Supplement

Unintended Consequences

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Stanford Social Innovation Review
Summer 2016

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Unintended Consequences
How a strategic investment steered an educational-technology startup into trouble.

BY DAVID BANK & DENNIS PRICE

Jamie Glenn, chief executive of a once-hot social media startup, was between a rock and a hard place. Or rather, between a binding legal agreement and a faltering business model.

Uversity, formerly known as Inigral, had been first to market with an app, built on the Facebook platform, that provided a safe, professional environment for incoming college students. As a condition of a $2 million investment from the Bill & Melinda Gates Foundation two years earlier, Uversity had agreed to focus a portion of its sales efforts on community colleges in addition to the four-year colleges that were its primary market.

Now, near the end of 2012, Glenn sat in his office, wondering how he was going to meet the year-end deadline for signing up eight community colleges as customers. The company had agreed to that goal as a condition of the Gates Foundation investment. Uversity's pipeline was thin. Even setting up initial sales calls with college administrators was challenging.

For the Gates Foundation, the binding agreement was meant to ensure that community college students, especially low-income students, had quick access to the capabilities of Uversity's app. It was based on a hypothesis that stronger social engagement would lead to increased retention and ultimately to higher graduation rates. Even now, barely one in four low-income community college students gains even a two-year degree.

Glenn and his team met the deadline. But determined not to have another near miss in 2013, the company offered deep discounts to the community colleges that pitched the best social media strategies. Glenn put a salesperson on the project full-time, and he and his sales chief stepped in to close deals.

Ultimately, Uversity surpassed the target by signing up 31 community colleges, but at an average price of only $3,000, compared to average annual licensing fees of $18,000 from the company's primary targets, the four-year colleges for whom the product was designed.

The investment in Uversity was the Gates Foundation's first equity program-related investment (PRI) in a for-profit startup, and Uversity had been eager to land it. Beyond the capital, the investment provided the company with the perception of a high-profile validation that helped establish its credibility. The foundation's focus on community colleges helped the company identify new customers and also make inroads into the higher-education market, where the foundation is well-connected.

But with the investment came a commitment to meet the charitable requirements of a PRI. In retrospect, both the company and the Gates Foundation now recognize that Uversity's decision to meet these special requirements diverted a portion of Uversity's efforts from its core market, just when it needed to prove it could scale up its business model quickly. The distraction also delayed the company's ability to break even in cash flow; Uversity's weaker financial performance contributed to a falling valuation and ultimately its loss of independence.

Uversity was acquired by TargetX in 2015. “That’s the cost of capital,” says Glenn. “You need to devote time and resources to the commitments.” He adds, “As a startup pivots, as they all do, the charitable commit-

The College of DuPage, a community college in Glen Ellyn, Ill., held its graduation ceremony in 2014.
from potentially more profitable institution-
al sales activity,” says Greg Ratliff, who led
the investment from the Gates Foundation’s
postsecondary education program.
Larry Mohr, a veteran Silicon Valley
venture capitalist and early investor in
Uversity, agrees. “Today, if you talk to any-
body around the deal, targeting community
colleges with the product was just a mis-
take,” he says. “There’s no doubt that what
they were trying to do was a diversion. It was
not part of the main strategy path.”
The experience taught the foundation’s
investment team that the best intentions
of an impact investor to steer technology in-
novation toward neglected markets and dis-
advantaged customers has the potential to
harm a company’s success, if those markets
are different from the company’s core mar-
ket. The requirements that came with the
Gates Foundation’s funding were not well
aligned with the strategies needed to grow a
nascent educational-technology company.
It’s a cautionary tale for entrepreneurs
and commercial investors looking to tap the
growing pool of mission-driven investors.
Such capital carries its own kinds of costs.
Although an investment from a high-pro-
file funder like the Gates Foundation may
provide the perception of validation and
cachet, fulfilling the required charitable
commitments may, without clear alignment
of objectives, pull a company away from
commercial success.
Julie Sunderland, who managed the
Gates Foundation’s strategic investment
team at the time, says she doesn’t regret the
investment, but she wishes the foundation
knew then what it knows now. “We learned
a lot about the types of support community
college students need as well as how to invest
as a foundation,” she says. “We now are much
more careful in looking for a high degree of
overlap between the company’s goals and
our charitable goals. We won’t do the deal if
we anticipate significant potential for con-
flict,” she says. “Undermining the long-term
viability of a company also undermines our
ability to achieve our charitable goals. The
first thing we think about is ‘Do No Harm.’”

