Program-Related Investments:
Financing Opportunities for Water Quality Projects in the Chesapeake Bay Watershed

Chesapeake Bay Funders Network, USDA Conservation Innovation Grant, EPA, National Fish & Wildlife Foundation

August 5, 2013

I. Introduction

EFC investigated private philanthropic program related investment (PRI) as a financing option for projects that promote water quality improvement initiatives within the Chesapeake Bay, such as manure-to-energy. The investigation occurred through a series of interviews with various philanthropic organizations to better quantify the opportunities associated with PRI funding. A list of interview questions was developed to provide essential information for establishing this portfolio option for Chesapeake Bay funding organizations along with a strategy to engage these groups. Foundations chosen for interview included entities located both within the Chesapeake Bay Region and those operating on an international scale.

During each interview, EFC explored the role the foundation's PRI plays in the overall investment portfolio, the motivation behind creating this type of investment as an option, and the opportunities and barriers in establishing the PRI fund. The questions focused on how risk is minimized in creating and operating the PRI. This paper includes a summary of findings, background information on the terminology of PRI funding, and overviews of interviews conducted. Key trends and commonalities have been described in the summary, and recommendations have been made as to how these findings can be applied to water quality projects within the Chesapeake Bay region.

II. What are PRIs?

A History of PRIs

Program-related investing was pioneered in 1968 by the Ford Foundation in order to create an alternative to traditional grantmaking[1]. Ford Foundation sought to increase the extent of its social investing while maintaining a consistent pool of capital from which to draw. PRIs offered a creative combination: the low-cost ready access to financing that grants offer to recipients, and the greater return on investment that traditional loans offer to lending institutions.

In the following decades, several other foundations established PRI funds but many did not meet with the same success, and ultimately, interest in PRIs waned[2]. Although thousands of foundations exist, it is estimated that fewer than 10% currently include a PRI option[3]. There has been a recent renewed interest; however, as organizations seek to leverage capital and lower the risk of funding startups and

[1] Program-Related Investment, The Ford Foundation, http://www.fordfoundation.org/grants/program-related-investment

[2] Representative of the Annie E. Casey Foundation, Personal interview, 15 Mar. 2013

[3] Knowledge Base: What is a Program-Related Investment? The Foundation Center, http://grantspace.org/Tools/Knowledge-Base/Grantmakers/PRIs

charitable causes. Creative financing options are needed more now in the face of an uncertain global economy and increasingly limited budgets.

More widespread resources and information on PRIs have contributed to greater rates of success in the past decade than previous efforts. By providing a crucial intermediate financing step, PRI funding has great potential to quickly transition pilot innovative projects, such as manure-to-energy technology, from purely grant-based support to being sustained in the private market.

PRI Requirements and Structures

The Internal Revenue Service (IRS) has set legal requirements to qualify an investment as a PRI. The IRS code is nuanced and complex concerning PRIs, but there are a few key requirements. The investment's primary purpose must be to advance the foundation's charitable objectives. Neither the production of income nor appreciation of property can be a significant purpose. The funds cannot be used directly or indirectly to lobby or for political purposes. The IRS provides several examples of qualifying investments for guidance[4].

PRIs can take many possible forms, e.g. an equity investment, a low-interest loan, a zero-interest loan, a loan guarantee, a line of credit, an asset purchase, or a recoverable grant. However, the most common structure is the low-interest or zero-interest loan, often lent by the foundation through an intermediary[5]. For additional information on financial intermediaries see Appendix 1.

Most PRIs comprise a small portion of a foundation's larger grant-making portfolio, which includes traditional grant making and broader mission-related investments[6]. (Mission-related investments lack the legal definitions and requirements associated with PRIs but in general have both a social mission and a financial return for institutions[7].) The majority of existing PRIs are targeted at community development and affordable housing, although several exist that are specifically dedicated to advancing environmental causes such as promoting clean energy and reducing agricultural nutrient runoff.

III. Interview Summary of Findings

Background Information on Interviews

Interviews with representatives of the following foundations were conducted:

1. February 13, 2013: The Ford Foundation
2. February 13, 2013: The Rockefeller Foundation
3. March 15, 2013: The Annie E. Casey Foundation
4. March 22, 2013: The Bill and Melinda Gates Foundation

For complete summaries of these interviews, see Appendix 2.

