Social Impact Bonds in Maryland

A report for the Maryland General Assembly, House Appropriations Committee

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Purpose & Introduction

At the conclusion of the 2013 Maryland General Assembly Session, the Honorable Mary-Dulany James and the Honorable John Bohanan of the House Appropriations Committee issued a letter to Dr. Lillian M. Lowery requesting a review of the merits of issuing Social Impact Bonds (SIBs) in Maryland. This request came as a result of a Department of Legislative Services (DLS) analysis on SIBs as a possible financing mechanism for the Department of Public Safety and Correctional Services (DPSCS). This analysis prompted the introduction of legislation on the development of SIBs in Maryland, which was ultimately withdrawn at the request of the sponsor. The request was for MSDE to, in partnership with other state entities, examine existing SIB models and the feasibility of implementing these models in Maryland, with the goal of fostering a better understanding of SIBs, including their functions and potential benefits for Maryland.

The Division of Early Childhood Development, led by Assistant State Superintendent Rolf Grafwallner, commissioned The Institute for Innovation & Implementation at the University of Maryland School of Social Work to chair and facilitate a SIB Workgroup and develop the report on the feasibility of SIBs in Maryland. Dr. Lowery invited representatives from multiple State Agencies as well as from the philanthropic and non-profit communities, private sector, and City of Baltimore to participate in the Workgroup.

The Workgroup convened on three separate occasions from July 2013 through October 2013 to hear presentations from national experts on different facets of SIBs and discuss the merits and challenges of development and implementation of SIBs in Maryland. The goal for the first meeting was to provide an overview of SIBs and SIB projects. The second meeting was designed to help participants identify how SIBs are being measured, which savings go to investors, and which applications might work under the SIB model. The third and final meeting was designed to give participants the opportunity to hear about how the philanthropic community is getting involved in SIBs and to discuss the recommendations for this report. Notes from the meetings can be found in the appendix along with copies of the presentations from these meetings.

Background on SIBs

The Pay for Success Toolkit

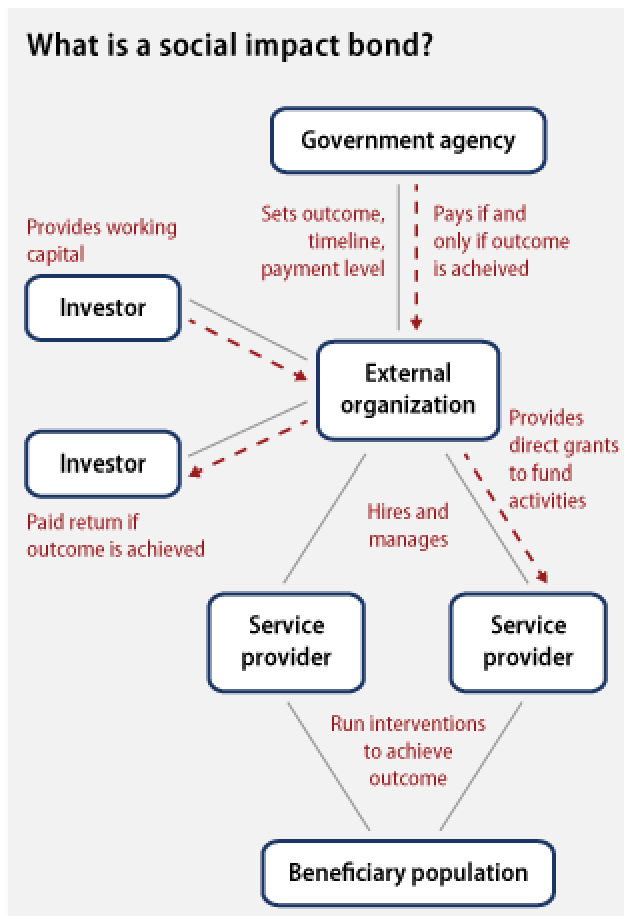
Pay for Success is a broad term used by the Obama Administration, among others, to describe innovative financing mechanisms that bring together public and private agencies and funders to create incentives for providers to achieve better outcomes at lower costs. Pay for Performance (P4P) is one Pay for Success contract type where financial incentives reward providers for achievement of a range of payer objectives, including delivery efficiencies, submission of data and measures to payer, and improved quality and patient safety (Agency for Healthcare Research & Quality, 2012). Shared savings are a financial incentive whereby the payer and provider share any accrued savings, rather than the payer keeping all of the savings in a traditional, fee-for-service model. The alternative to a shared savings model is a risk-based contract, where an organization is paid a fixed amount for a defined set of benefits regardless of the quantity or intensity of services provided. There are multiple types of risk, including utilization, morbidity, demand, price, and beta risk (Oss, 2013). Under a risk-sharing agreement, the payer and provider share both the financial risks as well as the savings that may occur.

SIBs are another type of financing mechanism within the Pay for Success toolkit. A SIB is a financing arrangement between the government and an external organization/intermediary. The government identifies the specific outcome (s) it wants to achieve related to a particular population over an identified period of time and agrees to pay the intermediary a pre-arranged sum *if* the organization achieves the desired outcome. The government does not contract for a particular *intervention* but rather for the *outcome*. The intermediary is responsible for contracting with service providers as well as obtaining investments from outside entities. If the outcome is achieved, the intermediary pays the investors a return on their money. The risk is held by the investor(s) and the intermediary, not the government, with the government only paying if the outcomes are achieved (Costa, Shah, Ungar, & The Social Impact Bonds Working Group, 2012; Spears, 2013).

Godeke & Resner explain that the term SIB was "first used in the UK to describe a Pay-for-Success model in which the outcome performance risk was entirely transferred from government to investors….While earlier discussions have emphasized the full risk transfer of the outcome performance risk from government to investors as essential to the structure, future transactions, especially in the US context, are expected to encompass risk sharing" (2012, p.5). They also note that, **despite the use of the word "bond," a SIB is actually a multi-stakeholder partnership based on contracts; the government's obligation to pay the investors is a contractual obligation and is "distinct from a general obligation, moral obligation or revenue bond**"[emphasis added](Godeke & Resner, p.5). SIBs are a type of social venture that bring together for-profit and non-profit sectors for investment and are an example of the larger realm of new philanthropy that utilizes tools from the business sector in the human services arena. Foundations can function as philanthropic banks and serve as key actors as they bring along the requisite private investors (Salamon, 2013).

Core Components of a SIB

This diagram depicts a typical SIB. In a SIB, the government sets the specific outcome it wants to achieve relative to a well-defined population over a given period of time and contracts with an intermediary to achieve this outcome. Investors provide the up-front capital to pay for the program and an intermediary engages the service providers to deliver the interventions. An independent evaluator monitors the progress of the interventions and an independent researcher determines if the performance targets have been met. If the target is met, the government repays the investor the principal plus interest. There are variations on the design of the SIB, but the key players remain the same (Spears, 2013).



Costa, Shah & Ungar, 2012

Success under a SIB can mean cost avoidance (actual reductions in government operating costs due to the intervention) and outcome improvement. "Success payments" are used by the intermediary to pay interest and principle to investors and pay bonuses to providers who exceed expected performance levels (Dugger, 2013). Social Finance (Leventhal, 2013) lists the following five key steps to launching and implementing successful SIBs:

1) **Originate the deal**: identify government champions and savings opportunities; vet proven models of intervention; perform

nonprofit due diligence; and conduct financial modeling;

2) **Secure government contract**: develop and secure government contract; secure authorization for multi-year contract, including addressing appropriation risk; and formulate a partnership agreement with metrics and payment terms;
3) **Structure the instrument**: develop the operating model and structure the investment vehicle; articulate cash flows, including financial and social returns for target milestones; and finalize the methodology, including metrics and the evaluation strategy;
4) **Raise capital**: recruit investors (foundations and charitable trusts, high net-worth individuals and family offices, institutional investors) and issue the instrument and raise investment capital; and,
5) **Manage the project over the instrument's life**: provide active ongoing project management and financial intermediation; make course corrections as needed; and, coordinate third-party evaluations.

How are SIBs being used—or considered for use?

Social Finance US has identified three tiers of assessment criteria that can be used to evaluate the appropriateness of an intervention to a SIB: whether the intervention is evidence-based, if there are sufficient net savings within the time horizon, and if it is replicable and scalable. Social Finance has identified a series of promising applications for social impact bonds, including prisoner recidivism, juvenile justice, early education, and chronic homelessness (Leventhal, 2013).

PROMISING APPLICATIONS FOR SOCIAL IMPACT BONDS

Preliminary Assessment

		Evidence-based intervention	Sufficient net savings within time horizon	Replicable and scalable
CRIMINAL AND JUVENILE JUSTICE				
Prisoner Recidivism	Post-incarceration programs to reduce recidivism	✔	✔	✔
Juvenile Justice / Disconnected Youth	Post/pre-adjudication intervention services to reduce out-of-home placements	✔	✓	✓
HEALTH CARE				
Aging in Place / Long-term Care	Supportive housing and care coordination to reduce out-of-home healthcare usage	✓	✓	✔
School-based Health Clinics	In-school primary care to reduce medical costs and improve outcomes	✔	✓	✓
Asthma Prevention	Education and home retrofits to reduce asthma-related emergencies	✓	✔	✔
Nurse Home Visiting Programs	Prenatal and early childhood support for first time, low-income mothers to improve family success	✔	✓	✔
OTHER				
Chronic Homelessness	"Housing first" supportive housing to reduce emergency health care and shelter usage	✔	✓	✔
Adult Education	Job training for hard-to-employ populations to fill skill gaps	✓	✓	✔
Early Education	Providing all children with the tools necessary to begin school ready to learn	✓	✓	✔

✔ Aligns with most assessment criteria ✓ Aligns with some assessment criteria ✗ Does not align with assessment criteria

Social Finance US (2013)

The only operational SIBs are found in Peterborough, England and New York City. The other activities described below are SIB designs that are in the process of being implemented, "pre-SIB" projects, or pilot projects intended to demonstrate the feasibility of entering into a SIB. Many states have or are introducing legislation related to SIBs, and Massachusetts is contracting to launch the financing for a SIB focused on juvenile justice and chronic homelessness (Leventhal, 2013).

In the Social Impact Tribune, Goldberg (2013, p.1-2) observes:

> *All this buzz about SIBs isn't just hype. There's something potentially significant going on here, and a lot of smart, serious people are trying to make good things happen. But it's really important to understand that we don't really know how to do any of this yet. Even in the UK, where SIBs started and are well ahead of the US, there are still no published results of any kind from even the first pilot project launched at the Peterborough Prison in September, 2010. Preliminary reports suggest the project seems to be going well, with many lessons learned and refinements made along the way, but we won't have any actual recidivism data until 2014. So we have no idea yet whether using SIBs to pay charities to meet released prisoners at the gate and provide them with comprehensive re-entry services reduces recidivism. And that's the SIB project that's the farthest along in the world.*

A table summarizing the current SIB and pre-SIB activities can be found in the appendix.

Peterborough

The Peterborough SIB in the United Kingdom was launched in 2010. The UK Ministry of Justice contracted with Social Finance to raise capital, structure the financing, and serve as the program intermediary to achieve a 7.5% reduction in recidivism for former prisoners. In this SIB, there was an investment of £5 million by private investors. Social Finance UK funded and managed the proven re-entry programs through select service providers, with the services provided to 3,000 male short-term prisoners released from the Peterborough Prison. If the outcome of lower recidivism of the population served as compared to a control group is achieved, the UK Ministry of Justice and the Big Lottery Fund will pay the intermediary (Social Finance UK) based on predefined metrics. The intermediary will then pay back the investors at a predetermined rate over 8 years (Leventhal, 2013).

The first payments under the Peterborough SIB are not due until 2014, so the success of the project remains to be seen. Detractors observe that neither the prisoners nor the prison itself were randomly selected for participation and that the data available from the Police National Computer (a national database of information available to police and law enforcement agencies throughout the United Kingdom) for the evaluation do not include such elements as mental health or substance abuse histories, which may impact recidivism (Fiennes, 2013). However, others note that the SIB is well-monitored and that the very structure of the SIB as a contract is an asset: "It is a contractual mechanism that ensures investors, commissioners and providers agree on outcomes and maintain constant communication about progress" (Blightly Britain, 2013, p.2).

New York City

New York City (NYC) identified the problem that youth who enter jail as adolescents have a high likelihood of re-entering the system in the years after their release, with 50% of adolescents who leave Rikers Island returning within one year. NYC has created a SIB using Adolescent Behavioral Learning Experience (ABLE), which is an intervention based on cognitive behavioral therapy models (which are evidence-based) that works with 16-18 year olds while they are in jail and post release to improve social skills, problem solving, self-control, and impulse management. The budget for this project is $2.4 million annually for four years (Misner, 2013).

The partners in the NYC SIB are Goldman Sachs (funding the project's delivery and operations through a $9.6 million loan to MDRC), Bloomberg Philanthropies (providing a grant to serve as a guarantee for Goldman Sachs for $7.2 million of investment), MDRC (a private organization responsible for managing daily operations, including oversight of the two service providers), The Vera Institute of Justice (independent evaluator), and the Department of Correction (pays MDRC based on reduced re-admissions). In this model, Goldman Sachs will receive the majority of its investment even if the savings do not accrue as a result of the guarantee fund from Bloomberg Philanthropies, which significantly decreases the risk for Goldman Sachs (Misner, 2013).

If the project achieves greater than or equal to a 10% reduction in re-incarceration, the City payment to MDRC is $9.6 million—the breakeven point. The City payment to MDRC continues to rise at specified intervals based on increased reductions in re-incarceration until the maximum of 20%. If MDRC achieves a reduction in re-incarceration greater than or equal to 20%, the City will pay out $11.712 million. The estimated long-term net savings from this reduction is projected to be $20.5 million, not including the savings used to continue funding the program delivery for youth at Rikers. This SIB is just beginning, so no data are available on its success (Misner, 2013).

Massachusetts

Massachusetts is pursuing two SIBs—one focused on youth transitioning out of juvenile justice and probation systems and a second on the provision of stable housing for chronically homeless individuals. Intermediaries and service providers have been selected for both projects, known in Massachusetts as Social Innovation Financing programs. Massachusetts has a legislatively established $50 million trust fund (with portions appropriated over several years) to support outcome payments for the contracts. Unlike other models, Massachusetts entered into separate procurement processes for the intermediaries and the service providers rather than allowing the intermediaries to select the service providers themselves (Costa & Kholi, 2012; Gilroy, 2013). As Costa & Kholi observe, Massachusetts will need to ensure that the intermediaries have retained enough power to modify the interventions and make adjustments as necessary. If the intermediaries are unable to replace the services or service providers, the SIB may not be successful (Costa & Kholi; Gilroy).

Fresno

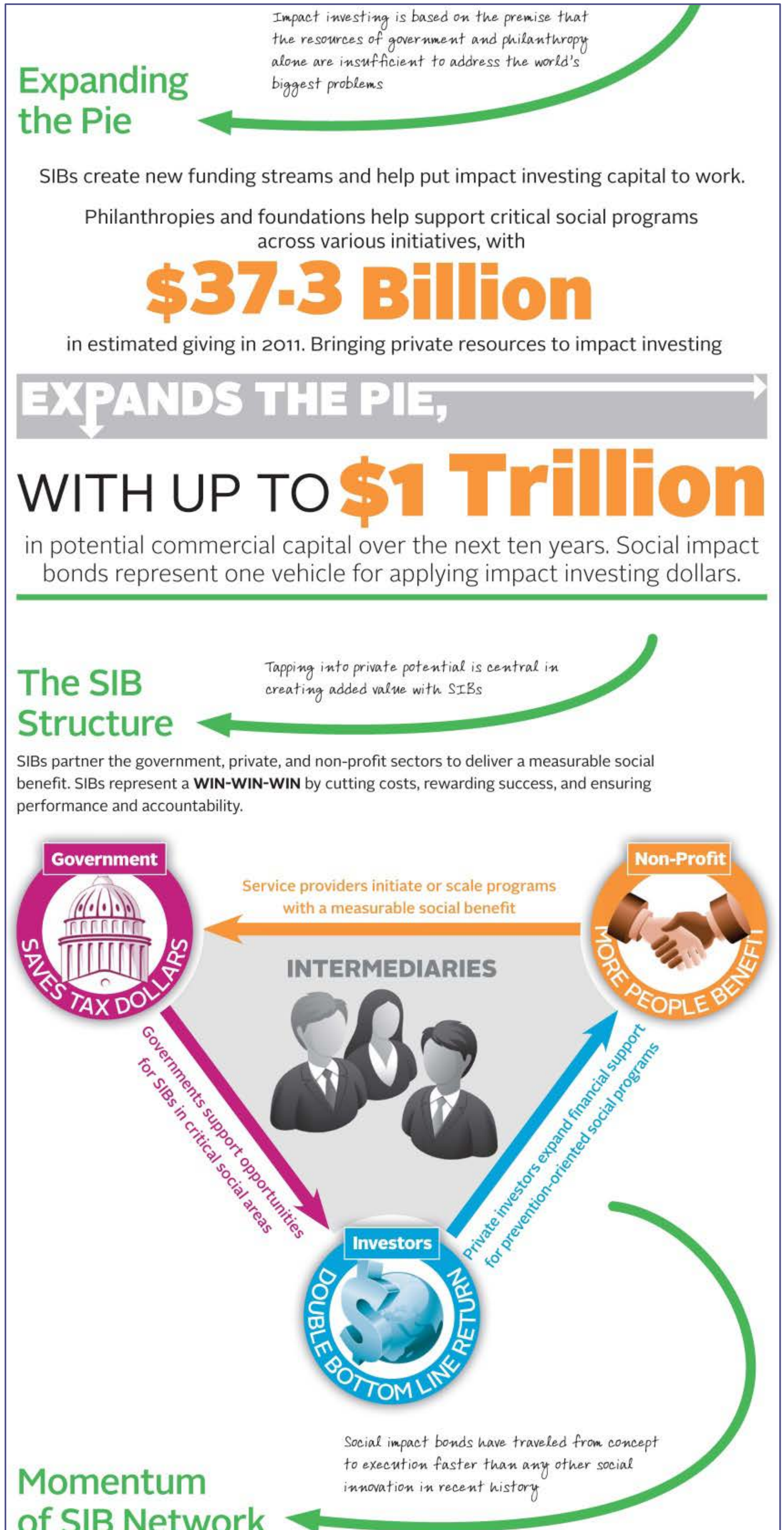
The California Endowment awarded Social Finance and Collective Health a grant to implement an asthma management and prevention program for 200 low-income children. The goal of this program is to improve the health of the children living with asthma and reduce costs from associated emergency room treatments and hospitalizations. In this pilot project, Social Finance is serving as the financial intermediary and Collective Health is the operational intermediary (Leventhal, 2013; Social Finance US, 2013). Two providers with track records in managing asthma will design and manage the program and a third partner will provide technical assistance. Under the project, families will receive home care, education, and support in reducing environmental triggers for asthma. (Social Finance US, 2013). If the project is successful, the partners will seek to create a SIB to serve a larger population (Leventhal, 2013).

Salt Lake City

The United Way of Salt Lake City, Utah has received a combined loan of $7 million from Goldman Sachs ($4.6 million) and J.B. Pritzker ($2.4 million) for its Utah High Quality Preschool Program with the goal of reducing the need for special education services for participants. The project is built upon the investment of the Kellogg Foundation with the Granite School District to identify the outcomes of children served and the cost avoidance that occurs from the children not needing to receive special education services in elementary and secondary schools. Voices for Utah's Children and The United Way are the intermediaries and the Granite School District is responsible for training, quality, and service provision. Utah State University will be evaluating the project and determining the specific quarterly payments over the 12-year term (Schoenberg, 2013). Goldman Sachs and Pritzker will receive 5% interest on their loans if it is successful, as well as specific fees (Alden, 2013). The partners in this SIB are referring to it as a "proof of concept" initiative. The Salt Lake County Council voted to contribute an additional $350,000 to the initiative (Eager, 2013). This occurred after the Utah State Legislature failed to approve financing to support the initiative. With the funds from the Council, the project will be able to serve up to 600 children, all of whom are below the federal poverty level (Schoenberg, 2013).

Benefits of SIBs

SIBs are one of several technologies within the "new frontiers of philanthropy" that utilize a limited supply of social funding and leverage it to provide more human services. Although very important, grant funding is traditionally inefficient because, once the money is spent, it is gone and unable to be reinvested (Salamon, 2013). SIBs offer States and local governments the opportunity to partner with intermediaries and service providers to utilize evidence-based and –informed practices to serve target populations in a



Excerpt of Infographic from the Rockefeller Foundation (Joseph, 2013) flexible manner to achieve stated goals. The States and local governments are not responsible for paying the full cost if the outcomes are not successful and are able to recoup additional monies to reinvest in program continuity if the outcomes are achieved. SIBs are a more sustainable model of financing that share the burden of funding across the public and private sectors. Although somewhat oversimplified, the infographic from the Rockefeller Foundation (Joseph, 2013) highlights the benefits of SIBs and why they are gaining momentum so quickly.

Challenges of SIBs

No SIBs have been proven yet and the challenge will be in quantifying and capturing the savings to fund the returns to the investors (Salamon, 2013). The list of key steps for launching and implementing successful SIBs (p.4-5) illustrates the complexity of successfully designing and implementing a SIB, including the need for active risk management throughout the process (Leventhal, 2013). The complexity of structuring and managing a SIB does lead some to wonder why State governments do not simply fund the evidence-based practices themselves, for those interventions that have demonstrated cost savings in addition to improved outcomes (e.g. Nurse Family Partnership and Multi-Systemic Therapy, see Goldberg, 2013c).

In addition to the costs of the intervention itself, funding needs to be available to pay for the third-party evaluators to certify the project and monitor the results (Duggar, 2013). Also, with the high level of detail that must be addressed, a SIB will only be successful if it is matched to the right intervention and the necessary partners are all at the table. The intermediaries and service providers need to have sufficient flexibility to change the intervention to reach the identified outcome; governments and investors are purchasing an outcome, not a particular service intervention, which is a large shift for many governments. Additionally, private investors may be reluctant to participate in a SIB if they think there is a risk that the government might not pay the investors after the outcome is achieved or if they think the risk is too great or the scale too small (Goldberg, 2013a).

Although many states have introduced or passed legislation relating to SIBs, few have gone beyond authorizing the Governor to sign a SIB contract. According to Goldberg (2013b, p. 12), legislation to establish a SIB would need to "(1) Authorize the SIB contract in which the government agrees to pay for certain outcomes; (2) Appropriate the money as of the payment due date; and (3) Make the appropriation irrevocable." Only Massachusetts has passed such legislation, by obligating the Commonwealth's full faith and credit up to a total of $50 million. In most instances, investors have been secured through a combination of grants and guarantees to mitigate the risk (Goldberg, 2013b).

Workgroup Findings

"Impact investing is going to involve a much bigger departure from business as usual than you think. Much bigger. There are pros and cons galore, and a new level of complexity that will try everyone's patience."
Steve Goldberg (2013, p.3)

The SIB Workgroup was fortunate to hear presentations from national experts on SIBs from multiple perspectives, including those of the intermediaries, government, funders, and technical assistance providers. After each of the meetings, SIB Workgroup participants were issued an anonymous, electronic survey for their completion. The survey was designed to serve as a straw poll to gauge interest in pursuing SIBs in Maryland and identify where participants had outstanding questions or concerns.

Survey respondents indicated that they were surprised to learn about the extent to which SIBs are being studied and implemented in various forms across the nation. Many noted that they now have a better understanding that a project must be the right fit for a SIB, including the timeframe for demonstrating results—ideally within 3-5 years. Others observed that there is a broad range of issues and types of investors that may be involved in SIBs, and that SIBs present a possible mechanism for bypassing policy or budget silos. Finally, several were interested to learn about the private and public funding that is being made available in some instances to guarantee the loans and reduce the risk for the investors.

