

Association of Small Foundations

PRI Makers Network

San Diego Grantmakers

Foundation Mission Investing

April 3, 2008

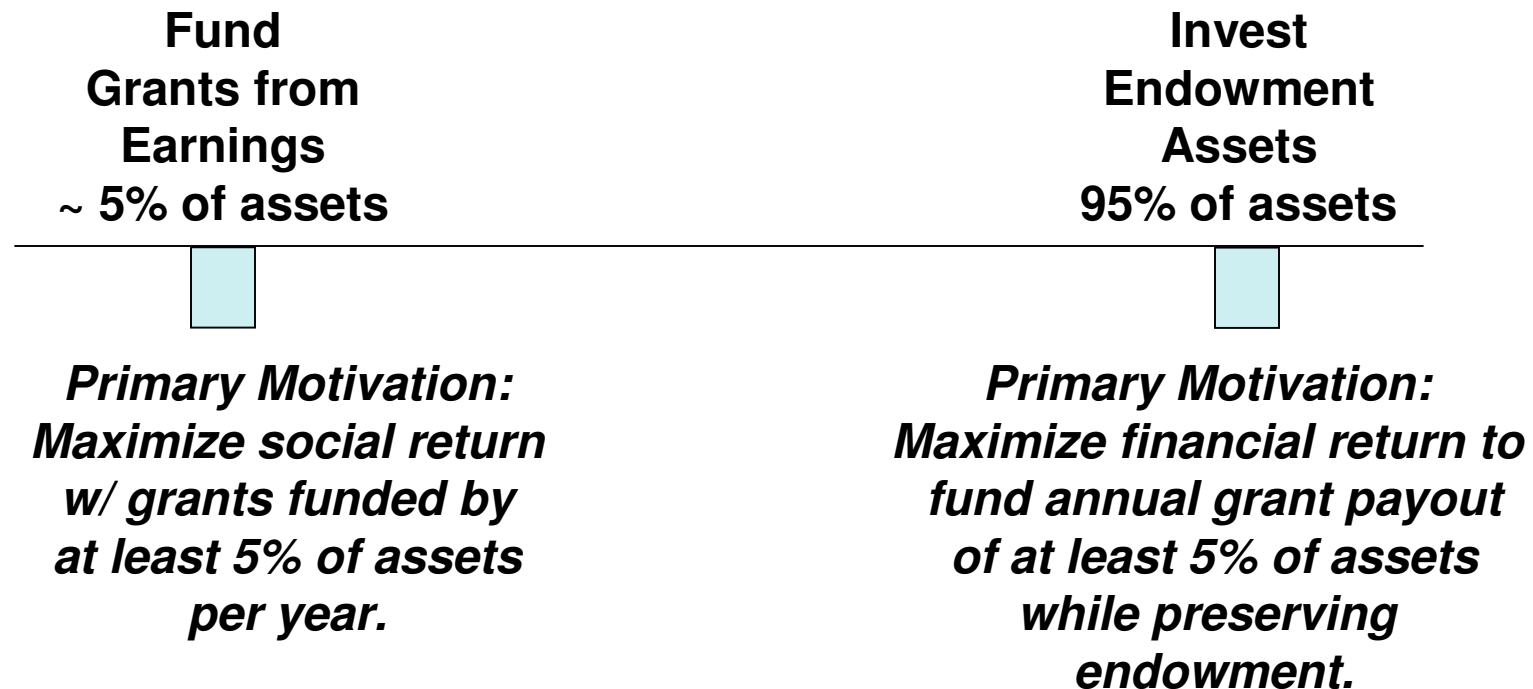
Lisa Richter, GPS Capital Partners

www.gps.capitalpartners.com

Outline

- **Foundation Mission Investing**
 - Motivation, Context, Definitions
 - Mission Investing Marketplace
- **Success Factors, Leverage, Partnership**
- **Next Steps**

Mission Investing Motivation: Conventional Philanthropic Investing Continuum



Mission Investing Motivation

- **Challenges:**

- Charitable needs/opportunities vastly outstrip grant resources.
- Limited capital sources and structures to drive nonprofit and other social enterprise growth and impact.
- Limited engagement of market energy and discipline.