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[4] Examples of program-related investments by private foundations, U. S. Department of the Treasury, Internal Revenue Service, http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Examples-of-Program-Related-Investments-by-Private-Foundations-%E2%80%93-Proposed-Regulations

[5] Lawrence, Steven, Doing Good with Foundation Assets: An Updated Look at Program Investments, The Foundation Center, http://foundationcenter.org/gainknowledge/research/pdf/pri_directory_excerpt.pdf

[6] Answers to Some Frequently Asked Questions About PRIs, The Ford Foundation, http://www.tgci.com/magazine/Answers%20to%20Some%20Frequently%20Asked%20Questions%20About%20PRIs.pdf

[7] Mission-related Investments (MRIs). Mission Investors Exchange, https://www.missioninvestors.org/mission-investing/mission-related-investments-mris

For a list of questions that were used as a guideline for these interviews, see Appendix 3.

PRI Structural Details
The PRI structure was fairly consistent among the foundations that were interviewed. Because collected information quickly became redundant, the number of foundation interviews was lower than originally anticipated. This consistency across PRI structuring is possibly due to the strong network of shared information that many foundations have created in order to increase the modern success of PRI investing that was lacking in the earliest days of PRI making.

The standard investment for the Ford Foundation is a 10-year low-interest loan with the principal paid in the last 2 to 3 years of the loan term. Both equity investments and low interest loans are made for PRI investments.

The Annie E. Casey Foundation recommends a minimum of $500,000 and a maximum of $1-2 Million per investment in order to reap the benefits of the PRI structure, because it is more resource intensive than traditional grant making. The Annie E. Casey Foundation is willing, in theory, to take losses through PRIs, but alternatively there is pressure in their overall portfolio strategy to make up for grant losses through PRI making[2]. The Gates Foundation's typical PRI investment is between $5-20 Million, making this foundation an uncommon example of "mega investing."[8]

Each new PRI transaction made by the Rockefeller Foundation is in the $1-3 Million range. The Rockefeller Foundation maintains a "risk-neutral" approach in their PRI-making strategy, thereby seeking no net loss[9].

An Example of the PRI Investing Process: The Annie E. Casey Foundation[2]
The Annie E. Casey Foundation described their standard process of making a PRI investment from inception to transfer of funds. More than a dozen of the foundation's employees are brought into the process, including representatives from each investment unit. This interactive approach fosters a sharing of expertise and information to improve the foundation's PRI making ability, and creates a heightened awareness of PRIs within the organization.

In the first step, the written request for a PRI is received by the foundation. The Director of Social Investments prepares an investment summary for review. Upon review, due diligence is performed and a site visit is conducted to gather additional information on the prospective recipient. All information is reviewed to determine whether the recipient provides the desired return on investment and aligns with the foundation's mission. Finally, the investment is formally recommended to the Chief Information officer (CIO) to approve, although the CIO is kept informed throughout the process and may halt the investigation at any time. The total turnaround time for these steps is typically 3 months if the recipient already has a grant history with the foundation, and 9 months if there is no previous transaction history. Typically, the foundation provides to the grantee both the PRI funding and the assistance of a third-party legal manager.

In addition to PRI making by a single foundation, multiple foundations may pool capital and share the costs of underwriting and managing the investment. A single investment is made to a recipient and the

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[8] Representative of the Bill and Melinda Gates Foundation, Personal interview, 22 Mar. 2013
[9] Representative of the Rockefeller Foundation, Personal interview, 22 Feb. 2013

association of foundations outsources management to a created LLC special purpose entity. This solution further enhances the increased leverage of capital that PRIs offer.

Pros and Cons of PRIs

The major benefit for the recipient is access to capital at market rates that are lower than what may otherwise be available. Additionally, recipients may lack the structural requirements or credit history required to qualify for market-rate loans, so that a PRI may be the only source of funding available. For the donor, the primary benefit is the ability to maintain a constant pool of funds to fund future projects in the long-term, as opposed to a gradually draining pool of grant funding. In this way, foundations may ensure that even in difficult economic years, programs can continue to operate and new projects can be funded[10].

It is typical for foundations to integrate a PRI fund into a larger portfolio of grants and mission-related investments, so that PRIs serve as another tool in the foundation's overall investment strategy. They offer a highly flexible alternative to other types of funding, in that they can be extensively tailored to meet the needs of the recipient. This flexibility increases the chance of success for repayment of the funds and the success of the funded project, in comparison to a project funded by a grant. Although all investees strive for success, their determination is even more so if a loan must be paid back to the donor[9].

