May 2024

PHILANTHROPIC ORGANISATIONS USING THE ENTIRE TOOLBOX FOR MORE IMPACT

Paper on foundation practice, as well as regulatory and policy environment

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Philanthropy and the continuum of capital

Where do philanthropic organisations fall along the continuum of capital, and how do they use their entire toolbox of financial and non-financial resources?

Philanthropic organisations have a great role to play when it comes to achieving and generating positive social change. Foundations can move along the continuum of capital,[1] adopting diverse strategies and benefitting from an extensive toolbox of non-financial and financial resources from their programme activities and the investments of their endowments.

Philanthropic organisations can deploy grants with a catalytic mindset, but they can also use repayable financial instruments and/or invest their endowment with social and/or environmental purposes. When it comes to repayable finance and impact investing, some philanthropic organisations are already important players in the ecosystem in Europe, and more philanthropic players are showing interest in entering the space. That said, it is important to acknowledge that impact investing will not be for all philanthropic organisations, as there are legal barriers to do this in several countries. Factors that influence the current and future engagement in impact investing include different cultures and laws, as well as varying statutes (which, for example, stipulate the will of the founder) and autonomy in deciding about the use of funds for grantmaking, projects and investment .

For those entering this space, there is a growing realization that involvement in impact investing may offer a chance to build on their organisational and social and environmental impact. On the one hand, philanthropic organisations are seeing opportunities to expand their toolbox by incorporating impact investing approaches into their grantmaking capacity. On the other hand, a wider societal shift in expectations for investments of their endowments to create more than financial returns has led to a growing interest in this area amongst philanthropic organisations when investing their endowments. Several foundations have also taken a new strategic direction to take a holistic approach towards their programme and endowment investing side.

This paper is jointly crafted by the key European philanthropy networks working in the field of philanthropic organisations and impact investing: Impact Europe, the European investing for impact network, and Philea - Philanthropy Europe Association. It builds on both organisations' resources and joint actions, in particular a multi-year joint working group on philanthropic organisations' use of the full spectrum of capital[2], which provided valuable insights and case studies.

The paper seeks to empower those who wish to learn more. It defines catalytic grantmaking, underlining its potential; highlights challenges and opportunities; and points to existing legal or statutory barriers to impact investing on programme and endowment sides. It will be followed by a second document, a collection of case studies to help bring these areas to life. It will hopefully act as a resource for those looking to foster change both in their organisations and more widely in the policy ecosystem.

[1] We refer to the continuum of capital to illustrate the entire spectrum of funding strategies that capital providers can adopt, ranging from grantmaking to sustainable and responsible investing. Philanthropic organisations move along this continuum when they use diverse financial instruments, while adopting different risk-return-impact profiles. While moving along the continuum, capital providers also offer different types of non-financial support.

[2] DOEN Participaties, Fondation Botnar, Fondazione Cariplo, Fondazione Compagnia di San Paolo, Fondazione Sviluppo e Crescita CRT, Fundação Calouste Gulbenkian, King Baudouin Foundation, Oranje Fonds, Robert Bosch Stiftung

Philanthropic organisations as catalytic grantmakers

Philanthropic organisations can give grants or run programmes and operations with a catalytic mindset. They can give grants to other social economy organisations and, where the law allows, to social enterprises. We refer here to "catalytic grantmaking" as a strategic approach to support impact ventures addressing social and environmental challenges, which are not yet ready for repayable instruments or lack a viable business model. Catalytic grants can change the trajectory of early-stage ventures, thanks to their versatility and flexibility. They complement early-stage income and offer valuable assistance in research, capacity building, and scalability testing, transforming early-stage ventures into financially viable organisations with scalability potential. This dual support de-risks social and environmental solutions, and attracts follow-on funding that might not have been mobilised otherwise. Catalytic grantmaking includes a strong commitment to addressing market gaps and failures, iteratively adapting financial and non-financial support while data are generated, ultimately ensuring both impact and financial sustainability in the long term.

Examples of the use of philanthropic grants as catalytic capital are growing in number, as evidenced by Philea and Impact Europe peer exchanges, and recent encouraging case studies.[3]

Philanthropic organisations as impact investors

Impact investing refers to investments made by different types of investors into companies, organisations, and funds with the intention to **generate a measurable, beneficial social and/or environmental impact alongside a financial return**.