- **Mission Investing Opportunity:**

- Extend foundation resources, respond to current needs/opportunity.
- Add new funding structures, leveraging market forces and driving different, greater, accelerated impact.
- Increase and stabilize philanthropic distributions over time.

Mission Investing Timeline

- **1790: Ben Franklin Trust lent to tradesmen--all races, married**
 - With strong repayment, \$300k grew to \$5MM by 1990s
- **~ 1970: Ford, Taconic Foundation PRIs (1968)**
 - PRI defined in Tax Code of 1969
 - “Socially Responsible Investing” (SRI) movement:
 - Screening of perceived evils (South African disinvestment)
 - Shareholder activism (Sullivan, Ceres principles)
 - “Alternative,” “community,” “proactive” investing
 - 1977 Federal Community Reinvestment Act for banks
- **2008 Mission Investing Lexicon** (only PRI defined in regs):
 - **SRI/SI**: investments w/social criteria
 - **MI**: foundation investments supporting mission
 - **PRI**: concessionary risk-adjusted return; can be payout
 - **MRI**: market / near market return; endowment assets
 - **CRA**: lending, investing, service in all Assessment Areas, including those that are low- to moderate-income (LMI)

Legal Perspective: Definition of PRI¹

- **The primary purpose** of the investment is to accomplish one or more of the charitable, religious, scientific, literary, educational and other exempt purposes described in section 170(c)(2)(B) of the Code;
- **No significant purpose** of the investment is the production of income or the appreciation of property; and
- **No purpose of the investment** is to lobby, support or oppose candidates for public office or to accomplish any of the other political purposes forbidden to private foundations by section 170(c)(2)(D) of the Code.

¹ Source: Tax Reform Act of 1969.