From the first survey after the July meeting to the second survey after the September meeting, the average rating for the feasibility of SIBs in Maryland increased very slightly. It also increased slightly from the second survey to the third survey at the beginning of October. Below is an excerpt with the survey results:

Based on the information you have received to-date, on a scale of 1-10, do you think a SIB could work for Maryland in the next few years? (1=SIBs are not at all feasible or realistic for Maryland in the next few years; 10=SIBs could definitely be implemented in Maryland to implement in the next few years)

1st Survey Responses:

Min Value	Max Value	Average Value	Standard Deviation	Responses
3.00	8.00	**5.22**	1.86	9

2nd Survey Responses:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.27**	1.35	11

3rd Survey Responses:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.58**	1.31	12

The second and third surveys asked respondents whether they were employees of a State Agency (DBM, DHMH, DHR, DJS, GOC, MSDE). The State Agency employees gave slightly higher ratings in the third survey than in the second survey, and there were more respondents in the third survey:

2nd Survey Responses for State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	7.00	**4.83**	1.17	6

3rd Survey Responses for State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.44**	1.42	9

The non-State Agency employees (5 in the first survey, 3 in the second survey), gave the following responses, which also increased slightly:

2nd Survey Responses for Non-State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.80**	1.48	5

3rd Survey Responses for Non-State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
5.00	7.00	**6.00**	1.00	3

The survey respondents were asked to describe their rationale for their ratings. Several respondents indicated that, **while SIBs are technically doable, they will only be feasible in Maryland if the leadership (at the Executive and Legislative branches) is supportive, if there are champions for the work within State government, and if funding is available to support all of the components of the SIB—including the future repayment and success payments. There was general agreement that, if the right project is selected for a SIB, it could be of great benefit to Maryland; however, there are still many details that would need to be addressed.**

As part of the final survey, respondents were provided with a list of populations/intervention areas for a potential SIB and were asked to select the topic areas that they thought have the greatest potential to work as a SIB in Maryland. The two topic areas selected most often were juvenile justice recidivism reduction (11 out of 12 respondents) and early childhood education/pre-K (8 out of 12 respondents).

Answer	Response
Asthma	4
Diabetes	2
Early Childhood Mental Health	3
Early Childhood Education/Pre-K	8
Home Visiting	4
Pediatric & Primary Care Integration	1
Juvenile Justice Recidivism Reduction	11
Prisoner Re-Entry/Recidivism Reduction (adult offender)	4
Child Welfare	3
Housing First/Homelessness-Chronic Homeless Population	3
Housing First/Homelessness-Families	1
Housing First/Homelessness-Youth Aging Out of Child Welfare/Juvenile Justice	3
Elder Care	1
Hunger	1
Other: Maryland Safety Compact	1

In its final meeting, the Workgroup discussed the multiple arenas in which SIBs are being discussed in Maryland, including by the Mayor of Baltimore City's Pay for Success Workgroup. The City of Baltimore applied to receive technical assistance from the Harvard Social Impact Bond Lab, and the Maryland Early Childhood Investment Council, a subgroup of the Early Childhood Advisory Council, is interested in SIBs and other alternative financing mechanisms. The Workgroup is hopeful that these entities and others will use the information gained through this process to assist them with decision-making regarding the pursuit of SIBs or other pay for success financing.

Conclusion

The workgroup emphasized two particular elements as critical for consideration by anyone interested in pursuing a SIB in Maryland:

1) The evaluation is a critical component; the contract must have clear, measurable indicators and outcome measures to attract investors; and,
2) SIBs require a negotiation process, and the government is not necessarily the driver of the negotiation process.

Based on the discussions at the Workgroup meetings and the results of the surveys, the Workgroup has indicated that SIBs could potentially be implemented in Maryland, if there is sufficient leadership from the Executive Branch and the General Assembly, as well as a clearly defined population and target outcome.

The Workgroup ultimately determined that SIBs have tremendous potential but the viability is dependent on the population and intervention. It is the collective hope of the Workgroup that Maryland continues to investigate and pursue creative financing options for human services, whether through SIBs or other financing mechanisms.

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APPENDICES

Appendix A: Table of SIBs, Pre-SIBs, and SIB-Like Activity

Appendix B: July 17, 2013 Meeting Materials

Appendix C: September 10, 2013 Meeting Materials

Appendix D: October 7, 2013 Meeting Materials

Appendix A: Table of Operational SIBs, Pre-SIB Activity, and SIB-Like Activity

Location	Population	Investor(s)	Intermediary(ies)	Evaluators	Notes on Initiation & Development
OPERATIONAL SIBS					
Peterborough, UK	Prisoner Re-Entry	Private, raised by Social Finance UK	Social Finance UK	RAND Europe	Launched in 2010; data unavailable until 2014. UK Ministry of Justice and the Big Lottery Fund will pay Social Finance UK who will pay the investors back at a pre-determined rate over 8 years.
New York City	Juvenile Offenders	Goldman Sachs	MDRC	The Vera Institute of Justice	Bloomberg Philanthropies provided a grant to serve as a guarantee for $7.2 million of the $9.6 million investment. Break-even point for the SIB is achieving a 10% reduction in re-incarceration.
PRE-SIB ACTIVITY					
Massachusetts	Youth transitioning out of juvenile justice & probation services	Private, raised by Third Sector Capital Partners	Third Sector Capital Partners (service providers are procured directly, although ROCA was selected in partnership with Third Sector)	Unknown (information not found)	MA has legislatively-established trust fund to support outcome payments. Separate procurements processes for the intermediaries and the service providers. In September 2013, MA received a federal grant that will expand the capacity of the SIB by an additional 400 youth.
	Chronically homeless individuals	Unknown (information not found)	Unknown (information not found)	Unknown (information not found)	
SIB-LIKE ACTIVITY					
Fresno, CA	Low income children with asthma	Grant from The California Endowment	Social Finance (fiscal intermediary) and Collective Health (operational intermediary)	Unknown (information not found)	Grant funded to test idea; if successful, plan is to create a SIB to serve a larger population.
Salt Lake City, UT	Low-income preschool children	Goldman Sachs & J.B. Pritzker	United Way, Voices for Utah's Children & Granite School District	Utah State University	Kellogg Foundation partnered with the school district to identify alternative financing based on outcomes over a period of several years. Salt Lake County voted to invest an additional $350,000, enabling the project to serve an additional 150 children. The SIB has a 12-year term, with quarterly payments.

APPENDIX B: July 17, 2013 Social Impact Bond Meeting

- July 17, 2013 Social Impact Bond Meeting Agenda
- July 17, 2013 Social Impact Bond Meeting Notes
- Resources on Social Impact Bonds (SIBs): Reading Materials
- Legislative Request and Department of Legislative Services Report
- Presentation by Dr. John Spears - Social Impact Bonds: Introduction
- Presentation by Dr. Lester Salamon - Towards a New Era of Social Purpose Finance
- Presentation by Dr. Robert Dugger - Early Child Human Capital Investment: "Pay for Success" Finance

Social Impact Bond Summer Study 2013

Wednesday, July 17, 2013

9:00 am to 12:00 pm

The Innovations Institute at the University of Maryland
School of Social Work Training Room
306 W. Redwood Street, Baltimore

Meeting goal: to provide an overview of Social Impact Bonds (SIB), and examples of SIB projects.

Agenda

9:00 am to 9:30 am	John V. Spears, PhD., has managed Towson University's budget forecasting and technical assistance contract with the Department of Human Resources and now the Maryland State Department of Education (MSDE) for the past 16 years. An earlier career in banking and experience with MSDE's Research Forum of last November provided additional interest in Social Impact finance. Dr. Spears will present the basics of Social Impact Bonds, and make the case for serious consideration of this new idea in the context of the summer study.
9:30: am to 9:40 am	Kyle McKay, Department of Legislative Services' (DLS) analyst, will present the DLS Report on SIBs –via conference call.
9:40 am to 10:40 am	Dr. Salamon, Founding Director of the John Hopkins University's Center for Civil Society Studies, will present a broad overview of the "new frontiers of philanthropy" including Social Impact Bonds. For over 20 years, Dr. Salamon has been exploring the important role that private, nonprofit organizations have come to play in the operation of public programs and the solution of public problems both in the U.S. and in the world.
10:40 am to 11:40 am	Robert Dugger, Chairman of the Board of Advisors at ReadyNation in Washington DC, will present "Early Childhood Social Impact Finance" and he will discuss the two most recent ReadyNation working papers which focus on contract specification and financial instrument choice - two critical operating features of early childhood pay for success projects.
11:40 am to 12:00 pm	Workgroup: Questions and Answers/Discussion

Social Impact Bond Summer Study 2013

Wednesday, July 17, 2013

9:00 am to 12:00 pm

The Innovations Institute at the University of Maryland
School of Social Work Training Room
306 W. Redwood Street, Baltimore

Meeting Notes:

Meeting goal: to provide an overview of Social Impact Bonds (SIBs also known as "Pay for Success bonds"), and examples of SIB projects.

Members in Attendance:
Michelle Zabel, The Institute for Innovation & Implementation, *Chair*
Nathan W. Bowen, Department of Budget & Management
Nancy Fitzgerald (for Marcella Franczkowski), Maryland State Department of Education
Jeanne-Marie Holly, Maryland State Department of Education
Farid Keshavarz, Department of Public Safety & Correctional Services
Delegate Samuel Rosenberg, Maryland General Assembly
Dan Feller, Governor's Office for Children
Angela Lagdemeo, Director of Policy and Planning, Department of Human Resources
Netsanet Kibret, Deputy Director of Government, Corporate and Community Affairs, Department of Human Resources
Miriam Shark, Annie E. Casey Foundation
Margaret Williams, Maryland Family Network
Beth Harber for Terry Staudenmaier, Abell Foundation
Rolf Grafwallner, Maryland State Department of Education

Observers: Ari Blum, George Failla, Louise Corwin, Renee Spence

Staff: John Spears, Roann Tsakalas, Tranae Hardy

Welcome by Chair, Michelle Zabel. Michelle briefly reviewed the statement of work and goals for the Summer Study on SIBs. Then workgroup members and observers introduced themselves.

The first presenter was **Dr. John Spears**, Senior Human Services Consultant at Towson University's Regional Economic Studies Institute and data analyst for the Maryland State Department of Education. Dr. Spears set the stage for an understanding of SIBs using his PowerPoint presentation entitled "Social Impact Bonds: Introduction." On Slides 2-5, Dr. Spears laid out the basic rationale for SIB's, including the important point that there are a number of human capital building programs, including early childhood health and education, prison recidivism and homelessness, that have very solid evidence of success and promise marketviable returns. Slide 5 underlines the large size of the potential market for SIBs totaling $80 trillion counting worldwide debt securities in 2011, of which even a tiny slice could revolutionize the potential for human capital investment in the US. Slide 6 provides definitions of SIBs, noting that they are very new, and that even basic descriptive terms in the literature can vary.

Slide 7, presented in five steps, built a schematic of the ideal SIB, with working definitions of each of the major component organizations (players) in the structure grouped on Slides 8 and 9. The role of intermediary was emphasized as central in organizing and supporting the undertaking. The success of the SIB relies on the success of the service providers, of course, but the essence of the SIB is the savings realized by government and refund of those savings to investors, based on the findings of the researchers that the service were successfully delivered and made a real difference in the subject population. If the program were unsuccessful, private investors could lose all or a portion of their investment.

Slide 10 showed a map of geographical distribution of SIB interest in the US as of early 2013. A number of states, including Maryland, have at least begun investigations of the idea (shown in gray). Light green shows more SIB activity. The next darker green is Utah and Massachusetts which are already involved in SIBs but have not yet completed implementation. Massachusetts is having trouble getting its SIB off the ground. New York is darkest green because New York City has the nation's only operational SIB as of July of 2013. If New York can reduce recidivism among juveniles incarcerated on Rikers Island by 10% in 2 years (considering several cohorts of inmates), Goldman Sachs stands to make a maximum of $2.2 million return on their $9.6 million investment. There might also be savings left for government if the program is extremely successful.

Question – how will Goldman get their return?
Response – Goldman will receive money from unspent government funds that did not have to be spent on jail services.

Kyle McKay, Department of Legislative Services' (DLS) analyst, presented the Department of Legislative Services Report Kyle by phone. Mr. McKay briefly reviewed the report listing his objections to the viability of the SIB concept. These included an apparent lack of sufficient savings to reward investors based on analysis of Maryland Dept of Corrections marginal cost data, a lack of existing mechanisms in Maryland to match one-year budget cycle planning to the long-term commitments needed to pay off SIB investors, and an assertion that, if the SIB programs were really so solidly successful, they should be financed with general revenue bonds.

Dr. Lester Salamon, Founding Director of the John Hopkins University's Center for Civil Society Studies, presented a PowerPoint entitled, "Towards a New Era of Social Purpose Finance." Dr. Salamon stated that SIBs are one method to fund human services, but that the traditional paradigm of philanthropy has changed. While the beneficiaries remain the same, there are new sources of funding, new actors, new tools, and new agents. Examples of new actors include capital aggregators, secondary markets, social stock exchanges, and foundations acting as philanthropic banks. These new methods are attracting the top foundations. There are about 415 new conversion foundations that fund the privatization of services (top slide of page 2). Leverage runs behind these new funding projects. These new frontiers of philanthropy, such as social ventures and investment capital, demonstrate a way to take a limited supply of social funding and leverage it to provide more human services. There has been a great proliferation in types of funders and the sheer number of funders over the last few decades.

There is investment capital willing to pay for operating expenses for human services programs. Grants are inefficient because once the money is spent it is gone and not able to be reinvested. These capital tranches have risk and return requirements. The low income housing model means that you need tax credits and other incentives to get funding from the bank and contracts with builders. Governments need to utilize resources to come up with guarantees for investors. For example Gates is putting money into charter schools that involve education management organizations. Social ventures are exploring a mix of investments in for profits and non profits. Governments may have to create legal structures for these investment strategies to work. SIBS rely on a social and financial return. The new focus in human service investment is on metrics and outcomes. People are still the beneficiaries as before in the traditional funding model of grants.

Page 3, bottom slide lists the new actors, and includes the new intermediaries. New tools equal new financing which was not used before in human services but used in business. The new agents are the new service providers. We are still in the early stages for new sources of funds. Capital aggregators are community development finance institutions, such as the Bank of America's Capital Access fund for housing development (page 4, top slide). Globally there is $300 billion being used by capital aggregators for operating funds. Page 4 slide 2 gives examples of social purpose secondary markets, such as Habitat for Humanity and Self Help North Carolina. The UK has established the Social Stock Exchange UK where investors can buy and sell stock when they want. New foundations are functioning as philanthropic banks. They utilize balloons and equity investment, and now are dipping into their endowments and principle funds. Foundations are key actors because they bring investors.

The ILO Microinsurance Innovation Facility is convincing insurance companies to provide low cost per unit insurance for pooled small companies. All-Life insures HIV/AIDS victims in South Africa which has resulted in improved client health. The UN World Food Program pays Ethiopian farmers for work on irrigation projects to protect against floods, and the insurance pays if the irrigation project fails and there is a flood. SIBs get ahead of the curve for trying something new. Government is willing to pay for things that may not work, whereas investors want proven strategies to increase the likelihood that they will have a return on their investment. No SIBs have been proven yet. The challenge is in capturing savings to fund the returns to investors.

The demand factors for human services have been present but what is new is the new supply of financing. A new set of actors have emerged globally. Social entrepreneurs are putting their talents to serve the world's problems. For example, the production process for one pair of eyeglasses in India is now $3. Creating competition and new financing brought down the price so many more children can attend school because they can see. Another example is the access to sanitary napkins and how to make sanitary napkins that are cheap and reusable for Third World women. *The Fortune at the Bottom of the Pyramid,* by C. K. Prahalad, argues that the bottom of the pyramid is penalized as these people pay more because there is no competition to provide them products. Competition will bring them cheaper products. These examples are business models that have a return and do something good for society. Dot-com investor, Charly Kleissner has invested $10b in Indian glass makers through impact funding (see KL Felicitas Foundation at http://www.klfelicitasfoundation.org/ .

Dr. Salamon referred to the book called *Philanthro-Capitalist,* by Matthew Bishop and Michael F. Green, which examines the work of "social investors" and how they are using business strategies to fund human services in exchange for results and accountability. He discussed an example of this perspective was evident at an Social Impact conference in Baltimore last year where business school students attended that want to make a financial and social impact. The next step is for government to visualize what can be done in terms of utilizing these new human service financing methods. Dr. Salamon's new book *New Frontiers of Philanthropy* may be translated into training materials. Last slide on page 9 lists implications of new financing strategies for states. Dr. Salamon stated that we need to do this locally in Baltimore and the State. The new financing strategies require new skills in order to bundle the factors together around concrete projects with potential.

Government needs to establish what problem it wants to solve, and talk to investors and they will be able to come up with financing strategies. Investors will help write a business plan and assist in going after the money. Enterprise brokers, like the Kellogg Foundation want to get into this arena, so they hired Blueprint Partners and they did a scan of what is impacting the food problem in the country. They presented what a few organizations are doing to help, and the Kellogg Foundation started to work with them. KIPP, an educational management organization, went to Gates Foundation for facilities money and Gates hired consultants to create a bond guarantee. Charter schools may fail 30% of the time which is a low failure rate and so bonds were sold successfully on Wall Street.

State government and local government need to sit down with the investment world to see what programs would work with these new financing models. Governments can incentivize investors with tax incentives and other tools to bring actors to the table and not use savings to fund investment. Maryland needs to look at laws, procurement and the budget process and how they could support this type of investment. Does Maryland have the ability to offer bond incentives that could be used for small programs, such as Friends of the Family?

Dr. Robert Dugger, Chairman of the Board of Advisors at ReadyNation in Washington DC, presented "Early Child Human Capital Investment: 'Pay for Success' Finance" PowerPoint, and he discussed the two most recent ReadyNation working papers which focus on contract specification and financial instrument choice. Dr. Dugger's experience is in government and banking. He worked in hedge funds for 20 years as partner, and then retired. His personal interest is in conservation in Tanzania. In order to conserve the wildebeest, which migrate outside the Tanzania National Park, Dr. Dugger formed the Vermitti Company which purchased an additional 350 acres to extend the national park. He worked with Maasai tribal groups to preserve this area which is the size of Delaware. This extension ended poaching which was out of control and threatening the wildebeest herds. The investors were able to realize a return on their investment because a few very exclusive hotels were built on the 350 acres to support the preservation effort and pay back the investors.

The ReadyNation organization was born from support from the Pew Charitable Trust. ReadyNation's focus is on building business leaders' interest in investing in children in their area in order to create the greatest growth in human capital. ReadyNation's study found that 100 million people are involved in raising children – baby food, doctors, parents, teachers, etc. The child powered industry is 30% larger than other business sector. Therefore, investing in children ages 0 to 5 will yield a high return. Dr. Dugger believes that the highest return is in investing specifically in the zero to 3 child population. Research indicates that pre-birth care postiviely shapes a child's life outcomes.

In order for governments to attract investors they must "monetize the game." The work must be organized by contracts and reflect a business model – see paper on http://www.readynation.org/sib. The role of ReadyNation is to convince businesses to invest in children. The key attraction to business is that an early investment in children will mean that they will cost less as they get older in terms of school and public health needs, and eventually, training needs at the time of employment.

On slide 3, Dr. Dugger points out that the Pritzker Foundation backed ReadyNation and Jeff Liebman's Social Impact Bond Lab at Harvard University. Pritzker and other foundations are working to get governments interested in SIBs. Slide 7 explains Pay for Success. Dr. Dugger explains that the object of investment is whatever outcomes we deem to be important. Slide 8 explains all the actors at the table and their roles. Slide 9 demonstrates how a SIB works. Third party evaluators cost money but their role certifies the project and is vital to investor buy in. Government must prove through independent statistical accountability that the project is working to satisfy the investor.

Slide 9 demonstrates how the SIB drives success. Eighty percent is ideally paid to the intermediary. Government needs a cushion of 20% which it reserves from the savings. There are contracts between the intermediary and the service provider, the intermediary and government, and a contract among all involved parties. Massachusetts created a special fund to prefund their SIB; this was done through a state statute to encourage agencies to enter into contracts and this money can be put aside in a "sinking fund." Right now the Bank of America in Maryland wants to get into social financing, for Community Reinvestment Act purposes. Maryland must create standardized contracts, standardized research methods, statutes, etc. if they want to begin a SIB financing strategy.

Slide 11 puts together all the necessary steps in a SIB. Salt Lake County Council voted to set aside $350K for success payments for the new PreK SIB program. These first early education SIB projects have taken 4 years to get to this point. Slide 13 lays out timeline of what needs to be accomplished to implement a SIB and how long each step takes. Slide 14 explains points of potential savings for a few children's programs. Slide 15 lists who invests in SIBs. Slide 17 demonstrates a PreK SIB 10 year payout. Another example - neo natal intensive care lasts on average 90 days and avoiding one hospital stay can realize a savings of $200k which can be paid back over time. Slide 18 shows examples of PreK savings realized through special education service avoidance. Slide 21 shows data from Lehigh Valley County School System, PA and the potential savings from Pay for Success. Slide 22 outlines the Pay for Success model for Salt Lake City, UT. The SIB contracts go to the Utah legislature in spring 2014 for approval.

The Chair, Ms. Zabel, thanked everyone for coming and thanked the speakers for their participation. She also reminded the group that the next meeting will be on September 10 from 9 am to noon at the Innovations Institute.

Approved at September 10, 2013 meeting.

Resources on Social Impact Bonds (SIBs)

Highly Recommended:

Community Development Investment Review. "Social Impact Bonds: Lessons Learned So Far." http://www.frbsf.org/publications/community/review/vol9_issue1/social-impact-bonds-lessons-learned.pdf, and other SIB articles.

Steven Godeke and Lyel Resner. "Building a Healthy & Sustainable Social Impact Bond Market: The Investor Landscape," for the Rockefeller Foundation, December 2012. http://www.rockefellerfoundation.org/news/publications/building-healthy-sustainable-social This publication surveys likely SIB investors, informing on a crucial element of SIB feasibility.

Jeffrey Liebman, "Social Impact Bonds: A Promising New Financing Model to Accelerate Social Innovation and Improve Government Performance," Center for American Progress, February 2011. http://www.americanprogress.org/issues/2011/02/social_impact_bonds.html

ReadyNation. Several papers on Social Impact Bonds. http://www.readynation.org/sib

Social Finance. "Peterborough Social Impact Bond." 2011. http://socialfinanceus.org/sites/socialfinanceus.org/files/SF_Peterborough_SIB_0.pdf

Recommended:

Lisa Barclay and Tom Symons, "A Technical Guide to Social Impact Bonds," Social Finance, January 2013. http://www.socialfinance.org.uk/sites/default/files/sf_svc_guide.pdf

Businesswire.Com. "Pritzker, Goldman Sachs Announce $20 Million First Phase of Early Childhood Innovation Accelerator Initiative." June 13, 2013. http://www.businesswire.com/news/home/20130613005888/en/Pritzker-Goldman-Sachs-Announce-20-Million-Phase

The Center for American Progress. http://www.americanprogress.org/search/?query=new+financing+tool – link to several reports on SIBs.

Kristina Costa, et al. "Frequently Asked Questions: Social Impact Bonds", Center for American Progress. December 2012. http://www.americanprogress.org/issues/economy/report/2012/12/05/46934/frequently-asked-questions-social-impact-bonds/

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Emily Bolton and Louise Savelle. “Towards a New Social Economy: Blended Value Creation through Social Impact Bonds.” Social Finance UK, March 2010, http://www.socialfinance.org.uk/sites/default/files/Towards_A_New_Social_Economy_web.pdf .

