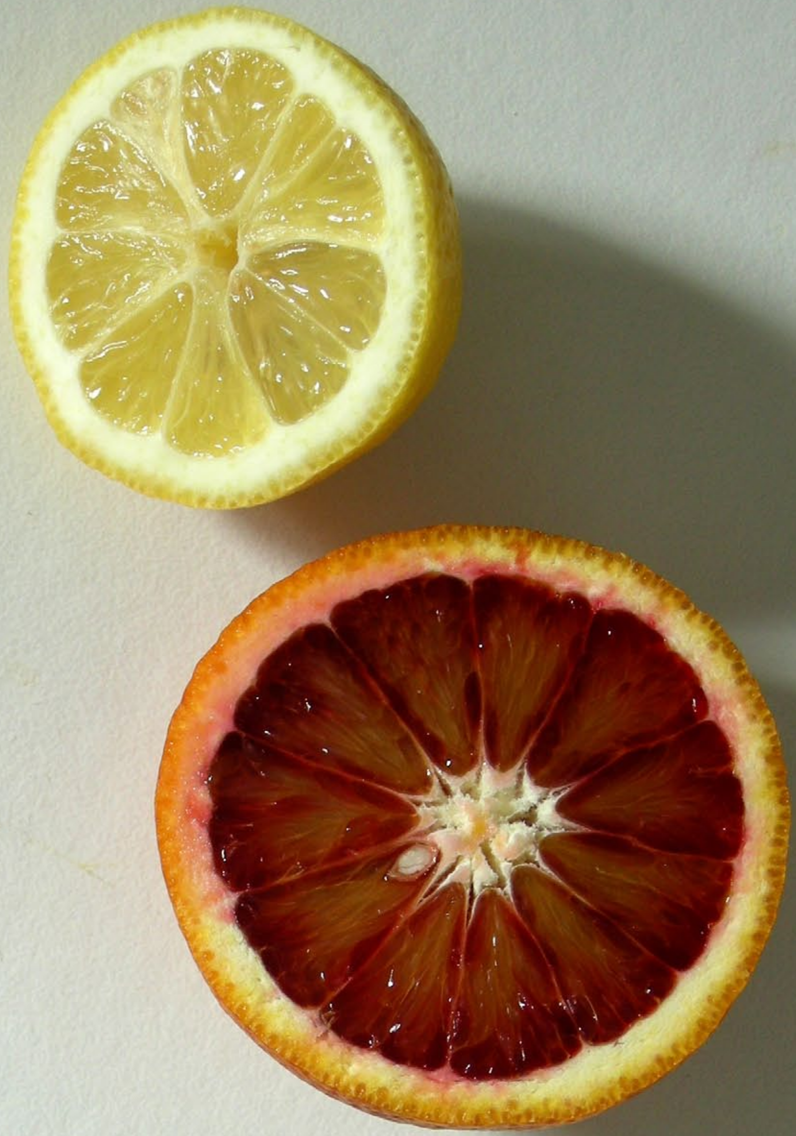

Oranges & Lemons

The State of Play of Impact Measurement among UK Social Investment Finance Intermediaries

A report by **Investing for Good**

Esmée Fairbairn Foundation

Big Society Capital

Investing for Good

Oranges & Lemons: The State of Play of Impact Measurement among UK Social Investment Finance Intermediaries
A report by Investing for Good
Commissioned jointly by Big Society Capital and Esmée Fairbairn Foundation

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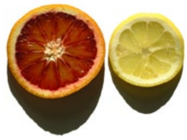
0. FOREWORD



Good practice in evidencing social change is key to unlocking the potential of social investment, and inspiring both investors and social sector organisations to maximise its use.

Much of the talk about what social investment can deliver has been theoretical or conceptual to date. It is now time to prove the tangible difference that social investment can achieve in tackling entrenched social issues by showcasing real life examples underpinned by solid impact evidence.

Impact evidence can be a powerful tool to help social sector organisations improve their performance and ultimately deliver better services to their beneficiaries, but it is all too often perceived as a top-down requirement from funders or investors. This should not be the case, and there is still work to be done to help social sector organisations implement appropriate impact approaches and promote the benefits of it.

We welcome the findings from this report which provide a useful overview of the current state of impact measurement practice across a sample of Social Investment Finance Intermediaries (SIFIs). The report highlights that varying approaches to impact measurement are being implemented across the social investment market with differing degrees of rigour.

Whilst we would not suggest there should be a one size fits all approach to evidencing and evaluating impact, at the very least, organisations who receive investment should be able to demonstrate how social outcomes are being achieved by gathering appropriate and useful impact data as determined by themselves. The level of the evidence captured should be proportionate, and vary according to the size, scope and scale of the investment. And it should likewise be realistic.

It is also necessary for funders and investors to be clear and transparent about their impact aims so those seeking investment can find the most aligned and congruent source of finance. As an industry we are still a long way from understanding the importance of this.

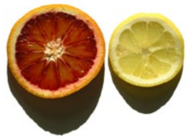
Impact measurement at its best can really add value to an organisation's work, but we recognise there are still challenges around having the capacity and resources to implement it. The proliferation of impact tools, standards and approaches can be confusing for many organisations who are new to the idea, and there needs to be further rationalisation to make these resources more user friendly.

We are both committed to building the social impact capability of SIFIs and the social sector organisations who receive investment from them. We will be setting up a forum to share peer-to-peer learning among social investors in response to the findings of this report. We hope this will help to improve and evolve the practice of embedding mission and impact into all aspects of the investment process.

Better evidence and practice will help both investors and social sector organisations understand which social investment approaches and products can best deliver real social outcomes, and ultimately drive more positive and lasting change in society.

Marcus Hulme, Social Impact Director, Big Society Capital
Caroline Mason, Chief Executive, Esmée Fairbairn Foundation

1. INTRODUCTORY SUMMARY



In 2012 Big Society Capital (BSC) commissioned Investing for Good (IFG) to conduct research on how UK Social Investment Finance Intermediaries (SIFIs) were dealing with impact, and to develop a set of investor guidelines for best impact practice. The results were published online on the BSC website, and in greater detail in the guide *The Good Investor*. At the time, the "best practice" laid out was quasi-theoretical — not least because many of the SIFIs, as well as their impact systems and investments, were then relatively young, and some of the techniques and principles involved consequently had limited track records. And so in 2014 we revisited the subject to investigate, two years down the line, what was happening in "actual practice".

To do this we interviewed ten of the UK's leading SIFIs, and reviewed their impact processes. The essential framework, we discovered, had not changed much, and section 3 of this report (3. What the SIFIs do) works through it, noting how impact is being managed by different SIFIs at each stage. We observed a spread of practices, including some normalisation toward the ideal "best", as well as significant divergences. In particular, there was variation regarding the extent to which SIFIs had systematised their approach to impact: at the one end using methodologies, scorecards, classified metrics, and aggregated data; and at the other, discussions, descriptions and case studies. This variation seemed to be due in part to the type of investment, with equity investments generally being accompanied by more rigorous and more systematised approaches, and in part to organisational culture.

A review of the drivers of impact measurement suggested that, for most SIFIs, current impact processes were fit for purpose, in that neither internal operations, nor external reporting obligations, were actively demanding more or more systematised information. This goes against a contemporary trend — stretching far beyond the impact investment universe, but felt within it too — to perpetually demand more data about everything. There is a risk that if the general call for impact data becomes stronger than the real operational need, especially in a context without either auditing or clear reporting rules, the result will be a form of impact datawash, akin elsewhere to greenwash or whitewash.

As practical measures to protect against this, and to continue making progress with the challenges that impact measurement undeniably presents, this report recommends two steps:

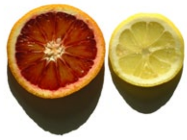
1. To draw up guidelines regarding what approaches to impact may be most appropriate for investments of different types, purposes, and lengths of term, acknowledging that these will not always be the same (the current literature for the most part fails to make such distinctions).

2. To establish a SIFI peer reviewing group to read and provide active feedback on each other's impact reports, and to bounce strategies off each other regarding impact accounting.

The report that follows lays out the research in straightforward fashion: sections 2, 3 and 4 lay out the approach, the scope, and the processes we found. Sections 5 and 6 then unpack more fully the findings and recommendations suggested above.

This report was commissioned by Big Society Capital and Esmée Fairbairn Foundation

2. WHAT WE DID — APPROACH



Approach

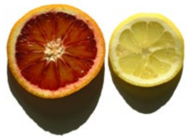
Over October to November 2014, Investing for Good (IFG) conducted interviews with ten Social Investment Finance Intermediaries (SIFIs) identified as leaders in the field of UK social investment. Most had participated in the previous research project, and most are (at the time of writing) current investees of either Big Society Capital (BSC) or Esmée Fairbairn Foundation, or both. These factors helped facilitate participation in the project. Interviews were carried out either with a social investment manager or the social impact manager, where the position existed, and were supported by desk research, encompassing the SIFIs' published materials (e.g. reports, websites), confidential materials where made available (e.g. portfolio details, proprietary methodologies), and general sector literature. Throughout this report, results have been pooled and SIFIs anonymised. The list of participants is given at the end.