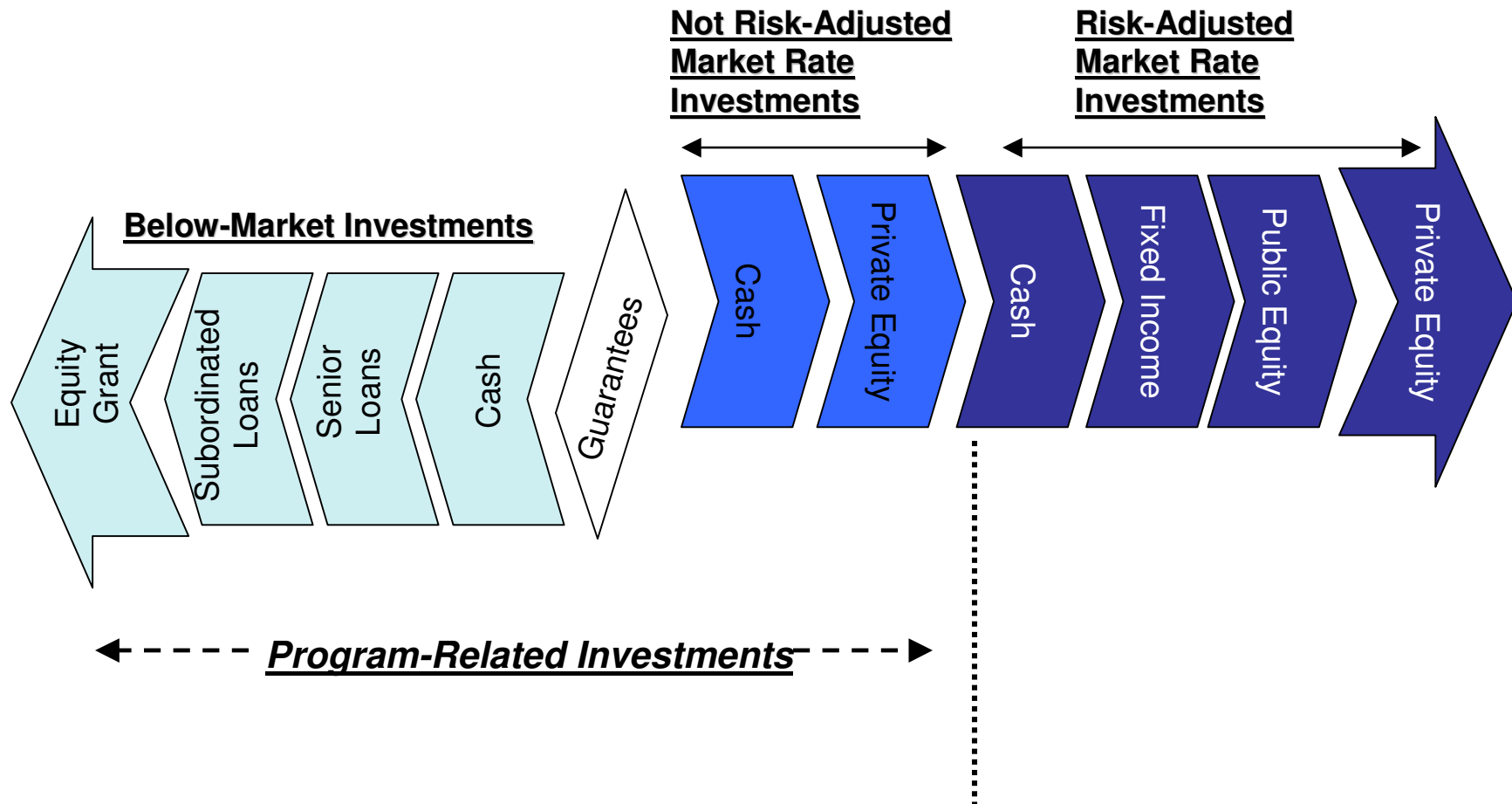
PRI Accounting

- PRI can be counted as part of 5% distribution in year that it is made.
- Asset value of PRI not included in Foundation's asset base and distribution requirement calculation during time PRI is outstanding.
- Income on PRI adds to general revenue.
- In year PRI matures, entire balance is treated as a "negative distribution" and is recycled into new grants or PRIs.
- A defaulted PRI (rare occurrence) becomes a grant.

Mission Investing Context: New Philanthropic Investing Continuum

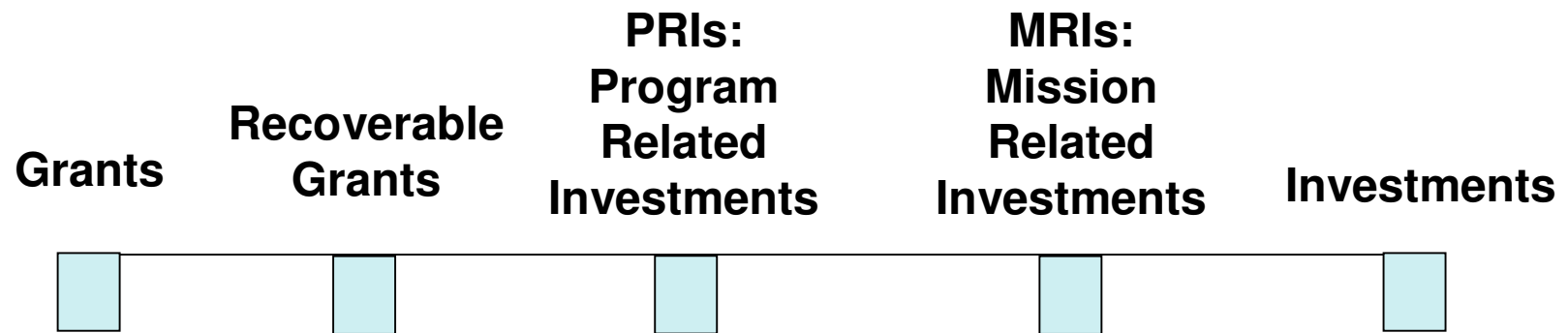
- **Proactive investments: range of “asset classes”—debt, equity, real estate, loan guarantees, deposits, structured as:**
 - **Program-Related Investments (PRIs):** concessionary risk-adjusted financial return; can be counted as part of private foundation’s distribution requirement, or
 - **Mission-Related Investments (MRIs):** from the endowment; provides sufficient risk-adjusted financial return to fulfill foundation’s fiduciary responsibility to preserve endowment and avoid “jeopardizing investments.”
- **Example: The F.B. Heron Foundation** invests 25% of assets to support mission: 7% PRI + 18% MRI (in addition to grants).
- **Example: Casey, Heron and Meyer Foundations** challenging foundations to dedicate 2% of assets--\$10 billion over 5 years--to mission investing.