Steve Goldberg. “The Social Impact Bond Tribune.” January 31, 2013.
http://payforsuccess.org/sites/default/files/sib_trib_no._2.pdf

Steven Greenhut. “California’s Scary New Way to Raise Public Money.” Apr 28, 2013.
http://www.bloomberg.com/news/2013-04-28/california-pushes-social-impact-bond-gimmicks.html

Jonathan Greenblatt. “Social Impact Bonds Bring Social Innovation to the Bay State.” March 28, 2012. http://www.huffingtonpost.com/jonathan-greenblatt/shot-heard-round-the-worl_b_858961.html

Goldman Sachs. “As city budgets decline, an innovative effort suggests a new way to leverage private capital.” http://www.goldmansachs.com/s/2012annual/client-stories/innovation/?cid=PS_01_43_06_00_00_00_01

Harvard Kennedy School, Social Impact Bond Technical Assistance Lab, http://hks-siblab.org/

Kyle McKay, the author of Md’s DLS report, in the Stanford Social Institute blog:
http://www.ssireview.org/blog/entry/debunking_the_myths_behind_social_impact_bond_speculation

J. P. Morgan. “Impact Investments: An emerging asset class.” Nov 29, 2010.
http://www.rockefellerfoundation.org/uploads/files/2b053b2b-8feb-46ea-adbd-f89068d59785-impact.pdf

Kauffman Foundation – ReadyNation. “Early Childhood ‘Pay-For-Success’ Social Impact Finance: A PKSE Bond Example to Increase School Readiness and Reduce Special Education Costs.” March 2012,
http://humcap.uchicago.edu/RePEc/hka/wpaper/Dugger_Litan_2012_early-childhood-pay.pdf Also, “Progress Report: Social Impact Finance.”
http://www.readynation.org/uploads/db_files/KauffmanReadyNationPKSEPresentation.pdf

Kauffman Foundation – ReadyNation.: A PKSE Bond Example to Increase School Readiness and Reduce Special Education Costs.” http://www.readynation.org/pkse-webinar-april-3

Kristina Costa and Jitinder Kohli. "Social Impact Bonds: New York City And Massachusetts To Launch The First Social Impact Bond Programs In The United States." November 5, 2012. http://www.americanprogress.org/issues/economy/news/2012/11/05/43834/new-york-city-and-massachusetts-to-launch-the-first-social-impact-bond-programs-in-the-united-states/.

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Third Sector Capital Partners. “Preparing for a Pay for Success Opportunity.” 2013. http://www.thirdsectorcap.org/wp-content/uploads/2013/04/Third-Sector_Roca_Preparing-for-Pay-for-Success-in-MA.pdf . This paper shows what ROCA, the service provider chosen to run Massachusetts’ juvenile justice intervention, went through to prepare for application to the state to be a part of the State’s social impact bond initiative.

THE MARYLAND HOUSE OF DELEGATES
Annapolis, Maryland 21401-1991

RECEIVED
APR 10 2013

April 9, 2013

Dr. Lillian M. Lowery, Ed.D., Superintendent
Maryland State Department of Education
200 W. Baltimore Street, Suite #1
Baltimore, MD 21201

Re: Social Impact Bonds

Dear Dr. Lowery:

The House Appropriations Committee would like MSDE to review the merits of issuing Social Impact Bonds (SIB) in Maryland. We encourage you to involve other possible state entities and to examine existing SIB models and the feasibility of implementing these models in Maryland. We have attached a copy of a Department of Legislative Services' report on Social Impact Bonds for your consideration as you do this review.

This study will foster a better understanding of SIBs, including their functions and potential benefits for Maryland. We ask that your report be provided to the Committee by December 1, 2013 to help guide any appropriate action that may be taken in the future.

Thank you for your consideration of this matter and if you have any questions please call Kaitlyn Shulman at (410) 841-3407.

Very truly yours,

Mary-Dulany James
State Delegate,
Harford and Cecil Counties

John Bohanan
State Delegate
St. Mary's County

cc: The Honorable Delegate Samuel I. Rosenberg
The Honorable Norman H. Conway

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Evaluating Social Impact Bonds as a New Reentry Financing Mechanism: A Case Study on Reentry Programming in Maryland

Department of Legislative Services
Office of Policy Analysis
Annapolis, Maryland

January 2013

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Executive Summary

Social impact bonds (SIBs) represent a relatively new concept for financing and contracting for the delivery of social service programs. They are designed with the intention of shifting the financial risk of performance-based payments from providers onto investors. This allows governments to, in theory, increase the portion of funding linked to the achievement of an outcome without damaging the funding of service providers.

Although actual bonds are not typically issued, the government contracts with investors, a program manager, and nonprofit service providers for a SIB program. If an independent evaluator finds that the SIB program produced outcomes equal to or greater than the targeted levels, then the government reimburses the investors for their capital, along with a return on investment. In the event that the program does not produce the targeted outcomes, then the investors receive no compensation from the government and lose their capital investment.

The Department of Legislative Services (DLS) has conducted a review of the feasibility, potential benefits, and risks associated with financing reentry programs using SIBs. Reentry programs are of particular interest to the Department of Public Safety and Correctional Services (DPSCS) based on its mission. Reentry programs are also generally considered a strong candidate for SIBs due to the potential for large cost savings to the government through the successful reduction of re-imprisonment. Based on the benefits commonly associated with SIBs, DLS evaluated the potential of SIBs to generate cost savings, help finance social programs, shift outcome risk, increase innovation in reentry programming, and build more rigorous evidence for policy decisions.

Even when using a set of highly optimistic assumptions, it is clear that pilot reentry programs cannot self-finance their operations. Because pilot programs cannot create a large enough reduction in demand to close a facility, the cost dynamics are driven by much smaller marginal cost savings. As a result, a program that produces a 10% reduction in recidivism for 250 prisoners per year over five years will only result in minimal avoided imprisonment costs. Before including the cost of direct services, the fixed costs of designing the contract, compensating a third-party intermediary, and conducting an independent evaluation, at \$700,000 collectively, would alone exceed the fiscal benefits. Including service costs of \$2,500 per participant, the program would result in a net fiscal impact of -\$3.9 million. Doubling the size or assumed effectiveness of the program would not result in a positive net fiscal impact.

These results indicate that the additional costs of a SIB program cannot be justified by offsetting savings. Other potential benefits do not justify the cost or complexity of a SIB program either. Given the difficulty of linking the evaluation of a social program to a highly complex contract centered on an outcome payment, the government may actually increase its operational risks in undertaking a SIB. The government would also need to budget upfront for the contingent liabilities of outcome payments. As a result, a SIB program would increase both budgetary pressure and operational risks.

Reentry programs can have great social value independent of their fiscal impact. The decision to finance them should be made independent of whether or not they can be self-financed through cost savings and a SIB mechanism. Because they are especially valuable and effective when integrated and combined with larger scale policies aimed at reducing recidivism and increasing public safety, DLS recommends that DPSCS continue to directly finance reentry programs while pursuing other organizational and policy changes likely to have greater impacts while posing less risk than a SIB financed program.

Evaluating Social Impact Bonds as a New Reentry Financing Mechanism: A Case Study on Reentry Programming in Maryland

Reasons for This Study

In the fiscal 2013 Overview of the Department of Public Safety and Correctional Services (DPSCS), the Department of Legislative Services (DLS) recommended that DPSCS begin examining the possibility of utilizing social impact bonds (SIB) by developing a request for information. In the interim, DLS has conducted a parallel review of the feasibility, potential benefits, and risks associated with financing reentry programs using SIBs.

The benefits commonly associated with SIBs are numerous. According to nonprofit organizations associated with their development, SIBs offer governments the ability to raise new revenue while shifting outcome risk for specific programs to the private sector. Under a SIB, the government contracts to reimburse investors only when positive outcomes are achieved. Payment amounts are based on the cost savings that the government realizes from the program. Because of the emphasis on outcome-based payments, SIBs help increase the rigor of evidence in policy decisions by requiring programs to be evaluated using advanced statistical methods.

These potential advantages are especially promising for reentry programming within DPSCS. Reentry programs can reduce the rate of recidivism, thereby reducing the long-term cost of incarceration. Beyond the potential cost savings, improving offender reentry into the community and reducing recidivism rates is a key part of the department's mission, especially as it moves forward with its reentry focused reorganization plan. However, past efforts to implement reentry programming in Maryland have not produced measurable improvements. Implementing a SIB, if feasible, could help stimulate innovation in programming while increasing the evidence base for future decisions.

This report evaluates whether SIBS can (1) generate cost savings; (2) help finance social programs; (3) shift outcome risk; (4) link payments to outcomes; (5) increase the rigor of evidence used in policy decisions; and (6) stimulate innovative solutions.

Following a brief introduction to the mechanics of SIBs, this funding option will be evaluated relative to each of these categories of potential benefits for a reentry program.

Background on Social Impact Bonds

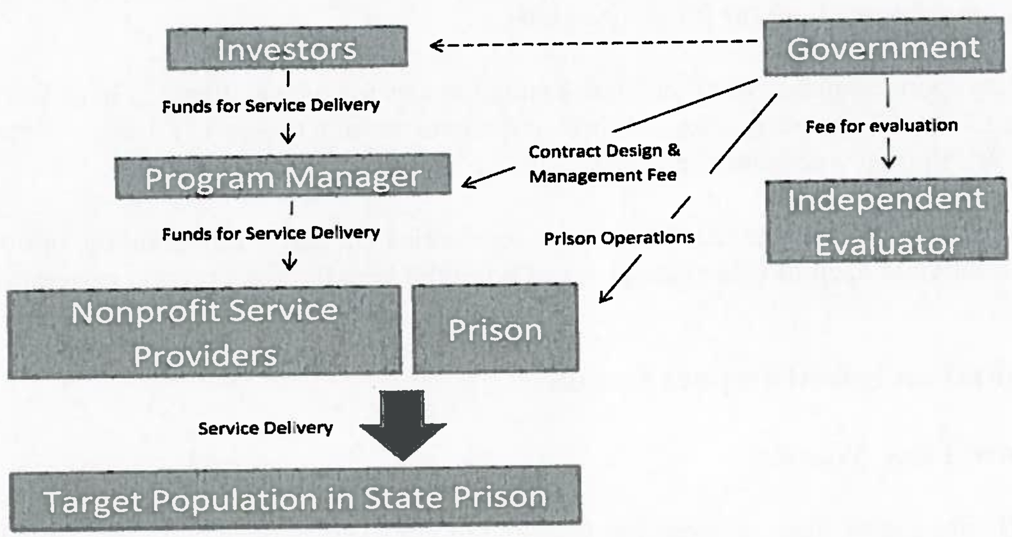
How They Work

SIBs are a new form of a performance-based contract. Under more traditional forms of performance-based contracts, governments typically provide a fixed rate of reimbursement based on the costs that contractors incur. In addition to this fixed rate, performance-based contracts include provisions for reimbursements based on some combination of quality and outcome measures.

Under a traditional performance-based contract, providers, especially smaller community based nonprofits, can have solvency challenges associated with unpredictable cash flows. If 20% of normal contract funding is based on an outcome that is not achieved, this may cripple the operational funding of the nonprofit. The design of a SIB is intended to remedy this problem by providing the upfront working capital to service providers from external investors. Thus, if an outcome is not achieved, it is the investors who lose money, not the service providers. This allows jurisdictions to, at least in theory, increase the portion of funding linked to the achievement of an outcome without damaging the solvency of service providers.

Exhibit 1 shows the key parties and relationships for funding and service delivery in a SIB reentry model. Although actual bonds are not typically issued, the government contracts with investors, a program manager, and nonprofit service providers for a SIB program. Investors provide funding to the program manager. The program manager disburses funds to nonprofit partners who deliver the services. As services are delivered, an independent evaluator funded directly by government conducts a rigorous statistical program evaluation. If the evaluator finds that the SIB program produced outcomes equal to or greater than the targeted levels, then the government reimburses the investors for their capital, along with a return on investment (ROI). In the event that the program does not produce the targeted outcomes, then the investors receive no compensation from the government and lose their capital investment.

Exhibit 1
Basic Illustration of a Social Impact Bond Reentry Model



Source: Department of Legislative Service

Regardless of the outcome, the government compensates the program manager and independent evaluator for the contract design, management fee, and independent evaluation. The government also operates the prison facility where the target population resides and the data systems used to conduct the evaluation. In Exhibit 1, the thin arrows represent funding flows, and the thick black arrow represents service delivery.

Under the traditional conception of a SIB, 100% of the payment is linked to the achievement of performance outcomes. In other conceptions, the risk incurred by investors can be decreased by tying less than 100% of the payment to an outcome. In all cases, the investors are compensated with a return on an investment that resembles the interest on a bond if the outcomes are achieved.

Peterborough Pilot Program

SIBs originated in the United Kingdom (U.K.) with a pilot program currently active in Peterborough. The program is intended to reduce one-year recidivism rates among short-term incarcerated offenders. Though SIBs are usually associated with payments linked to cost savings, payments are structured differently in Peterborough.

As one of the primary nonprofits associated with SIBs articulated, "SIBs… allow[] governments to transfer the financial risk of prevention programs to private investors based on the expectation of future recoverable savings."[1] However, in Peterborough, payments are based on an undisclosed, negotiated value that includes consideration for the cost savings to the government but was ultimately based on negotiations between the government and third parties, representing an acceptable level of return for the third party intermediary and investors. The payments were justified in terms of social value for the government "on the basis that the SIB was innovative."[2]

In the Peterborough pilot, the national U.K. government will reimburse investors if an independent assessor concludes that the program achieves a recidivism reduction of 7.5% or greater in the local prison. Returns to investors may be as high as 13.0% per year over an eight-year period, depending on the amount by which the program exceeds the 7.5% target.

Social Finance U.K. serves as the project manager and receives a management fee. Multiple nonprofit service providers, selected based on their reputation for high performance, operate in cooperation to provide reentry programming for prisoners leaving a single host prison. The U.K. government issued no actual bond. Instead, it contracts with the relevant parties. The complexity of these contracts is the primary reason why the project took two years to develop, a timeline consistent with experiences in Massachusetts, a state which has been developing a similar pilot program.

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[1] *A New Tool for Scaling Impact*, available at SocialFinanceUS.org.

[2] *Lessons learned from the planning and early implementation of the Social Impact Bond at HMP Peterborough*, RAND Europe, 2011

Evaluating the Potential for Cost Savings

The majority of cost savings from a reentry program are associated with avoided reimprisonment. Within this category, the largest cost savings come when an agency can close a wing of a prison or an entire prison due to a drop in the number of prisoners. In Maryland, this typically requires a reduction of at least a few hundred prisoners per year. Until this threshold is obtained, DPSCS can only save on marginal costs for inmate wages, contractual services, materials, supplies, food, and medical costs. These marginal costs are approximately $4,623 per inmate per year for the department.

Statistics on recidivism and reimprisonment are not available for Maryland. **Exhibit 2** depicts the national trends for reimprisonment used for the financial models described below. Between 1994 and 1997, nationally, 5.0% of released prisoners returned to prison within six months. An additional 6.0% returned between six months and one year after release. In total, 27.0% of prisoners returned to prison within three years. This is based on a re-arrest rate for new crimes of 71.6% and a reconviction rate of 50.2% within three years of release from a state prison. The re-arrest and reconviction rates are two of the more common rates reported as the "recidivism rate" for jurisdictions. The reimprisonment rate is relevant to this analysis. A three-year, 27% rate of reimprisonment is broadly consistent with more recent studies conducted across a number of states by The Sentencing Project.[3]

Exhibit 2
National Reimprisonment Rate
Calendar 1994-1997

Time	Percent
6 months	5%
Up to 1 year	11%
Up to 2 years	20%
Up to 3 years	27%

Source: Bureau of Justice Statistics, Prisoner Recidivism Data Analysis Tool

Based on an extensive review of the research literature, highly effective programs can be expected to reduce the recidivism rate by a maximum of approximately 20.0%. Applying this 20.0% reduction in general recidivism to a three-year reimprisonment rate of approximately 27.0%, the total number of reimprisonments avoided as a result of a highly effective reentry program is proportionally a small reduction of 5.4% of the total number of inmates released

[3] *State Recidivism Studies*, 1995-2009

within the hypothetical reentry program. The cost savings for this 5.4% must therefore be equal to or exceed the cost of providing services to the 5.4% of participants avoiding reimprisonment and the remaining 94.6% of program participants.

Scenario One: 10% Recidivism Reduction

Using the national reimprisonment rates from Exhibit 2 and the marginal cost per inmate of $4,623 in Maryland, an optimistic model was constructed. It was assumed that prisoners served an average of three years after reimprisonment. The relationship between the program effect and the effects on the broader demand for prison beds was assumed to be equal. If, as a result of the program, 10 fewer individuals were reimprisoned each year, it was assumed that this directly resulted in a drop in demand of 10 beds per year.

The pilot program was also assumed to be effective with a reimprisonment reduction effect of 10%. This program effect of a 10% reduction in recidivism is in the upper range of effective programs. Many programs produce no measurable change in recidivism, and many successful programs produce a reduction smaller than 10%. To account for this fact, cost-benefit analysis in criminal justice commonly uses the average program effect, which would be even lower than the 10% used here.

The pilot program was assumed to have 250 participants per year. Realistically, operating a pilot program with this many participants may be difficult to achieve, considering this represents approximately 4% of total fiscal 2011 releases in Maryland. Reentry pilot programs, including some programs offered in Maryland, commonly aim for 250 total participants over the life of the pilot but often have difficulty achieving this much lower target.

Exhibit 3 depicts the number of prison beds saved by the Division of Correction per year under these assumptions and the associated cost savings. Over time, each operating year has a higher number of prison beds saved based on the cumulative effect of prisoners serving three-year terms (with staggered start times throughout each year). Although this program would be considered effective, it would result in a maximum of 19 saved prison beds in fiscal 2016 for a fiscal benefit of $89,571 in that year. The program would yield a total fiscal benefit of $247,908 in cost savings from avoided marginal costs over a five-year period.

Exhibit 3
Schedule of Benefits, Scenario One
Fiscal 2012- 2016

Year	No. of Program Participants	Returning to Prison Before Program Effect (No. of Persons)	Program Effect (No. of Persons Not Going to Prison) Current Year	Prison Beds Saved	Cost Savings
2012	250	27.5	-2.75	1	$6,357
2013	250	50.0	-5.00	5	24,271
2014	250	67.5	-6.75	11	51,431
2015	250	67.5	-6.75	17	76,280
2016	250	67.5	-6.75	19	89,571
Total	**1,250**	**280.0**	**-28.00**	**54**	**$247,908**

Source: Department of Legislative Services

Exhibit 4 details the costs of operating the program and reveals the total net fiscal impact after including the benefits from Exhibit 3. The cost of direct services was budgeted at $2,500 per participant. A cost per participant of $2,500 is on the lower end of the program cost spectrum but reflects the costs associated with a more intensive reentry program that is more likely to show a positive program effect.

Exhibit 4
Total Net Fiscal Impact, Scenario One
Fiscal 2012-2016

Total Benefits	
Marginal Cost Avoidance (Exhibit 3)	$247,908
Variable Costs	
Direct Services at $2,500 Per Participant	-$3,125,000
Investor Return	
Return on Investment at 10%	-$312,500
Fixed Costs	
Program Evaluation	-$150,000
Contract Design	-300,000
Management Fee to Intermediary at $50,000 Per Year	-250,000
Net Fiscal Impact	**-$3,889,592**

Source: Department of Legislative Services

The remaining cost assumptions were also optimistic.

- The program evaluation costs were assumed to be at the lowest possible cost. Program evaluations frequently cost more than double the $150,000 budgeted in this scenario.

- The contract design cost was budgeted at $300,000. Each SIB contract is unique to the local program and jurisdiction. As such, each contract design will be expensive and time consuming, and Maryland cannot simply replicate an existing contract model to avoid the costs of designing the contract with local and national partners. Maryland can expect a full design process to take approximately two years.

- The management fee to the intermediary is only large enough to pay for $50,000 per year in management fees at $250,000 over five years.

- The return to investors was budgeted at 10%, below the maximum 13% ROI amount used in Peterborough.

Using these figures, the fixed costs would equal $700,000, and total variable costs would equal $3,125,000. Combining these costs with the ROI and the fiscal benefits, the net cost of the program to the department would be approximately $3,889,592, as depicted in Exhibit 4.

This optimistic scenario reveals that a successful reentry program cannot self-finance using the cost savings to the government. The marginal cost avoidance represents less than 6% of the total costs of operating a SIB financed reentry program. If the program failed to demonstrate the targeted outcomes after a full five years of operations, the government would, at a minimum, incur $700,000 in costs as a result of the financing mechanism, due to the costs of the program evaluation, contract design, and management fee. The department's avoided cost of direct services, funded by the loss of investors' capital, would depend on the ability of the contract to effectively shift financial risk onto investors – an issue explored in greater depth in the limitation section of this analysis.

Scenario Two: 20% Recidivism Reduction and Lower Costs

Even if the assumptions in the first scenario are each modified to reflect a more optimistic set of assumptions, the net fiscal impact of a successful program would still remain negative.

Two primary adjustments were made to model a highly optimistic scenario:

- the program effect was revised upwards from 10 to 20%; and

- the management fee to the intermediary was revised downward from $250,000 to $150,000.

As **Exhibit 5** depicts, an increase in the expected program effect from 10 to 20% results in a 100% increase in the prison beds avoided and total cost savings from Scenario One. Before including the costs of operating the program using a SIB, the savings from a reduction in reimprisonment represent a maximum fiscal benefit per year of $179,141 and a total fiscal benefit of $495,817 over a five-year period. However, even under this highly optimistic set of assumptions, only a maximum of 39 prison beds are avoided in fiscal 2016. The department is only able to close a facility when the number of beds saved each year is consistently at least several hundred per year.

Exhibit 5
Schedule of Benefits, Scenario Two
Fiscal 2012-2016

Year	No. of Program Participants	Returning to Prison Before Program Effect (No. of Persons)	Program Effect (No. of Persons Not Going to Prison) Current Year	Prison Beds Saved	Cost Savings
2012	250	27.5	-5.5	3	$12,713
2013	250	50.0	-10.0	11	48,542
2014	250	67.5	-13.5	22	102,862
2015	250	67.5	-13.5	33	152,559
2016	250	67.5	-13.5	39	179,141
Total	**1,250**	**280.0**	**-56.0**	**107**	**$495,817**

Source: Department of Legislative Services

Exhibit 6 provides a comparison of the cost savings with the variable and fixed costs. Using these benefits to inform an assumption about the cost of direct services, it is apparent that a program that approaches fiscal balance would have very little funding available for direct services. Even after doubling the assumed efficacy of the program, the fixed costs of a SIB program alone would exceed the fiscal benefits. This means that any money spent on direct services increases the net negative fiscal impact of the program to the government.

Exhibit 6
Total Net Fiscal Impact, Scenario Two
Fiscal 2012-2016

Total Benefits	
Marginal Cost Avoidance (Exhibit 5)	$495,817
Variable Costs	
Direct Services at $250 Per Participant	-$312,500
Investor Return	
Return on Investment at 10%	-$31,250
Fixed Costs	
Program Evaluation	-$150,000
Contract Design	-300,000
Management Fee to Intermediary at $30,000 Per Year	-150,000
Net Fiscal Impact	**-$447,933**

Source: Department of Legislative Services

Using $250 per participant to illustrate the fiscal dynamics at the lowest conceivable cost still results in a net fiscal impact of -$447,933 over the life of the program. A program with only $250 to spend on direct services per participant would provide very limited services. Low intensity interventions are not likely to produce a reduction in recidivism close to 20%. Exhibit 6 depicts the total net fiscal impact of the program across all five years of program operations using this second order, final modification of the assumptions from the first scenario.

Doubling the size of the program does not alleviate the negative fiscal impact. Even under highly optimistic assumptions, a program that had 500 participants complete the program each year would only reduce the demand for prison beds by a maximum of 78 beds in year five of the program, a reduction in demand well below the number needed for even a partial facility closure. For a pilot program then, the fiscal impact is determined by the benefits associated with the avoided marginal costs per inmate and the costs of offering the reentry programming. Given these dynamics, even under optimistic assumptions, it is apparent that a highly effective program cannot self-finance.

Accuracy of Fiscal Estimates

These projections are not intended to reflect actual DPSCS experiences with reentry programming. The actual relationship between reentry programs and the demand for prison beds is unknown. Because the department has discretion over facility use and prison bed demand is driven by complex interactions between crime, detection, the judiciary system, sentencing, and DPSCS discretion, a one-to-one relationship between recidivism and State prison bed demand is unlikely. The relationship between reentry programs and prison bed demand was assumed to be direct in the scenarios above, yet the cost dynamics were not positive. The true interactions are likely to be less favorable to strategies attempting to finance pilot reentry programming through cost savings experienced during the life of the program.

Both scenarios described earlier neglect the fiscal impact outside of the cost of reimprisonment for expenditures related to parole and broader social services funded by the State. In the case of avoided parole, there may be some additional savings, but the cost of parole is generally much smaller than the marginal cost of imprisonment. For other cost dynamics, reentry programming may increase direct costs to the State, at least in the short term, by increasing the percentage of released former inmates who enroll in State-funded social service programs.