Although the more interconnected relationship between foundation and recipient increases the likelihood of financial return and a successful project, it also creates additional challenges for the foundation. Because the fund is a loan, there is added operational intensity. A repayment plan must be established and monitored by financial staff, necessitating additional supervision by foundation staff, possibly the hiring of additional staff, and often a third-party to outsource fund management. PRIs are designed to be a flexible and innovative type of funding, but typically, the more innovative the PRI is, the more time is spent in managing its details[9].

If several foundations work together to invest in a single recipient, as previously described, the complexity of the undertaking can potentially be even greater, as foundations work to coordinate their efforts, share information, avoid redundancy and duplication of efforts, and fulfill each individual foundation's mission[2].

Advice Provided By Foundations

The Ford Foundation strongly recommends contacting the Mission Investors Exchange to obtain additional information and tools. They have furthermore offered to assist the Chesapeake Bay region foundations and funding organizations in setting up PRIs[11].

The Annie E. Casey Foundation collaborates with other foundations to leverage capital, an essential component of maximizing success. This is especially helpful for smaller foundations that do not have the team of experts available to manage this type of fund. However, they note that this strategy is challenging for various reasons. In their experience, each foundation has a different strategy in achieving its mission, and unneeded information is given to each foundation to satisfy the requirements of the other group members. Nevertheless, this collective approach is highly recommended based on a past

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[10] Joseph, James P., and Andras Kosaras, "New Strategies for Leveraging Foundation Assets," Taxation of Exempts, http://www.arnoldporter.com/resources/documents/TaxationOfExempts_Article_Jul-Aug08_2.pdf

[11] Representative of the Ford Foundation, Personal interview, 22 Feb. 2013

experience in which Casey Foundation and other foundations were all working with one recipient on an individual basis; the process was an inefficient use of everyone's time and it was discovered that the recipient was playing the foundations off each other. Because of additional informational resources available to foundations, PRIs are less likely to fail now as they did in the 1960s when they were first pioneered[2].

They further recommend that foundations that are new to PRI investing begin slowly with small investments and gradually increase their scale. Additionally, they advise foundations to ensure that they have strong confidence in their organization's expertise, and that they create realistic financial models and goals[2].

The Rockefeller Foundation emphasizes that having leadership, such as a Board, that buys into the concept of PRI investing is critical for foundations when starting up a fund. They further recommend the creation of an overall PRI making strategy, and the hiring of staff with both the financial skills and social insight necessary to most successfully manage PRI investments[9].

The Bill and Melinda Gates Foundation advises that intermediaries are a necessity, as well as a committee formed specifically to review and approve each PRI. Finally, each project and company that is invested in as part of the PRI must have full commitment and support for the life of the PRI to ensure success[8].

IV. How Can PRIs Be Utilized By Water Quality Improvement Projects?

To advance the financing of water quality improvement projects such as manure-to-energy in the Chesapeake Bay region, the specific technical questions and financial scenarios that a particular project entails must be considered when determining how to establish a supporting PRI fund. A number of resources exist that are able to assist in addressing these specific challenges. PRI-making foundations have a strong national network and share advice freely with each other and with the public to enhance the efforts of everyone involved. They are an extremely helpful source of guidance and, in the EFC's experience, are very generous with their time and with advising in the details of PRI management.

The Mission Investors Exchange is an organization created for philanthropic innovators to exchange ideas, tools, and experiences to increase the impact of their capital. The organization also helps beginner and advanced foundations set up PRIs and MRIs. The Exchange has more than 200 member foundations and mission investing organizations.

Confluence Philanthropy is a non-profit network of over 175 private, public, and community foundations. They build capacity and provide technical assistance to enhance the ability of foundations to align the management of assets with organizational mission to promote environmental sustainability and social justice. It is a recognized affinity group of the Council on Foundations that is supported by their members.

In addition, each of the major foundations interviewed posts details of their investment portfolio online including information on their own PRI investments. Each foundation has also developed helpful guidance documents, brochures, and fact sheets for frequently asked questions available online for the public. Information is also shared during forums and informational workshops hosted by these networks throughout the year. These resources are an excellent starting point for any project manager who is considering establishing a PRI financing option as part of their existing financing portfolio. Program-related investments are a much needed innovative financial tool for pioneering projects attempting to succeed with limited resources. EFC strongly recommends that this option be explored as a funding strategy for water quality improvement initiatives in the Chesapeake Bay region.

