital	Nonprofit social investment fund	Debt	Provides debt financing for short-term working capital and long-term fixed assets to small grassroots businesses (the "missing middle" between microfinance and commercial lending) in rural areas in developing countries.[b]
Social Finance	Nonprofit impact investment firm	Social impact bond	Aims to connect the social sector with capital markets by structuring and managing innovative investment instruments that generate both social benefit and financial returns.[c]
Acumen Fund	Nonprofit social investment fund	Debt, equity	Supports entrepreneurial approaches to solving the problems of global poverty. Uses philanthropic capital to make disciplined investments that yield both financial and social return. Typical commitments are $300k–$2.5M in debt or equity, with payback or exit in 8–15 years.[d]
Grassroots Business Fund	Nonprofit impact investing fund	Debt, equity, convertible loans, guarantees	Provides investment capital and capacity building to high-impact businesses creating economic opportunities at the base of the pyramid in several developing countries across the globe.[e]
Omidyar Network	Philanthropic investment firm that is a combination LLC and 501(c)3[f]	Blended approach (grants, debt, equity)	Supports market-based approaches with the potential for large-scale, catalytic impact. Uses variety of financing working with both for-profit companies and nonprofits, with both BoP in emerging markets and in the developed world encouraging individual participation in media, markets, and government.[g]
IGNIA	Impact investing venture capital firm	Equity	By providing effective responses to the enormously underserved needs of low income populations, as consumers as well as productive agents in value-added supply chains, IGNIA empowers entrepreneurship and generates social impact while creating attractive financial returns for its investors.[h] Focus on BoP in Latin America.

Source: Compiled by authors.

[a] Edna McConnell Clark Foundation, "Edna McConnell Clark Foundation: Our Investment Approach," *Edna McConnell Clark Foundation Web site*, n.d., http://www.emcf.org/how-we-work/our-investment-approach, accessed October 2011.

[b] Root Capital, "What We Do," *Root Capital Web site*, n.d., http://www.rootcapital.org/what_we_do.php, accessed October 2011.

[c] Social Finance, *President Clinton Highlights Social Finance, Inc. at the Clinton Global Initiative for Its Commitment to Develop and Its Commitment to Develop and Launch Social Impact Bonds in the U.S.* (Social Finance, September 22, 2011), http://www.socialfinanceus.org/sites/default/files/CGI.pdf, accessed October 2011.

[d] Acumen Fund, "Investment Discipline," *Acumen Fund Web site*, n.d., http://www.acumenfund.org/investments/investment-discipline.html, accessed October 2011.

[e] Grassroots Business Fund, "FAQ," *Grassroots Business Fund Web site*, n.d., http://www.gbfund.org/FAQ, accessed October 2011.

[f] Omidyar Network, *Omidyar Network Frequently Asked Questions* (Omidyar Network, n.d.), http://omidyar.net/sites/default/files/file/ON_FAQs_063011.pdf, accessed October 2011.

[g] Omidyar Network, "Approach," *Omidyar Network Web site*, n.d., http://www.omidyar.com/approach, accessed October 2011.

[h] IGNIA, "IGNIA: Investing in the Base of the Pyramid," *IGNIA Web site*, n.d., http://www.ignia.com.mx/bop/what-we-stand-for.php, accessed October 2011.

Exhibit 3 Industry Infrastructure

GIIN—*Collaborative network* Launched in September 2009,[a] the Global Impact Investing Network (GIIN) aims to foster collaboration and infrastructure development for the impact investing industry. Fiscally housed within Rockefeller Philanthropy Advisors, it is a nonprofit organization with support from the Rockefeller Foundation and J.P. Morgan, among others.[b] It engages in research and dissemination of best practices through its Investors' Council, builds industry infrastructure through IRIS, and conducts outreach to bring more attention to the industry. ("By highlighting exemplary impact investments, industry progress, and best practices, the GIIN aims to increase the scale and effectiveness of impact investing."[c])

ANDE—*Collaborative network* Launched in 2009, Aspen Network of Development Entrepreneurs (ANDE) is a global network of over a hundred organizations that invest in and provide technical assistance to small and growing businesses (SGBs) in emerging markets.[d] Its goal is to act as both a resource and advocate for its members through its knowledge sharing events, online resource library, training programs, and capacity building fund, and is a core partner in the development of IRIS.