Philanthropic organisations traditionally have two major capital levers at their disposal to engage in impact investing: acting as investors via their programme activities and/or through the asset allocation of any endowment or investment assets.

Philanthropic organisations that engage in impact investing show variation when it comes to using the programmatic side, the endowment side, or both. Experts have reported that where philanthropic organisations do not distinguish between impact investing via the endowment and programmatic side, they often had no strict view on wanting to be there in perpetuity (including possible spending-down).

Impact investments can either lean towards investing with a "finance first" approach or with an "impact first" one. In the latter case funders may not insist on dividend payments, because they want to see that the investee can use profit for reinvestment and further growth. However, an investment is not a grant. If the recipient of the impact investment can materialise an exit, then the foundation that has invested may want to recuperate the capital sum of the investment, possibly with a financial return.

Use of the programme side for impact investing

On the programme side, many philanthropic organisations have already started going beyond grantmaking by using different financial instruments (e.g., loans as well as equity and hybrid instruments, such as mezzanine and convertible loans[4]) coupled with non-financial support.[5]

[3] Gaggiotti, G. et al. (2023) "Catalysing Impact - Catalytic Capital in Europe Whitepaper". EVPA (see pages 29-33). Available at: https://www.impacteurope.net/stream/catalytic-capital

[4] https://www.impacteurope.net/insights/financing-social-impact-financial-instruments-overview

[5] For more information on Non-Financial Support: https://www.impacteurope.net/stream/non-financial-support or Tailored Financing https://www.impacteurope.net/stream/tailored-financing

Philanthropic organisations have seen benefits in using repayable finance to support impact organisations, responding to their needs and helping them scale and increase their positive impact. At the same time, the use of returnable financial instruments has enabled philanthropic organisations to increase the impact reach of their own finite resources. Both Philea and Impact Europe members have provided numerous successful examples of this, showcased on our websites;[6] further examples from both organisations are forthcoming in a follow-up paper.

Whilst programmatic impact investing is established, barriers remain. For example some national laws do not allow for the programmatic side to generate financial returns. In other jurisdictions tax-exempt philanthropic organisations are not permitted to support financially for-profit actors even if they are social enterprises.[7] These barriers exist alongside a variation in both appetite and knowledge across differing markets.

As mentioned above, impact investing looks for a financial return alongside positive impact. However, foundations can engage in impact investing with an "impact first" approach, meaning that the investment can also happen without getting a repayment of the sums invested. In this case, foundations may want to allow the investee to "keep all profit" for re-investments, rather than making a dividend payment.

Use of the endowment for impact investing

Foundations can also use the asset allocation of the endowment for impact investing. In this case, they wish to generate a financial return and deliver a positive impact.

For the majority of philanthropic organisations, **asset administration of their endowment and their grantmaking/operational/programme activities are two separate areas of activity** without much interlinkage.

Historically and often legally required, this approach to asset administration has been fed by a focus on the endowment side to create capital returns for the grantmaking and programme side to pursue the foundation's mission. Whilst not possible or even desirable for all, some organisations have begun to consider using their endowments more as tool to further social and environmental impact, with a view to create positive impact not only via their programmatic/grants side but also via the investment of their endowment.

More philanthropic organisations have started considering that their asset administration/investment of the endowment should at least, to some extent, be linked to their mission[8] and/or follow sustainability criteria.

Mission-related investment refers to linking (parts of) a philanthropic organisation's asset allocation/investment of its endowment to its public-benefit mission. Some examples are a philanthropic organisation with a cultural background investing in a theatre start up, or a philanthropic organisation investing in social housing/real estate.