Appendix 1: Intermediaries

What are financial intermediaries?
Financial intermediaries act as an alternative investment mechanism to the traditional banking system[12]. Specific to foundations making PRIs, many types of intermediaries exist, including for-profit and nonprofit entities, community development financial institutions, loan funds, and equity funds. Venture capital funds have more recently served as intermediaries for PRIs. Angel investment funds are also serving foundations by supporting economic development[10].

A CDFI is one type of financial intermediary.
In the broadest sense, a CDFI is a financial institution that places community development as its primary mission. It is a non-governmental financing entity that serves a target market by providing development services and that remains accountable to its community. CDFIs provide credit and financial services to underserved markets and populations[13].

Examples of CDFIs include community development banks, community development credit unions (CDCU), community development loan funds (CDLF), community development venture capital funds (CDVC), and community development corporations. CDFIs are certified by the Community Development Financial Institutions Fund (CDFI Fund) of the U.S. Department of the Treasury. The CDFI Fund was created by the federal government "to promote economic revitalization and community development through investment in and assistance to community development financial institutions (CDFIs) through training, tax credits, awards and bond guarantees[14]."

What are the goals and mission of financial intermediaries, and what types of capital do they use to achieve these goals?
Because there are many types of intermediaries, their goals and types of funding will vary. CDFIs may receive capital from many different groups. Large banks and thrifts often lend funds for re-lending, and in return they receive Community Reinvestment Act credit for lending to CDFIs. Additionally, most finance companies, insurance companies and mutual funds contribute loan funds to CDFIs. Corporations and wealthy individuals may also invest in CDFIs[15].

What role does an intermediary play in the PRI process? I.e. how are responsibilities delegated among the funder, the intermediary and the recipient? How is this delegation decided?
The details of an intermediary's role were not found in any references, documents, or reports. However, based on the interviews with other foundations, the role of intermediaries in the PRI process is likely determined on an individual basis. A couple scenarios mentioned during the foundation interviews demonstrate varying capacities:

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[12] Appelbaum, Eileen, Rosemary Batt, and Jae Eun Lee, Financial Intermediaries in the United States: Development and Impact on Firms and Employment Relations, Center for Economic and Policy Research, http://www.cepr.net/documents/publications/financial-intermediaries-2012-08.pdf
[13] CDFI Types: Comparing Different Types of CDFIs, The Coalition of Community Development Financial Institutions, http://www.cdfi.org/about-cdfis/cdfi-types/
[14] Community Development Financial Institutions Fund, United States Department of the Treasury, http://cdfifund.gov
[15] CDFI Fact Sheet, CDFI Coalition, http://cdfi.org/uploads/other/CDFI_Fact_Sheet.pdf

1. Multiple foundations pool together their resources to hire a 3rd party financial consultant to manage the PRI[2]
2. Foundation works with a single intermediary with both parties providing technical/financial expertise to varying extents not made clear in the interview[9] [11]

What are examples of intermediaries that our interviewed foundations have worked with?
The Ford Foundation works with Living Cities Catalyst Funds to make below-market rate loans to finance neighborhood stabilization, energy efficiency retrofits, public education and access to fresh foods and health care. The Annie E. Casey Foundation also currently works with Living Cities Catalyst Funds.

The Rockefeller Foundation works with Root Capital to lend financial capital and provide financial training to small agricultural businesses in Africa and Latin America.

The Annie E. Casey Foundation works with other foundations to create a PRI for Goodwill Industries International to provide short-term financing to high growth potential Goodwill stores and donation centers to accelerate job creation.

How are intermediaries selected or created by foundations?
The Ford Foundation utilizes CDFIs because they have a lower investment risk. Most CDFIs have 20 percent (%) equity on their books and have a history of providing social outcomes. The Annie E. Casey Foundation's commonly selects PRI recipients from current grantees, who have a proven track record with the foundation and who have expressed an interest in PRIs.

What are the benefits of using intermediaries?
Intermediaries create economies of scale by aggregating investors and investees with the hope of achieving greater impact. They make use of specialized expertise to improve performance, and lower transaction costs through economies of scale. They reduce financial and reputational risk, leverage tax credits and private (nonphilanthropic) capital[10]. Intermediaries also broaden the pipeline of potential investments, remove the administrative burdens of strict due diligence and oversight requirements, and accelerate access to capital and other resources to those in underserved markets. CDFIs can allow a foundation to make PRIs easily, particularly those intermediaries that have strong track records and experience with foundation investors. Below-market rate deposits in CDFI banks or credit unions can furthermore be insured, thus lowering a foundation's risk considerably[16].