Mission Investing Continuum



Adapted with permission from F.B. Heron Foundation's "New Frontiers in Mission-Related Investing"

Mission Investing Context: New Philanthropic Investing Continuum



***Primary Motivation:
Social Return***

***Primary Motivation:
Financial Return.***
*Foundation may screen
endowment assets and/or
vote proxies on holdings for
mission alignment.*

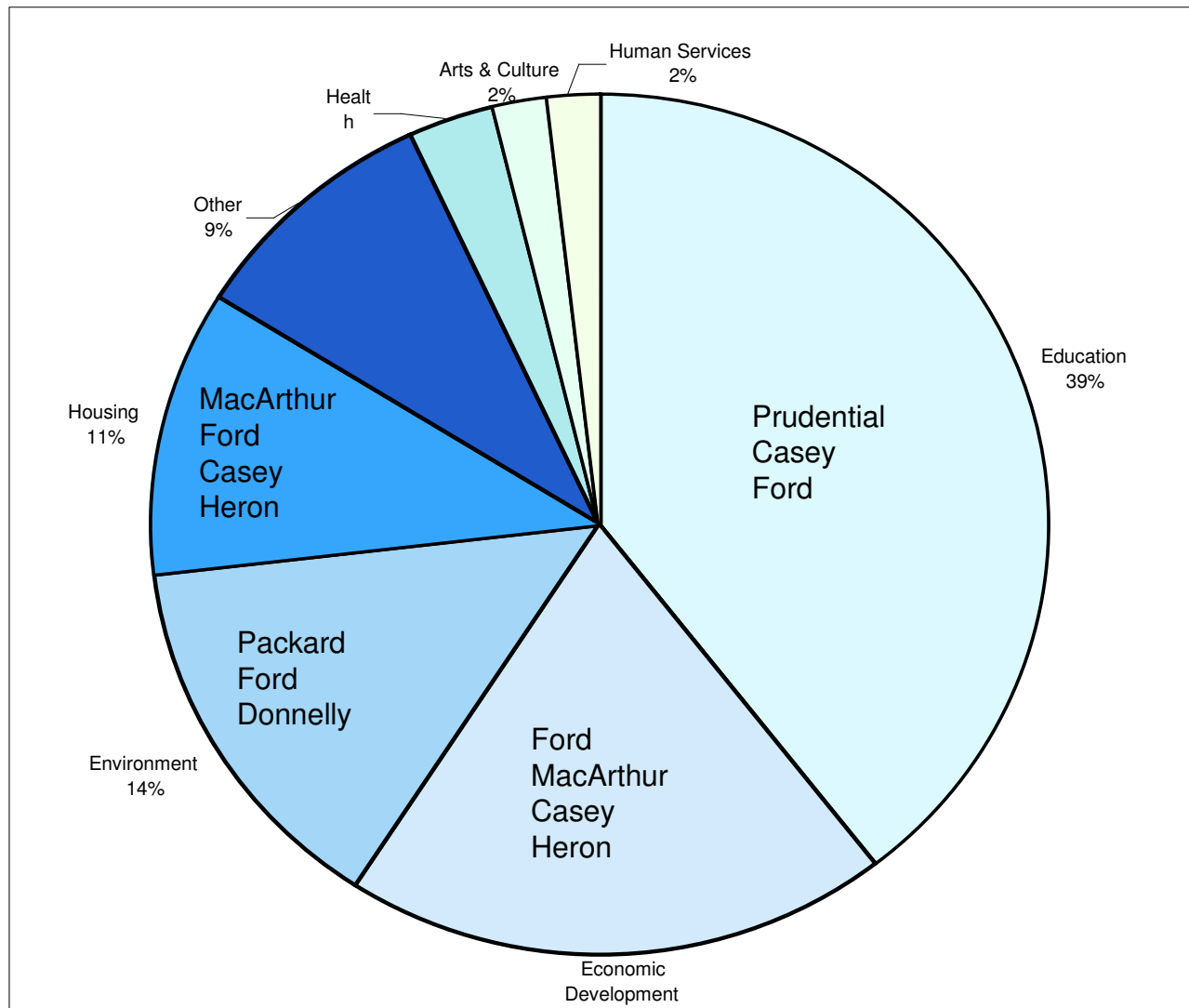
Mission Investing Marketplace: Supply

- **Significant unrealized potential, despite track record:²**
 - 92 foundations, 40 years, \$2.3 billion--85% PRIs:
 - 96% repayment on debt, correcting for outliers; 75% w/ 0% default.
- **Market at an inflection point:**
 - \$100 - 160 million annual mission investment (< 0.03% assets).
 - 16.2% annual volume growth last 5 years v. 2.9% prior 32 years.
 - Use of intermediaries increasing; 25% of dollars in 2001 - 2005.
 - Historically, four leading PRI funders in four program areas:
 - Ford, MacArthur, Packard, Anonymous in Economic Development, Housing, Environment, Education.
 - Today, 44% of new volume from smaller foundations.
 - Every PRI investor has different profile based on mission, geography, risk/return appetite, experience; some invest endowment assets.

² FSG Social Impact Advisors, 2007.