When endowments engage impact investing approaches, they do so across different asset classes, providing returns ranging from below-market to market rates, depending upon the circumstances. Rather than including the whole endowment, "carve outs" – specific percentages of assets dedicated to a more impact-centric approach – are often used. These

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[6] www.philea.org & https://www.impacteurope.net/stories
[7] https://philea.issuelab.org/resource/comparative-highlights-of-foundation-laws-the-operating-environment-for-foundations-in-europe-2021.html
[8] For a definition and some examples of the so-called „mission-related investments" please see: https://ssir.org/articles/entry/unleashing_the_power_of_endowments_the_next_great_challenge_for_philanthropy

“carve outs” are often perceived as higher risk and can often sit alongside a wider, more conservative ESG (Environmental, Social and Governance) or return positive asset allocation strategy for the wider endowment.

Some foundations are also considering taking a sustainability approach towards their endowment investments by either investing in ESG funds, or in listed or non-listed companies that contribute to certain SDGs or other sustainability or ESG criteria. This approach may or may not be linked to a foundation’s mission. There is generally greater interest in ESG investing on the side of philanthropic endowments as compared to mission-related investing. While doing ESG oriented investing, foundations can (i) exclude certain companies from investment mandates via negative screening, and/or (ii) do positive screening and invest in companies and enterprises that are “best-in class for societies and ESG”.[9]

However, Philea’s latest legal mapping[10] revealed that **barriers and legal uncertainty around this type of investment of the endowment exist** in some countries. Some national laws require a preservation of the value of the endowment. Mission-related investment or investment in impact enterprises do not always generate the required financial returns (or are considered as too risky), or giving loans is not permitted. Sometimes the laws are simply unclear or not explored; see for example the work of the Impact Investing Institute in the UK[11] to clarify national laws for philanthropic organisations.

Even in a flexible legal environment, such actions may not be in line with the **mission/statutes/will of the founder, which may suggest a low risk appetite**. That said, as a first step, many philanthropic organisations have started negative screening and/or more conscious decision-making about sustainable/green asset allocation/mission-related asset allocation when investing their endowment. Tools such as stewardship or shareholder activism, whilst small in number, these options offer the opportunity for further ways to deploy the wider endowment for positive impact without affecting financial returns.

Ways policymakers can further stimulate impact investing activities of philanthropic organisations

At the national level, policymakers could be encouraged to consider, review and enable different impact investing approaches of philanthropic organisations and to enlarge the toolbox. Governments are lagging behind in understanding that foundations want to invest instead of (only) donate and give grants.[12]

Over the past years, the European Commission has stated an interest to stimulate more mission-related/sustainable investments and impact investing activities of philanthropic organisations more broadly, in particular also in the context of the end 2021 Social Economy Action Plan and its InvestEU programme.

Already the 2018 study written by the Expert Group on “Foundations, Venture Philanthropy and Social Investments”[13] encouraged the European Commission to look into **“how foundations can use their endowments and their grants in a more flexible way”**, taking

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[9] https://philea.issuelab.org/resource/philanthropy-back-to-the-drawing-board-shaping-a-future-agenda.html pages 143ff.
[10] https://philea.issuelab.org/resource/comparative-highlights-of-foundation-laws-the-operating-environment-for-foundations-in-europe-2021.html
[11] See for instance their report Can charities invest their endowment with Impact
[12] https://philea.issuelab.org/resource/philanthropy-back-to-the-drawing-board-shaping-a-future-agenda.html, page 157
[13] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4008384

into account the findings of the Philea Country Profiles and Comparative Highlights, which outline some existing stumbling blocks for impact investing activities in national laws.[14]

The 2021 Social Economy Action Plan and the 2023 European Investment Advisory Hub's "Philanthropic Capital study"[15] include some recommendations around innovative ways to stimulate more **mission-related asset allocation** and impact investing, as well as public/philanthropy collaboration. For instance, there is potential with **InvestEU**, and with the European Investment Bank (EIB), the European Investment Fund (EIF) or National Promotional Banks (NPBs) as implementing partners, to design products or develop tools within a co-investment facility that could stimulate more mission-related asset allocation.

In line with the European Philanthropy Manifesto[16], Philea continues to monitor and explore ways for the European Union to leverage the impact of private resources for the public good, for example by introducing financial instruments that stimulate new impact investing tools for institutional philanthropy. The Manifesto also includes a call to Member States to empower philanthropy and to provide for a more enabling framework for impact investing at the national level.