What are the costs and challenges of using intermediaries?
There is the risk of misaligned goals since the foundation gives up a certain level of control over the selection of investees. Intermediaries also create less direct interaction between foundations and investees. There are also additional overhead costs in management fees, although this is compared to the costs the foundation would incur by hiring its own staff to source and oversee PRI activity[10].

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[16] Program Related Investments: Leverage Your Assets for Greater Impact, Association of Small Foundations, http://www.smallfoundations.org/downloads/educational-programs/Amp_Up_Your_Impact_with_Program_Related_Investments_2.pdf

Appendix 2.1: Interview Summary – The Annie E. Casey Foundation

Overview
EFC staff met with for a representative of the Annie E. Casey Foundation in Baltimore on March 15, 2013. The Annie E. Casey Foundation modeled their PRI program on that of the Ford Foundation, with the exception of using their endowment to fund investments, as opposed to their grant budget. During his time with the foundation, former President and CEO Doug Nelson worked to maximize the amount of investment in charitable causes. Approximately $40 Million is currently invested in PRIs, as part of $125 Million that is allocated to Social Investments.

Findings
Because of limited staff available, the foundation prefers to invest through intermediaries in the form of non-profit loan funds, specifically Community Development Financial Institutions (CDFIs). Through this method, the foundation performs the task of underwriting the loan funds whereas the intermediary manages the projects directly. The foundation notes that an advantage of PRIs is easier deployment of capital. There is no official expectation of return on investment; instead it is decided on an individual project basis, and trustees are very willing to take losses. The foundation has an 8-9% target overall return on investment, and there is pressure to make up loss gaps through PRIs. A minimum of $500,000 and a maximum of $1-2 Million per investment is recommended in order to reap the benefits of the PRI structure because it is more resource intensive than grant making. Larger investments are termed Big Bets by the foundation because they involve extra staff, capital and senior leadership support. The current default rate is less than 1%. The foundation does not accept collateral to avoid being involved in a foreclosure in case the venture fails.

The PRI Investing Process for the Annie E. Casey Foundation

- More than a dozen foundation employees, including representatives from each investment unit, are involved in the PRI process.
- In the first step, the written request for a PRI is received and the investment summary is written up and reviewed.
- The second step involves due diligence and a site visit.
- Finally, the investment is formally recommended to the CIO to sign off on, although the CIO is made aware of progress throughout the process and may halt the process at any time.
- Typical turnaround time is 3 months if the recipient already has a grant history with the foundation, and 9 months if there is no transaction history.
- In one possible collaboration structure, foundations pool capital, share costs, and perform underwriting but a single investment is made and the management is outsourced to a created LLC special purpose entity.
- Another possible structure involves a single foundation providing to a grantee both the PRI and an outsourced legal manager.

Words of Advice
The Annie E. Casey Foundation collaborates with other foundations to leverage capital, an essential component of maximizing success. This is especially helpful for smaller foundations that do not have the team of experts available to manage this type of fund. However, it was noted that this strategy is

challenging for various reasons: each foundation has a different strategy in achieving its mission, and unneeded information is given to each foundation to satisfy the requirements of the other group members. Nevertheless, this collective approach is highly recommended based on a past experience in which Casey Foundation and other foundations were working together with one recipient but communicating individually with the recipient; the process was an inefficient use of everyone's time and it was discovered that the recipient was playing the foundations off each other. Because of additional informational resources available to foundations, PRIs are less likely to fail now as they did in the 1960s when they were first pioneered.

The foundation further recommends that foundations that are new to PRI investing begin slowly with small investments and gradually increase their scale. She further recommends that foundations ensure that they have strong confidence in their organization's expertise, and that they create realistic financial models and goals.