Limitations

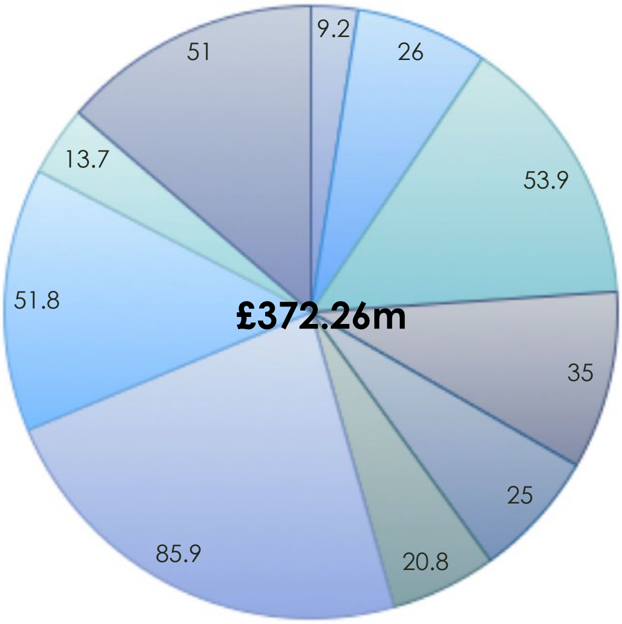
Our approach was designed to be open and produce thorough results. It is important however to acknowledge some limitations:

- Access to proprietary data was limited, as, understandably, not all SIFIs were willing to share full details of their methodologies, impact rating systems, internal reports, or investment portfolios.
- Access to primary impact data, as reported to SIFIs by their investees, was also limited as this was often deemed confidential to that relationship.
- Some SIFIs or sub-funds were too new at the time of interview to have made any investments, or too young to have started receiving significant impact data back. This meant the teams could not always share practical examples or discuss challenges based on existing investments.

3. WHO THE SIFIS ARE —THE SCOPE OF THE RESEARCH



All ten SIFIs are UK-based and focused, with funds representing a total of £372m in social investment capital. A number of individual SIFIs manage several funds, and we have included in this report those that have a dedicated social purpose, bringing the total number of funds in scope to twenty. In most cases, SIFIs treat impact measurement in the same or a similar manner across the funds they manage (when not so, this is clarified).

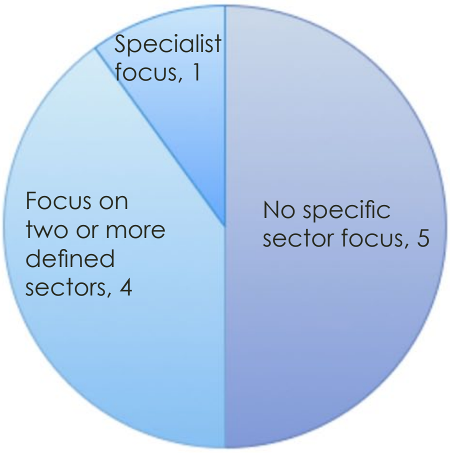


TOTAL SIZE OF FUNDS MANAGED BY THE SIFIS IN SCOPE

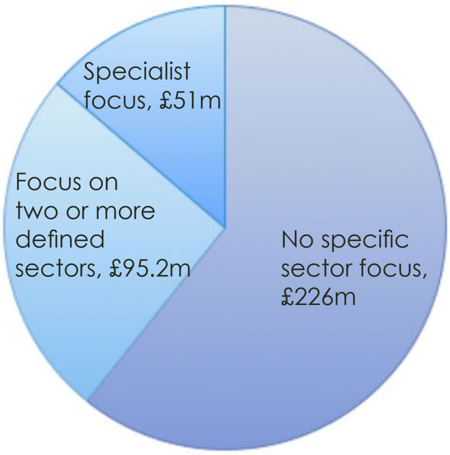
SIFIs by investor type		SIFIs by years of experience in impact investing		SIFIs by social impact resources	
Institutional	10	0-2 years	2	Blended approach: investment manager responsible for both financial and impact information	4
		2-5 years	0	Impact falls under appointed staff member's remit, managed alongside other fund responsibilities	2
		5+ years	8	Dedicated impact manager	4

All SIFIs define themselves as "impact first" investors, and invest only in organisations that have a clear, and often primary, social purpose. Such SIFIs seek to maximise social outcomes, and while maintaining a floor for the financial return, are willing to take on levels of risk that are not compensated, according to normal market measures, by that return (this would exclude many typical ethical or environmental funds).

None derive from mainstream commercial financial organisations (e.g. investment banks), and most of the founders come from a background in the social sector. None rely on Environment, Social and Governance (ESG) to understand impact (indeed only two use ESG at all, and then chiefly to evaluate governance), but instead deploy dedicated techniques to assess what real social and environmental benefits are being generated through the activities of their investees. All have social goals embedded within their organisational structures.



Number of funds by sector focus



Equivalent in fund sizes

Target Sector

Four of the SIFIs have two or more defined target sectors in which they invest (e.g. education, the arts, an ageing population). Five are "cause agnostic", requiring only that investees can demonstrate a social impact. One is a specialist SIFI, managing three funds, each with a particular focus.

Sectoral breakdowns across the social space are notoriously intractable. Very often investments straddle several sectors, with no easy rule as to how to apportion how much is in one sector as opposed to another (to provide a nonsense example, with an investment in housing for disabled people, what proportion is in disability and what in housing?). This is further complicated by the fact that most SIFIs have their own definitions as to what the various sectors are, and how to ascribe organisations and investments to one, another, or several. It was consequently not feasible to give a meaningful sectoral division of the invested capital.

Sources of capital

Nine SIFIs have raised capital from a range of sources, the majority of which is institutional (including banks and foundations based either in the UK or EU), often complemented with private investment from individuals and donors. In one case this included committed philanthropic capital, and in another, parts of the SIFI's own endowment. One SIFI, operating as a bank, also invests depositors' capital. One is wholly funded by its own endowment. Seven SIFIs have received investment from BSC, Esmée Fairbairn Foundation or both, four from foundations (excluding Esmée Fairbairn), two from a selection of sophisticated private investors, and four from institutional corporate banks.

Investment Size

Typical investments were in the range between £200,000 and £300,000. At the lower end, investments of less than £100,000 took place but were less common; at the upper end, many funds had individual investment limits in the region of £1.5m to £2.5m.

Lending Rates

Five SIFIs publish their expected return rates from investees, and these range from 5% to 15%, with simple loans at the lower end, and equity-type investments at the higher. Across the seven SIFIs we had information for, the average stated minimum interest rate for debt loans is 7%. The one SIFI that is funded entirely from its own endowment, and so hasn't received external investment, charges lower rates, with a minimum of 1 to 2%.

Loans rates charged by SIFIs are often comparable to those of mainstream sources of capital. The appeal to the social organisation of borrowing from a SIFI may be:

- risk tolerance: the mainstream financial sector may deem the social organisation too risky and/or unfamiliar, and not be prepared to engage in unsecured lending
- greater understanding: social organisations may feel that SIFIs understand their business models and motivations better
- support: many SIFIs offer capacity building and support to enable the organisation to take on debt that mainstream financial providers would not offer

These services are unquestionably of great value to the sector. It is worth noting however that SIFIs are attractive on these terms, rather than on price, and there is limited evidence to suggest there is a significant pricing discount available to borrowers for their social impact: i.e. an organisation's "social return" is tradable against risk, understanding and support, but not directly against financial return.

As for the risks SIFIs surveyed are willing to take, these vary, and are not strictly quantified against social impact, though this does play into the balance (see 4. What the SIFIs do). Some SIFIs who manage multiple funds have specific funds set up to take on more financial risk when presented with the potential for greater impact.

Maturity of organisations they target

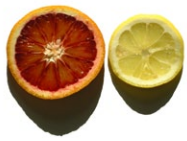
Three SIFI state their openness to investing in early stage ventures, and one takes that as its specific focus. One SIFI targets mature organisations or proven models. The rest are open to organisations of any stage provided there is strong evidence of, or potential for, impact.

Types of investment products

The SIFIs use a range of financial products: variable rate loans, fixed rate loans (including charity bonds), equity, quasi-equity, and revenue participation shares. None set targets or quotas against each type of investment; rather, they assess the relevance of a product to the organisation and its needs.

Five SIFIs invest 95% or more of their capital in straightforward loans. Four focus mostly on equity, though provide a mix of equity-like investments and loans (the precise split was not available). One SIFI has a fairly even split among equity-type products (such as quasi-equity, including revenue participation agreements), loans (secured, unsecured, fixed and variable rates), ring-fenced facilities, and Social Impact Bonds.

4. WHAT THE SIFIS DO — THE USE OF SOCIAL IMPACT MEASUREMENT, METRICS AND METHODOLOGIES THROUGHOUT THE SOCIAL INVESTMENT PROCESS



The social investment framework set out in The Good Investor was derived from the state of play in 2012, and the essentials have not changed significantly since. This section follows through the same key stages, noting for each how current practice is developing.