An updated version of the Manifesto was published on 29 November 2023 with a view to also reflect on recent policy opportunities. We would welcome others to join us in support of the implementation of the Manifesto.[17]

Holistic organisational approach

The divide between asset allocators and programmatic approaches can seem artificial. However, over the past years we have seen philanthropic organisations using a mix of financial tools to do impact investing via the programme side (which can take more risks) and the endowment investment side (which can take fewer risks). By taking on impact investing approaches, foundations are hence exploring different ways to realise their missions.

Furthermore, some foundations do not distinguish between the investing (endowment) and spending (grants/donations) sides, but put different sources into one pool that is then used for impact investing.

Additionally, philanthropic organisations can also mix catalytic grantmaking with repayable financial instruments to support the same social economy actor/social enterprise/start up. These examples are encouraging, pointing to the potential multiplier effect of combining the traditional strengths of both approaches – grantmaking and impact investing.

Nurturing collaboration to spur more impact investing

The extensive toolbox at the disposal of philanthropic organisations presents a unique opportunity. Considering the existing and emerging practice as laid out in this paper, what can we do to further enable philanthropic organisations to benefit from this entire toolbox? Beyond programmatic, endowment and holistic approaches to impact investing, some philanthropic organisations, together with innovative civil society actors, other impact investors and social impact entrepreneurs, also act as **thought leaders and incubators for social impact**

[14] https://philea.eu/how-we-can-help/policy-and-advocacy/analysing-the-legal-environment-for-philanthropy-in-europe/; https://philea.issuelab.org/resource/comparative-highlights-of-foundation-laws-the-operating-environment-for-foundations-in-europe-2021.html
[15] https://advisory.eib.org/publications/attachments/the-philanthropic-capital-study.pdf
[16] https://philea.issuelab.org/resource/european-philanthropy-manifesto.html
[17] In view of the European elections, Impact Europe will also launch an Investing for Impact Manifesto where it will reinforce Philea's call for financial instruments that will enable philanthropic organisations to engage in impact investing with both their programme and endowment investments.

investments. There is an opportunity to connect these different actors and approaches more systematically. To make this happen, it would be important to highlight good practices and to break internal silos, having the two areas – programmatic and endowment – working together and cross-pollinating each other's strategies. Buy-in from leadership would also be needed.

This is why, since 2018, Philea and Impact Europe have joined forces around the topic of philanthropic organisations moving across the continuum of capital. A joint working group was set up in 2019 (the "Foundations along the spectrum of capital" initiative), composed of joint Philea and Impact Europe members. The working group exchanges on best practices/opportunities and challenges around impact investing and explores potential collaboration opportunities. Philea and Impact Europe will continue to explore the use of the entire toolbox foundations have available along the continuum of capital. We will look to collaborate in fields such as data collection, knowledge sharing, peer-exchanges, legal analysis and policy engagement work.

Key events in the pipeline include a session on impact investing at the Philea Forum 2024, followed by webinars targeting the programme, endowment and leadership aspects of impact investing. We will reconvene interested stakeholders on the occasion of the European Day of Foundations and Donors on 1 October 2024, and will host a session at the Impact Week 2024 and at EuroPhilantopics 2024. With this, we envisage to lay the groundwork for a further two-year initiative which will be built by the community and guided by its needs.

Contact

Please do get in touch if you would like to learn more, or contribute to moving this area forwards:

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About Impact Europe and Philea

Impact Europe (formerly **EVPA**) is *the* investing for impact network, gathering impact capital providers along the full continuum of capital (foundations, impact funds, banks and financial institutions, corporate impact actors, public funders). We work together to increase prosperity and social progress for all, fix inequalities and injustices and preserve the planet. And we do so by rallying people, capital, knowledge and data to catalyse, innovate, scale and safeguard impact.

Philea nurtures a diverse and inclusive ecosystem of foundations, philanthropic organisations and networks in over 30 countries that work for the common good. With individual and national-level infrastructure organisations as members, it unites over 7,500 public-benefit foundations that seek to improve life for people and communities in Europe and around the world. Philea galvanises collective action and amplifies the voice of European philanthropy by co-creating knowledge; learning from effective practices; collaborating; and promoting enabling environments.