Mission Investing Marketplace: Supply

Mission Investing 2001 - 2005



Mission Investing Marketplace: PRI Supply 2000 – 2001

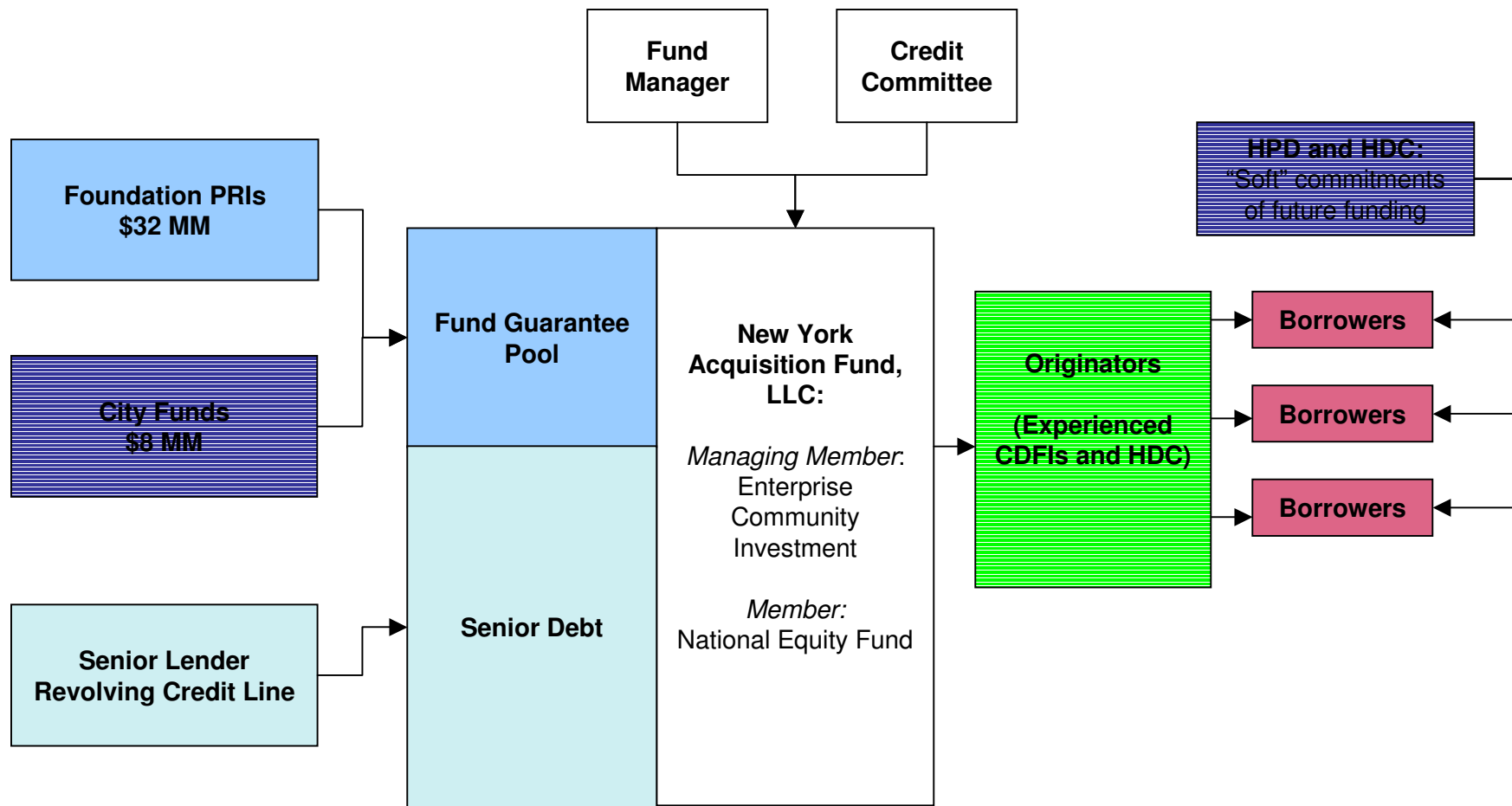
PRI Amounts	#	%	\$_(000s)	%
\$10 million +	2	0.3	24,911	7.1
\$5 – \$10 million	8	1.2	51,225	14.6
\$1 – \$5 million	96	14.9	176,747	50.3
\$500,000 – \$1 million	61	9.4	36,567	10.4
\$100,000 – \$500,000	233	36.1	52,491	14.9
\$50,000 – 100,000	95	14.7	5,795	1.6
\$25,000 – \$50,000	76	11.8	2,549	0.7
\$10,000 – \$25,000	75	11.6	1,199	0.3
Total	646	100.0	351,484	100.0

Source: Foundation Center, 2003

PRI Marketplace: Demand/Opportunity

Program Area	PRI Investee	Foundation Investors
Community Development	LISC, Enterprise, ShoreBank, IFF, NFF, Bridge Housing, Market Creek Plaza, Cleveland Theaters	Ford, MacArthur, Heron, Cleveland
Education	IFF, Indianapolis Charter School Credit Enhancement Fund, Council for Adult & Experiential Learning, Greater Newark Charter School, Howard U. Press	Prudential, Casey, Ford, MacArthur,
Healthcare	NCB Capital impact, NFF, Community Health Facilities Fund, Working Today, West Alabama Health Services Inc., AIDS Housing of Washington	RWJ, Ford
Human Services	IFF, LIIF, NFF, ShoreBank, Eliza Bryant Center (eldercare), Pioneer Human Services	RWJ, Ford, Rockefeller
Environment	Trust for Public Land, Sea Change Fund, Enterprise Green Building, Wetlands Initiative, Lyme Timber LLC	Packard, Donnelly, Gund, Ford
Arts, Culture	NFF, Boston Community Capital, Children's Museum of Los Angeles	California Community, Ford, Heron