The stages are identified as follows:

1. Screening and Mapping	**2. Analysis**	**3. Investment Decision and Deal Making**	**4. Monitoring and Evaluation**	**5. Reporting**
Screening the pipeline of investments for potential matches, identifying key features	In depth analysis of the investee organisation and its impact (typically performed alongside financial due diligence). A scorecard or methodology may be used, the details of which will reflect the individual investor's aims and strategy.	Integrating the results of impact analysis into the investment decision-making process. Agreeing with the investee organisation what the impact goals of the investment will be, and how progress toward them will be measured and reported to the investor.	Monitoring the investee organisation's progress on impact and evaluating results.	Reporting by the impact investor to stakeholders at the portfolio level.

1. Screening and Mapping

Criteria for eligibility and suitability are defined, providing a screen to facilitate pipeline management; core information is extracted and mapped prior to in depth analysis.

Investors seek assurance that a potential investee organisation presents a true "impact investment", and that social impact is central to its work. In some cases specific legal structures will be required (e.g. registered charity, CIC). However there is still no iron definition or clear test as to what does or does not qualify as a (sufficiently) impact-driven — or mission-driven, social-purpose etc. — organisation.

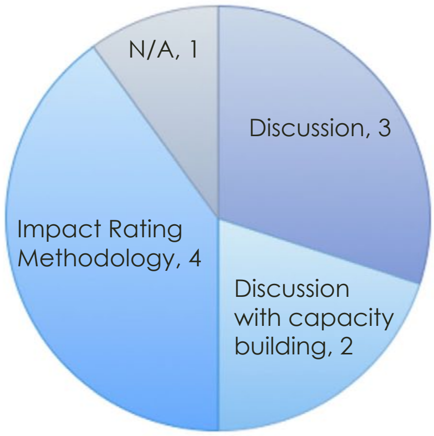
SIFIs variously screen and map against sector, region, and stage of development, and do so in ways peculiar to their own definitions and areas of interest.

2. Analysis

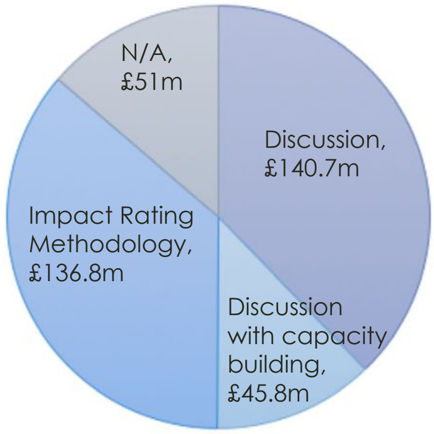
In depth analysis of the impact of the investee organisation and the specific investment opportunity is carried out (typically alongside financial due diligence).

With regards to impact, the analysis stage is where all the SIFI managers spend the most time. All have an approach to assessing how impactful an investment may be, and these are more or less formalised depending on the SIFI. The different forms of analysis can be loosely categorised as follows:

1. A discussion with the investee organisation
2. A discussion with a capacity building element
3. An impact rating methodology



Number of funds by Impact Analysis Approach



EQUIVALENT IN FUND SIZES

Forms of Impact Analysis Among SIFIs

The "Not Applicable" applies to a SIFI who works with one specific partner organisation, and so does not assess multiple potential investees in the same way

1. A discussion

Three SIFIs rely on conversations and a series of information exchanges to: determine the (potential for) impact of the prospective investee organisation; understand what if any form of impact measurement approach is in place; ascertain what the investment capital will be used for and how it plays into the generation of impact.

These SIFIs have little by way of a formalised and documented procedure, but use their experience to inform analysis. The SIFIs know what to ask and look out for, and pay particular attention to the organisation's structure, governance, mission alignment, impact evidence and transparency. Carrying out analysis in this fashion allows for a nuanced understanding, but does mean that, when different analysts are involved, there is no clear or consistent means to weigh opportunities against each other, particularly over longer periods of time; nor to go back to an initial assessment, and directly see how far the organisation has progressed.

Discussions of this kind are used in particular when the investment in question is short term, such as a bridging loan. If, for example, a charity purchases a building and is awaiting a VAT refund, the SIFI may lend the capital required to continue operating in the meantime. The discussion approach is taken by at least two SIFIs who carry out score-driven analysis for longer term investments (and are counted in the third category in the pie above), but who do not so when presented with short term straightforward lending. The core objectives of the deal may simply be the continuing existence of the organisation, and the efficient management of its cash flow, with limited longer term interest in the organisation's precise level of impact generation — not least because the SIFI would be little able to attribute much of any observed change to itself.

2. A discussion with a capacity building element

This approach is used mostly when the SIFI is involved in equity-type investments and therefore has a more "hands on" involvement with investee organisations. The investment manager and/or social impact manager will enter in discussions with the prospective organisation to understand their social impact, as above. However, where there is a desire to pursue the opportunity, the SIFI will work with the investee to help them articulate their impact better. This will often start with putting together a theory of change, and establishing a set of Key Performance Indicators (KPIs) (see Investment Decision and Deal-Making below). This process may take months, and goes on in parallel with general capacity building aimed at getting the organisation ready for investment.

3. An impact rating methodology, including a scoring and weighing system that takes into account the fund's priorities

Four of the SIFIs have a formalised approach to impact measurement. These approaches are all unique, and were developed by the SIFIs themselves to meet their needs and priorities (no off-the-shelf methodologies were in use, and SIFIs had either customised existing ones or created their own de novo).

Using this approach, the SIFIs allocate scores to prospective investee organisations on a variety of impact-related measures, as well on general operational and governance measures, each of which may be weighted according to the SIFI's own particular priorities. Bridges Ventures provides one example. In its Impact Approach Report,* Bridges details how it scores prospective investees on risk and return in relation to Target Outcomes, Additionality, Alignment, and ESG (see figure). Bridges will look for opportunities where the returns exceed the risks; and where this is not the case, the team may help organisations improve if a significant potential for impact is sensed, or the organisation is otherwise of particular interest.

Bridges Ventures Impact Radar

* http://www.bridgesventures.com/wp-content/uploads/2013/11/IMPACT_REPORT_2013_Final_hires-spreads.pdf

The use of scoring enables a more consistent approach, and produces results that allow for more clear-cut comparisons of investment opportunities. Three of the four scoring SIFIs have explicitly defined criteria and definitions as to what constitutes the various scores on their scales, and the fourth is planning on developing these to ensure more robust results (having found there was too much subjectivity without). For none of the four do the scores become the ultimate investment arbiter, or get plugged into higher level assessment systems, but rather are looked at individually, and used to inform the decision-making process.

Scoring may be supplemented by further social due diligence, including talking to a sample of beneficiaries, and comparing the investee organisation with competitors and with standards and external assessments where these exist. Again this process may take months, and be ongoing with detailed financial due diligence.

One SIFI made a conscious decision to avoid a rating system on the basis that it would be unable to take into account all the factors that can influence an investment decision, and that the risks and complexities encountered by smaller organisations are too different from those of larger ones to be subjected to the same tests.

While many SIFIs look for quantitative data, several noted the importance of qualitative data also in their analysis, and look to include narratives and case studies in their decision making. As many investee organisations aren't "impact ready" and don't already have a system in place, with hard metrics and pre-existing evidence, some investors focus more on the potential for impact, particularly with long term investments. This necessitates a slightly more judgement-driven, and less data-driven, analysis.

3. Investment Decision and Deal-Making

The results of analysis are passed on to the investment committee, where impact risk and generation, and financial risk and return, are considered prior to investment decision-making. A subsequent deal may include terms regarding impact reporting and performance.

This section focuses on: what is presented to the investment committee; the management of trade-offs in the decision-making process; and the incorporation of KPIs into the investment deal.

Presenting to the Investment Committee

What the investment committee sees depends somewhat on the previous analysis stage. If the SIFI uses a scoring methodology, the committee will be presented with a series of scorecards as well as notes across the opportunities. If the analysis is based on a series of discussions, the information will be summarised in a consistent report format.

Content will generally include a description of the social impact, an assessment of the financial risk, the suggested return, and details of the proposal and the governance of the organisation. One SIFI's investment team puts together reports of up to 30 pages for the committee's review, and at times invites the prospective investees to present to the committee. Other SIFIs present 2 page summaries.

How are trade-offs managed?

The trade-offs that take place — chiefly between the four key parameters of impact risk and generation, and financial risk and return, but also potentially regarding portfolio composition, and alignment with the SIFI's approach — are articulated and discussed in the investment committee meeting. While there are not clear rules as to how these are balanced in practice, some points of note came up:

- One SIFI manages a fund dedicated to higher risk opportunities and organisations that have been excluded from other means of finance. Substantial losses are expected, and greater emphasis is placed on impact.

- At least two SIFIs manage an Evergreen fund, where there is a primary need to ensure capital is repaid and recycled into new investments. One of the guidelines for the investment team is to determine whether any impact evidence supports the application; in practice, the starting point for the committee is usually financial risk.

- One SIFI invests only in tried and tested models, and organisations with track records.

- One SIFI who used a rating methodology, but without clear guidelines as to what constituted a high, medium or low score on the various measures, discovered that analyst-subjectivity produced significantly divergent scores, thus compromising the extent to which they could be used to assess trade-offs. Guidelines are now being developed.