A more accurate forecast would require significant investments in data collection and analysis. Beyond developing a working model of the relationship between sentencing and prison demand, modeling cost dynamics prospectively would also require forecasting crime levels, prison populations, policy changes, and funding streams from non-State sources. Even retrospectively, it can be very expensive due to the difficulty of collecting and harmonizing data collected in separate systems. At the current time, Maryland does not even have the capacity to estimate general population reimprisonment rates (though DPSCS is implementing a new data system that should improve data collection and analysis abilities within the department).

Though it may be difficult to model the cost dynamics with greater accuracy, the general dynamics will not change. Prior experiences with programs for reentry, including the Peterborough SIB program, have demonstrated that effective pilot programs cannot finance themselves with cost savings. An independent evaluation, commissioned by the U.K. Ministry of Justice and conducted by RAND Europe found that the reentry pilot program in Peterborough is "too small to deliver substantial 'cashable' savings (monetized benefits)."[4] Additionally, a study entitled *Impact and Cost-benefit Analysis of the Maryland Reentry Partnership Initiative*, conducted by the Urban Institute Justice Policy Center, found that a pilot reentry program offered in Baltimore did not produce savings for the government. The report noted that "when community-justice partnerships work – whether they are reentry programs, drug courts, or some other intervention – the benefits tend to disproportionately accrue to private citizens, rather than public agencies. That is, public agencies looking to programs…as a means of creating revenue streams that more than offset the cost of the program are likely to be disappointed." The

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[4]*Lessons learned from the planning and early implementation of the Social Impact Bond at HMP Peterborough*, RAND Europe, 2011, pg. iv.

Maryland Reentry Partnership Initiative cost $3,476,240 to administer for a cost of $6,213 per participant. It saved public agencies $2,961,650, though the estimate for correctional spending was made using average costs instead of the more accurate marginal cost methodology. Even with this generous inflation of avoided correctional costs, the program still had a net cost. These examples suggest that direct cost savings are insufficient to finance pilot reentry programs.

Nonfiscal Value of Programming

It is important to note that this case study centers on the efficiency and cost effectiveness of a SIB for financing and operating reentry programming, relative to direct government operations. Reentry programming should be as cost effective as possible and operated in the most efficient and equitable ways available. But the decision to engage in reentry programming hinges on much broader, nonfiscal considerations than whether or not a SIB is an efficient way to finance reentry programs.

Reentry programs are intended to help prisoners who are leaving incarceration successfully return and adjust to their local communities. Incarcerated individuals undergo a very difficult adjustment process upon entering incarceration that "can create habits of thinking and acting that are extremely dysfunctional outside the prison walls."[5] The longer individuals are incarcerated, the more they adapt to a prison environment that encourages heavy dependence on institutional structures, hypervigiliance and interpersonal distrust, and social withdrawal, among many psychologically painful effects. Simultaneously, prisoners experience diminished ties to their family and social networks.

At the time of the release, individuals return to the community with norms and attitudes that are maladaptive to society outside of the prison walls. Compounding the problem, many, if not most, have weak labor market attachments and social supports. Reentry programming can thus provide a highly socially valuable set of services, independent of the fiscal impact, that contribute toward stronger and safer communities when former inmates are able to begin rebuilding healthy and productive lives.

Limitations of the SIB Model

Substantial Risk Shifting Unlikely to Occur

Even if a SIB reentry program cannot self-finance through cost savings, the potential to shift outcome risk to the private sector could in theory provide benefits to the government that justify the added costs incurred in this financing mechanism. Unfortunately, there are no tangible examples of significant risk shifting occurring in practice for SIBs.

There are two primary obstacles to shifting risk. First, there must be an investment market with a tolerance for a high degree of risk in the outcomes of social programs. Second, the

[5] *Prisoners Once Removed,* The Urban Institute, pg 39.

contract design must provide an enforcement mechanism to prevent investors and providers from terminating the contract early.

Unlike municipal bond markets, a market for high-risk instruments to finance government social programs does not currently exist. The department would have to incur substantial costs in selecting partners and designing the contract in order to discover whether or not there was indeed an appetite for a reentry program in the State.

Furthermore, eligible partners must tolerate long-term financial risk that is enforced by a mechanism that prevents early termination. Without such a mechanism, the ultimate financial and operational risk would be with the government. The only risk shifting that would occur without an enforcement mechanism would be for the initial operations that are necessary for the third parties to evaluate cost and the likelihood of achieving the specified outcomes.

Peterborough provides insufficient guidance on how to design such a contract. An independent evaluation found that the risk "transfer, and the contracts themselves, are untested in many respects: issues that challenge the contractual arrangements and/or require clarification through the contracts could still arise in the course of implementation."[6] A large amount of this uncertainty is driven by the complexity of the contract: "Complexity in some instances meant that the actual transfer of risk is not clear."[7]

Even if a contract could be designed to effectively limit investor termination, there would still be the possibility that the funds would not cover the cost of program operations. Under more standard forms of performance-based contracting, providers and the government can renegotiate the contract when the cost drivers differ from initial estimates. The inclusion of external investors and a rigorous independent evaluation in a SIB, however, significantly limits the flexibility to renegotiate contracts – a flexibility that has been critical for many jurisdictions engaged in more standard forms of contracting for human services.

To remedy the cost reimbursement problem, some hybrid models of social impact bonds have been proposed where the government assumes from the start a majority of risk. Under these proposals, the government pays for a substantial portion of the program operation costs. In some proposals, the government would guarantee 70% of program costs. However, in a SIB model where the government guarantees 70% of the program costs, the costs of designing the contract and compensating a third-party intermediary are close to the dollar value of the risk shifting for the government.

In short, even if a market for investments in Maryland based SIBs were to exist, it is unlikely that the government will be able to shift the financial outcome risk for the program substantially onto the private sector given the difficulty of preventing service providers and investors from leaving a potentially underfunded and/or unsuccessful enterprise. If risk cannot

[6] *Lessons learned from the planning and early implementation of the Social Impact Bond at HMP Peterborough*, RAND Europe, 2011, pg. 54.

[7] *Ibid.*

be in practice shifted to the private parties through an effective enforcement mechanism to prevent early termination, Maryland would in fact be increasing its operational and financial risks with the decision to engage in the project. In the event that the private parties cancelled the contract, there may be strong political, ethical, and administrative reasons for continuing a program through direct government funding.

Added Expenses in SIB Model Create Additional Budgetary Pressure

Implicit in discussions of SIBs is the notion that they can alleviate underfunding of specific social services by leveraging private capital. The ability of SIBs to alleviate funding challenges is based partly on the idea that capital projects are typically better financed, due to recognition that the benefits of capital projects accrue over a long time period. In order to spread the cost of capital projects across the useful life of a project, governments typically borrow money through bonds and repay them over time, breaking the limiting link between upfront costs and total benefits. Social programs, in contrast, are constrained by annual appropriations in the operating budget – even though the benefits also accrue over a long time period. Preventing a future violent crime may cost more in the short term but will save a large sum of money over time through avoided incarceration, for example.

Even if a specific social program could reap fiscal savings with increased upfront funding, SIBs would not solve this problem. Because of the uncertainty of the payments made by the government, both Massachusetts and the U.K. government have planned in their budgets to make the full payment necessary to fund the program and pay investors their ROI.

Budgeting for contingent liabilities is good fiscal policy. It would be risky and imprudent long term to incur contingent liabilities without providing funding. But in practice, this means that operating expenditures for a SIB program will be allocated either in advance or annually for the full cost of the program, in the event that the program works and the government must make the outcome-based payments. The government, therefore, realizes no upfront savings to finance the program and is still limited by current operating budget constraints.

High-stakes Payments May Distort Evidence

Common conceptions of SIBs assume that unproven programs are the types that investors, providers, and the government will prefer for high-risk outcome payments. However, given the financial and reputational stakes attached to SIBs, governments and parties to the SIB are more likely to select programs and partners with well-established records of performance. Selecting providers based on their likelihood to succeed, in the case of a SIB pilot, can create the false impression that the specific intervention could be scaled to a larger operation.

In Peterborough, for example, the program location and partners were not chosen randomly from a pool of qualified providers and relevant locations. Instead, the providers were selected based on their existing partnerships, proximity to the prison, and established track record for high performance. Even if the Peterborough SIB achieves positive outcomes, it will still be unclear if this type of program can be replicated in other locations without the advantages produced from location and partner creaming.

Additionally, even if new programs are piloted, if private parties cannot in practice be prevented from leaving contracts early, this may distort the nature of the evidence base. In the event that private actors decide not to wait for medium- to long-term positive outcome indicators and cancel the program when the short-term outcomes appear unfavorable, this would distort the production of new evidence for any programs that may require longer periods of time to demonstrate efficacy.

The Evaluation May Be Inconclusive

SIBs are designed with the intention of offering governments the ability to increase the portion of payment based on performance. This is one of the primary innovations of the SIB concept. In order for this to function, there must be an increased confidence in the assessment of the outcome and its causal drivers.

It is not sufficient to say that a treatment group exceeded the average outcome. Instead, evaluators must build a group to control for effects of causal factors that are independent of the specific intervention. In the most rigorous evaluations, research protocols are designed around random assignment to minimize the effect of unmeasured differences between the control group and the treatment group in the program. Random assignment can be both operationally and cost prohibitive, however. In the Peterborough pilot, for example, there were concerns about denying treatment randomly within a single prison. Many evaluations and research studies construct simulated control groups instead (usually by using propensity score matching). This is considered the next most rigorous form of evaluation.

However, the simulated control groups are not capable of controlling for unmeasured variables, as the control groups are not random but rather assembled based only on observed characteristics. This means that there is an unknown risk that the observed outcome was caused by an unmeasured variable. This problem was noted in a government commissioned evaluation of the Peterborough program.[8] The report indicated that the methodology used in Peterborough did control for basic demographic data and was the most rigorous methodology available apart from random control assignment. But it "cannot take account unmeasured differences…aside from treatment received."[9]

However, regardless of the technique, in small studies it is harder to tell whether or not the intervention was the result of random variation. In other words, even if there is conclusive evidence that the treatment group differed in important ways from the control group in terms of outcomes, this difference may be random. The risks of this occurring are higher in smaller samples.

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[8] *Peterborough Social Impact Bond: an independent assessment*, May 2012, Ministry of Justice Research Series, pg 8.

[9] *Ibid.*

In practice, expert researchers rarely use a single study as proof that a type of intervention works. The value of research and program evaluation is in the cumulative evidence. A problem with SIBs is that they depend on a high degree of confidence in a single evaluation for the entire payment.

SIBs and Narrow Policy Change

Program models for a SIB financed reentry program start services with individuals at the time of release and provide social services, such as housing, job counseling, and therapy. From a broader policy perspective, this type of reentry program represents a very narrow policy change relative to the total number of practices and policies that impact rehabilitation, community reentry, and recidivism. Other jurisdictions, including jurisdictions in Maryland, address reentry programming as a comprehensive process that begins at admission to the prison. As such, if the goals surrounding reentry programming are to reduce expenditures on imprisonment while increasing public safety and social welfare, a host of broader policy changes can be enacted in complement to programs that provide services directly at the time of release. Many of these, in fact, have already been identified by the Maryland Task Force on Prisoner Reentry.

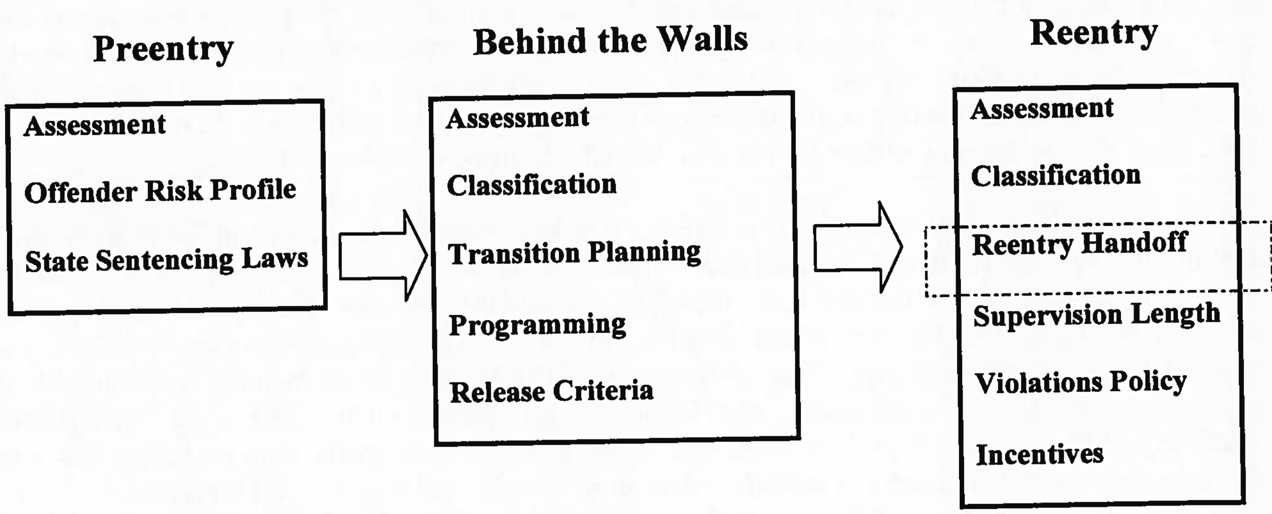
Post-release employment, for example, is a key causal determinant of both successful community reintegration and reduced recidivism. While reentry programs can help facilitate prisoners' adjustment to reentry and, therefore, potentially increase their employability, the difficult barrier of employment discrimination for those with criminal histories remains. To combat this problem, in a report issued last year, the task force recommended a law to shield criminal records for nonviolent convictions from public view after an appropriate waiting/proving period. This is an example of the types of synergistic policy change that can complement reentry programs to save the State money while increasing social welfare.

The policy mechanisms with the greatest leverage available to reduce prison expenditures while enhancing public safety exist in sentencing and release criteria reforms. Whereas reentry programs work to reduce the number of prisoners indirectly, sentencing and release criteria reforms can directly decrease the number of low-risk offenders who are sent to and/or retained in prison. As one example, in the 2012 *Joint Chairmen's Report* response on the Plan for Reducing the State Inmate Population, the department estimated that increasing the number of good conduct credits that nonviolent prisoners are eligible to earn could save the department up to $29 million annually. The department found that this was a sustainable option that provides extra incentives for good behavior to inmates coming into the system and would increase safety in prison facilities.

This type of policy would complement reentry programs, as prisoners who spend longer time periods incarcerated generally have a harder time re-integrating into their local communities. Longer separation periods, for example, decrease the likelihood of mothers retaining custody of their children. Reducing the time served in prison for offenders who would be more effectively and safely rehabilitated in the community, while maintaining supervision by the department, would help reduce the heightened psychological difficulty of reentry associated with longer prison terms.

A reentry program financed by a SIB, in contrast, represents a very narrow policy change, as depicted in **Exhibit 7**. A privately operated reentry program would start services at or near the point of release for prisoners, labeled as the "reentry handoff" in Exhibit 7. This is just one of a larger number of institutional policies and practices that impact the community reintegration and/or recidivism of those committed to the department's supervision.

Exhibit 7
Policies and Practices That Effect Recidivism



Source: Adapted from the Pew Center on the States

The narrow focus of a SIB reentry program poses three problems to a state engaged in or considering broader policy change:

- Because SIBs require high degrees of statistical control in order to determine causality, the confidence in the justification for the high-stakes outcome payments may be placed in jeopardy when a large number of important environmental and demographic factors are modified during the pilot program. If it were possible to control for these changes, the baseline outcome goals may still require modification to account for demographic and environmental changes. Making these modifications to a contract would be time consuming and expensive.

- A SIB financed program would create a new system of private service delivery external to the department. In some cases, this may be counterproductive where integration between current DPSCS programs would increase efficiency and efficacy. Reentry programming often starts in many jurisdictions at the point of entry into the prison system. Creating a parallel system separately administered by the private sector may impede operational integration, a problem that may be especially difficult if the department were to engage in large scale re-organization and/or policy change.

- Building a highly sophisticated contracting mechanism to focus on one narrow aspect may impede the capacity of agencies and the State to engage in broader policy evaluation and change. Developing a SIB for a reentry program would require significant investments of staff time to design and manage the contracting process. This may impede the department's ability to simultaneously enact other large complementary changes that require budget, contracting, and senior staff time.

Conclusion

A reentry program financed using a SIB would not produce sufficient benefits to justify the operational costs or risks of engaging in this form of high-stakes contracting.

A social impact bond financed program would:

- increase budgetary pressure compared to direct financing, due to the necessity of funding contingent liabilities and the added expenses of features unique to SIBs;

- not produce cost savings when outcomes are achieved, even under highly optimistic assumptions;

- be unlikely to shift outcome risk;

- possibly exclude new providers and program types that do not have a well-established record of success through investors seeking to minimize risk; and

- potentially distort evidence used in policy decisions.

The primary weakness of a SIB is in the complexity of its moving parts and the high-stakes nature of the financing mechanism. A SIB contract would only be advantageous to Maryland, if, at minimum, all of the following conditions were met:

- Maryland could create a contract that guarantees investors and providers will continue program operations for the entire life of the contract, even when it is apparent after the program starts that the outcomes are unlikely to be achieved.

- Nonprofits would continue service delivery when reimbursements are below costs or all parties could effectively and efficiently renegotiate the contract without jeopardizing the evaluation and value of the risk shifting to the government.

- An independent program evaluation could definitively show that the program either did or did not cause the target outcomes to be achieved.

- The additional costs inherent to the SIB financing mechanism would be sufficiently lower than the cost of providing the service, so as to justify the value of these services to shift the outcome risk.

- A private market can be created for investing in unproven forms of reentry programs.

- The department has the operational capacity to engage in a SIB pilot program while undertaking other organizational and policy changes.

- There is sufficient State funding in the operating budget available to fund the contingent liabilities of a SIB program.

- The value of shifting the risk for a negative outcome is monetarily large enough to the government to risk the added costs of the SIB and the potential for an investor ROI given a positive outcome.

If any one of these conditions cannot be met, then a SIB model is not an ideal financing or contracting mechanism for reentry programs in Maryland. Given the difficulty of shifting the outcome risk and the countervailing incentives for many of these conditions, it is unlikely that these conditions will be met.

Reentry programs can have social value well beyond the direct fiscal costs to the government. They are especially valuable and fiscally beneficial when developed in tandem with complementary policies that have an even greater impact on recidivism. However, SIB financing mechanisms create a host of problems that collectively limit the purported benefits of the financing mechanism and the ability of governments to engage in broader policy changes.

Recommendation

DPSCS should continue to directly finance and operate reentry programs while pursuing other organizational and policy changes likely to have greater impact while posing less risk than a SIB financed program.

Social Impact Bonds

Introduction

July 17, 2013

Why don't we fund more large, public cost-saving initiatives?

There are a number of programs that promise very large improvements in social outcomes and potentially large cost savings to State government

with solid research studies backing up the promise

examples:

- early childhood interventions for health or education
- prison recidivism reduction
- homelessness prevention

Human capital improvement

Why don't we fund more large, public cost-saving initiatives? (2)

BUT

- They are programs with long-term benefits coupled with large up-front costs . . .

- And it is difficult to interest the public in investing in even excellent programs with such a long pay-back period.

A Solution:

- Suppose you could fund such programs by creating a
  - financial instrument (loan) that could
  - tap global debt markets by
  - rewarding <u>private</u> investors in the <u>long-term</u>
  - for putting up substantial funds <u>now</u>?

- That is the idea behind **Social Impact Bonds** aka “Pay for Success” Bonds.

A Solution (2):

- Why go to the trouble?

Revolutionary potential for social improvement

A potential market of $80 trillion

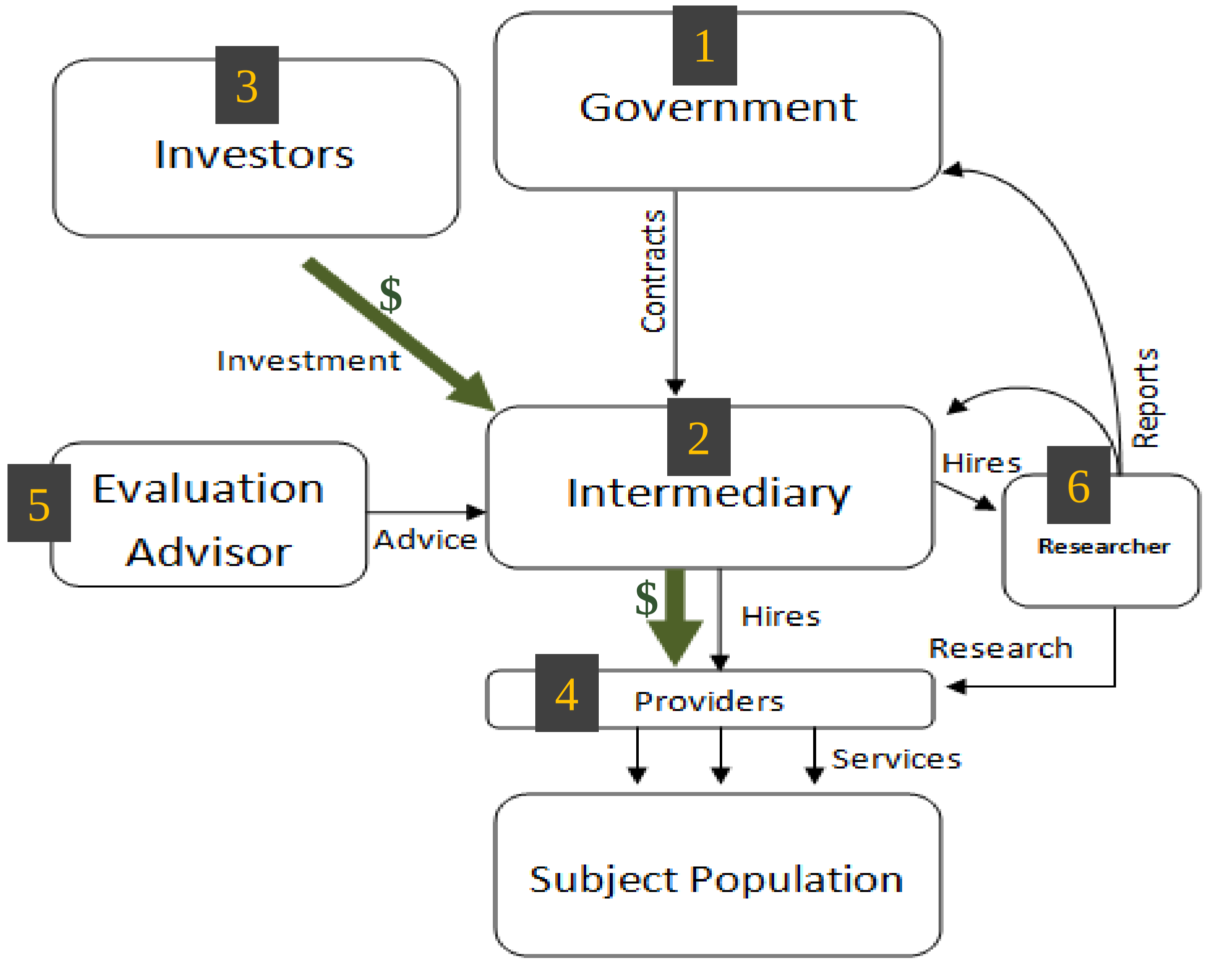
(a very large number!)

What are Social Impact Bonds?

A new idea for financing social programs.

- A Social Impact Bond (SIB) is a contract with the private sector in which a commitment is made to pay for improved social outcomes that result in public sector savings.[1]
- SIB's provide funds for "initiatives that have the potential to mitigate serious social problems and reduce government costs for later remedial services."[2]
- It is not technically a bond, but a "multi-stakeholder partnership" without guaranteed interest rate or repayment schedule.