IRIS—*Measurement* Impact Reporting and Investment Standards (IRIS) is an initiative of GIIN aimed at developing a shared taxonomy for reporting social and environmental impact and creating a repository of IRIS data to allow for comparison of mission-driven organizations across and within sectors and regions. Formed in 2009, it is supported by the Rockefeller Foundation and USAID, and based on work by Rockefeller Foundation, Acumen Fund, and B Lab. The use of a shared measurement system will allow aggregation of data across organizations for analysis for benchmarking purposes by organizations such as GIIN and GIIRS. The goal is to reduce transaction costs and increase transparency and credibility in tracking social and environmental impact across the sector. IRIS is collecting voluntary, anonymous reports of metrics from organizations across a variety of sectors in order to have a robust data set to begin analyzing performance different regions and sectors.

Funders can select which performance metrics investees must report on. When investees report, they utilize IRIS metrics, which require data be input in a standardized way. This allows for comparison between organizations with similar activities or objectives. Performance metrics are broken into three main categories: financial performance, operational impact, and product description and impact. Financial performance includes all the standard financial reporting measures used in for-profit companies, such as income statement items and financial ratios, as well as less common indicators such as "microfinance personnel efficiency," which is defined as personnel expense divided by average loans receivable gross.[e] Operational impact is broken into seven sub-categories: governance & ownership, social policies, environmental policies, environmental performance, employees, wages, and training & assessment. Specific metrics within operational impact include: use of green building practices (selecting from a predetermined set of options), number of employees receiving a healthcare benefit, female ownership percentage, and methods employed to protect client information. Examples of product description and product impact metrics include: socio-economic status of target beneficiaries, number of immunizations, a "textbook-to-student" ratio for educational organizations, and number of individuals receiving technical assistance. In addition, IRIS currently allows organizations to categorize themselves as falling within one of the following sectors: agriculture, education, energy, environment, financial services, health, housing/community facilities, and water.[f]

In its first report, *Data Driven: A Performance Analysis for the Impact Investing Industry* (2011), IRIS states that the data thus far is drawn from too small a pool of organizations to extrapolate financial or social/environmental performance for various sectors or regions. This initial report discusses profit margins by region and sector, but has insufficient data to discuss operational or other impact metrics without jeopardizing responding organizations' anonymity.

GIIRS—*Measurement* The Global Impact Investing Rating System (GIIRS) formed in September 2009. Modeled on the B Lab's B Impact Rating System and utilizing IRIS metrics, GIIRS aims to provide ratings of mission-driven organizations based on social and/or environmental impact performance, in a role within the impact investing industry that would be "analogous to Morningstar investment rankings or S & P credit risk ratings."[g] GIIRS is currently in private beta and aims to launch its GIIRS Assessment in the third quarter of 2012.[h]

PULSE—*Measurement* Developed by Acumen Fund and Google, PULSE is a measurement system that allows mission-driven organizations to collect and report financial, social, and environmental data using IRIS taxonomy to show impact. It is available via the Salesforce.com platform and can be used to monitor performance on both investments and grants.[i]

Source: Compiled by authors.

[a] GIIN, *New Industry Group Launched to Facilitate For-Profit Investing that Addresses Social and Environmental Challenges* (GIIN, September 25, 2009), http://www.thegiin.org/binary-data/MEDIA/pdf/000/000/4-5.pdf, accessed October 2011.

[b] GIIN, "Global Impact Investing Network: About Us," *GIIN Web site*, n.d., http://www.thegiin.org/cgi-bin/iowa/aboutus/index.html, accessed October 2011.

[c] Ibid.

[d] ANDE, "About ANDE," *The Aspen Institute Web site*, n.d., http://www.aspeninstitute.org/policy-work/aspen-network-development-entrepreneurs/about-ande, accessed October 2011.

[e] IRIS, "Microfinance Personnel Efficiency," *IRIS Web site*, n.d., http://iris.thegiin.org/indicator/microfinance-personnel-efficiency, accessed October 2011.

