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Mission-related investments are a powerful tool for social change

Today's charities and charitable funders are increasingly breaking down the historic division between their social mission and their investments. More charities are realizing that their investments can also be a powerful tool for change. And in a period of extreme volatility in traditional investment markets and limited resources for program and grant expenditures, the idea of devoting a portion of investment assets to furthering social goals has strong appeal.

These mission-related investments, or MRIs, as they are known, come in a wide variety of shapes and sizes.

MRIs may be loans or equity investments. They may be intended to generate a market rate of return, or they may be purposefully designed to allow below-market returns in order to achieve a mission goal. An organization may vet its equity portfolio to include only socially and environmentally responsible companies, or it may make low- or no-interest loans to small charities, businesses or individuals that do not have access to conventional sources of capital.

The Seattle Foundation, for example, extends low-interest loans to other established nonprofit organizations that have the capacity and expertise to administer loan programs for minority and immigrant small business owners, affordable housing and other community projects. Strategies like these can leverage an organization's assets and complement traditional grant-making approaches.

The meteoric rise of microfinance lending, funded by organizations such as Seattle's Global Partnerships, which provides opportunities for individuals living in poverty to improve their lives, is another dynamic example.

MRIs blur the lines between investments and charitable programs and may require collaboration between investment and program officers. At the Bill & Melinda Gates Foundation, if a program officer proposes to further the foundation's mission by making an MRI, the investment team analyzes the anticipated rate of return compared to the 5 percent annual rate the foundation expects from its traditional investments. If the estimated rate of return from the MRI is less than 5 percent, only the difference between the estimated rate of return and 5 percent is charged against the program budget, whereas the entire amount of a grant made for the same purpose would be charged against program expenses. This provides a budgetary incentive for program officers to think outside the usual grant-making box.

MISSION POSSIBLE

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Since MRIs necessarily straddle the lines of authority between investment and program officers, they provide an opportunity to strengthen an organization's team and develop a more holistic approach to achieving the mission.

MRIs can raise questions regarding legal standards for investments of charitable assets.

Washington's Uniform Prudent Management of Institutional Funds Act (UPMIFA), enacted in 2009, generally requires managers of charitable assets to act prudently in making investment decisions, taking into account risk and return objectives. A foundation's below-market loans to small businesses in order to spur job creation may not satisfy this prudent investor standard.

The good news is that there is a special exception to the general prudent investor rule for "program-related assets," i.e., assets held primarily to accomplish the organization's charitable purpose, and not primarily for investment. Any organization that relies on this exception should document carefully that the primary reason for the investment is to accomplish a charitable purpose.

The terminology surrounding MRIs can be confusing. Some observers use the term "program related investment" (PRI) interchangeably with MRI. Others, such as PRI Makers Network, a Seattle-based national network of organizations that use investments to achieve charitable goals, use the term to describe an MRI that is expected to produce a below-market rate of return.

PRI has a more technical definition for legal purposes. Charitable organizations that are classified as "private foundations" under federal tax law are required to expend at least 5 percent of their asset value annually to further charitable purposes. Investments that meet the tax law definition of a PRI under the private foundation rules count toward this 5 percent payout requirement. To qualify as a PRI, an investment must be made primarily to accomplish charitable purposes, rather than to achieve a rate of return, and must meet certain other stringent requirements as well. These technical rules apply only to private foundations and not to other charitable organizations.

By any name, MRIs can be an effective strategy to align a charity's actions more fully with its mission and to achieve greater impact with limited charitable resources.

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