- One Fund that rates opportunities on financial and social impact elements breaks down the social impact rating into four categories, which are weighted according to the SIFI's priorities. There is a defined minimum score below which opportunities don't make it to the investment committee.

In the majority of cases, if an opportunity reaches the investment committee but doesn't win investment, the reasons are predominantly financial. In one sense this implies the analysis stage is working well, as prospective investments are not being found wanting with regard to impact (in one particular SIFI, it is taken for granted that investments that have reached the committee have been deemed sufficiently impactful, and attention is therefore focused mostly on financials). That is not to say that further evidence of impact is never required, or that the committee doesn't question the level of impact, but it is not the primary focus. However this does suggest that impact analysis is operating to some extent as a "deep screen", and that prospective investments are perhaps not competing for capital on a rigorous impact-basis to the same extent that they are on financial terms. It also accords with the earlier observation that levels of impact are generally not being used explicitly or directly to move price.

Key Performance Indicators (KPIs) — Selection Process

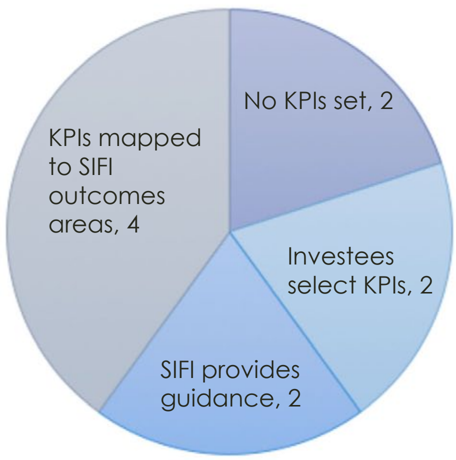
Once the committee has decided to make an investment, the investment manager or social impact manager will work with the organisation to determine how the impact will be monitored. Nine out of ten SIFIs regularly include an impact monitoring clause in their loan or investment agreement. However, the SIFIs varied as to what form this monitoring would take, and how any metrics or KPIs that investees would be obliged to report upon would be selected. The approaches can be loosely categorised as follows:

1. No KPIs set; agreed outcomes to be reported in narrative form

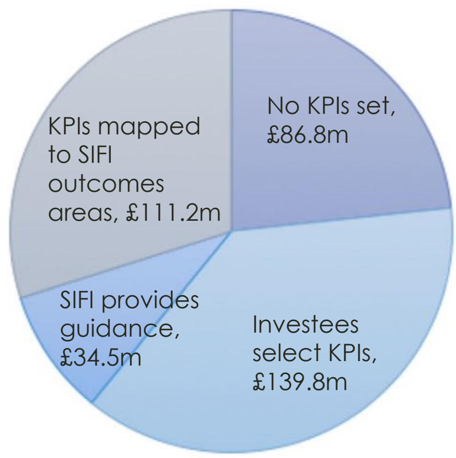
2. Investees select their own KPIs without SIFI input

3. SIFI provides guidance; final KPI selection determined by the investee

4. Joint discussion; KPIs ultimately mapped to SIFI outcome areas



NUMBER OF FUNDS BY HOW THEY SELECT KPIS



EQUIVALENT IN FUND SIZES

KPI Selection Among SIFIs

The categories above are based on the SIFIs' practices for their main funds. Two SIFIs manage a sub-fund for which the KPI selection process differs from their main funds. One SIFI who manages three funds is counted above as "investees select their own KPIs", though for one fund investees are provided with a menu of KPIs from which to choose (this is due to that fund being part-funded by a body that stipulates this requirement). One SIFI who manages three funds is listed above as "no KPIs set", though one of its funds more accurately falls under "joint discussion; KPIs ultimately mapped to SIFI outcome areas". One of the SIFIs listed as "joint discussion; KPIs ultimately mapped to SIFI outcome areas" uses a menu of KPIs.

1. No KPIs set

Two SIFIs don't require their investees to report on specific KPIs. Rather, one lets the investee choose a set of outcomes which they will report on in narrative form, and metrics are not attached. The other SIFI (for two of its three funds) consults its investees once a year and asks them to assess and rate their own impact on a simple scale with respect their particular area of focus.

2. Investees select their own KPIs

Two SIFIs leave it to the investee organisation to decide what they will report on, and provide little to no input in the selection process. This is based on the view that social purpose organisations are best placed to know how to evaluate the success of their own interventions, combined with a disinclination to be prescriptive. There was also a desire to avoid adding to the burden of investee work by demanding data that was not already being collected. Some managers added that when the investee organisation is small, the focus of efforts should be on growing the business rather than implementing a raft of new measures. One SIFI manager mentioned that they point organisations to freely accessible resources, and try to minimise the time spent by SIFI staff on working with investees on impact measurement. One drawback of investees selecting their own KPIs however is that results, when subsequently collected, are very organisation-specific (both in terms of content and approach), and difficult to compare across investments.

3. SIFI provides guidance

One SIFI deliberately gets more involved. They spend time with investees providing guidance on how to determine what to measure, and how to gather data. The ultimate decision of what to measure is left to the investee organisation, but the SIFI will have helped mould the approach.

4. KPIs mapped to SIFI outcome areas

Four SIFIs guide the investees' selection specifically toward indicators that will feed into their own high level target outcomes. Organisations can still tackle social issues in their own ways, but are conceived as working toward the same end goals. Having broad outcome categories enables the fund to understand what is being achieved in each area they've invested in, while leaving the investee with some freedom as to how exactly to capture their own data. The level of imposition is generally regarded as low, though this is helped by the fact that investees have, by this stage, been selected precisely because their activities are a good fit for the fund's outcomes. A possible risk here is that the fund may become less sensitive to innovative forms of impact that fall between or beyond their categories.

One of these four SIFIs provides its investees with an actual menu of KPIs, 70% of which are IRIS metrics. While IRIS is reported to be widely used outside the UK,* this is the only one of the ten SIFIs interviewed to do so.

In addition to building reporting requirements into the deal documentation, half of the SIFIs regularly take a position on the board of their investee organisations (especially when the deal is equity or equity-like). This allows the SIFI, during the subsequent stage of Monitoring and Evaluation (see below), to stay closer to how the KPIs are being used, and what the results are and mean.

In one case, to ensure the focus at meetings can be on impact, social investors have created a board sub-committee for social performance. This kind of structure is only useful however where the investee organisation is sufficiently mature.

* In the JP Morgan/GIIN 2014 impact investor survey *Spotlight on the Market*, 80% of respondents reported using metrics that align with IRIS or other external standards, 56% of whom specifically use IRIS. This survey however was of a much broader slice of the impact investment market, including investors who practice some form of social or ethical investment, but who would not necessarily define themselves as "impact first". They may consequently have different requirements to our cohort of UK impact first SIFIs.

A New Approach to KPIs at the point of Deal-Making: Carried Interest

One new approach (not included in the above categories as it is yet to be fully operationalised), is to apply the idea of "carried interest" to impact investing. Carried interest refers to the practice, used among traditional financially-motivated funds, of the fund manager investing their own capital in, and receiving profits directly from, the fund (typically up to 20% of the total profits once the limited partners have received repayment of the original investment plus a defined hurdle rate). In the context of impact investing, this translates to managers similarly investing in the fund, but receiving the carried interest only when financial *and* social impact targets are met. These social impact targets relate to a set of impact KPIs, against which results are collected and weighted into an average, and the average is then tied to a sliding scale of repayment. By this, should the success rate against the initial impact targets be 80% or above, 100% of the carried interest is paid to the fund manager; should the success rate be only 60-80%, 50% of the carried interest is paid; at success rates of below 60%, there is no carry.

The selection of the KPIs and the setting of targets, according to the categories defined above, would fall into 'SIFI provides guidance'. The fund manager works with the investee organisation to develop their impact measurement system, and helps select appropriate metrics and realistic targets.

This approach presents four striking features:

- By tying financial aspects of fund performance to social impact, fund managers are given an increased incentive to ensure that impact systems are in place, and impact data duly collected and reported. (This stems from an acknowledgement that in some cases, when impact is not bound to the financial side, it can be easier to let slip).

- The fact that fund managers stand to benefit financially from performance against impact targets they help to choose and set could be seen to present a conflict of interest. The use of financial incentives may also be problematic in a context in which results are not independently audited against well-defined standards (evaluating results may be made more difficult by the fact that the KPIs are also non-standard, with little necessary consistency or opportunity for benchmarking from one fund manager to the next). The risk is of weak or perverse targets and distorted data. To address this, fund managers stress the integrity of their team, and their commitment to investing in a responsible and impactful way.

- The application of carried interest to the social sector presents something of a jarring of cultures, essentially taking a profit-motivated practice, and applying it to what traditionally has been a not-for-profit (or not-very-much-profit) space. In response, fund managers who are uncomfortable with the idea are being offered the option to reinvest their carried interest in charities of their choice.