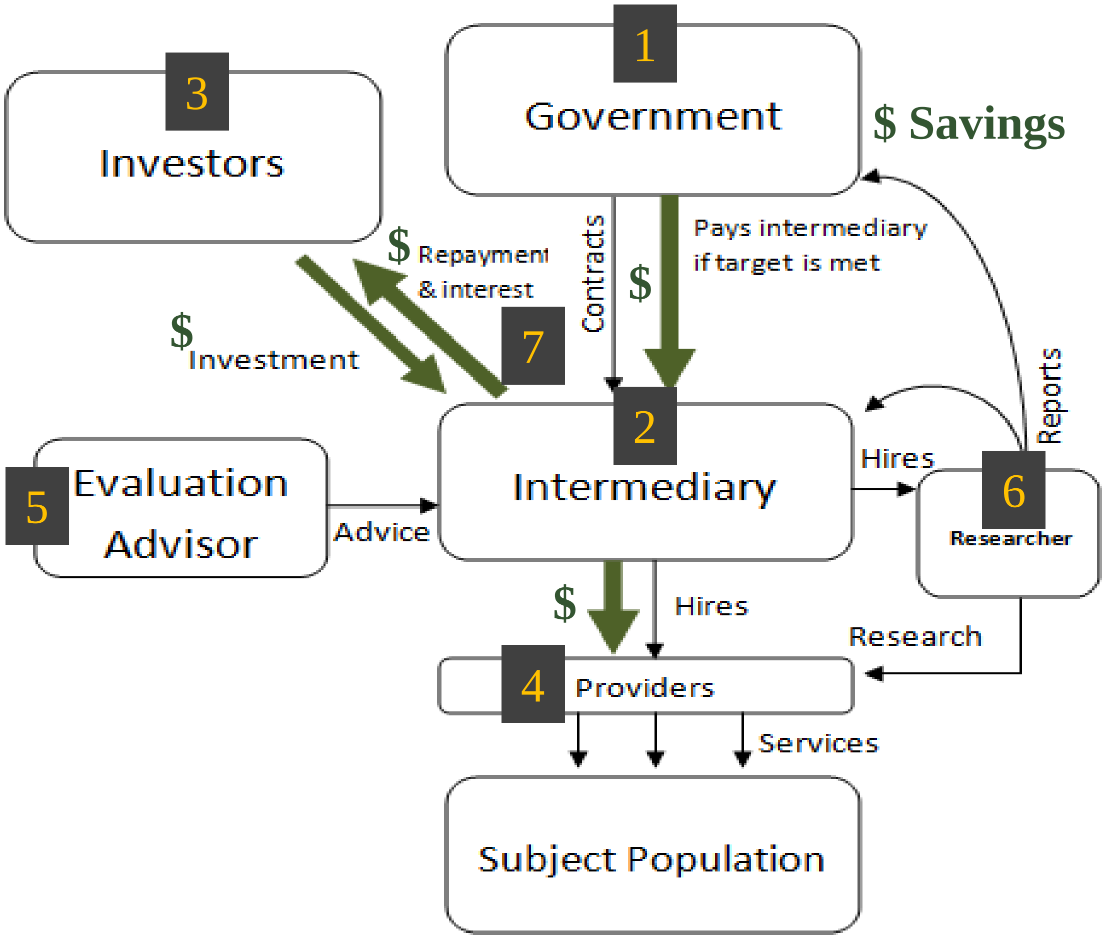
Ideal Social Impact Bond design



Social Impact Bond Participants

1. The government sets a specific <u>outcome</u> it wants to achieve relative to a well defined population over a given time period.
2. The government contracts with an intermediary to <u>achieve</u> the pre-set outcome.
3. Investors provide up-front capital to pay for the program in question.
   - Investors are repaid their capital plus a return only if the target outcome is met.
4. The intermediary engages service providers to deliver evidence-based programs.

Ideal Social Impact Bond design(2)



Social Impact Bond Participants(2)

5. An independent evaluation advisor monitors the progress of the interventions.
6. An independent researcher determines if predetermined performance targets have been met.
7. If the target is met, the government repays investor principal plus interest.

Note: there are many variations on this structure, as different governmental entities wrestle with how best to structure the deal.

Promising Interventions

- Projects that aim to reduce recidivism among those released from prison- **NYC** example, also **Peterborough**
- Homelessness prevention services- **Massachusetts** is working on it
- Prenatal, early childhood and pre-school services- **Utah and South Carolina** examples
- Preventive healthcare interventions, such as those for asthma or diabetes- **Fresno** example
- Home based services designed to keep the elderly out of nursing homes
- Employment/workforce development services

Resources

1. Steven Godeke and Lyel Resner, "Building a Healthy and Sustainable Social Impact Bond Market: The Investor Landscape," Godeke Consulting and The Rockefeller Foundation, November 2012, available at www.rockefellerfoundation.org/news/publications/building-healthy-sustainable-social
2. Center for American Progress, " Frequently Asked Questions: Social Impact Bonds," Dec 5, 2012, http://www.americanprogress.org/issues/economy/report/2012/12/05/46934/frequently-asked-questions-social-impact-bonds/
3. Nonprofit Finance Fund, "Pay for success/Social Impact Bond Initiative," http://nonprofitfinancefund.org/pay-for-success
4. Social Finance (UK) http://www.socialfinance.org.uk/resources/social-finance/technical-guide-developing-social-impact-bonds
5. Dugger and Litan, "Early Childhood 'Pay-For-Success' Social Impact Finance: A PKSE Bond Example to Increase School Readiness and Reduce Special Education Costs," A Report of the Kauffman Foundation – ReadyNation Working Group on Early Childhood Finance Innovation, p. 3 at http://ideas.repec.org/p/hka/wpaper/2012-007.html
6. The Economist, "Performance bonds Who succeeds gets paid" from **The Economist**, Feb 17, 2011 http://www.economist.com/node/18180436?story_id=18180436 See also Jonathan Greenblatt and Annie Donovan, "The Promise of Pay for Success" in Community Development Investment Review, April 2013 at http://www.frbsf.org/publications/community/review/vol9_issue1/review-volume-9-issue-1.pdf
7. The New York Times, "Getting Back More Than a Warm Feeling" Nov 8, 2012 http://www.nytimes.com/2012/11/09/giving/investors-profit-by-giving-through-social-impact-bonds.html?pagewanted=all&_r=0 ; also, Mayor Bloomberg's press release, Aug 2012 at http://www.goldmansachs.com/what-we-do/investing-and-lending/urban-investments/case-studies/social-impact-bond-pdf.pdf ; also, Hannah Azemati, et al., "Pay for Success Financing" in the SF Fed's Community Development Investment Review, April 2013, p. 25 at http://www.frbsf.org/publications/community/review/vol9_issue1/review-volume-9-issue-1.pdf

John V. Spears

RESI of Towson University

July 17, 2013

Finis

TOWARDS A NEW ERA OF SOCIAL PURPOSE FINANCE

Dr. Lester M. Salamon

Johns Hopkins University

July 17, 2013

WHAT'S HAPPENING? *PHILANTHROPY'S BIG BANG*

- Beyond grants
- Beyond bequests
- Beyond foundations
- Beyond cash

LEVERAGE

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

PHILANTHROPY’S BIG BANG

Prosper.com
Network for Good
Standard & Poor’s
NESTA
Bovespa
Pooled Income Funds
Impact investing
Social enterprise
Gifts in Kind
Aquinas Growth Fund
Foursome Investments (UK)
Volkswagen Foundation
Guggenheim Partners
Neighborhood Housing Services of America
Compagnia di San Paolo
Innovest Strategic Value Advisors
Charitable Remainder Trust
Schwab Charitable Fund
DonorsChoose.org
Sea Change Capital Partners
Venture philanthropy
Oppenheimer Legacy Program
Women’s Funding Network
Blended value
Securitization
Kiva
California Wellness Foundation
Social Capital Partners (Canada)
TechSoup
Accion
Fidelity Charitable Gift Fund
Keystone
Community Wealth Ventures
New Profit
Acumen Fund
Mission investing
Charity Navigator
Bank Intesa (Italy)
echoDonations
Community Reinvestment Fund
Impact Partners (India)
Social Venture Partners
Calvert Foundation
Vanguard Charitable Endowment Program

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

NEW FRONTIERS OF PHILANTHROPY PARADIGM

PHILANTHROPY =

The mobilization of private resources for social and environmental purposes

TRADITIONAL PHILANTHROPY	NEW FRONTIERS OF PHILANTHROPY
Foundations, Individuals	Individual and institutional investors
Operating income	Investment capital
Grants	Diverse financial instruments/capital tranches
Nonprofits	Social ventures
Social return	Social + financial return
Limited leverage	Expanded leverage
Output Focus	Outcome focus/ metrics

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

NEW FRONTIERS OF PHILANTHROPY ECOSYSTEM

NEW SOURCES OF FUNDS

NEW ACTORS

NEW TOOLS

NEW AGENTS

BENEFICIARIES

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

ACTORS/TOOLS

TYPES OF ACTORS

- Capital Aggregators
- Secondary Markets
- Social Stock Exchanges
- Foundations as Philanthropic Banks
- Quasi-Public Investment Funds
- Enterprise Brokers
- Capacity Builders
- Online Portals
- Corp-Originated Charitable Funds
- Conversion Foundations
- Funding Collaboratives

TYPES OF TOOLS

- Loans / Credit Enhancements
- Bonds
- Securitization
- Equity Investments
- Social Impact Bonds
- Insurance
- Social Investing & Purchasing
- Prizes, Crowd-sourcing

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

CAPITAL AGGREGATORS

EXAMPLES:

- Community Development Finance Institutions (CDFIs)
- BAML Capital Access Funds
- ACCION International
- Economic Innovation International (EII)

METRICS:

- Globally, Capital Aggregators – $300 billion US (215 billion euro)
- 1,300 CDFIs / $19.7 billion of investments
- BAML – $300 million of pension fund capital invested in 25 funds
  EII – $20 Billion Triple Bottom Line equity funds

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

SECONDARY MARKETS

EXAMPLES:

- Community Reinvestment Fund (CRF)
- Habitat for Humanity
- Self-Help North Carolina
- BRAC

METRICS:

- CRF – $1 billion in loans purchased
- Habitat Flex Cap Program – leverages $1 billion
- Self-Help North Carolina – $4.5 billion in mortgage investments
- BRAC securitizing $180 million microfinance loans

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

SOCIAL STOCK EXCHANGES

EXAMPLES:

- Social Stock Exchange UK
- Impact Investment Exchange (IIX) Asia
- Chicago Climate Exchange (CCX)
- Bovespa (Brazil)

METRICS:

- IIX has established an arrangement with the Singapore Stock Exchange to list the bonds and stocks of social enterprises
- Eur Climate Exchange ECX – 5.3 billion tons CO2 Equivs in 2010/ US$85-90 billion ; Global carbon credit market= US 142 billion

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

FOUNDATIONS AS PHILANTHROPIC BANKS

EXAMPLES:

- Fondazione CRT in Italy
- F.B. Heron Foundation
- Annie E. Casey Foundation
- K.L. Felicitas Foundation

METRICS:

- Fondazione CRT:
  42% of grant-making towards mission/impact investing
- F.B. Heron Foundation: 43% of assets in mission/impact investing
- Multiple tools beyond grants

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

ACTORS/TOOLS

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- Prizes, Crowd-sourcing

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

INSURANCE

CONCEPT :

- Less than 3 percent of low-income people in world's 100 poorest countries have insurance
- Key defining feature: RISK POOLING
- ILO Microinsurance Innovation Facility
- LeapFrog microinsurance investment fund

METRICS:

- Potential market for micro-insurance – 1.5 to 3 billion people
- All-Life: Insures HIV/AIDS victims in South Africa; 200 percent growth in client base in 2010 + 15% improvement in client health.
- UN World Food Program pays Ethiopian farmers for work on irrigation projects with drought insurance

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

SOCIAL IMPACT BONDS

EXAMPLES:

- UK Social Impact Bond
- Pay for Success — MA, Minnesota, NYC

HOW DOES IT WORK? UK Social Impact Bond

- UK Gov't offers to repay private investments in services to reduce recidivism at Peterborough prison—with dividends
- Sliding scale of dividends keyed to program success
- Metrics and control group to measure success
- Monetizes savings from program success—Gov't pays 10 million GBP for 20 million GBP of program savings

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

WHY NOW?

DEMAND FACTORS:

- Persistent poverty
- Population pressures
- Global warming/ environmental crises
- Failed states/ Governmental retrenchment

SUPPLY FACTORS:

- Social entrepreneurs/ Prahalad —"BOP penalty"
- Dot-com Philanthrocapitalists / Net Impact
- Tepid traditional capital markets
- Psychological impact of financial crisis

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

NEXT STEPS

- ✓ VISUALIZE
- ✓ PUBLICIZE
- ✓ INCENTIVIZE
- ✓ CAPACITIZE
- ✓ ACTUALIZE

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

IMPLICATIONS FOR STATES

- ✓ NEW PARTNERS
- ✓ NEW FINANCIAL MECHANISMS
- ✓ NEW SKILL REQUIREMENTS
- ✓ NEW AUTHORITIES?

SOURCE: Lester M Salamon, Ed., *The New Frontiers of Philanthropy*, New York: Oxford University Press, 2013 (forthcoming).

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Early Child Human Capital Investment: “Pay for Success” Finance

Social Impact Bond Summer Study 2013

Innovations Institute, School of Social Work

University of Maryland

Robert H. Dugger

Co-Chair, ReadyNation

July 17, 2013

Today I will present the results of two recent publications on early childhood "pay for success" finance

The two most recent ReadyNation working papers focus on contract specification and financial instruments choice, two critical operating features of early childhood pay for success (PFS) projects. www.ReadyNation.org/PFS

"Early Childhood Pay for Success Social Impact Finance: Organizational Steps, Memorandum of Understanding and Contract Outlines." Report of the ReadyNation Working Group on contracts in Early Childhood Social Impact Finance, ReadyNation Working Paper, June 10, 2013.

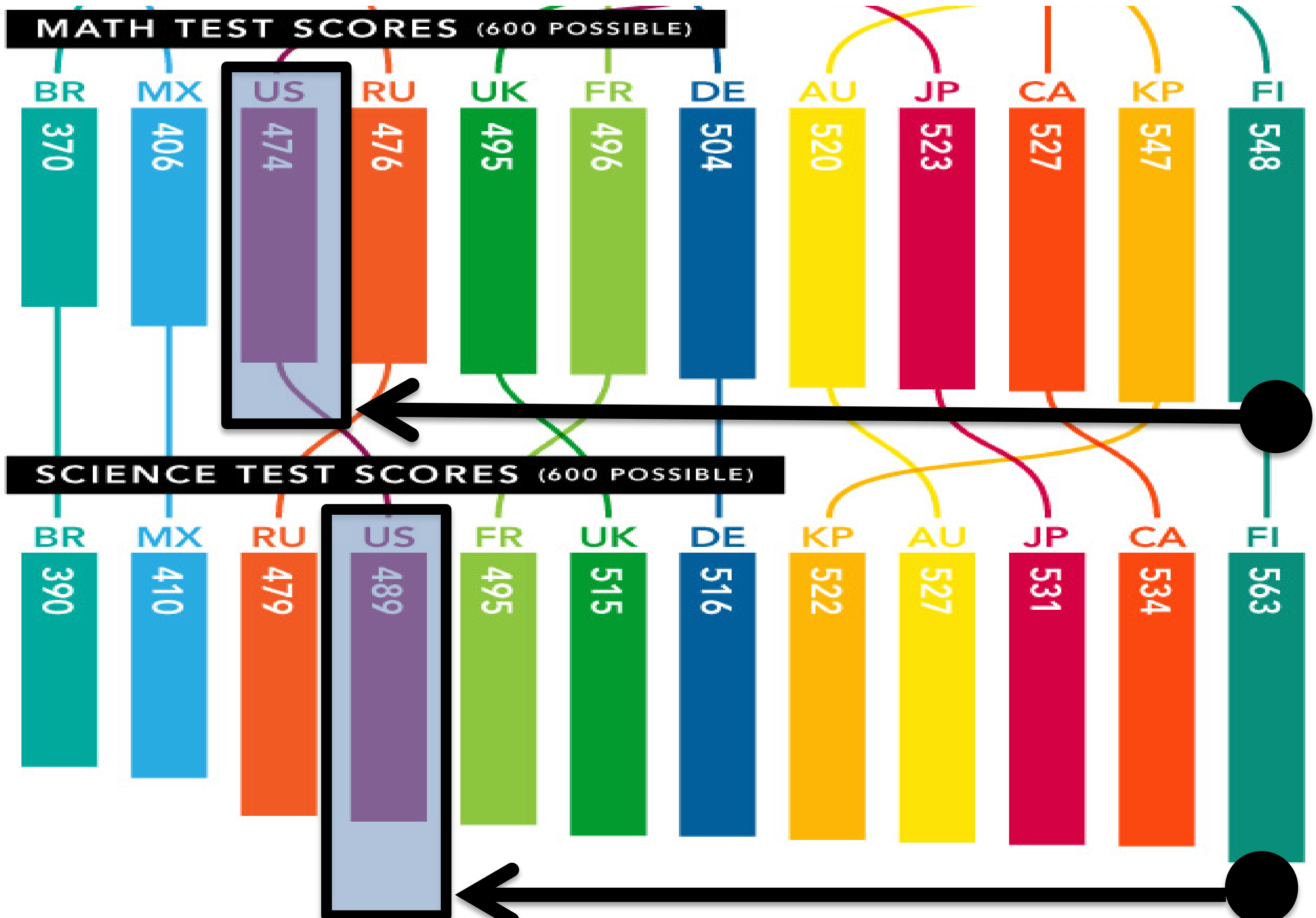
"Financing Human Capital Development for Economically Disadvantaged Children: Applying Pay for Success Social Impact Finance to Early Child Development." Janis A. Dubno, Robert H. Dugger, and Michelle R. Smith. ReadyNation Working Paper, June 10, 2013

First a word about ReadyNation…

ReadyNation Social Impact Finance Portfolio of Work

- ✓ Convene national work group on early childhood SIBs: A "Five Year Vision" for pay-for-success assets
- ✓ Working papers on early childhood social impact finance structure and contracts
- ✓ Hub of working documents from state and local initiatives
- ✓ *EC Social Impact Performance Advisors*, funded by the Pritzker Foundation: *C*ollaboration and training consultancy for senior investment, legal and public finance experts
- ✓ ***Join the EC SIB listserv at* www.ReadyNation.org/PFS**

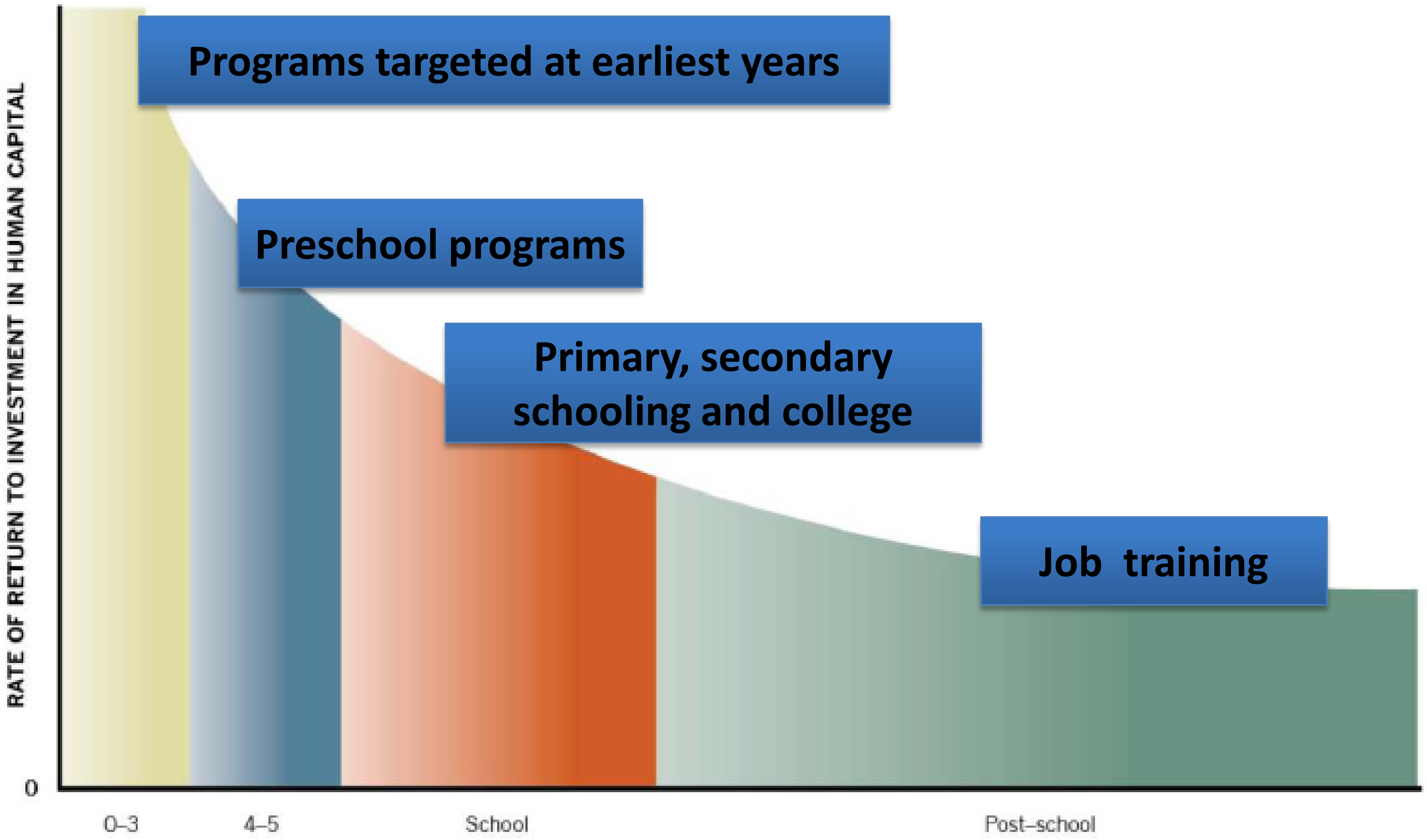
Education is the key: The US used to be first. Now we're just average…



To produce globally competitive young adults..

…you must first produce school-ready five year olds.

