

Impact Investing through Donor Advised Funds at Community Foundations

Assessing Feasibility

Kathy Merchant & Amy Cheney, The Greater Cincinnati Foundation
Taylor Jordan, Imprint Capital

This webinar is part of a project to develop an impact investment toolkit for community foundations funded by The Rockefeller Foundation

Outline of Today's Webinar

- Background on Rockefeller Foundation-funded community foundation impact investment project
- Recap of Webinar #1: models and approaches for community foundations and donor-advised funds
- Options for donors to participate in impact investment programs
- Greater Cincinnati Case Study: Step-by-step process for assessing the feasibility of engaging donors in impact investing
- Next steps: Webinar #3 (program design and structure) and Webinar #4 (toolkit for community foundations)

Background

- **Objective:** Develop by February 2012 a toolkit for community foundations to include their Donor Advised Funds in Impact Investments
 - Grounded in practice and oriented around tools and experiences
 - Rooted in diverse context of multiple institutions
- **Process:** Work with up to five community foundations to develop toolkit
 - Quarterly update webinars to share lessons, get feedback, and leverage capacity and partnerships
 - Broader strategy to roll-out tool kit and support for community foundations at conclusion of the project

Impact Investment Toolkit

- Provide content for donor focus groups
 - ▣ Impact investment primers and deal examples
 - ▣ Presentation and “term sheets” on structural options
- Provide tools and templates
 - ▣ Investment Policy Statement
 - ▣ Program description and marketing material templates
 - ▣ Investment committee job description
- Provide ongoing technical assistance

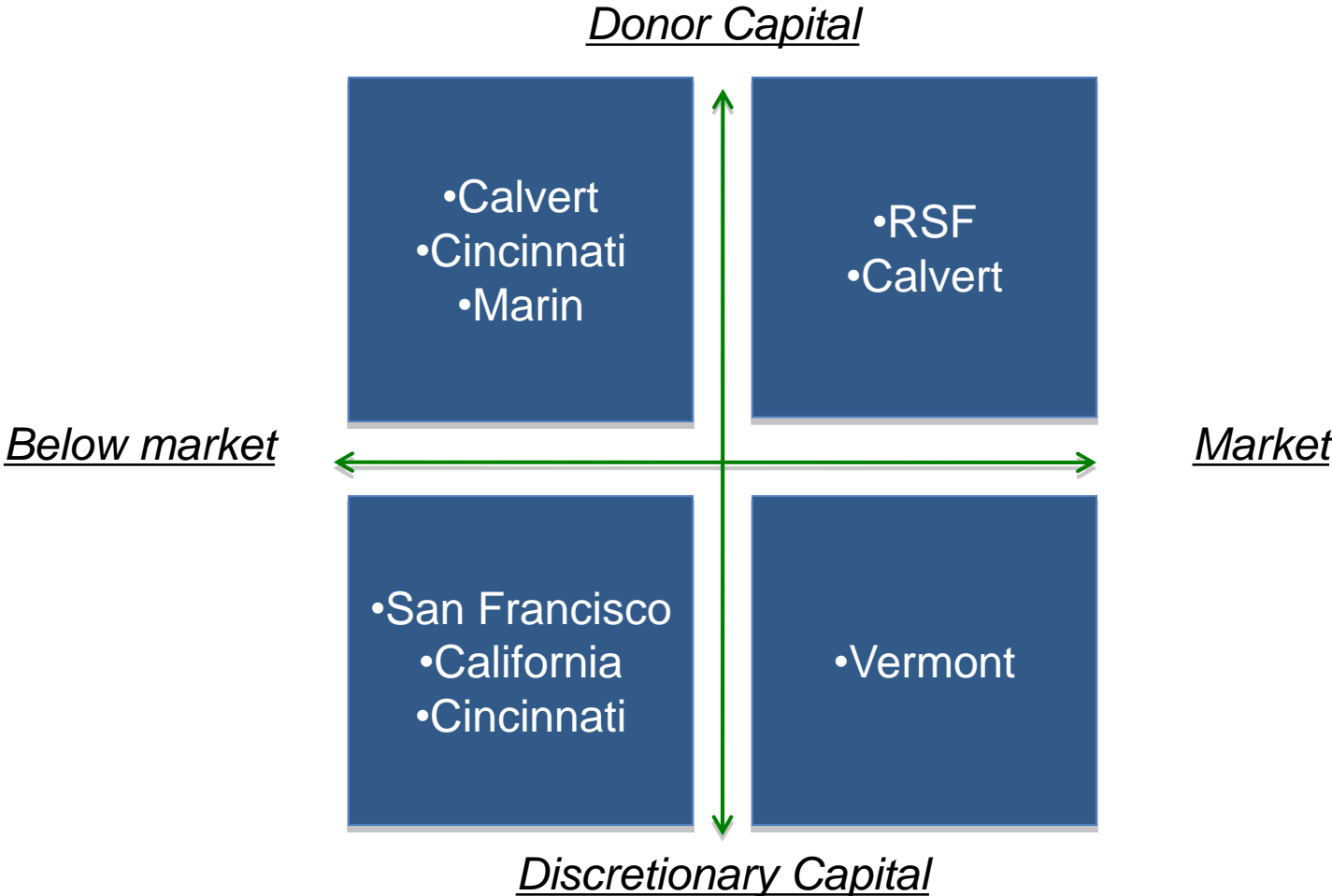
Review: What is Impact Investing?