- Carried interest has come under criticism in mainstream finance due to the way it ties fund management into the fund manager's personal financial situation, and potentially their spending plans. For example, a fund manager who is in the middle of an expensive home refurbishment may become more risk-seeking, spurred on by the promise of carried interest. Or alternatively, a manager who has just finished paying off their mortgage, and is feeling financially comfortable at the time of considering one or another deal, may become more risk-averse.

The introduction of carried interest to impact investing is a pilot of the Social Impact Accelerator (SIA), which itself is an initiative of the European Investment Fund (EIF, a European Fund of Funds, somewhat akin to an EU-wide BSC). SIA invests in SIFIs, and requires these SIFIs to adopt the approach.

4. Monitoring and Evaluation

Monitoring and evaluating the impact of the investee enables the SIFI to determine if the investment is having the intended effect, and proving to be an impact-effective use of capital.

Overall, it was noted that social investment managers spend significantly less time on monitoring the social impact of their investments than they do on the earlier stage of analysis.* For analysis, most had some form of formalised approach, but with monitoring and evaluation, processes were less well-defined, and implemented with a different level of rigour.

This section considers three aspects of monitoring and evaluation:

- frequency of monitoring
- underlying investee impact measurement system
- type and treatment of collected data

Frequency of monitoring

The frequency with which SIFIs required their investees to report impact information varied between quarterly and annually, mostly depending on the type of investment. Equity-type investments tended to come with more frequent reporting, and straightforward loans with less.

While, as noted above, nine out of the ten SIFIs include an impact monitoring clause in the loan or investment agreement, all nine have confirmed having had difficulties at one point or another in obtaining impact information from their investees in a timely fashion. However none have ever withdrawn funds for a lack of impact reporting. Difficulty in obtaining impact information occurs more often with straightforward loans than with equity-type investments, where SIFIs are typically in much more regular contact with investees, and frequently will also have a representative on the board. There were no incidents of an "impact default".

One SIFI tried to implement reporting requirements retrospectively for one of its funds, for which the initial reporting requirements were insufficiently clear or stringent. This was met with some reluctance from investees, and the SIFI is still struggling to establish data for past investments.

Underlying investee impact measurement system

The content of the reported information will depend on what was agreed at the time of deal making (e.g. the KPIs), but will be significantly influenced by the investee organisation's underlying impact measurement system, and what it can realistically deliver.

While SIFIs would generally favour information on outcomes, the majority recognise this is difficult to obtain, and rely mostly on outputs. This is regarded as "better than no information", and does provide useful figures regarding the organisation's reach. Some SIFIs do not attempt to distinguish between outputs and outcomes, and focus rather on understanding whether any change is taking place. One SIFI commented that only 25% of investee organisations in its current portfolio would meet best practice in impact measurement. All SIFIs who have provided guidance in determining KPIs expect the

* This is line with the JP Morgan/GIIN 2014 survey Spotlight on the Market, which found that "the measurement of impact post-investment is viewed as essential by 51%, preferred by 24%, while 14% say that they are indifferent and 11% prefer to avoid it." (p.14)

level of impact reporting to be proportional to the organisation's size, capacity, and kind (depending on the organisation's approach, and the field in which it works, rigorous information may be regarded as more or less critical and/or feasible).

Overwhelmingly SIFIs are "methodology agnostic", and neither recommend nor exclude any particular approach to impact measurement. One SIFI is very closely involved in helping investees develop a rigorous measurement system, and does so by applying their own specific standards to the organisation's needs and activities.

One SIFI commented on a previous fund they had managed which, by way of a demonstration or "test" project, used SROI specifically as a means for a small proportion of investees — around 10% — to measure their impact, and indeed, to repay in part the loan (substituting a value in SROI for a financial amount). SROI training was provided for investees, but it was found that the resources, time and commitment demanded by the approach limited the extent to which the training was put into practice, and as the timelines for repayment by SROI came up, the SIFI had to review progress and identify what additional information was needed, including supporting evidence, in order to assess whether the value of the SROI was sufficient to consider the loan repaid. The approach has not been repeated. Other SIFI managers judged the SROI method to be valuable for organisations to think about in relation to the steps involved in impact measurement, but that the time required for a full SROI assessment would be an obstacle for their investees, especially since most are still getting to grips with the basics of impact measurement.

In no cases were independent audits of the reported impact data requested (except with Social Impact Bonds).

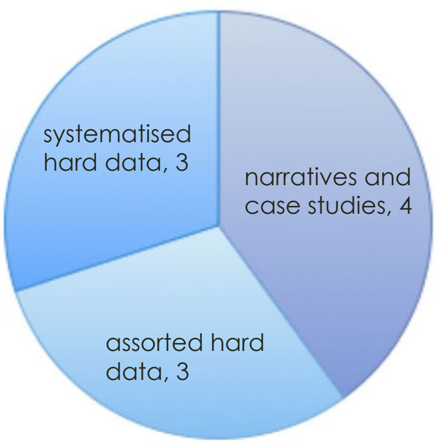
Type and treatment of collected data

The format in which the information is reported varies from free text to explicit scorecards, with direct implications for the type of data that will be collected, and for what can subsequently be done with it. The forms of data type and treatment are characterised as:

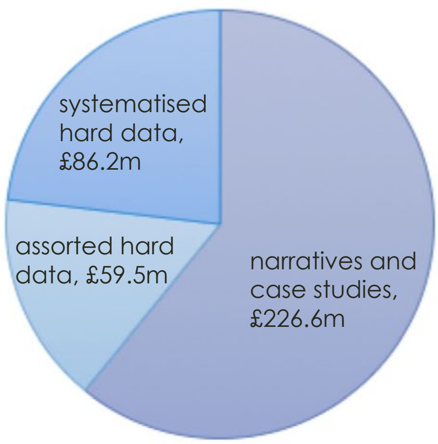
1. Narratives and case studies

2. Assorted hard data

3. Systematised hard data



NUMBER OF FUNDS BY HOW THEY TREAT IMPACT DATA



EQUIVALENT IN FUND SIZES

1. Narratives and case studies

Four SIFIs rely primarily on narrative information and case studies to understand the impact of their investments. Updates arrive in free format, and often without specific KPI or other metricised information. SIFIs maintain a good sense of their organisations, but little hard impact data on individual investments or across their funds.

2. Assorted hard data

Three SIFIs collect hard data on the agreed KPIs, as well as monitoring contextual and general progress updates. The format is free but with the KPI requirement. Information is stored and compiled longitudinally for each investment, though the format may change over time. This facilitates a more precise knowledge of individual investments, with some ability to compare individual performance over time (though the data may not always be in a readily accessible or flexible format). Consolidating or even relating understanding across investments however remains hard as information is compartmentalised and discontinuous from one investment to the next.

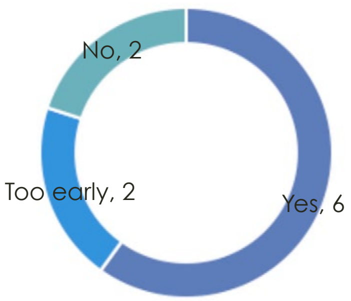
3. Systematised hard data

Three SIFIs seek to collect and systematise data — i.e. hard data is received from individual investments, and categorised and accumulated in some way at the sector or outcome area level. This is made easier through the use of supplied scorecards for investee reporting (devised by the individual SIFIs), which ensure the use of consistent formatting and categories across investments. Collected information can thus be shared more easily between investment officers and teams, and provides a basis for data consolidation.

The kind, quality and quantity of information SIFIs are able to collect and digest through monitoring and evaluation informs reporting at the fund level.

5. Reporting

Impact investors are held to the same standards of accountability and transparency as their investees. Reporting can be to investors, wider stakeholders, and to the sector and public at large. It also serves to ensure investors are regularly reviewing themselves, and assessing their own impact.



Published impact reports among SIFIs

Two SIFIs are relatively young and are yet to make sufficient investments to warrant the publication of an impact report, though both have plans to do so in the future. Two SIFIs compile a summary overview of the portfolio's performance for an internal investment committee review, but do not publish an impact report. Six do.

More than half the SIFIs have produced at least one social impact report or an annual report that covers both financial and social impact performance. What information is included is up to the SIFI. Generally, feedback from private investors is that they have enjoyed reading the reports, and been satisfied with the level of information produced. Where reports have been tailored to investors (in the case of one SIFI), or events organised for investors to visitor or speak to investees (in the case of three SIFIs), these have proven very popular. Reports have likewise been sent to institutional investors (where applicable), though they have been less vocal in their response. For all SIFIs producing reports, there is currently no investor-side pressure to change reporting standards.

The two SIFIs who haven't yet produced a report have raised investment from corporate and institutional bodies as well as foundations and private individuals, and plan on publishing a report for these parties. The two SIFIs who haven't published external impact reports are those who have invested their own endowment or foundation capital.

Regarding the six SIFIs who have produced impact reports:

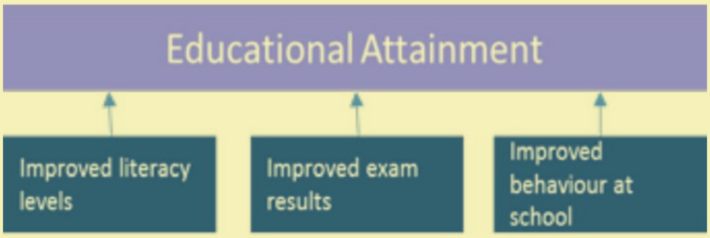
- Two focus chiefly on case studies of their investee organisations, which are individually listed and described. While both of these SIFIs collect data on impact KPIs, only one includes it explicitly in the report.