Rate of return on investments in human capital by age…



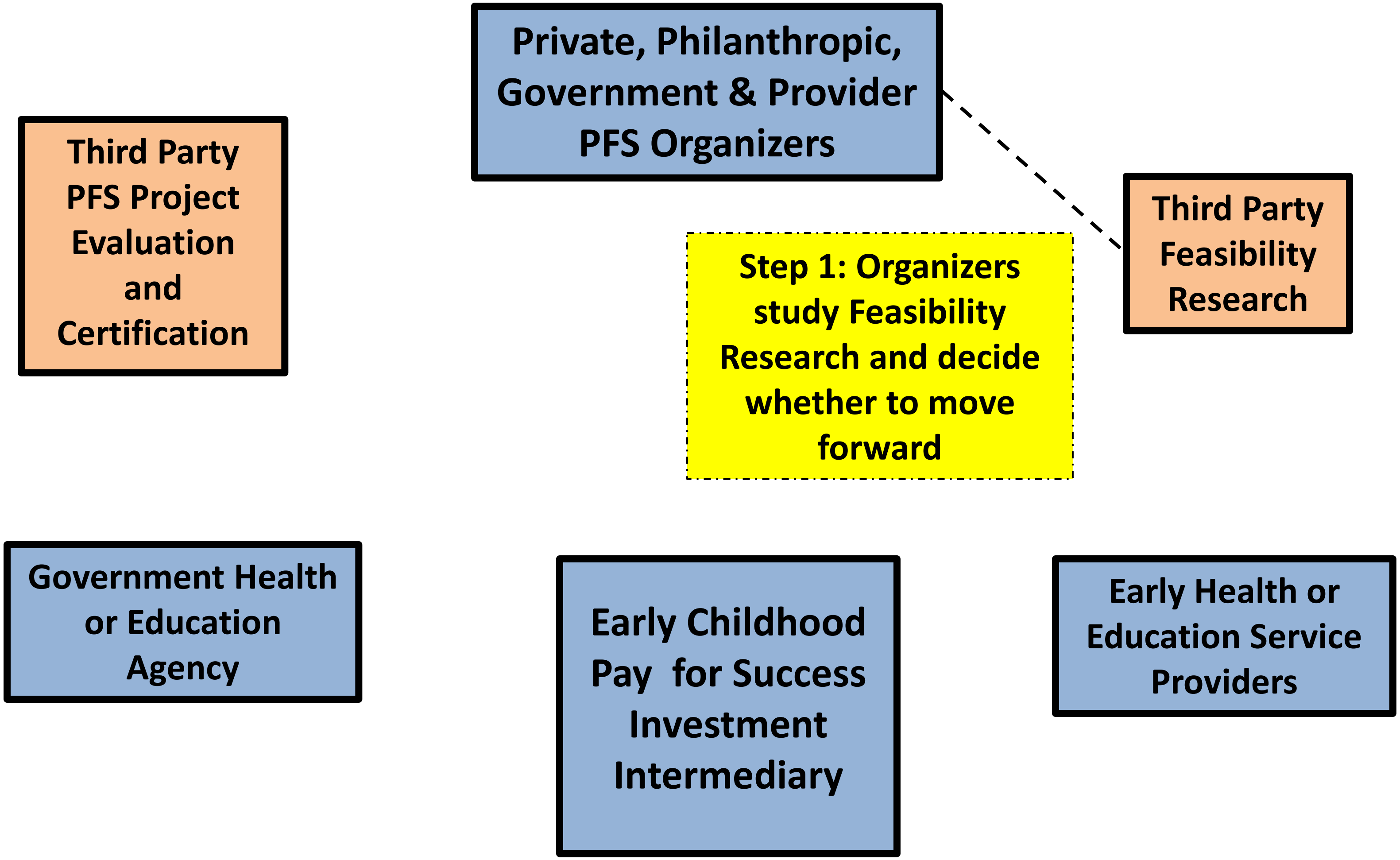
Source: James Heckman, Schools, Skills, and Synapses, *Economic Inquiry*, 2008

“Pay for Success” Social Impact Finance

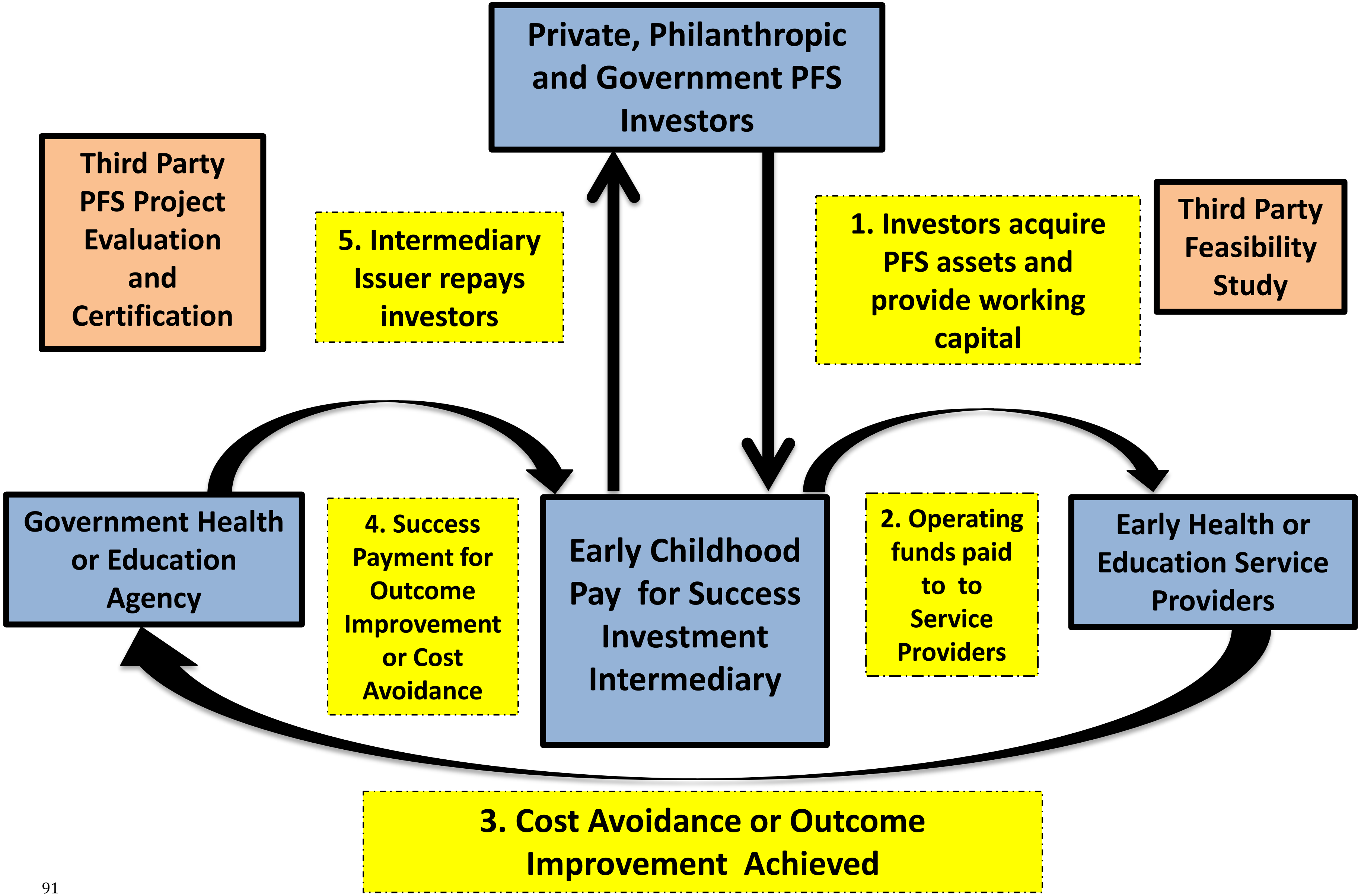
- ❑ **“Pay for Success” refers to performance-based contracting** between government and providers of social services arranged by an intermediary or lead contractor. Government pays only when results are achieved.

- ❑ **“Success” has two meanings** –
  - ✓ **“Cost avoidance”** actual reductions in governments operating costs that are the result of an intervention
  - ✓ **“Outcome improvement”** measured changes in outcomes in desired directions that are the result of an intervention

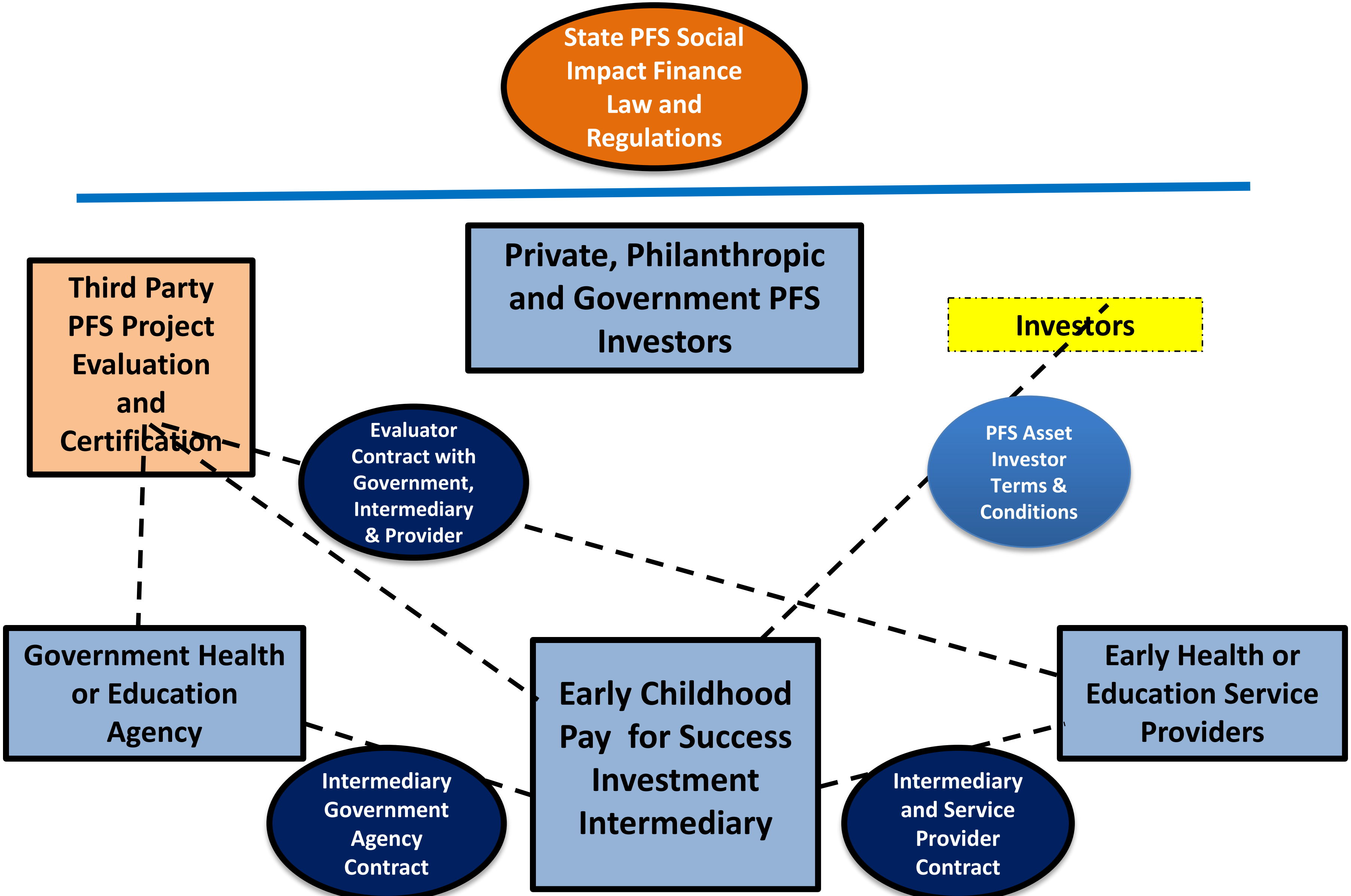
Main Participants in a Pay for Success Project



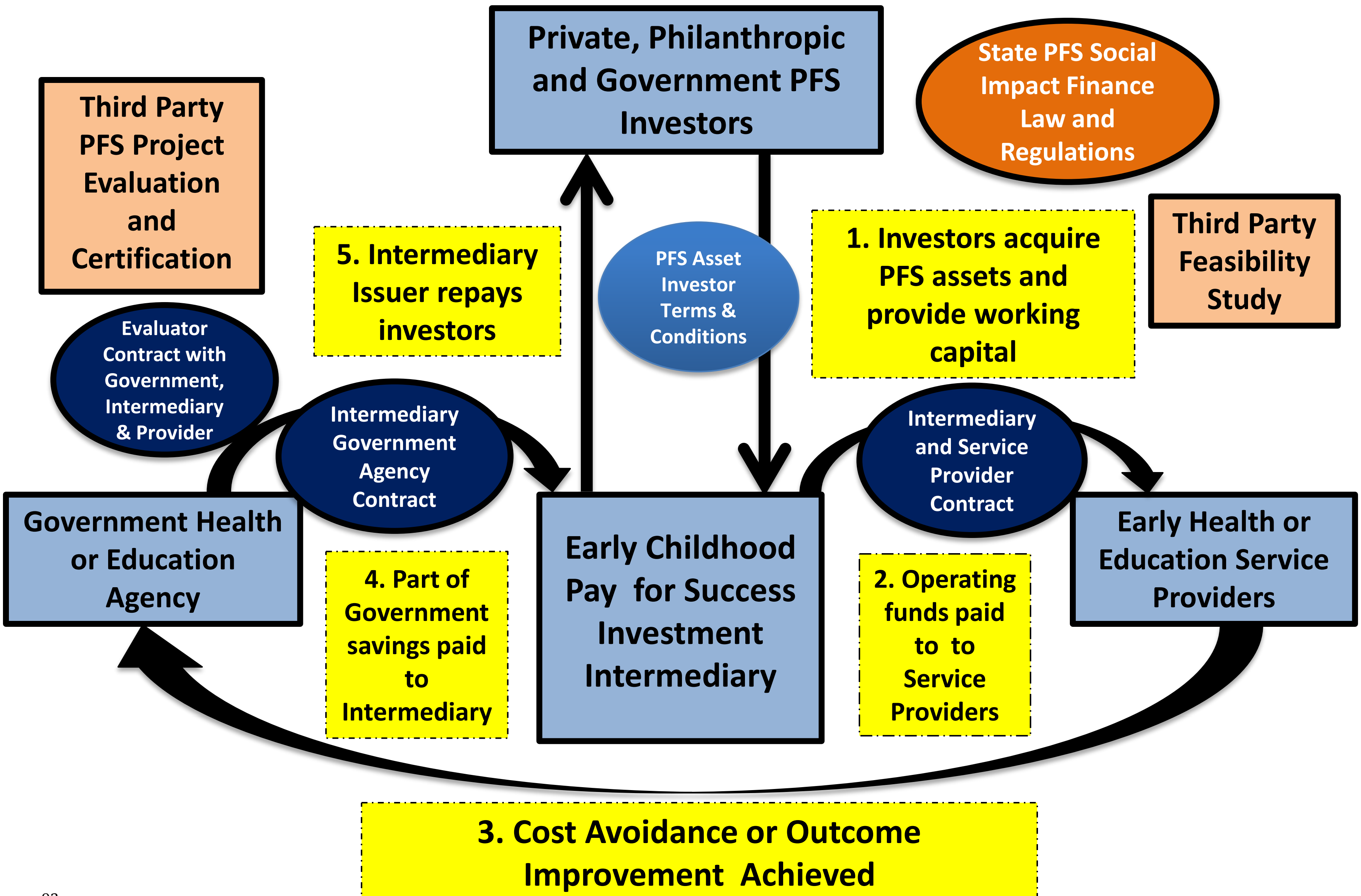
Flow of Funds in a Pay for Success Project (arrows)



Pay for Success Statute and Contract Agreements (ovals)



Putting it all together -- A Pay for Success Project



“Success Payment”

- ❑ **“Success Payment”** is the portion of the government operating cost reduction paid to the Intermediary for successfully reducing the operating costs of the Government, or a payment for achieving specific outcome improvements

- ❑ **Intermediary** uses the success payments to
  - ✓ **pay interest and principle** to investors
  - ✓ **pay bonuses to providers** who exceed expected performance levels

Establishment and Funding Time Line

State Law and Regulation Enactment: Unknown

Establishment and Fundraising Phase: 18 Months

Stakeholders agree to organize an Early Childhood Social Impact Enterprise

Third Party Feasibility Study Done

Early Child Social Impact Enterprise Established

Contracts with Service Providers, Government Agencies & 3rd Party Certifier Completed

Social Impact Assets Issued and Funds Received by ECSIE

2 months

6 months

2 months

6 months

2 months

Total: 18 months

Intervention Service and Investment Success Time Line

Intervention Service Delivery and Initial Success Indication

- 8 months for prenatal (5 mo average prenatal + 3 mo postpartum)
- 60 months for pre-k (2 yrs pre-k, 3 yrs k-2nd grade when 90% of special-ed assignments completed)

Operating funds paid to to Service Providers

Early Health or Education Service Provided

✓5 months for prenatal health
✓2 years for pre-k

Cost savings generated and confirmed by initial evidence

✓3 months for prenatal health
✓3 years for pre-k

3td Party Evaluator Certifies Savings to Government Agency, Intermediary & Service Providers

1 month

Government Health or Education Agency pays large portion of savings to Intermediary

Intermediary repays investors

1 month

10 to 62 months total

Why do investors invest?

Private Individuals and Funds – Invest to obtain interest earnings and return of principle

Philanthropic Institutions –

- ✓ Make PRI investments for interest earnings and principle repayment if possible (first-loss tranche)
- ✓ Make grants to obtain the benefits of long-term all-in outcome improvements that come from interventions such quality prenatal counseling or prekindergarten

Local Governments – Invest to obtain more efficient near-term operations and to obtain long-term all-in outcome improvements

State and Federal Governments – Invest to obtain long-term all-in outcome improvements and stronger economic and per capita income growth

Longer-Term All-In Outcome Improvement Benefits

Government and philanthropic investment in PFS pre-k projects should be viewed in the context of the all-in benefits of to the public sector.

For pre-k these benefits include everything from lower special-ed costs to higher tax revenues from higher-earning employment. Many studies have looked at the cost/benefit question. Estimated returns on quality pre-k range from 7% to 18% per year.

Monetizable and Non-monetizable Benefits

✓ **Monetizable benefits are ones that can be accurately measured and captured in workable contracts within investable timeframes** from twelve months to ten years. Non-monetizable benefits may be extremely valuable to individuals and society, but they are difficult to measure and capture in workable contracts. Such returns also often take more than ten years to realize.

✓ **Near-term special-ed and infant intensive care cost reductions are monetizable,** that is, the cost avoidance can be measured accurately and a portion of it can be paid as a “success payment”

PFS Fundamental Relationships

__Cost Ratio__ **- The ratio of intervention cost to remediation cost.**

The higher the cost of remediation is relative to the cost of intervention, the higher the possible cost avoidance will be, other things equal. For example, the more special-ed costs relative to pre-k, the less pre-k needs to reduce special-ed assignment rates in order to achieve threshold feasibility.

__Effect Ratio__ **- The ratio of intervention effect to non-intervention effect.**

The more the intervention achieves the desired outcome, the more cost avoidance is achievable. For example, the more pre-k reduces special-ed assignment rates, the less difference there needs to be between the cost of pre-k and the cost of special-ed.

__Investor Ratio__ **– The ratio of investor capital to philanthropic and government capital.**

The more philanthropic and government capital there is in a PFS project , other things equal, the better will be the risk and return profile of the project for investors.

Two Examples: Prekindergarten Returns and Benchmark Prekindergarten Programs

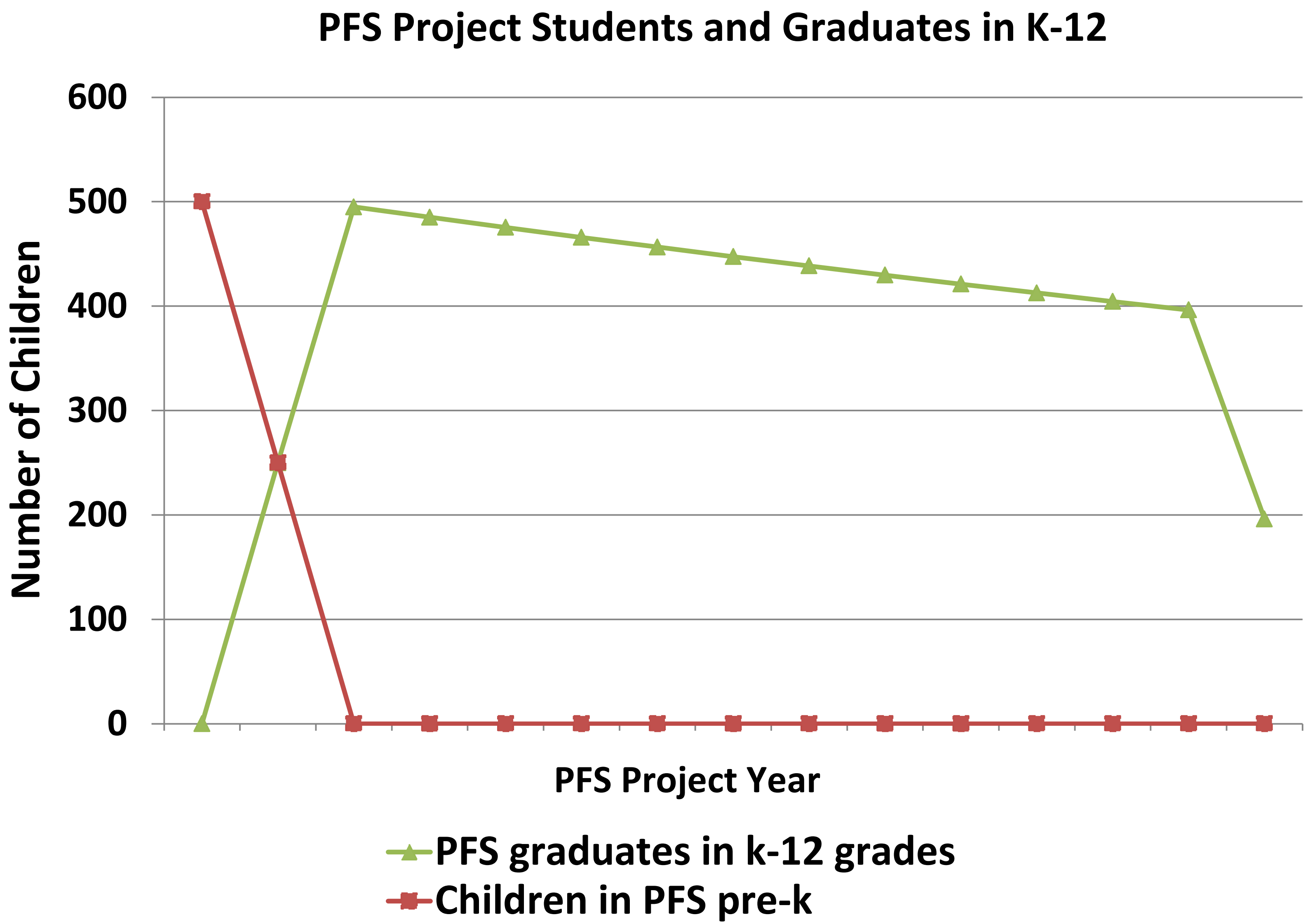
Granite School District Preschool Program

- ✓ Cost Ratio: Pre-k/Special-Ed = 47%
- ✓ Effect Ratio: 30% of 737 at-risk children potentially eligible for Special Education at 4 years old; 1.5% assigned to Special Education through elementary school

Bethlehem Area School District Preschool Program

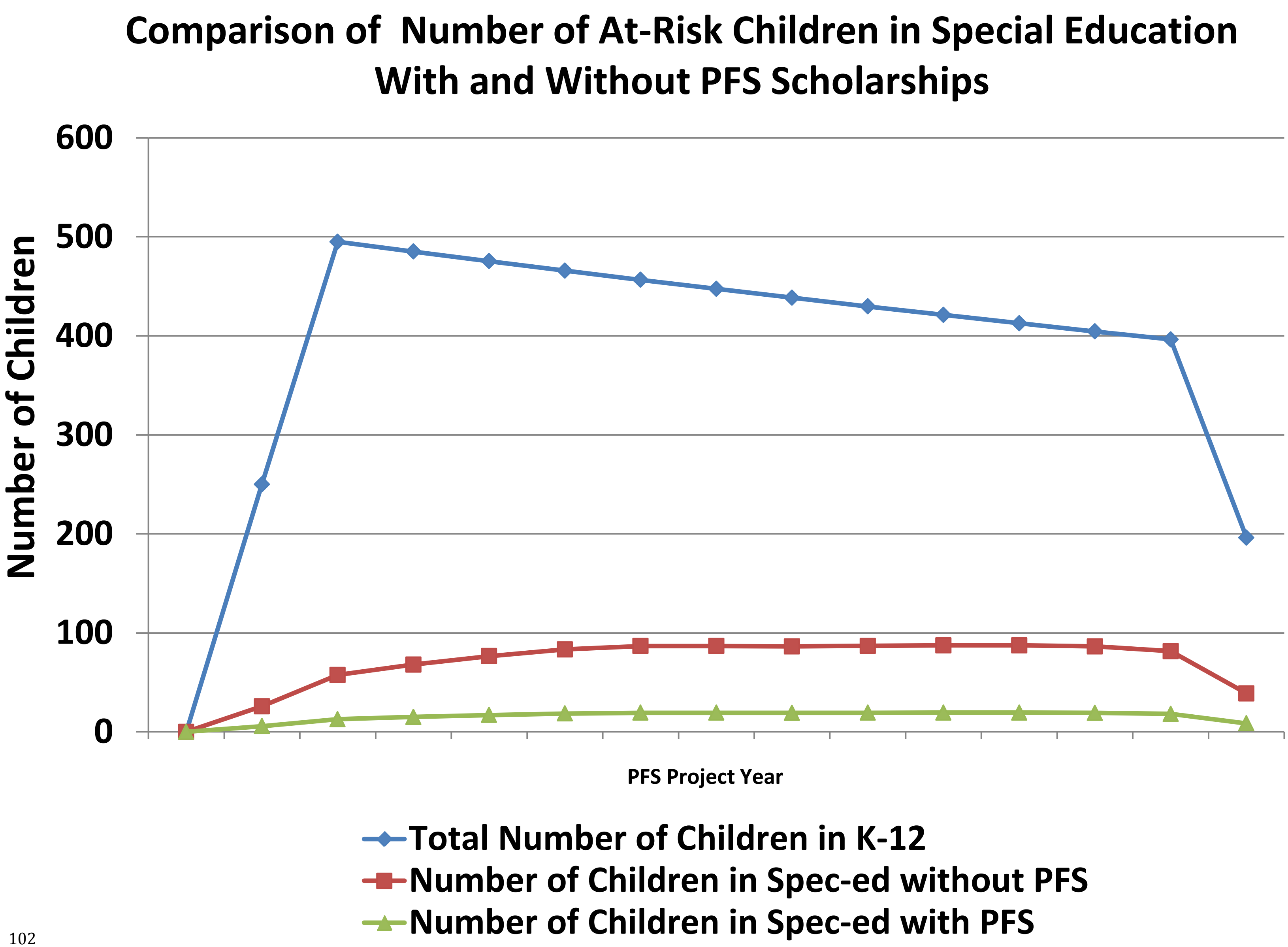
- ✓ Cost Ratio: Pre-k/Special-Ed = 65%
- ✓ Effect Ratio: 18% assignment rate for low income students without pre-k to 2.5% with pre-k