PRI Leveraging Banks in Affordable Housing: NYC Affordable Housing Acquisition Loan Fund



PRI for Green Affordable Housing: Bridge Housing (San Francisco)

- **Using PRIs, Bridge develops Green affordable rental and homeownership units:**
 - The 83-unit Arnett Watson Apartments in the Tenderloin District features:
 - An Energy Star roof
 - Drought-resistant trees
 - Attractive architecture design that blends with the surrounding community.
 - Close proximity to several metropolitan transportation hubs.
- **Ford, MacArthur, Heron PRIs to Bridge have terms of 5 to 10 years, rates of 1 - 4% and use of proceeds including predevelopment.**

PRI in the Conservation Economy: Organic Dairy Financing - ShoreBank Pacific

- **Using PRI debt, the nonprofit loan fund ShoreBank Enterprise Cascadia finances Tom and Diana Brown to:**
 - Adapt organic farming practices
 - Build seventy-five percent of their farm buildings--with reclaimed lumber.
 - Host tours for local school children and share ideas with other farm families in Oregon's Coquille Valley.
- **Ford, Heron, Meyer PRIs have terms of 5 - 10 years, rates of 1% - 4.25% and use of proceeds to finance green businesses and housing.**

Mission Investing Success Factors : Strategic Benefits

Foundation	Impact (different type of Growth Capital), Recyclable, Size, Leverage, Payout, Partnership, Learning
Investee	Capacity/Leverage, Managerial Discipline, Sustainability, Credibility, Partnership
Society/ Market	Market Development (catalyst for innovation), Policy Catalyst, Efficient Use of Charitable Resources, Accountability in Social Sector, Sustainable Organizations

Mission Investing Success Factors: Leverage

- **Mission investing leverages foundation assets and influence, giving seat at table with institutional partners:**
 - Banks fulfilling CRA requirements
 - Credit unions demonstrating sensitivity to LMI communities
 - Community Development Financial Institutions (CDFI intermediaries) with underserved place- or population-based financing strategies
 - Governments supporting economic development
 - Insurance companies demonstrating public interest
 - Corporations delivering Corporate Social Responsibility
 - Pension funds investing in beneficiary communities
 - Faith-based investors for systems change to address needs of poor
- **Foundations can take the long view to benefit all community residents and stakeholders.**

Mission Investing Success Factors: Partners

Example:

Bank Partnerships

Why:

- Partnerships are key to leverage
- With banks, goals in common with CRA activities
- Nonprofits = growing bank target market
- Market knowledge exchange between banks / foundations yields deal flow and better risk management
- Syndicate / Due Diligence Partners

How:

PRIs or MRIs (in addition to grants):

- Guarantees
- Subordinated Debt in Participations or Funds
- Deposits / CDARS for over \$100,000 in Banks
- Equity investment in screened banks
- Grant support for Financial Education

CDFI and government partnerships can increase leverage, as in NYC Housing Acquisition Fund.

Next Steps

- **Propose:**
 - Continue dialogue to set stage for foundation - bank - other institutional investor - CDFI - community organization - government partnerships
 - Plan future networking events
 - Track results
- **For further information:**
 - www.smallfoundations.org
 - www.primakers.net
 - www.sdgranmakers.org
 - www.aecf.org
 - www.heronfdn.org
 - www.mmt.org
 - www.jacobscenter.org
 - www.cdfifund.gov
 - www.gpscicapitalpartners.com