- Four aim to provide more fund and sector level information, and to give an account of their impact by sector and outcome area. Three foreground their impact processes by outlining their analysis methodologies, and summarising results from various impact metrics across different investments (the fourth does not collect metricised impact data, and instead averages self-reported scores). Several SIFI managers commented on the difficulty of aggregating data (see box on Data Aggregation). For all four, this consolidated information is then followed by details of individual investments in case study format (including impact data for the three where this is collected).

Impact Data Aggregation

Three SIFIs perform some form of data aggregation or accumulation. Key to this process is the collection of hard data, but also the use of consistent formats or classification tools. The way in which the data is collected, sorted, stored and managed (in terms both of informational structure and IT systems) is a critical determinant of what it is possible to do with it.

SIFIs with specified target outcomes are more likely to be able to think about data aggregation as the outcomes will elicit commonalities among investees, and provide a basis for impact measurement categories (there may also be more commonalities given that the SIFIs will inevitably seek investees that are a good fit for their outcomes). During the analysis stage, impact managers may guide the KPI selection toward those that feed into their outcomes, and this supplies the framework for the data collected in the subsequent monitoring and evaluation stage. The diagram below shows an example of proxy indicators at the investee level mapping to a target outcome at the fund level.



EXAMPLE OF USE OF PROXY INDICATORS THAT FEED INTO FUND TARGET OUTCOME

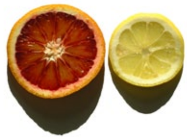
Note however that the proxies themselves remain different, as will the specific pieces of data collected. Several SIFI managers commented on the difficulty of aggregating data given how KPIs are rarely the same, even for organisations working in the same sector. Differences among approaches, interventions, and beneficiaries further complicate the matter. The SIFI of the above example does not seek to aggregate data, but focuses rather on ensuring that information relating to the activity of different organisations and interventions with regard to their outcomes remains accessible. This is the core purpose of organising the data.

An additional concern regarding data aggregation is the quality and nature of the data itself. SIFI managers spoke of the time it takes for investees to develop and put in place appropriate impact measurement systems, and even then, there is the further time required to confirm that the data coming out of them is the right data, and produces a fair account of the impact being achieved. Refining this process can take years — and especially so when the impact itself is not a quick fix, but a distance travelled over a period of years, as may often be the case when dealing with vulnerable beneficiaries. Throughout these years the monitoring and evaluation is ongoing, but the exact meaning and quality of the data may remain moot, or at least partially undetermined. There was a belief that good evaluation does lead to good information, but not necessarily quickly, and often not in readily aggregatable columns. And then there is the further issue that if systems and indeed services are being updated and improved over the course of an investment, this mixes more dissimilarities into the numbers. Among some SIFIs interviewed, there was concern that sector calls for data aggregation, harmonisation and standards may be emphasised over the essentials of good data practice.

Overview Table — the use of social impact measurement, metrics and methodologies throughout the Social Investment Process

Screening and Mapping	• 5 SIFIs have no specific social sector focus (including one fund which invests only locally) • 4 have two or more specific target sectors • 1 manages specialist funds only
Analysis	• 3 SIFIs analyse opportunities and proceed to social due diligence by engaging in discussions with potential investees • 2 engage in discussions as well as helping potential investees build up their impact measurement approach • 4 analyse opportunities through an impact rating methodology • This stage doesn't apply to the remaining SIFI due to its investment partnership model.
Investment Decision and Deal-Making	• 2 SIFIs don't require their investees to report impact through the use of KPIs, and let them decide what information to report • 2 let the investee organisation decide what social impact metrics they will report to investors (in KPI format) without actively taking part in the selection process • 2 engage in discussions with investees and provide guidance on how to choose the best metrics while leaving the final decision with the investee • 4 guide the investees through discussions to agree metrics that ultimately fit into the SIFI's own target outcomes, one of which also offers a menu of KPIs, each ascribed to the various outcome categories
Monitoring and Evaluation	• 4 SIFIs rely on narratives and case studies to understand the impact of their investments • 3 use the information received to compile hard data per investment • 3 further systemise the information and classify it by sector to better understand impact at the portfolio level
Reporting	• 6 SIFIs have produced at least one impact report • 2 are too young, but intend to do so in the future • 2 choose not to share impact reports externally but produce summary reports for their investment committees

5. OBSERVATIONS AND THOUGHTS



Throughlines

The above section gives an account of how a cohort of UK SIFIs are handling impact at each individual stage of the investment process. Having laid this much out, the immediate next question is, what are the throughlines? How does the behaviour of individual SIFIs concatenate across the stages?

As readers will probably have felt, there is an on-going stage-by-stage variation as to how "systems-driven" the approach is, and unsurprisingly, there is a fairly high level of consistency from one stage to the next as to which SIFIs fall into which categories. Indeed to some extent, choices made at each stage set up the next: e.g. at analysis, a SIFI uses a highly defined scoring card; the results suggest appropriate KPIs at deal-making; these in turn provide hard data during monitoring and evaluation; and so feed into the final report. Alternatively, a SIFI that takes a less systematised and more personal approach, starts with a discussion, maintains a listening relationship, and at the end produces a descriptive case study. It is important to note that all the SIFIs interviewed take impact seriously, and have thought through the processes they use for dealing with it. Also important to remember is that no SIFI is entirely either/or — those that rely more on discussions nevertheless have a developed sense of what these must cover, and what questions need to be asked. And equally, those that engage more with scoring and systems-driven techniques, very much still depend on discussion with their investees, and have by no means reduced things to the plugging of impact numbers into a portfolio management formula.

However, a spread between less formal and more formal, or less systematised and more systematised, does inevitably emerge. And so what does the use of more rigorously defined impact systems mean for a SIFI? The clear advantages are that they tend to produce more quantitative data, and (where appropriate procedures and guidelines exist) more consistency. These are unquestionably of value when it comes to attempts to review investments against each other, against time, and in the context of the portfolio as whole. But the limits of quantification and consistency remain clear: no SIFI is ready to do away with individual case studies (either for internal or external reports), or with taking a personalised approach to each investment. And at a higher level, the fact that the systems in use are all unique to their SIFIs speaks of how personal these systems really are.

A further point that comes out of looking at throughlines is a strong correlation between the level of systematisation and the investment type. In short, equity-type investors tend to be more systems-driven and debt investors less. On the one hand, this makes perfect sense: equity investors spend more time with their investees, go deeper into them, and, given that they are often taking on greater risk, need to be that much more thorough. Complex impact processes are resource intensive, and it follows therefore that equity investors should be the ones willing to take them on. Also, where equity investors sit on the boards of their investees, they are automatically in a much stronger position to ensure the desired impact systems are implemented, and that impact data is reported on time and in the appropriate format. However, it could on the other hand be argued that the reverse should be the case: i.e. that straightforward lending should be managed more by systems, and specialist equity investments by more individual approaches. What this points toward, and what is certainly the case in practice, is that the use of impact systems, given the current market context, is more time consuming not less, and — paradoxically almost — more "hands on".

And so, what does it yield? The more systematised approaches certainly accord more closely with what has previously been set out as best practice, but in real world practice, what does it do for the SIFI? Most importantly, can we say that those SIFIs that apply more rigorously defined impact systems thereby achieve a more efficient use of impact capital, and so have more impact?

The answer is: it's hard to say. Certainly one can say that their impact strategy is in better order, and to some extent bears up better to scrutiny. And, for people who generally believe in systems in and of themselves (and therefore like things like detailed processes, clearly defined criteria, the presence of metrics etc.), there is something of an assumption that this should automatically lead to better results. What doesn't exist however is a clear body of evidence to demonstrate that the more systems-driven SIFIs have greater impact — not least because the impact evidence all SIFIs are collecting, both in quantity and kind, is so dissimilar. What further isn't altogether clear is that there is a direct line between a SIFI's level of impact systematisation, and its ability to attract investment.

In a commercial context, there's a good test for best practice: if a business uses it, it does better; if it doesn't, it gets outcompeted in the marketplace, and cannot amass capital. These are the drivers. But given that this isn't immediately the case in relation to impact best practice, it is worth investigating what alternative drivers there are.

Getting value out of impact: the drivers of impact systems

The theoretical arguments for high levels of systematisation in the measurement and treatment of impact suggest there should be drivers in four key areas:

1. investment selection: consistent impact measures provide a basis for making more impactful investments

2. investment management: impact data demonstrates how impactful different investments are, with implications for how to manage them

3. reporting: impact data meets the demand for transparency and accountability (just as financial data and reporting do on the financial side)

4. portfolio management: consolidated impact data provides key signals at the fund and fund of funds levels

It is worth working through the extent to which these drivers are present and active in practice.