- Use of investment capital to address social and/or environmental challenges while achieving a financial return
- Span a broad range of structures and approaches
 - ▣ Asset classes: From cash to venture capital
 - ▣ Geographies: From local to global
 - ▣ Return profiles: From below market rate to market rate
 - ▣ Structures: From funds & intermediaries to direct transactions

Why Impact Investing and Community Foundations?

- Beyond grants: tools to deploy foundation assets
- Leverage scarce resources: recycle investment capital vs. grants and catalyze additional investment
- Greater community impact in multiple sectors
- Donor demand – more entrepreneurial and investment-minded donors; generational shift
- Competitive positioning vs. commercial DAF providers
- Broader trend advancing practice of impact investing

Impact Investment Models





Donor Participation Options

Potential Options for Participation

1. Grant into an evergreen impact investment fund
2. Create a separate impact investment pool (investment proceeds are recycled into DAF)
3. Integrate into existing investment pool
4. Co-invest DAF on an opt-in basis into specific impact investments
5. Invest non DAF, private money into impact investment fund managed by foundation

Option 1: Grant into Fund

- *Contribute directly to foundation's Impact Investment Fund*
 - ▣ Donors' grants are pooled with foundation's capital
 - ▣ Investment returns flow back to fund to make additional investments

- *Advantage:* Increases pool of funds available for impact investments

- *Disadvantage:* Funds are not recycled back to donors, may affect interest

Option 2: Separate Investment Pool

- *A separate, mission focused pool is established for DAFs*
 - ▣ Impact investment option in which DAFs invest prior to making grants
- *Advantage:* Establishes a distinctive and separate investment option given unique mission objectives
- *Disadvantage:* Potentially necessitates a more complex administrative structure and more active management of liquidity and cash flows

Option 3: Integrated Investment Pool

- *Integrate impact investments into existing investment pool*
 - ▣ Allocate percentage of pool to impact investments
- *Advantage:* Seamless option that requires the least amount of donor education and effort
- *Disadvantage:* May constrain options to market rate “mission related” opportunities, difficult to make below-market rate investments into market rate pool

Option 4: Deal by Deal

- *Donors opt in and participate in impact investments on a deal-by-deal basis*
 - ▣ Funds could be transferred from existing DAFs or new donor sources
- *Advantage:* offers donors control and flexibility to pick and choose among investments based on their preferences
- *Disadvantage:* more cumbersome to manage investments when having to rely on uncertain levels of donor participation

Option 5: Investment Fund

- *Separate fund managed by foundation*
 - Establish charitable vehicle to manage pool of impact investments from donors and other entities
- **Advantage:** Positions the Foundation as a wholesale intermediary and manager of impact investments; potential to attract capital from other funders into target communities
- **Challenge:** May be difficult to raise funds from donors and be duplicative of local intermediaries



Greater Cincinnati Case Study

Assessing GCF Donor Demand

1. Identify donors and prospects for focus group
2. Test program strategy elements
 - a) Explain the concept
 - b) Test options for participation
 - c) Use concrete investment examples to elicit reactions
 - d) Ask a series of targeted questions
 - e) Narrow down structuring options
3. Board decision: go/no go

Demand-Testing Questions

- Would an impact investment be an attractive philanthropic tool for DAFs?
- For what purposes would you like to see impact investments used?
- How much would you be willing to allocate for a DAF impact investment?
- What level of financial return would you seek to achieve?
- Would you be comfortable with investment decisions being made by the community foundation's governance process?