Appendix 2.2: Interview Summary – The Ford Foundation

Overview

EFC staff met with a representative of the Ford Foundation in New York on February 13, 2013. The foundation manages a $280M international and domestic PRI fund. The Foundation began making PRIs in 1968. Reasons for beginning the fund are varied but the foundation wanted to *test* innovation. PRIs, by their very nature, carry more risk than traditional investments and much more risk than traditional grant making. The foundation never expected to manage the Fund to cover all of their costs and were willing to take a financial risk. The foundation believes that PRIs offer a new kind of funding source outside of traditional grant making that can help incentivize and promote both the mission and goals of the foundation as well as the recipient(s) of the funds themselves. It is important to note that the Ford Foundation only invests PRI funding into projects/programs that will advance the mission of the foundation. This helps offset the risk associated with the funding and helps to justify to the Board of Directors why a particular project/program should receive PRI funds. The Ford Foundation Board of Directors does not review each PRI application nor do they approve or deny an individual application. The Board approves an annual amount of funding to be set aside for PRIs. The President of the PRI program makes the final decision on each application.

How PRI Investing Works for Ford

- It is important to ask the question of "Risk" i.e. How much risk can your foundation afford? The Ford Foundation has accepted a 20% loss risk.
- Standard investment for the Ford Foundation is a 10 year low interest low with the principal paid in the last 2 to 3 years.
- The foundation does both equity investments and low interest loans for PRI investors.
- The investment should help meet the mission of the foundation.
- Safer investing: Community Development Financial Institutions. Most CDFIs have a 20 % equity on their books and they have a history of providing social outcomes. (Example: Living Cities Catalyst Funds – usually for urban areas). The Ford Foundation has invested over $200M in CDFIs and has never lost. Also, Bank of America has invested over $1B in CDFIs.
- Riskier investing: Direct and venture capital investments.

Additional Recommended Resources

Mission Investors Exchange

The Ford Foundation is part of the Mission Investors Exchange which is where philanthropic innovators exchange ideas, tools, and experiences to increase the impact of their capital. The organization also helps beginner and advanced foundations set up PRIs or Mission Related Investments (MRIs). The representative noted that the Exchange has more than 200 member foundations and mission investing organizations.

Confluence Philanthropy

Confluence Philanthropy is a non-profit network of over 175 private, public, and community foundations. We build capacity and provide technical assistance to enhance the ability of foundations to align the management of assets with organizational mission to promote environmental sustainability and social justice. Confluence is a recognized affinity group of the Council on Foundations. We are supported by our members. *Confluence is not an investment advisor. Therefore we do not provide advice or guidance to venture funds, social enterprises, or grant seekers about how to secure program-related investments nor any other form of capital. We do not share the contacts of our members nor do we network fundraisers to philanthropic investors.* Other excellent resources include The Packard Foundation, the MacArthur Foundation, the Moore Foundation, and the Casey Foundation.

Appendix 2.3: Interview Summary – The Bill and Melinda Gates Foundation

Overview
EFC staff met with for a representative of the Bill and Melinda Gates Foundation, via conference line, on March 22, 2013. The foundation is headquartered in Seattle, Washington. The Gates Foundation PRI fund is set up similar to the Ford, Rockefeller and Annie E. Casey Foundation's PRI program. However, unlike the other foundations interviewed, the Gates Foundation invests over $1 billion annually around the world with focus areas in Southeast Asia and sub-Saharan Africa.

Findings
The Gates Foundation offers a view into the extreme side of PRIs, with over $1 billion annually; the foundation offered us a view into "mega" investing. Due to its size of investing, we found that the Gates Foundation offered little in terms of how we should structure small investments for Chesapeake Bay water quality projects, however, the way they set up the fund and administer the fund was helpful nonetheless. The foundation has invested with upwards of 15-20 companies/project each funding cycle. The Gates Foundation utilizes a very small staff (1 to 2 persons) with intermediaries to help balance their investing portfolio. Like most other foundations, they focus on achieving both financial and mission related goals. The foundation manages their risk in a variety of ways by utilizing a strong background check method as well as partnering with other companies to help leverage finances and technology. Investments are usually between $5-20 million.

The PRI Investing Process for the Gates Foundation
- Very limited staff (1 to 2 persons) manages the PRI process.
- Intermediaries are used to help manage project investments.
- Like most foundations, they follow a scoping process for a particular project, complete a full investigation and sign off through an extensive legal process.
- Typical turnaround time can be very short but may take up to 2 years to get a project ready to advance.
- Partners and other companies are sought out to help leverage the financial burden as well as to provide technical assistance and to leverage technologies.
- Risk is managed through a variety of ways by leveraging other partners, and by having a reputable intermediary and a strong legal framework.
- Investment opportunities include: Debt instruments such as loans to NGOs, financial institutions or companies; Equity instruments, investments in funds or purchases of shares in companies; Guaranty instruments such as bond back-stops or credit guaranties.