1. Investment Selection

As noted above, the analysis stage is where SIFIs spend the most "impact time". Where formalised frameworks have been developed (in six out of ten cases), these are used and certainly inform understanding — though the same can also be said of less formalised analyses. Frameworks do prove useful in pointing to ways in which SIFIs may work with potential investees on capacity building, and developing investee impact measurement systems. Notable however is that SIFIs generally agreed that if an investment proposition made it through analysis to the investment committee, it was in effect deemed "impact worthy", and the committee-level decision was more likely to be influenced by financial factors. In this sense the analysis is effectively operating as a screen. What there was less evidence for was of investment committees being faced with multiple opportunities of equal financial attractiveness, which therefore compete on the basis of impact. To some extent, this relaxes the need for explicit, comparative scoring, and therefore, the drive to build and have such systems.

This situation may in part be due to a weak investment pipeline. Were the practical reality one in which committees were regularly flooded with highly investable opportunities, there would be a more clear-cut need for competitive scores.

2. Investment Management

Here the research suggested that in practice SIFIs have less time for following up on what their investments are actually achieving (see Monitoring and Evaluation above). Resource limitation and competing priorities play an inevitable role, with SIFI managers acknowledging: a need to downplay impact in their daily operations; the lack — in most cases — of a dedicated impact resource; and the reality of financial concerns often taking precedence over impact. There are also the very valid factors that many of these investments are still relatively young, and operating in contexts in which measurement is far from mature, both of which contribute to a situation in which decisive impact data is limited. This creates a context in which the extent to which impact can usefully feed into management decisions is likewise limited. The fact that the research uncovered no examples of "impact defaults", or cases where investments were being "written down" in some sense due to impact failures, is telling. Without this edge, investment managers are not in practice faced with impact concerns according to the rules or logic of investment.

3. Reporting

All SIFIs do engage in some form of impact reporting, and in most cases are expected to do so by external parties. At the same time, a matter brought up several times in interviews was the lack of impact reporting demands from the SIFIs' investors, and in no cases were those receiving reports expressing dissatisfaction or a desire for more information, or specific kinds of information that were not being provided. This is the case in spite of the fact that the reports themselves varied considerably in terms of content, approach, level of systematised impact data etc. This shows that non-standardised reporting is not running into a serious problem of an investor-demand for standards. Consequently the question of what to put in an impact report is largely a matter for SIFIs themselves, and there is little external drive on this front.

4. Portfolio Management

As discussed above, one notable finding of the research was that systematised impact measurement was most prevalent among equity-type investors, who also took a "hands on" approach, involving close personal dealings with investees and often sitting on boards. Due to the nature of this kind of investing, the numbers of investees in such cases tended to be relatively low (there are only so many boards one SIFI can sit on, investees it can capacity build etc.). What we did not find was an example of a SIFI with a large portfolio, say of several hundred investments, and with high levels of systematised impact data that it used to inform portfolio management. The key difference is that when the portfolio is small, systematised information serves chiefly to support an in depth individual knowledge of each investee. The system provides a process for how that knowledge is built, and substantiates it with results, but these results are not expected to stand alone, and nuance still plays a vital role. When the portfolio is large however, and the individual knowledge removed, there is a much greater pressure upon impact data to deliver the correct signals in itself. The real driver for the data is scale, and the need for scalable (i.e. non-personal) systems. Again this is not obviously present in the current context at the fund level (equity-type investors necessarily have modest numbers of investees, and SIFIs with large loan portfolios don't have complex data on their investees). Funds of funds do accrue considerable scale, and operate at a remove from individual investments, but the problem that immediately surfaces here is that the impact systems among the funds they invest in, when present, tend to be unique. Consequently they do not readily build together in such a way as to provide fund of funds managers with clear impact data that can be accumulated under a single system, and guide decisions at the portfolio level.

All of this suggests that the theoretical drivers of systematised impact measurement in practice remain weak — or, to be more accurate, much of their drive is satisfied by where current practice is. A slow pipeline, limited resources, the absence of the threat of an impact default, content investors to report to, and a lack of scale, all contribute to a context in which even relatively unsystematised approaches to impact are not obviously breaking down. In reality there isn't an overwhelming operational need for heavily systematised impact measurement.

And yet some SIFIs do have very developed and thorough systems. Why? The answer may well be that, as much as anything, it is a question of organisational culture. Different staff, different boards, different ethoses, lead to different stances on how best to do impact, and how far to go with scorecards, frameworks, KPIs and so on. In short, SIFIs are more or less "systemsey" according to who they are.

Getting into trouble with impact: the challenges to impact data

As well as drivers, there are obviously challenges to working with impact, and it is similarly worth considering how these are showing up in practice. They are most apparent in relation to the impact data itself, and all the efforts that go on around it (collecting, organising, sharing etc.). The research indicated four key areas of difficulty:

1. sticky data

2. discontinuous and category-resistant data

3. quantity and quality of data

4. how as a SIFI to handle data

1. Sticky data

SIFIs for the most part know their investees, and a good deal about their impact, but much of this knowledge is in the form of a unique expert (the investment officer dealing with each investment), and their unique description. Here very often the understanding is rich, but the underlying information is "sticky". It doesn't transfer easily from that person to other formats, and doesn't slot neatly into spreadsheets, or separate into clear quanta of data. It sticks to the person, to their reports, and to their presence in meetings.

2. Discontinuous and category-resistant data

As pointed out above (and as is much discussed generally), the indicators in use, even within sectors, are rarely the same, resulting in discontinuous sets of reported data. In addition to this, the broader landscape of the social sector itself is full of overlaps and indistinct boundaries, and gets carved up in many different ways. Where any one piece of data falls is frequently a judgement call, and with little conformity about how such judgements are to be made. From one SIFI to the next, sectors and outcomes are defined differently, with information often wanting to sit in two or more categories, or no categories.

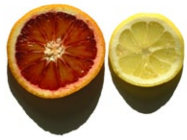
3. Quantity and quality of data

SIFIs are reliant on investees for primary impact data, and yet there was overwhelming agreement that impact measurement among investees, and collecting impact data from them, was frequently a problem (with the typical obstacles of limited investee resources, capacity, and not knowing what to measure). Reporting clauses are often written into investment deal contracts, but are not always followed up as rigorously as they might be, and the quantity of data that comes back can be patchy. Also, as one SIFI pointed out, the contracts do not cover the quality of the data. Investee data comes in self-reported, without auditing, and where there are things like scores on potentially subjective measures, there may be little assurance these have been defined and understood in a consistent fashion.

4. How as a SIFI to handle data

With the data SIFIs do receive, there continue to be major questions over how to handle issues such as attribution and double-counting. If a SIFI's investment is anything less than 100% of an investee's capital, how much of the impact is attributable to the SIFI? If a percentage, is this of a percentage turnover, of balance sheet total etc.? What if the investment is not actually in impact-generating activities (e.g. is for the purchase of an office building, or a new IT system)? Should the impact of an equity-type investment be counted in the same way as a loan? How should the impact be counted when the term of the investment is different from that of the intervention and the change it brings about? Where an investment spans multiple outcome areas, how to avoid double-counting beneficiaries, or the amount invested in each? Carve it up? If so, how? And so on. These are very real accounting questions, and there are no agreed rules as to how to deal with them. Nevertheless, figures are being construed, and placed on the front pages of impact reports.

6. CONCLUSIONS AND RECOMMENDATIONS



Given a practical context in which the operational drivers for impact systems are not at their maximum, and the challenges to impact data remain considerable, what are the implications for a working SIFI? SIFIs clearly do care about impact, and adopt more or less formal strategies as to how to deal with it, according, at least in part, to their own organisational culture. But a further important aspect for the sector as a whole is the greater cultural context, which currently is very much in love with data. Contemporary interests in big data range across everything from dating apps to climate modelling, and from government surveillance, to a giant European neuroscience project that aims to simulate the flow of data throughout every cell in the human brain. These are clearly times in which dataphilia, or even datamania, is prevalent. And for impact investment equally, there are significant cultural expectations for lots of impact data to exist, and to be presented, preferably — seeing as it's the most obvious comparison — in forms that look like financial data. The very real risk, when these expectations outrun the genuine operational need for valid data, and when the data itself isn't being audited, is that it just turns into *datawash*.

To avoid datawash, it's important that expectations for impact data are matched by its actual use, and that impact systems are reviewed against what they are being used for. The accuracy and completeness of the data will invariably correspond much more to this operational side than to clamours from sector commentators for it to be more one thing or another. Use in itself is hard to change point blank — issues like pipeline and scale are at present as they are, and remain reliant on a vast number of factors well beyond the control of how impact is being managed. However the other side of the potential mismatch — i.e. how the data is being called for and received — can be rethought much more easily. One thing to look at is the expectation in different contexts; and the other, how the published impact data is being read.

Expectation: investment structure

It is clear from the research that different terms and types of investment are treated differently by SIFIs with respect to impact, and one recommendation of this report is that expectations regarding impact measurement and reporting should differ accordingly. It is obvious that neither the impact of, nor the SIFI's capacity to gather impact information about, a short term loan, for example, will be the same as for an equity-type investment. Yet while this distinction clearly exists in practice, there is little in the current investor guidelines as to how it may be done, or reflected in investor reporting.