SIDE LETTER
A partnership between an educational-
technology social media startup and the
world’s largest private foundation held a
world of possibility. In 2010, the potential
of social media was not widely understood.
Uversity (then Inigral) attracted name-
brand venture investments from Peter
Thiel’s [Founders Fund and Mohr’s [Retro
Venture Partners]
The company’s “Schools” app was built
on Facebook, combining a familiar user
interface with a protected environment
designed for incoming and new college stu-
dents. The idea was to help students navigate
the college experience together with other
students, faculty, and school administrators.
One school admissions counselor described
it as interacting in an online student union.
Other social media environments were more
like meeting students at a bar.
That caught the attention of the Gates
Foundation’s Postsecondary Success pro-
gram team. If an online environment could
replicate some of the peer support and
friendship that had been shown to increase
student retention at residential colleges,
Ratliff thought it might help two-year com-
unity college students succeed as well.
“The first thing I got asked by invest-
ment committee: ‘What is a social media
technology?’” says Ratliff, who before
coming to the Gates Foundation had man-
aged PRIs for the [John D. and Catherine T.
MacArthur Foundation]. “People were un-
clear about what this was at that time.”

At the time, Uversity had only a dozen
customers and barely $100,000 in reve-
nues. The company’s founder, 25-year-old
Michael Staton, was eager to get the Gates
Foundation’s endorsement. He flew to Seat-
ttle with Mohr to meet the investment
team.
The investment took months to negoti-
ate, in part because of the need to document
the charitable commitments required for
the foundation’s first-ever equity PRI in
an early-stage company. The Gates Foun-
dation’s legal and investment teams used
an approach that opened the door for all
of its subsequent equity PRIs. Along with
the typical financial deal terms, the teams
negotiated a legally binding side letter that
defined Uversity’s agreed charitable com-
mitments. As a condition of the investment,
the Gates Foundation and Uversity agreed
that the company would focus a portion
of its sales efforts on reaching community
colleges, which disproportionately serve
students from low-income households.
Uversity agreed to sign up a quota of new
community college customers each year.
As a legal and programmatic matter, the
foundation needed the company to meet its
charitable obligations. The agreement in-
cluded a right of withdrawal—requiring that
Uversity repay the Gates Foundation if the
company was unable to meet those objec-
tives. Ratliff says he told Glenn to “Hold fast
to the charitable goals.” Putting it bluntly, he
added, “If you’re not valuable to those stu-
dents, you’re not valuable to us.”

PRODUCT/MARKET FIT
With the legal framework in place, the Gates
Foundation made a $2 million PRI to ac-
quire a 20 percent stake in the company. The
investment was part of the company’s 2010
Series B financing round of $3.4 million led
by Mohr at Retro Venture Partners.
The Gates Foundation also provided a $1
million grant to a consortium of community
colleges to establish and test the feasibility
and effectiveness of social media programs,
which often included signing up for Uversi-
ty’s product. The grant supported research-
ers at the University of Arizona to partner
with the company to study the effect of its
products on student retention and engage-
ment and to publish the results. “Having
Gates on board gave us immediate credibil-
ity within higher education, which is a sig-
ificant challenge for a startup,” says Glenn,
who took over from Staton as CEO in 2011.

Most of Uversity’s early community col-
lege clients were effectively handed to it as
part of the research project. The company
achieved the community college target in
2013. But meeting the charitable commit-
ments took the company six months, during
which it neglected higher-paying, potentially
longer-term customers—four-year private
colleges. The company missed its revenue
targets. Between defections and layoffs,
Glenn lost most of his sales team.