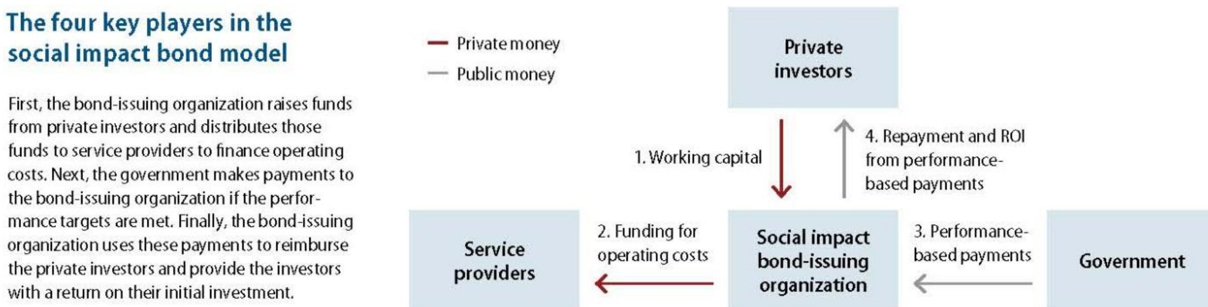
[f] Examples and descriptions in this paragraph are drawn from the IRIS's standards section of its website. IRIS, "IRIS Standards," *IRIS Web site*, n.d., http://iris.thegiin.org/iris-standards, accessed October 2011.

[g] GIIRS, "What GIIRS Does," *GIIRS Web site*, n.d., http://giirs.org/about-giirs/about, accessed October 2011.

[h] GIIRS, *GIIRS Q1 2011 Progress Report: Building a Credible Rating System* (GIIRS, 2011), p. 12, http://giirs.org/storage/documents/GIIRS_2011-Progress-Report-Final.pdf, accessed October 2011.

[i] Acumen Fund, "Pulse," *Acumen Fund Web site*, n.d., http://www.acumenfund.org/investments/investment-performance/pulse.html, accessed October 2011.

Exhibit 4 Social Impact Bonds



Source: Jeffrey B. Liebman, *Social Impact Bonds*, Center for American Progress, February 2011, p. 11.

The social impact bond is designed to address specific types of social or environmental projects. Social Finance has identified a set of criteria that must be met for a social bond to be successful: there must be high net benefits, measurable outcomes, a well-defined treatment population, and credible impact assessments. In addition, failure of the program must not cause harm to treatment populations (i.e. a core service cannot be allowed to fail).[a]

[a] Liebman, *Social Impact Bonds*, pp. 3–4, 18.

Exhibit 5 Corporate Structures

Structure	Objectives & Details	Country / State	Foundation Funding Eligible for	Access to Debt	Access to Equity	Tax Exemptions	Tax Advantages to "Donors"	Example
Nonprofit 501(c)3 (private foundation or public charity) (US)	May generate a profit, but cannot share it with corporation's decision-makers. Primary objective is not generating profit (generally organized around pursuing a public benefit).	U.S.	Grants, PRI, other loans and loan guarantees.	Yes. Mainly tax-exempt bonds.[a]	No.	Does not pay corporate income taxes unless income is determined to be "unrelated business income."[b] Does pay employment taxes; may be eligible for some state tax exemptions.[c]	Donor tax breaks for most 501(c)3 organizations.[d]	YMCA, City Year, Ford Foundation
Community Interest Company (CIC)	Company's activities must fulfill a community purpose. Company assets and profits are locked to use for specified community purpose. Since creation in 2005, over 5,400 CICs have formed.[e]	U.K.	Some grants (depending on the foundation and CIC), other investments.[f]	Yes (loans and bonds).[g]	CIC limited by shares can sell shares.[h]	None.[i]	None.[j]	Pathfinder Healthcare Developments, Sunlight Social Enterprises
Benefit or B Corporation	Obligated to "create a general public benefit."[k] Annual report on social/ environmental performance required. Legislation only recently passed; first was MD in April 2010.[l] B Corps must also undergo certification from B Lab.	CA, HI, MD, NJ, VA, VT.[m] Not recognized at federal level.	PRI (in some cases), MRI, and regular investment.	Yes.	Yes.	None.[n]	None.	King Arthur Flour, Partnership Capital Growth Advisor
L3C (low-profit limited liability company)	Must "significantly further the accomplishment of one or more charitable or educational purposes" and has "no significant purpose" to generate profits or pursue a political agenda.[o] L3C legislation first passed in VT in 2008.	IL, LA, ME, MI, NC, RI, UT, VT, WY.[p] Not recognized at federal level.	Easier qualification for PRI,[q] MRI, and regular investment.	Yes.	Yes.	None.[r]	None.[s]	MOOMilk, Women News Network
Flexible-purpose company	Company can pursue objectives other than maximizing profits, such as social impact. It can convert into a nonprofit or for-profit corporation.[t] Legislation passed in CA on Oct. 9, 2011.[u]	CA. Not recognized at federal level.	PRI (in some cases), MRI, & regular investments.	Yes.	Yes.	None.[v]	None.	New structure; no examples exist yet.