Words of Advice
- Gain full commitment and support from the project/company you are investing in for the life of the PRI (5 to 10 years);
- Intermediaries are a necessity; and
- Form an investment committee that reviews and gives approval for each PRI.

Appendix 2.4: Interview Summary – The Rockefeller Foundation

Overview

EFC staff met with a representative of the Rockefeller Foundation. The foundation began making PRIs, informally, in the 1980s and formally adopted the program in 1997. Rockefeller spends $25 M annually on PRIs.

How Investing in PRIs works for Rockefeller

There are five areas in which the Rockefeller Foundation bases their decision to fund a project:

1. The PRIs are used to support core areas and missions;
2. PRI funding goes to financial institutions are intermediaries;
3. They look for transactions that are innovative, which also means more risk;
4. They look for the opportunity to leverage commercial capital; and
5. Targeted financial return is return of capital, in the form of debt equities and guarantees.

The foundation has no standard investment term, like the Ford Foundation, the investment can be up to 10 years. Each new PRI transaction that the Rockefeller Foundation has is $1-3M. Also, unlike the Ford Foundation, Rockefeller has a risk neutral strategy. In other words, they try to break even.

Pros

- PRIs are useful as another tool of capital
- It is a different relationship than grant making with more strings attached. There is money to be paid back, capacity building occurs, etc.
- The investee is financially (more so) and socially disciplined if they have to pay back a loan.

Cons

- Operational intensity
- The more innovative the more time spent to manage
- Investing with others is sometimes messy

Highlights and Words of Advice

- Having a Board or leadership that buys into the concept of PRI investing is critical for foundations when starting up a fund.
- Create a strategy; hire staff with financial skills and a staff with social insight.

Appendix 3: Interview Questions

1. What was your motivation for setting up this fund? What results are you hoping for? What have you been able to do with PRI's you could not have done with standard grant making?
2. Were there key people whom you worked with to make this happen, whom you feel were essential to realizing this? Were there other critical steps to setting up this PRI?
3. What were the opportunities and barriers to establishing this fund? Specifically opportunities and barriers that would also relate to M2E technology?
    a. What has been the support of your Board – did they have initial concerns?
4. How do potential recipients find out about the opportunity?
5. How is the fund accessed by current recipients? E.g. is there a point of contact that gets in touch with them?
6. What role does an intermediary play in the process?
    a. Which organization is the intermediary?
    b. How did you select/create this entity?
    c. How are responsibilities delegated among the funder, the intermediary and the recipient? How was this decided?
7. What are the details of this PRI?
    a. Is this an equity investment, a low-interest loan, a zero-interest loan, a loan guarantee, a line of credit, an asset purchase, a recoverable grant, etc.?
    b. Have you considered a sustainable legacy component?
    c. What are the requirements to qualify for the PRI, and how do you verify these requirements (both to verify identity and minimize risk for yourself) e.g. credit check? How do you work risk analysis into your approval process
    d. How did you determine the minimum initial investment, the number of initial recipients, and how to allocate the money among them?
    e. Is the PRI managed in-house or by contract management support? Why?
    f. What was the timeline to design and implement this PRI? When did you establish it?
    g. What percent of giving is in PRIs versus standard grant making? How does this PRI fit into your portfolio?
    h. What are the financial terms?
        i. E.g. loan rate, minimum/maximum loan amounts, payment schedule, payback timeline, number of payments, transaction cost, downside protection, secured
        ii. To minimize risk, do these terms change depending on the lendee's financial situation or needs? E.g. sliding interest rate depending on loan repayment term or loan amount? Is there any required collateral?
8. How are these details decided on?
    a. What kind of flexibility is there in fitting the funding to a project?
    b. What kind of flexibility is there to change the terms along the way if needed?
    c. Has there been any adjustment of terms e.g. defaults, requests for extensions?
        i. What is the percentage of defaults?
9. Are you likely to continue this fund in the foreseeable future? I.e. have there been unintended setbacks or is it not working well with your overall financial goals? What would you do differently?

10. What are some of the most critical questions a foundation should ask itself prior to setting up a PRI? In setting up this PIR, do you feel that the questions asked and the steps taken differ per sector/industry?
11. What are the cost differences between PRI and your other more standard grant making options?