In some cases, the investment is clearly aimed at growing the impact of the investee organisation. In others it may be to strengthen the organisation itself; in others still, simply to provide better solutions to issues of financial management. A significant role for impact investment is to supply the basic financial infrastructure and services that a functioning market of social enterprise requires. The impact of capital used in this fashion is neither necessarily less, nor, from having been recycled many times, several fold more than that of a single long term direct investment. But the mechanisms that will be best suited to assessing the impact of such capital, and delivering realistic information back to the sector, will be different.

With a considerable range of terms and investment structures in use, further work will need to be done in this area to draw out and formalise the current understanding, and define the appropriate impact measurement tools and guidelines for SIFIs.

Reading: peer group review

As noted above, there is little evidence of active pressure from investors for more or different forms of impact reporting. SIFIs essentially devise their own impact reports, including what information to put in them, and how to treat and present it. The argument for more or better impact reporting has generally been made in positive terms: i.e. that it's a noble thing to do, and good practice recommends it. However there is relatively little by way of a negative alternative scenario. If a SIFI were to ask itself, 'What if I don't do an impact report?' or more, 'What if I don't include x in my impact report?' or, 'What if do include *y*? Is *y* acceptable? What if I add up these figures in this way, or that? Or draw a pie like this? What then — ?' In reality, there is often little by way of consequence. And as a result, the extent to which publishing an impact report represents true accountability is significantly compromised. If the figures don't come under external scrutiny, and aren't being used for immediate internal purposes, there simply isn't the same pressure to get them right. And this slackness then runs down the chain: the exigency with which information will be collected from investees, and properly verified — especially where priorities compete and resources are stretched — will inevitably be that much less.

There is little point in saying investors *should be* more demanding, critical, interested, etc.. But a different, and perhaps more helpful, form of accountability is possible however, and at present is underleveraged: that of SIFIs' accountability to each other. The second recommendation of this report therefore is the formation of an explicit SIFI peer group for the reading and reviewing of impact reports.

A peer group of SIFIs clearly exists already (those interviewed for this research form an obvious core), as do a number of networks, alliances, and agreements around principles. What is less apparent however is clear peer group activity, in particular in the form of mutual reviewing. SIFIs are currently aware of each other's reports, but a peer group review could go further, asking SIFIs not only to read but to provide critical feedback. This would include criticism, necessarily, but also suggestions and support.

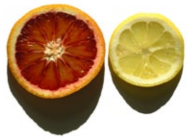
Simply the knowledge that such a review would take place could affect the way SIFIs approach impact reporting, and indeed give the impact process a clear end point (rather than allowing it to be some floating thing that the SIFI has to do). But more than this, the activity of reviewing would necessarily force SIFIs to confront in a group format questions around how to handle persistent challenges to impact data and reporting, including those outlined above. It would thus form a basis for starting to develop common rules around fundamental accounting issues, such as attribution and double-counting, as well as to share ideas around systematisation, and how to cope with issues like sticky and category-resistant data.

One reason investors may be relatively undemanding when it comes to impact reporting is that they don't know what to ask for or complain about in an impact report. Through the group however, SIFIs themselves would take charge of defining what good reporting looks like — and not just in terms of aspirational principles, but in relation to the concrete cases of their own reports, and their treatment of real data. And they would also, through a form of mutual accountability, provide a tangible reason to refine and maintain standards.

If such a group were to work well, it would also provide an opportunity for greater levels of sharing among SIFIs. This may relate to the sharing and comparing of techniques, but also the to the sharing of data. If pooled, this could allow for much more effective tests of different systems in the face of real data at meaningful scale. It would also help SIFIs develop a more secure sense of the lay of the social investment landscape itself, in such terms as how big it is, how fast it's growing, how it's carved up etc..

Such a group could be self-assembled and self-run by the SIFI members. Alternatively an independent body or party could be entrusted with the task of coordinating group activity. Either way, the initiative would clearly require some form of leadership, with responsibilities including: managing and overseeing the feedback process; writing up ideas and prospective systems, rules or guidelines coming out of the group; setting agendas; and managing group information and (where applicable) confidentiality and anonymity.

7. KEY FINDINGS



One of the conclusions of this report is that there are impact ideals, and there are operational needs, and that the one without the other may not mean much. For this reason, we have limited ourselves to two explicit and simple recommendations: that some distinctions regarding the handling of impact measurement for different investment types be generally and formally set out; and that SIFIs should form a group and meet regularly to review each other's work, discuss problems, and drive practice forward.

A number of further points are made over the course of the report, and which SIFIs may wish to consider and take action or not according to their needs and situations. For ease of use, these are collected together below, and may form starting points for subsequent discussions. (N.B. the findings are inevitably broad in nature; they represent tendencies not laws, and there are exceptions to many.)

- There were no cases of "impact defaults", in which funds were withdrawn or investments written down on account either of insufficient impact data being reported, or of the impact data being reported showing that insufficient impact was being generated. This would imply that, according to a pure investment logic, impact is not an investment concern.

- There is greater focus on the pre-deal analysis of the proposed impact than on the subsequent monitoring and evaluation of the actual impact. An implied risk here is that the analysis is not being properly tested (i.e. it is not determined whether investments deemed to be higher or lower impact at the moment of investing prove to be so), and that less time is spent on understanding impact or learning from past investments than on servicing the need to make new deals.

Analysis and Price

- Pre-deal impact analysis can act more as a form of screen or impact hurdle, with financial considerations coming to the fore once it has been cleared. This implies there is less one to one competition among investments on pure impact grounds.

- There is little evidence for impact explicitly or directly moving price. Investors may be prepared to take on extra risk for high impact, and expend more resources on capacity building, but clear processes by which e.g. a high impact organisation can be charged 3% for a loan whereas a lower impact organisation would pay 7%, are less apparent.

Systems and Standards

- Approaches to impact measurement largely follow investment types. Equity often corresponds to more rigorous analysis, more frequent monitoring, more oversight (with a board position), and more metrics and systematisation. Debt corresponds to less rigorous analysis, less systematisation, more emphasis on discussion, fewer metrics and more free-form reporting.

- No off-the-shelf methodologies are being used by SIFIs to measure their impact, and instead all are individually developed and unique. Furthermore, SIFIs are overwhelmingly "methodology agnostic" when it comes to how their investees measure impact. This lack of standards persists in spite of much talk around standards, and the presence of a number of would-be standards.

- Scoring, quantification, impact data, and systems in general are applied and interpreted overwhelmingly at the individual level, and are not being plugged into higher level systems or automated forms of aggregation or interpretation (or only in a limited way). Systematisation does not in this capacity readily roll out to large scales. Instead it is in some ways closer to being an in depth process for work taking place at the individual level, and as such is more rather than less demanding in terms of time.

- Key operational drivers for highly systematised impact processes include scale at the pipeline end (i.e. a large number of investable opportunities competing on the basis of impact), and scale at the portfolio end (i.e. a large number of investments with rich monitoring impact data on all of them). In the current operational context however scale is limited on these two fronts.

Reporting

- There is little independent auditing of impact data, either as reported from investees to investors at the monitoring and evaluation stage, or as reported by investors to their stakeholders. An obvious barrier here is resources, though it does also imply a ceiling as to what that data can really be used to do. If unaudited data, for example, were to be used to influence price, then clear incentives would be created, if not explicitly to cheat, then at least to make judgement calls that favour a particular result.

- SIFIs lack accounting rules regarding what to do with the impact data they collect. Questions of attribution and double-counting remain unresolved, as do those surrounding how to treat and count different investment types.

- What is in — or not in — an impact report is largely up to the SIFI writing it. SIFI's investors were largely found to be satisfied, and not to be actively demanding more information, specific kinds of information, or more standardisation, even though the reports themselves varied considerably. An impact report being more one thing or another does not lead to obvious consequences.

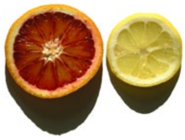
- If the expectations and rhetoric around impact data outrun the operational use of impact data, there is a significant risk of datawash. Data produced primarily for communication and PR purposes will not attain the same level of quality or meaningfulness as data that is actively used for decision-making.

Data

- A major underlying problem is the quality of primary impact data from investee organisations. Organisations can be given support and capacity building, but good impact data in practice is often slow. To create and implement an impact measurement system, and to verify that the results it produces are meaningful, complete, accurate etc. will often be the work of years. Quick and dirty alternatives have obvious appeal, but may be counterproductive if the data they produce is inaccurate or incomplete to the extent that the signal is wrong.

- Data that is forthcoming, even when good, remains disparate and sticky.

8. ACKNOWLEDGEMENTS



This report was commissioned by Big Society Capital and Esmée Fairbairn Foundation. The SIFIs that participated in the research and who are included in this report were: Big Issue Invest, Bridges Ventures Social Entrepreneurs Fund, Charity Bank, Esmée Fairbairn Foundation, Impact Ventures UK, Nesta, Social Investment Business, Social Investment Scotland, Resonance, Venturesome. We also thank the Social Impact Accelerator at the European Investment Fund, Ethex, and Social Finance for taking part in interviews.

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