Structure	Objectives & Details	Country / State	Foundation Funding Eligible for	Access to Debt	Access to Equity	Tax Exemptions	Tax Advantages to "Donors"	Example
Cooperative for-profit business	Democratically controlled and owned by members.	Any	PRI (in some cases), MRI, & regular investments.	Yes.	No.	None.[w]	None.	Ocean Spray, State Employees Credit Union
For-profit company (privately held)	Company can pursue objectives of owners in addition to profit.	Any	PRI (in some cases), MRI, & regular investments.	Yes	Yes	None.	None.	
For-profit company (publicly held)	Obligated to maximize shareholder wealth.	Any	PRI (in some cases), MRI, & regular investments.	Yes	Yes	None.	No.	

Source: Compiled by authors.

[a] Stephanie Strom, "Nonprofits Paying Price for Gamble on Finances," *New York Times*, November 23, 2009, http://www.nytimes.com/2009/09/24/us/24debt.html, accessed October 2011.
[b] IRS, "Unrelated Business Income Tax," *IRS Web site*, October 29, 2010, http://www.irs.gov/charities/article/0,,id=156395,00.html, accessed October 2011.
[c] IRS, "Applying for Exemption: Difference between Nonprofit and Tax-Exempt Status," *IRS Web site*, September 6, 2011, http://www.irs.gov/charities/article/0,,id=136195,00.html, accessed October 2011.
[d] IRS, "Exempt Organizations General Issues: Charitable Contributions," *IRS Web site*, November 1, 2010, http://www.irs.gov/charities/article/0,,id=139023,00.html, accessed October 2011.
[e] CIC Association, "What is a CIC?".
[f] Department for Business Innovation and Skills, "Community Interest Companies: Information and Guidance Notes, Chapter 7," *Department for Business Innovation and Skills Web site*, n.d., p. 17, http://www.bis.gov.uk/cicregulator/guidance, accessed October 2011.
[g] Community Interest Companies, *The Benefits of a Community Interest Company (CIC)*, The CIC Regulator Case Study Series (Community Interest Companies, n.d.), http://www.bis.gov.uk/assets/bispartners/cicregulator/docs/leaflets/10-1388-community-interest-companies-benefits-of-a-cic-leaflet, accessed October 2011.
[h] Ibid.
[i] Ibid.
[j] Ibid.
[k] B Corporation, "What is a B Corp?," *B Corporation Web site*, n.d., http://www.bcorporation.net/about, accessed October 2011.
[l] CSRWire, "Maryland First State in Union to Pass Benefit Corporation Legislation," *Corporate Social Responsibility Newswire*, April 14, 2010, http://www.csrwire.com/press_releases/29332-Maryland-First-State-in-Union-to-Pass-Benefit-Corporation-Legislation, accessed October 2011.
[m] Issie Lapowsky, "The Social Entrepreneurship Spectrum: B Corporations," *Inc.*, May 2011, http://www.inc.com/magazine/20110501/the-social-entrepreneurship-spectrum-what-it-takes-to-be-a-b-corporation.html, accessed October 2011.
[n] CSRWire, "Maryland First State in Union to Pass Benefit Corporation Legislation."
[o] New York Times, "New Companies Combine Profit and Charity."
[p] Carter G Bishop, *Fifty State Series: L3C & B Corporation Legislation Table*, Research Paper No. 10-11 (Suffolk University Law School, May 26, 2011), http://ssrn.com.ezp-prod1.hul.harvard.edu/abstract=1561783, accessed October 2011.
[q] New York Times, "New Companies Combine Profit and Charity."
[r] White & Case LLP, *Client Alert: Tax/Securites* (White & Case LLP, March 2010), http://www.whitecase.com/files/Publication/1a64f5f2-86e3-447a-a904-a974efdea94c/Presentation/PublicationAttachment/9a361c07-59ee-4975-92a0-af1583672463/Alert_Opportunities_for_Investors_to_Partner_with_TaxExempt_Private_Foundations.pdf, accessed October 2011.
[s] Tracy Kaufman, "Nonprofit? For-Profit? A Little Bit of Profit? Selecting a Legal Form for Your Social Enterprise," *Foundation Center*, October 13, 2010, http://newyorkblog.foundationcenter.org/nonprofit-organizations--finance/page/2/, accessed October 2011.
[t] Deborah B. Andrews, "The 'L3C': The new double-hybrid entity," *Philanthropy Journal*, December 10, 2010, http://www.philanthropyjournal.org/resources/managementleadership/%E2%80%98l3c%E2%80%99-new-double-hybrid-entity, accessed October 2011.
[u] California Senate, "Senate Bill No. 201: Flexible Purpose Corporations."
[v] Sara Randazzo, "Creating a New Corporate Structure, and Maybe a New Practice Niche to Boot," *The AmLaw Daily*, October 18, 2011, http://amlawdaily.typepad.com/amlawdaily/2011/10/new-corporate-form-creates-work-.html, accessed October 2011.
[w] Ibid.