Two Options Emerged From Focus Group

1. Donors co-invest with GCF on an opt-in basis into specific impact investment transactions
 - *Almost universally top choice because it gives donors greatest control*
2. Provide impact investments as an investment option for existing or new DAF assets
 - ✓ *Almost universally considered to be best option paired with #1 because it could use existing donor assets as a starting point*
 - ✓ *Donors would have a third investment option for their assets*

Perceived Risks & Mitigants

Risks

Reputation

- Investments are unsuccessful or poorly underwritten

Insufficient investable deals

- Geographic concentration increases risk
- Investments likely to be high risk relative to level of financial return
- Investments will be illiquid

Mitigant

Execute

- Focus on “early wins”
- Expand Impact Investment Committee with relevant capabilities

Proactively source opportunities

- Actively source deals with local investors
- Provide clear & transparent communication
- Cap percentage of donor assets allocable to impact investments

Donor Recommendations to GCF

1. Proceed incrementally, initially using GCF's discretionary funds.
2. Offer participation into existing deals and bring in donors' funds on a deal by deal basis to reduce the foundation's own capital into each deal
3. Target donors who are most likely to participate and who have disproportionate influence on other donors
4. Set up a GCF Impact Investment Fund to hold the foundation's and donors impact investments (back office function)
5. Focus on the most financially viable investments to build as many exemplars of success as possible
6. Be clear and transparent about financial risk, illiquidity and need to cap the percentage of donor assets allocable to impact investments

Donor Recommendations to GCF

7. Build out organizational complexity to accommodate non-donors AFTER you have traction with donors
8. Use as light and simple an organizational rubric as possible
9. Build out execution capacity
10. Establish a dedicated Impact Investment Committee:
 - ❑ Recommend at least 5 members
 - ❑ Populate with relevant skill sets, ideally drawn from potential or existing donor networks: venture capital; lending; corporate; entrepreneurial
11. Develop clear investment criteria and process

Next Steps

1. Include an opportunity for donors to participate in four existing GCF impact investments at par
2. Expand impact investment committee
3. Market impact investment offerings to GCF donors
4. Revise GCF's processes and procedures for making and structuring impact investments
5. Set up GCF Impact Investment Fund to hold GCF's and donors' impact investments
6. Begin to identify 2 - 3 new impact investments under the revised procedures
7. Implement donor advised impact investment offering when an investable deal opportunity is identified by GCF

Board Decision: Go/No Go

Decision criteria:

- Donor demand
- Pipeline of investible deals
- Fees to cover the community foundation's expenses
- Efficiency in deploying capital flexibly
- Risk management
- Accounting
- Reporting on financial and social returns

Board Decision: Go/No Go

Present program design:

1. Define preferred program strategy elements
2. Provide sample term sheet
3. Identify governance mechanisms
 - a) Expenditure authority and fee structure
 - b) Structures for assessing social and financial return
 - c) Decision-making authority
4. Identify pipeline of investible opportunities
5. Identify potential donors
6. Outline next steps: policies and procedures, term sheets, marketing materials



It's a "Go"!

(December 2010)

Next Learning Opportunity!

Please join us in San Francisco
at the Fall Conference for Community Foundations

Monday, September 19, 2011

4:30 – 6:00 pm

“Impact Investment:
Deepening Impact and Donor Engagement”

Contact

Kathy Merchant, Greater Cincinnati Foundation
merchantk@gcfdn.org

Amy Cheney, Greater Cincinnati Foundation
cheneya@gcfdn.org

Taylor Jordan, Imprint Capital
taylor@imprintcap.com