Prekindergarten: 500 At-Risk Students in PFS Pre-k and K-12

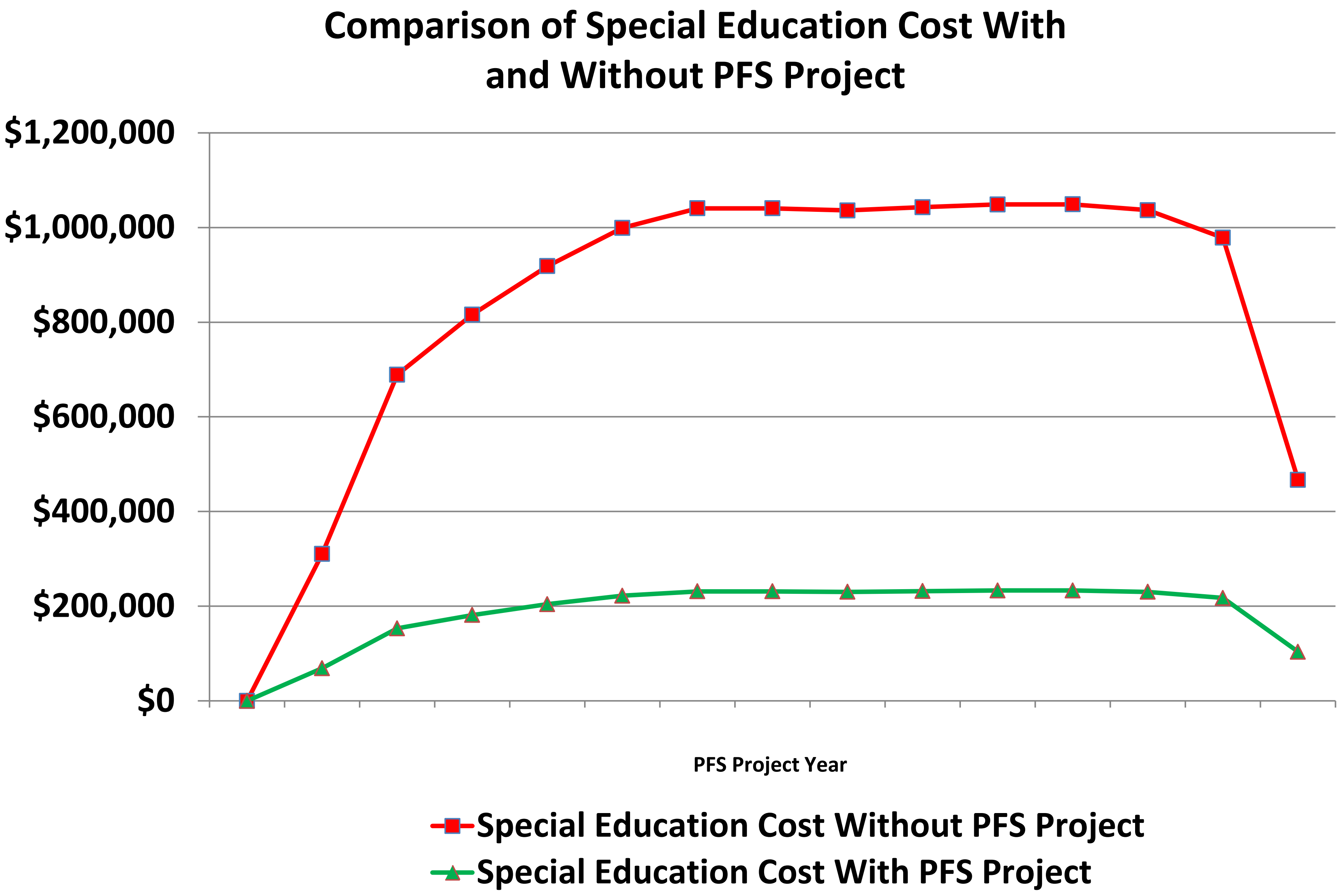


Source: "Financing Human Capital Development for Economically Disadvantaged Children: Applying Pay for Success Social Impact Finance to Early Child Development." J A Dubno, R H Dugger, and M R Smith. ReadyNation Working Paper, June 10, 2013

Projected Reduction in Spec-Ed Assignment for 500 Students



Projected Spec-Ed Cost Avoidance for 500 Students



Description of the Financing Model: Fixed-Debt

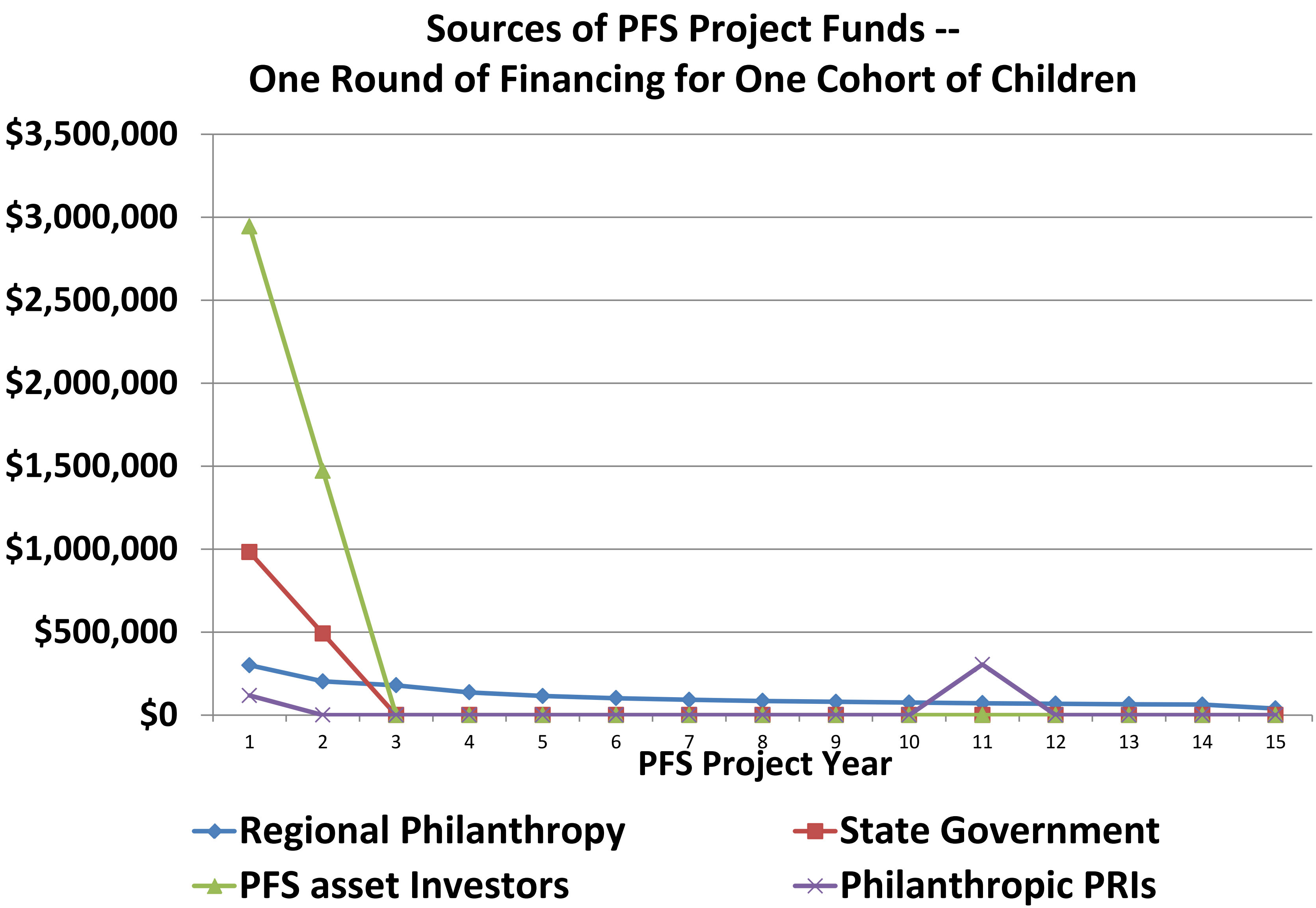
a. Investors receive fixed interest and principal payments on a loan or bond with a given maturity, such as five or ten years.

b. Investor funds are used to provide "scholarships" that pay for prekindergarten education services.

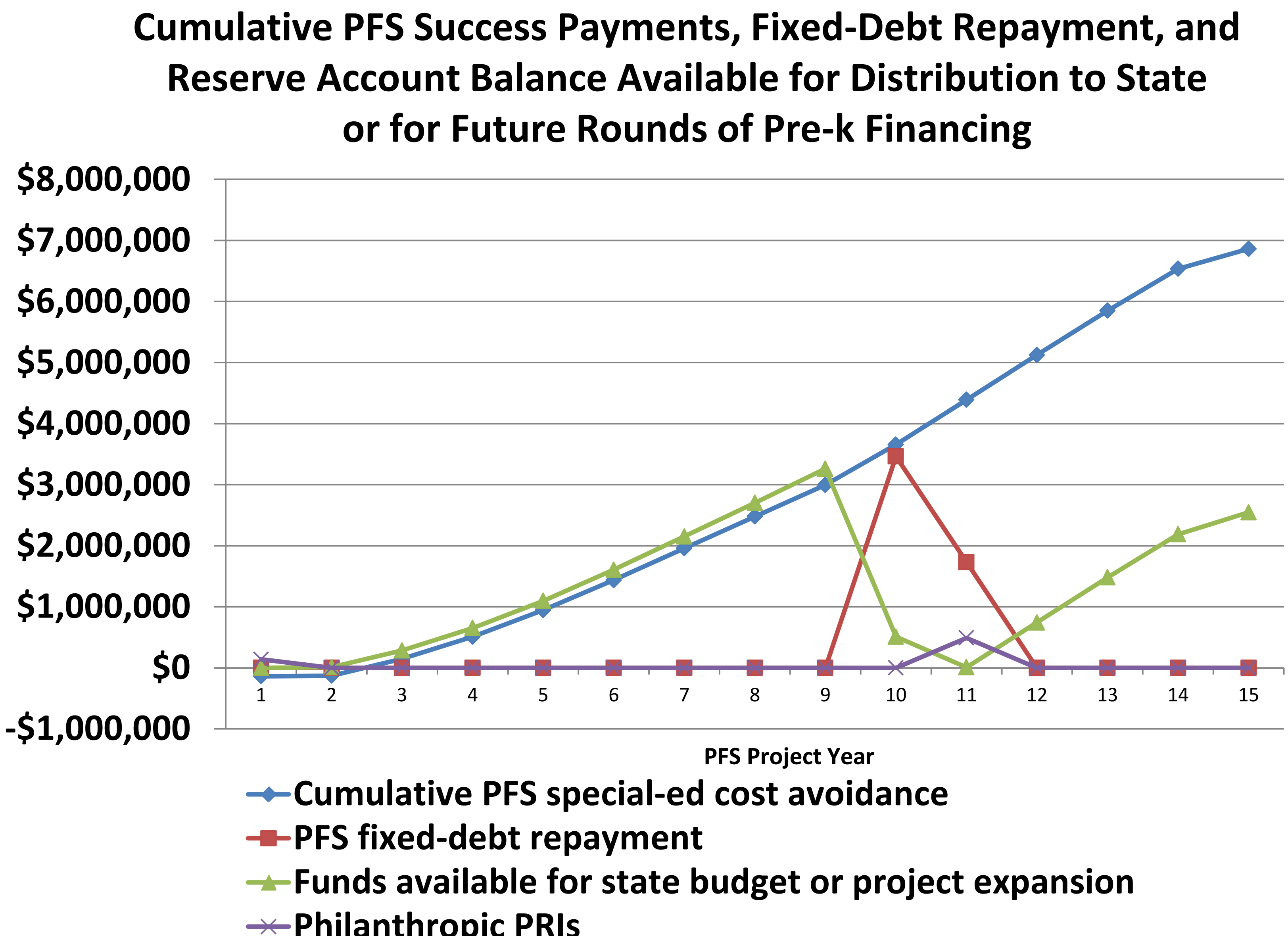
c. Success Payments after interest expense accrues in a reserve account to be available for later payments of principal. Any amount in the reserve account after PRI investments are repaid are paid to the state.

d. The timely payment of fixed-debt interest and principle is guaranteed by philanthropic foundation PRI investment commitments to cover periods of negative cash flow -- expected in the first few years when operating expenses exceed Success Payments, and when large payments need to be made to repay debt principle.

Fixed Debt Structure



Fixed Debt Structure



Description of the Financing Model: Fixed-Debt

PFS Project Results:

PV of special-ed cost without PFS project	$	8,053,880
PV of special-ed cost with PFS project	$	1,342,313
PV of special-ed cost avoidance (budget savings)	$	6,516,084
Cost avoidance as a percent of special-ed cost without PFS		81%
PV of Success Payments to the Intermediary	$	5,864,476
Success Payments as percent of special-ed cost without PFS		73%

Funding Source Amounts:

PV of philanthropic grants	$	1,420,789
PV of philanthropic PRIs	$	334,123
PV of state government investment	$	1,415,131
PV of federal government investment	$	-
PV of private source investments	$	4,245,393
PV of project funding from all sources	$	7,415,436

Results of the Financing Model: Fixed-Debt

Investor Results:

PV of Intermediary fixed-debt obligations acquired by Investors	$	4,245,393
PV of principle and interest payments to Investors	$	4,615,610
IRR to Investors (Yield to Maturity, not Coupon))		4.17%

Philanthropic PRI Results:

PV of Intermediary PRI obligations acquired by philanthropies	$	334,123
PV of principle and interest payments to philanthropies	$	295,932
IRR to PRI investors		1.29%

Government Results:

PV of Government investment	$	1,415,131
PV of payments to Government less PRI for gen'l budget or more pre-k	$	1,121,823
IRR to State Government (incl inv inc & assuming PRI repay in 15th yr)		1.26%

Description of the Financing Model: Pass-through

a. Investors receive annual payments consisting of a percentage of the Success Payments.

b. These payments constitute interest payments and principle repayment. The actual yield on the Pass-Through depends on the amount and timing of the Success Payments.

c. Pass-Through payments may vary from year to year because they depend directly on the amount of Success Payments actually earned.

d. In the Pass-Through structure, the debt instrument stands on its own – neither payments nor a given return on investment are assured by philanthropic PRI investment commitments.

e. Pass-Through obligations have higher investment risk than fixed-debt obligations.

f. The state receives the success payments not paid to support the Pass-through in the year in which it occurs.

Description of the Financing Model: Pass-Through

PFS Project Results:

PV of special-ed cost without PFS project	$	8,053,880
PV of special-ed cost with PFS project	$	1,342,313
PV of special-ed cost avoidance (budget savings)	$	6,516,084
Cost avoidance as a percent of special-ed cost without PFS		81%
PV of Success Payments to the Intermediary	$	5,864,476
Success Payments as percent of special-ed cost without PFS		73%

Funding Source Amounts:

PV of philanthropic grants	$	1,420,789
PV of philanthropic PRIs	$	-
PV of state government investment	$	1,415,131
PV of federal government investment	$	-
PV of private source investments	$	4,245,393
PV of project funding from all sources	$	7,081,313

Results of the Financing Model: Pass-Through

Investor Results:

PV of Intermediary fixed-debt obligations acquired by Investors	$	4,245,393
PV of pass-throughs to Investors	$	5,181,264
IRR to Investors		6.0%
(Percentage of Success Payments to Investors that Results in Requried IRR)		88.35%

Philanthropic PRI Results:

PV of Intermediary PRI obligations acquired by philanthropies	$	-
PV of principle and interest payments to philanthropies	$	-
IRR to PRI investors		0.00%

Government Results:

PV of Government investment	$	1,415,131
PV of pass throughs to Government	$	683,211
IRR to State Government (continuous payment)		-6.27%

Financial Model Projection Results Variations

Variation A: Funding Source: 75% Investor, 10% state, 15% federal

	Fixed-Debt Structure	Pass-through Structure 88.35% of Success Payments paid to Investor to reach Target Return
IRR to the Investor	4.17%	6.00%
IRR to PRI	1.29%	0%
IRR to the State	8.28%	5.82%

Variation B: Funding Source: 50% Investor, 50% state

	Fixed-Debt Structure	Pass-through Structure 58.9% of Success Payments paid to Investor to reach Target Return
IRR to the Investor	4.17%	6.00%
IRR to PRI	1.39%	0%
IRR to the State	2.14%	0.75%

Variation C: Funding Source: 50% Investor, 25% state, 25% Federal

	Fixed-Debt Structure	Pass-through Structure 58.9% of Success Payments paid to Investor to reach Target Return
IRR to the Investor	4.17%	6.00%
IRR to PRI	1.39%	0%
IRR to the State	7.45%	11.63%

Financial Model Projection Results: Sensitivity to Spec-ed Rate

Variation A: Funding Source: 75% Investor, 10% state, 15% federal

Fixed-Debt Structure

	Reduction of special education assignment rate due to PFS pre-k					
	from 18% to 3%	from 18% to 4%	from 18% to 5%	from 18% to 6%	from 18% to 7%	from 18% to 8%
IRR to the Investor	4.17%	4.17%	4.17%	4.17%		
IRR to PRI	1.29%	1.23%	1.22%	1.22%		
IRR to the State	8.28%	5.34%	0.74%	-11.96%	*Return too low*	*Return too low*

Pass-through Structure

	Reduction of special education assignment rate due to PFS pre-k					
	from 18% to 3%	from 18% to 4%	from 18% to 5%	from 18% to 6%	from 18% to 7%	from 18% to 8%
IRR to the Investor	6.00%	6.00%	*Below target rt*	*Below target rt*	*Below target rt*	*Below target rt*
% of Success Payment Payout	88.35%	94.65%				
IRR to the State	5.82%	-5.48%	*Return too low*	*Return too low*	*Return too low*	*Return too low*

Financial Model Projection Results Sensitivity Analysis

Variation C: Funding Source: 50% Investor, 25% state, 25% Federal

Fixed-Debt Structure

	Reduction of special education assignment rate due to PFS pre-k					
	from 18% to 3%	from 18% to 4%	from 18% to 5%	from 18% to 6%	from 18% to 7%	from 18% to 8%
IRR to the Investor	4.17%	4.17%	4.17%	4.17%	4.17%	4.17%
IRR to PRI	1.39%	1.39%	1.39%	1.39%	1.39%	1.29%
IRR to the State	7.45%	6.26%	4.88%	3.22%	1.13%	-1.70%

Pass-through Structure

	Reduction of special education assignment rate due to PFS pre-k					
	from 18% to 3%	from 18% to 4%	from 18% to 5%	from 18% to 6%	from 18% to 7%	from 18% to 8%
IRR to the Investor	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
% of Success Payment Payout	58.90%	63.10%	67.95%	73.65%	80.35%	88.35%
IRR to the State	11.63%	8.54%	5.09%	1.10%	-3.79%	-10.59%

Conclusions and Future Research

Implementing operational PFS projects will be helped if future research focuses on at least five areas of PFS finance:

1. **<u>Standard error estimates</u> of the distribution of returns on PFS assets.**
2. **PFS project <u>capital structures, risk, subordination</u> and loss absorption.**
3. **<u>Sensitivity analysis</u> of returns to variations in parameter values and financial structures.**
4. **<u>Pre, concurrent and post intervention data</u> needed to evaluate near-term financial returns and longer-term all-in outcome improvements.**
5. **<u>Research methodologies</u> to use when needed data are limited.**

Pay for Success Reading and Resource List -- ww.ReadyNation.org/PFS

Working Papers for Discussion and Comment

"Early Childhood Pay for Success Social Impact Finance: Organizational Steps, Memorandum of Understanding and Contract Outlines." Report of the ReadyNation Working Group on contracts in Early Childhood Social Impact Finance, ReadyNation Working Paper, June 10, 2013.

"Financing Human Capital Development for Economically Disadvantaged Children: Applying Pay for Success Social Impact Finance to Early Child Development." Janis A. Dubno, Robert H. Dugger, and Michelle R. Smith. ReadyNation Working Paper, June 10, 2013

Click here to access the PFS Social Impact Finance Spreadsheet

Recommended General Reading

"Social Impact Bonds: A Guide for State and Local Governments." Social Impact Bond Technical Assistance Lab (SIB Lab), Harvard Kennedy School. June 2013.

"Pay for Success Financing." *Community Development Investment Review* 9 (1). Federal Reserve Bank of San Francisco. April 2013.

"Case Study: Preparing for a Pay for Success Opportunity." Third Sector Capital Partners. April 2013.

Megan Golden. "Developing a Social Impact Bond: Lessons from a Provider." The Children's Aid Society. January 2013.

Laura Callanan, Jonathan Law, and Lenny Mendonca. "From Potential to Action: Bringing Social Impact Bonds to the U.S." McKinsey & Company. May 2012.

“What Is Pay for Success?” Third Sector Capital Partners. October 2012.

"A New Tool for Scaling Impact: How Social Impact Bonds Can Mobilize Private Capital to Advance Social Good."Social Finance. October 2012.

Michael Bloomberg, City of New York, "Bringing Social Impact Bonds to New York City" August 2012.

Jeffrey Liebman. "Social Impact Bonds: A Promising New Financing Model to Accelerate Social Innovation and Improve Government Performance." Center for American Progress. February 2011.

APPENDIX C: September 10, 2013 Social Impact Bond Meeting

- September 10, 2013 Social Impact Bond Meeting Agenda
- September 10, 2013 Social Impact Bond Meeting Notes
- September 2013 Survey Results
- Presentation by Ms. Rebecca Leventhal – Maryland Social Impact Bond Summer Study 2013 Working Group Meeting #2
- Presentation by Ms. Kristin Misner – Bringing Social Impact Bonds to New York City

Social Impact Bond Summer Study 2013

Tuesday, September 10, 2013
9:00 am to 12:30 pm

The Institute for Innovation & Implementation, UM SSW
306 W. Redwood Street, Baltimore

Workgroup Meeting #2 Agenda

Workgroup Goal: Report to the House Appropriations Committee on the merits of Social Impact Bonds (SIB) and their relevance and applicability to Maryland.

Meeting Goals: Identify 1) how Social Impact Bonds (SIBs) are being measured; 2) which savings go to investors; and, 3) which applications will work under the SIB model?