Exhibit 6 Use of IRIS Metrics[a]

KL Felicitas Foundation (KLF), a private foundation based in California, adopted Impact Reporting and Investment Standards (IRIS) metrics in 2009 to measure performance of its investments. It focuses on alleviating poverty by supporting small and growing social enterprises in rural communities. In addition to its grant-making activities, the foundation aims to utilize the bulk of its assets to serve its mission; in 2009, 55% of its assets were invested in impact investments.

KFL selected a mix of metrics: a core group of IRIS indicators to allow for comparisons across all investments, a set of sector-specific IRIS indicators to allow for comparisons within each sector, and a proprietary set of qualitative indicators to capture additional information not covered by IRIS's quantitative metrics. Shown below is a sample of indicators KLF selected to apply to all investments.

Sample of Core IRIS Indicators for KLF

	IRIS INDICATOR	DEFINITION*
PRODUCT IMPACT	Number of Clients **(PI7094)***	The number of individual consumers served by the organization
	Jobs Created in Financed Enterprise **(PI3687)**	Net number of new FTE jobs at financed enterprise (including self-employed individuals and owners of businesses)
FINANCIAL PERFORMANCE	Direct Investment—Number of Investments **(FP4359)**	Number of debt and equity investments on balance sheet
	New Investment Capital **(FP8293)**	Value of cash flows from both loans and investments
	Contributed Revenue **(FP3021)**	Contributed revenue (operating grants and in-kind donations)
	Earned Revenue **(FP5958)**	Revenue resulting from all business activities
	Net Income **(FP1301)**	Net income from all business activities, including all contributed revenue.

**Each IRIS performance indicator has a standardized definition which enables consistent reporting by all IRIS users. Similarly, each IRIS indicator is assigned a unique identification number which provides stability even as the IRIS taxonomy is revised to reflect up-to-date performance reporting best practices.*

Source: *KL Felicitas Foundation Case Study*, IRIS, April 2011, p. 3, http://iris.thegiin.org/files/iris/KLF_IRIS_Case_Study.pdf, accessed October 2011.

The use of IRIS metrics allows for the creation of a performance measurement tool similar to the balanced scorecard concept; there is no single rating that combines financial, operational, and social or environmental performance. Although KLF is in the early stages of adopting IRIS metrics and will need further data collection and analysis to generate comparisons of investments across and within sectors, this initial effort illustrates how IRIS metrics can be used.

[a] The information in this exhibit draws heavily from IRIS, *KL Felicitas Foundation Case Study* (IRIS, April 2011), http://iris.thegiin.org/files/iris/KLF_IRIS_Case_Study.pdf, accessed October 2011.