In those two years, between 2011 and
2013, it became clear that the prob-
lem wasn’t just that community colleges
couldn’t pay as much as others; the app,
which was designed for four-year colleges,
was a poor fit for two-year schools. The core
value of Uversity’s social media product
for four-year colleges was as a recruitment
tool, to encourage college applicants who
had been admitted ultimately to choose to
attend. That’s of little value to community
colleges, which accept all qualified students.

Although the research suggested that
community college students who used
Uversity’s app indeed showed increased
retention and higher GPAs, not enough stu-
Students took advantage of the app, and most community colleges didn’t have the time or budget to launch the product properly.

Still, the company had delivered on program and operational goals, and the Gates Foundation stood by its investee. Two subsequent investments, for which the foundation received commitments that aligned with its programmatic objectives, totaled $1.75 million. The last infusion was in a “down” round that valued Uversity at less than the previous investment, effectively wiping out the foundation’s previous equity investment.

Members of the Gates Foundation’s team did make efforts to ameliorate the conflict between its charitable goals and the company’s business goals. They allowed some four-year colleges with large numbers of low-income students to be counted against Uversity’s charitable commitment. They made introductions to community colleges and other potential customers. They featured the company and the research at conferences and panels and pushed the notion that social media could benefit students in higher education. “We became in some ways proselytizer of the potential of this,” Ratliff said.

Mohr says the new crop of mission-driven investors bears some resemblance to “strategic” corporate investors who also dabble in funding startups to identify technologies or products for acquisition. Impact investors are similarly looking for approaches that fit into broader strategies. “The parallel is that they both have objectives that are totally unrelated to the company,” Mohr says. “As a venture capitalist, I want the manager to make a lot of money on the deal. That doesn’t matter to the Gates Foundation or the corporate investor.”

Despite the difficulties, Mohr said he would do the deal with the Gates Foundation again. The foundation brought considerable value with its perceived endorsement of the product and access to customers and partners. “Having the Gates Foundation as an investor was quite valuable.”

Glenn agrees. He says the zigs and zags were just part of the startup game. “Ultimately the product evolved and was no longer a fit for community colleges, as the company found more opportunity by focusing on the recruitment challenges faced by four-year traditional institutions,” he says. “Startups move much faster than a foundation, and they need to realize this and be more fluid when things change on the ground.”

The convergence of low-cost solar technology, nearly ubiquitous mobile phones, and increasingly robust systems for mobile payments has unleashed a wave of entrepreneurship and investment across Africa and Asia. Off-grid solar electric systems are leapfrogging decrepit utility grids in much the same way as mobile phones leapfrogged landlines.

And solar power is just the start of an even bigger revolution in consumer finance. Pay-as-you-go financing is making electricity accessible and affordable for low-income households where the power grid is unreliable or nonexistent. By demonstrating that low-income customers can pay for high-value goods and services reliably, the new business model has the potential to bring products and services even to villages at “the last mile.”

Indeed, it was finance, not solar, that attracted the Bill & Melinda Gates Foundation to M-KOPA, one of the hottest off-grid solar startups. The foundation turned down a chance to invest in 2011, when the Nairobi, Kenya-based M-KOPA was raising money from impact investors and venture capitalists. Worthy as it was, solar energy solutions had plenty of other sources of capital.

The Gates Foundation, however, was interested in demonstrating something perhaps even more powerful: that low-income consumers, making affordable payments for products and services that improved their lives, represented a new financial asset class safe enough to qualify for commercial bank financing. The test was whether commercial

Banking on the Poor
Using the off-grid solar revolution to unlock credit for low-income customers in Africa.

BY DENNIS PRICE

Leah Talam, of Eldama Ravine, Kenya, uses M-KOPA solar lighting to help her child do homework at night.

PHOTOGRAPH BY GEORGINA GOODWIN, COURTESY OF M-KOPA

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