9:00-9:30 am	**Discuss results of the participant survey (Michelle Zabel)**
9:30-10:15 am	**Presentation by Jeffrey B. Liebman, PhD, Malcolm Wiener Professor of Public Policy at the John F. Kennedy School of Government, Harvard University** *Dr. Liebman will present on his work with SIB pilot tests, including the Massachusetts SIB project (authorized by the Legislature to work on SIB initiatives involving individuals who are homeless and youth involved with the criminal justice system).*
10:15-11:00 am	**Presentation by Rebecca Leventhal, Director on the Business Development Team** *Ms. Leventhal will present on Social Finance's SIB projects, including in the UK (Peterborough) and Fresno, CA. The Peterborough SIB involves recidivism for parolees, and the Fresno SIB is to reduce the need for children in the area to visit emergency rooms and hospitalization for asthma problems.*
11:00-11:15 am	**Break**
11:15am-12:00pm	**Presentation by Kristin Misner, Chief of Staff to the Deputy Mayor for Health and Human Services in the Office of the Mayor, New York City** *Ms. Misner will present on the NYC SIB effort that included Goldman Sachs, Bloomberg Foundation, the Mayor's Office, and the NYC Department of Corrections to implement a program for 16- to 18-year-olds detained at Rikers Island with the goal of reducing the high recidivism rate for this population by focusing on personal responsibility education, training, and counseling.*
12:00-12:30pm	**Facilitated Workgroup Discussion**

SIB Summer Study Contact: Roann Tsakalas, rtsakalas@msde.state.md.us , (410)767-7802
Next Meeting: Monday, October 7, 2013, 9AM-12:30PM

Social Impact Bond Summer Study 2013

Tuesday, September 10, 2013
9:00 am to 12:30 pm

The Institute for Innovation & Implementation, UM SSW
306 W. Redwood Street, Baltimore

Workgroup Meeting #2

<u>Workgroup Goal</u>: Report to the House Appropriations Committee on the merits of Social Impact Bonds (SIB) and their relevance and applicability to Maryland.

<u>Meeting Goals</u>: Identify 1) how Social Impact Bonds (SIBs) are being measured; 2) which savings go to investors; and, 3) which applications will work under the SIB model?

Meeting Notes:

Members in Attendance:
Michelle Zabel, The Institute for Innovation & Implementation, *Chair*
Nathan W. Bowen, Department of Budget & Management
Donna Riley (for Marcella Franczkowski), Maryland State Department of Education
Jeanne-Marie Holly, Maryland State Department of Education
Farid Keshavarz, Department of Public Safety & Correctional Services
Delegate Samuel Rosenberg, Maryland General Assembly
Dan Feller, Governor's Office for Children
Netsanet Kibret, Department of Human Resources
Miriam Shark, Annie E. Casey Foundation
Margaret Williams, Maryland Family Network
Terry Staudenmaier, Abell Foundation
Rolf Grafwallner, Maryland State Department of Education
Al Zachick, Department of Health and Mental Hygiene
Ilise Marrazzo, Department of Health and Mental Hygiene

Observers: George Failla, Caroline Boice, Steven Schreiber Stahl

Staff: John Spears, Roann Tsakalas, Deborah Harburger

Discuss results of the participant survey-

Deborah Harburger reviewed the survey findings (see handout). Workgroup members will receive basically the same survey after this meeting to see if some questions were answered by the presenters and if participants' feelings have changed. The workgroup reviewed the notes from the July meeting, and Miriam moved for approval of the notes and Margaret seconded. The notes were approved. Thoughts shared by members:

- LMBs were interested in the idea of using bonds to pay for intervention services.
- Speakers added value to what members already knew.
- Early childhood is difficult to find the payoff because the dividends are realized so much further down the road and therefore hard to cash in on.

- Member suggested that asthma would be a place where savings are seen up front but the devil is in the details.
- It is important for the group to hear about the downside of SIBs. Asthma example is tough because managed care for Medicaid would realize the savings. Is it worth the cost of the borrowing?
- Are there things that we should be doing now that we are not doing and we could finance through a SIB. It was suggested that perhaps the Department of Juvenile Services may have a program that would benefit.
- Ask in the next survey about specific programs that could work.
- Lead paint exposure abatement as savings down the road.
- Early identification of programs to scale – home visiting, early childhood, expanded school mental health – take a few jurisdictions where we know there are problems, and take the continuum of services to full scale.
- Members should think about grants that you have applied for and think about some savings that you may realize that may be a conversation for a SIB.

Michelle Zabel introduced Dr. Liebman -
Dr. Liebman is a Malcolm Wiener Professor of Public Policy at the John F. Kennedy School of Government, Harvard University. Dr. Liebman presented on his work with SIB pilot tests, including the Massachusetts SIB project.

First, Dr. Liebman described what the process has been like in New York and Massachusetts. Second, he will provide lessons learned. The idea of SIBs has spread faster than he thought. For 3 years, President Obama has put SIBs in his budget, New York City has started implementation of their project, New York State and Massachusetts have gone through procurement to put together projects. Massachusetts projects are for the homeless and juvenile offenders. New York State's SIB is for adult offenders. The Rockefeller foundation has enabled Dr. Liebman has placed a full time staff in Massachusetts and New York State to help put together the projects. This has expanded to 10 states – see map in presentation.

Three currents have come together to push SIBs forward –

1. Much more measuring of outcomes of social programs is needed;
2. In the current budgetary environment when no government can afford to keep doing what it is doing much less start something new; and
3. The sense that we are not making enough progress on social problems. There is a sense that "something is broken" here. There are innovative non profits doing successful things but no evaluation to support their work. SIBs may be a way to scale up successful programs and fund innovative approaches to social programs.

Steps in Massachusetts and New York State that made "Pay for Success" an option.

1. Decide it is a good fit for your goal.
2. Senior government person (champion) that thinks this is going to work. It takes a year to put together, and someone has to own this, such as the Governor or Mayor.

3. A SIB is not worth doing for small objectives. Envision a big impact for an entire population, and make it a top priority. A small program that has a path to go statewide. It is best if the big goal is on the top 5 or 10 list of chief executive.
4. Choose a project that you can share across government agencies. So that agencies can share data and break down barriers to measure over time. New York State can now follow juvenile offenders through state education and other agencies' data systems into adulthood.

Implementing a SIB is a 3 track process –

- Experts in government need to brainstorm where a SIB would fit. Is there an underinvestment in prevention? Are there good programs that were cut in the budget cycle? Could a good evaluation bring out the value of the program? Are their programs with long wait lists? Should get 30 or 40 ideas for a potential "Pay for Success" program.
- Then you find that half the programs on your list can't measure success. So you could do an RFI to get additional ideas.
- Examine lists of proven programs nationally from other places for serious consideration.
- Need to be sure providers of services are in the local community.

This whittling down process helps you to see what you want to go forward on. What will give you the big benefit? Does it have scalability? Is there an effective way to evaluate the outcomes? Government needs to decide what it can handle –more than 3 SIBs would be crazy.

Conduct a real procurement process to get partners. Massachusetts let 2 RFPs for intermediaries, and then one for the provider of service. New York State asked for bids from teams (intermediary and provider as a team). There are lots of ways to do this.

Question –Cost benefit analysis: What is needed to do this?

Response - Have to do some initial rough cost benefit analysis. There must be potential for high net benefit. What do we think is out there for program models that would provide benefits? Recidivism is a good example. Government must do a lot of data work to prepare for receiving the RFPs:

(1) Government must conduct a vigorous cost analysis to see what it is willing to pay for the reduction based on 10% or 12% or 15% for example. This is the payment schedule and is needed for the procurement process.

(2) How many people are you trying to serve? Where are they geographically? How much additional service are you adding (data work)? Can you use historical data from specific providers of service and compare their results?

(3) Do you have the legislative authority to support the SIB? Are your evaluation partners in place?

(4) In order to enter into negotiations you must have exact payment terms for providers. The government must have a view of its savings before negotiating. The benefits must be above the cost of services. The range of outcomes and benefits must be higher than the costs so that a project can get done.

(5) Negotiate how much savings go to investors and what savings go to government. The surplus is shared through the contract. Investors get most of the savings.

(6) Need a plan in place for when the project is over so that if it is successful you capitalize on the work and go forward.

Lessons learned –

- It is hard to find solid evidence that a project is going to work. There are a lot of innovative programs but even the best often lack full proof evaluations. If a SIB is using an innovative program without solid evaluation, you will learn more because you are testing things but investors are taking on more risk.
- In this circumstance the structure of investment will require more socially minded investors. For example, in New York City the Bloomberg Foundation backed the SIB project to provide some protection for the investors. Goldman Sachs risked $2m to make $2m more. Goldman has a 50-50 gamble on the project. Most projects will not have such a generous back stop. In New York City, the government will absorb at least one quarter of the risk, investors will take one quarter of the risk, and the foundation half of the risk.
- The SIB contract states who gets paid back first and what percentage or amount they get of the savings. Then, as you go down the list and distribute the money, some down the list may not get paid back. Other contracts may stipulate that there are multiple pay backs but no one gets the full amount back that they invested.
- The major point to remember is that there is a lot of risk. A government will not do this with all investors' money.
- You can have a situation where everything goes right, but other external factors such as unemployment rises and/or crime goes up and interferes with the effect. So the program works but the data does not demonstrate it. Use a comparison group to mitigate this risk and show how the program performed. This is the reason for a detailed evaluation plan.
- One of the greatest benefits of the SIBs is that contracts are binding so that if the administration changes, actors need to continue with the contract. The long term plan is committed in the contract and should ensure no changes to the SIB.
- The SIB project has to last at least 3 years to realize good data. Dr. Liebman pushes regularly for projects of at least 4 years duration in order to assemble evidence for the renewal of the project.
- Dr. Liebman is still trying to see what risk tolerance that investors have. New York State's programs are known to be effective in the community and it was easier to sell the investor, but it is still too early to know.
- The SIB must serve at least a couple hundred of people in order to have a good sample size for the data.

Michelle Zabel introduced Ms. Rebecca Leventhal –

Ms. Leventhal presented on Social Finance's SIB projects, including in the UK (Peterborough) and Fresno, CA. The Peterborough SIB involves recidivism for parolees, and the Fresno SIB is to reduce the need for children in the area to visit emergency rooms and hospitalization for asthma problems.

How is social finance is different from other presenters?

- Jeff is an advisor to governments. Social Finance (SF) deals with the government leaders and acts as an intermediary in the SIB process. See PowerPoint presentation, slide 4 which lays out the key steps to launching and implementing successful SIBs. Rebecca explained that a lot of work comes from government side in step 1. The government's cost benefit analysis is crucial in finding the savings.
- Key questions: What is the government's willingness to pay because cost benefit may be after the 3 years of the contract? Social Finance works with investors to see what they are willing to accept.
- SF works with providers and investors to determine what the right investment model is, and what the right metric is to measure success. What can be monetized? Does one outcome speak more to the theory of change than another? What is the outcome number that allows the government to pay out the savings?
- The ability of tapping into capital markets is unique here, and is extremely valuable. Don't underestimate their ability to be important players.
- SF works to raise the capital. In the NYC SIB, the provider had a 30 year history of good service, and was a good match to implement this new intervention. But because the type of program was new to the provider, the risk for the new program was high, so investors were not willing to step up. So the Bloomberg Foundation has backed stopped the SIB. NYC wants to use the SIB to spur innovation in human services. In other deals, you are seeing more strongly evidenced programs that are already implemented in the state, and have external evaluations with detailed data to show how participants gained from programs. This affects what kind of capital comes into the deal.

What makes for a good SIB project?

- Good SIB projects will work best when government knows the program is effective and does not have money to implement it. SF taps into capital markets that normally are not accessible to these projects. It is a delicate balance to be sure when you are building the kinds of models that will be able to spur more capital investment.
- The right mix of philanthropy and capital to support the transaction in the long term will create a market for the program down the road. SF acts as the issuing agency. Step 5, slide 4 – project management must make course corrections as needed and evaluate the data constantly. The intermediary can deliberate the contract if situations change (i.e. problem is changed based on external circumstances).

SF is funded a few ways: philanthropy (the Rockefeller Foundation) has funded them which provided some flexibility to push the SIB effort forward. In the long term, SF's goal is to become self sustaining and to find financing in the overall transaction. Right now sometimes, SF is paid by government up front to develop the transaction or through savings. SF also receives many combinations. Government has used executive office budgets to contract with SF because the cost has been under $100k.

Slide 5 lists SIB risks. Data helps mitigate the risk for investors. Execution risk is the risk that implementation falls short for various reasons. It is important to mitigate execution risk upfront by identifying needs for support prior to the provider's implementation. Right now, SIBs are too new to see investors back out of deals. Active project management is important to mitigate this. Government's risk is of defaulting. Massachusetts appropriated $50m in savings to protect the investors. NYC has not made any legislative changes, but the Bloomberg Foundation has created protections and the contract can protect the investors.

In Fresno the State/local government is not involved, but rather the California Endowment. In the UK SIB, the contracting party is the Ministry of Justice, and both the Ministry of Justice and the National Lottery are lending important support. The UK does not have a specific law to protect the investors.

Slide 6, in a SIB the benefit/cost savings must exceed the cost of intervention. The SIB contract must have an acceptable length of time for investors. You don't want it to be too long to see results.

From the PR standpoint, the emphasis on criminal justice, the current issue, is a disadvantage. Investors are interested in deals in early childhood. Because they want something more story worthy. High net worth clients sell the investment with early childhood to tell a better story, and health also makes for an appealing story. You want to get a max bang for your buck and cause no harm.

Question: how are savings realized by government to pay back investors?

- In Massachusetts the project is to reduce the number of chronically homeless that go to ERs too often. First, they are addressing housing to lower ER visits. 400 homeless people targeted. By reducing hospital costs, Massachusetts wants to reduce the amount of money the state is paying out every year in perpetuity. One goal may be to reduce recidivism by 10% for example. Government agrees to bear risk to a certain point in the contract. Government pays back the negotiated amount in the contract. Government has said that if we get back in the end that is good. Massachusetts is not worried about the payout. Government sees benefit to taxpayers over the long haul. This is the art of putting a deal together.

Slide 12 demonstrates the Fresno, CA SIB. The goal is to reduce asthma incidence in children. Existing data did not show a connection to saving money. This project is trying to realize and document the economic savings of this work, and is not a SIB at this time, but rather a Pre-SIB. The grant from the California Endowment is covering the cost of the project. The provision of service is asthma education in order to reduce hospital visits. The project is studying cost reductions to State Medicaid and also private payors. The SIB will also look at economic effects on parents who are hourly wage workers and are able to go work more steadily. Fresno hopes to take to the project to scale as a SIB. The current Pre-SIB is an18 month project, launched in May and beginning to serve people in late August.

States would be able to access President Obama's $300m in his Pya-for-Success initiative to pay the federal portion of savings for a state SIB project if it were to be passed by Congress. That would create some support for savings realized in federally funded programs.

Question: is legislation needed? Do investors need protection? Do agencies need authority to do this?

- Other states have not gotten into these questions prior to getting into a SIB. So they are doing a look back in some cases. Massachusetts did do the legislation prior to SIB and created the fund. Philanthropy is the hardest capital to bring on board.

Michelle Zabel introduced Ms. Kristin Misner–

Ms. Kristin Misner, Chief of Staff to the Deputy Mayor for Health and Human Services in the Office of the Mayor, New York City presented on New York City's Rikers Island SIB.

The partners in the NYC SIB include Goldman Sachs, the Bloomberg Foundation, the Mayor's Office, and the NYC Department of Corrections. Corrections is implementing a program for 16- to 18-year-olds detained at Rikers Island with the goal of reducing the high recidivism rate for this population by focusing on personal responsibility education, training, and counseling (in a program called ABLE, for Adolescent Behavioral Learning Experience).

Ms. Misner said that "everyone [in City government] felt excited about the endeavor." It was people's "second or third" job, working evenings and weekends to make it happen.

SIBs are appropriate for effective programs where savings can be realized, and services that are not mandated. The third party evaluator is necessary to ensure that services are delivered according to contract. Why was a young men's initiative pursued by for NYC? The purpose is to give juvenile offenders hope and a future, and change the trajectory for young men so that Rikers is not their way of life. NYC wants these success stories to set examples for younger kids. Mayor Bloomberg's launched Young Men's Initiative was a high priority for his third term, and this SIB is part of this initiative. Department heads were asked to think of programs and ideas to make a difference for these young men. There were no new dollars for a new program but there was a passion for this program. The SIB created the ability to think about transformative initiatives. Various ideas were vetted with investors.

Slide 3, MDRC is the intermediary and provides the evaluation. There is a lot of evaluation on this approach. They are using the ABLE curriculum (cognitive behavioral therapy recommended by MDRC) because it works well with participants who may drop in and out unpredictably. The service is being delivered to 3,000 young men served each year over 4 years, both on Rikers and in the neighborhoods. The program went full scale in January 2013. Two non profits are delivering the service.

The goals are to reduce incarceration and crime. There was a goal for 20% reduction of recidivism for the 1st year of the program, but a breakeven point at 10%. The Budget Office and the Dept of Corrections negotiated the cost structure for the program.

Slide 4, how did we do this? First NYC established a baseline, and looked at a 5 year cohort based on bed use at Rikers. The cost saving is realized by reducing the number of bed days. There was a lot of back and forth with the budget office and Corrections on what would be saved. The savings are small until avoiding the return of 100 adolescents, at which point the savings are boosted to $100,000 per adolescent because a wing could close. What percentage of beds do we need to save in order to see a savings for all parties to the contract? Ten percent and NYC would save $9.6m.

Slide 5, lists the actors and their roles and costs. Slide 7 lists the pay outs. 8.4% reduction would enable NYC to pay back investors. 10% reduction is a break even for the city. If the reduction is at 20% then the city keeps all the savings above 10%. The project will have a “go no-go” decision in Year 3 based on the recidivism in the first annual cohort, with a 9% rate being the threshold.

During constrained government funding, SIBs are a way to fund innovative strategies/programs. The SIB helped the non profits to continue to serve this population and not reduce service completely, which happens with a budget cut. They also reduce risks for government and quantify the social benefits. There is real value in deciding what a high school diploma is worth, whether $10,000 or some other number.

Question: Are there annual milestones? Or are they calculated by the full length of the project?

- NYC set 2 markers for recidivism at the end of year 1 and year 2. So at end of year 3, you see the first cohort over 2 years. After year 3, if 9% or greater have not come back to Rikers, then NYC pays out. Then after year 4, after 2 years of lower recidivism, then a payout.

Question: how did you balance what happened in the community vs. the service on Riker’s with the Budget Office?

- They involved budget office in the planning of the evaluation. The evaluation was quasi historical and looked back at a cohort which was divided into a treatment group, and a control group at Rikers.

Presentations ended, and Michelle stated that Dr. Liebman’s questions in his presentation would be in the survey to the work group.

Then, work group members shared their thoughts about SIBs?

- Great job jumping into this issue. State agencies need to do a feasibility study to see what programs would work. Programs do cross agencies. Data analysis needs to be done internally before negotiations begin. In the current political climate, we may not have a champion in place at this time.
- It could be something that is a new job for someone. Managing a SIB cannot be added to a present employee’s plate.
- How do we build to scale initiatives that we have going to get capital? It is a bi-partisan concept.
- How could this work for childhood hunger? The benefits to reducing hunger are disbursed across agencies but it is not easy to measure.
- Is the SIB the right financing option? Or are other options presented at meeting 1 better for Maryland?

- Deborah has a web site for public policy that lists an inventory of savings in various human service areas.
- Currently, there is $2m in early intervention for mental health for children zero to five. It would be beneficial to increase funding to realize greater results through behavioral mental health programs.

Staff will develop a survey based on information provided by the presenters to create some guidance for agency conversations. It is important for members to provide feedback through the survey for the development of the first draft of the report, which will be reviewed at the October 7th meeting.

The Chair, Ms. Zabel, thanked everyone for coming and thanked the speakers for their participation. She also reminded the group that the next meeting will be on Monday, October 7 from 9 am to 12:30 pm at the Institute for Innovation and Implementation.

The meeting adjourned at 12:30 pm.

Approved at October 7, 2013 meeting.

Social Impact Bond Summer Study 2013

Participant Survey Results

September 10, 2013

This survey was issued to all Social Impact Bond (SIB) Summer Study Workgroup members and designed to serve as a check-in with all participants to identify current thinking about and questions regarding SIBs in general and in Maryland. This survey will be re-administered after each of the SIB Workgroup Meetings.

1. Did you attend the first meeting of the SIB Summer Study Workgroup (Wednesday, July 17, 2013)?

There were 11 respondents to the survey; 6 of them attended the first meeting of the SIB Summer Study Workgroup on Wednesday, July 17, 2013. (All participants have received materials regardless of attendance at the meeting.)

2. What information about SIBs (either from the meeting or the resources shared) have surprised you or challenged your ideas about SIBs?

- Presentation by Dr. Salamon about the variety of new financing options through the private market
- The fiscal analysis done by the Department of Legislative Services is sobering.
- I was surprised to discover the breadth of literature in this area as it is relatively new to me. I was also interested to learn of the existing SIBs and their structure.
- I like the model in concept, am still trying to understand the complexities of the financing mechanism and am concerned about what sound like high legal and transactional costs of creating a SIB. Also, if an investor requires a guarantee, as in the NYC Rikers Island SIB, that would make it more expensive and more difficult to put in place.
- It was a wonderful learning experience for me. I was only vaguely familiar with social impact bonds and I learned a lot about the types of initiatives around SIB. The resources provided a great background.
- There is often significant private capital spurring development like the Bloomberg example in NY

(6 respondents)

3. Questions about SIBs: I have questions about SIBs in relation to:

Answer		Response
Determining the population focus		3
Organizing the financing for the SIB		7
Recouping savings from the SIB		8
Challenges to developing and implementing a SIB		4
Benefits of implementing a SIB		4
Other (please state):		4
• Clarifying the purpose/best use and expected results in addition to financing benefits (if any).		
• I am unfamiliar with this issue		

(11 respondents)

4a. Based on the information you have received to-date, on a scale of 1-10, do you think a SIB could work for Maryland in the next few years? (1=SIBs are not at all feasible or realistic for Maryland in the next few years; 10=SIBs could definitely be implemented in Maryland to implement in the next few years)

Min Value	Max Value	Average Value	Standard Deviation	Responses
3.00	8.00	**5.22**	1.86	9

4b. Please explain your rating in 4a.

- Under the MD School Construction law, the State subsidizes the construction of school buildings, including early learning sites on the campus of the renovated or newly constructed sites. The State match depends on the local wealth of the jurisdiction. The local share could be supplemented with SIB funds for the construction of an state-of-the art early learning center. The occupant of the center would pay interest on the bond in lieu of rent, e.g. $2,500 monthly on a bond of $1 mi with 3% interest. The term of the bond could be structured to benefit the investor from community development tax credits.
- Maryland has greater capacity than many states and could certainly master the technical and financing details. But for SIBs to be worth the time and effort invested, they have to achieve something beyond financial repayment. Are there programs within state government with the desire and capacity to use SIBs to accomplish reforms?
- I think that fiscal constraints, logistical concerns, and the annual focus of the budget (rather than longer term) present very large hurdles for the implementation of SIBs in Maryland. However, there is obviously some interest in the State in moving forward with a SIB of some form.
- With a restructuring of current State resources there is a likely potential for a SIB to work in Maryland.

- Given that these have been done successfully elsewhere it seems feasible, and it may be a good way to raise funds needed to scale up promising programs, but it sounds like questions related to the financing mechanism may make it difficult. Also I think Maryland has generally done a reasonably good job of funding social programs with public dollars so there may be a question whether we need a private investor that will receive a potentially generous return.
- My response is based upon the fact that I still feel I need to know more about SIB. In some instances, if there were adequate investors, I believe that it could work.
- There needs to be a continuation of political will through the change in Administration.
- We would still need to educate public policy experts, elected officials and the general public on this issue. The issue does not have a "champion" at the moment. Not many model SIBs in existence.

4c. If you answered with a rating of 5 or greater on question 4a (could SIBs work in Maryland), what are the populations and programs that you think could potentially be feasible for a SIB in Maryland?

- Aging seniors, child welfare, juvenile justice, early childhood.
- Young children and their families birth – 5
- Early childhood programs -- e.g., home visiting or early childhood education; programs to reduce chronic homelessness; prisoner re-entry; programs to reduce number of youth in foster care
- Workforce re-entry/DPSCS population.

5. What additional information would you like to receive to assist with the development of the recommendation to the General Assembly?

- A description of an existing model and its funding arrangement is needed to articulate the feasibility to legislators. However, the example listed above (SIB funded early learning center being part of school construction request) would not require legislation.
- What/where is the appetite for program innovations/reforms within state government where SIBs could be a useful tool?
- More detail regarding the legal/budgetary roadblocks that exist in Maryland, and how the State could overcome these hurdles.
- I would like to hear about more areas that are using SIB to solve problems as was stated in the first meeting.
- I would like more information on quantifying the savings over time as that is often compelling for legislators

MARYLAND SOCIAL IMPACT BOND SUMMER STUDY 2013
WORKING GROUP MEETING # 2

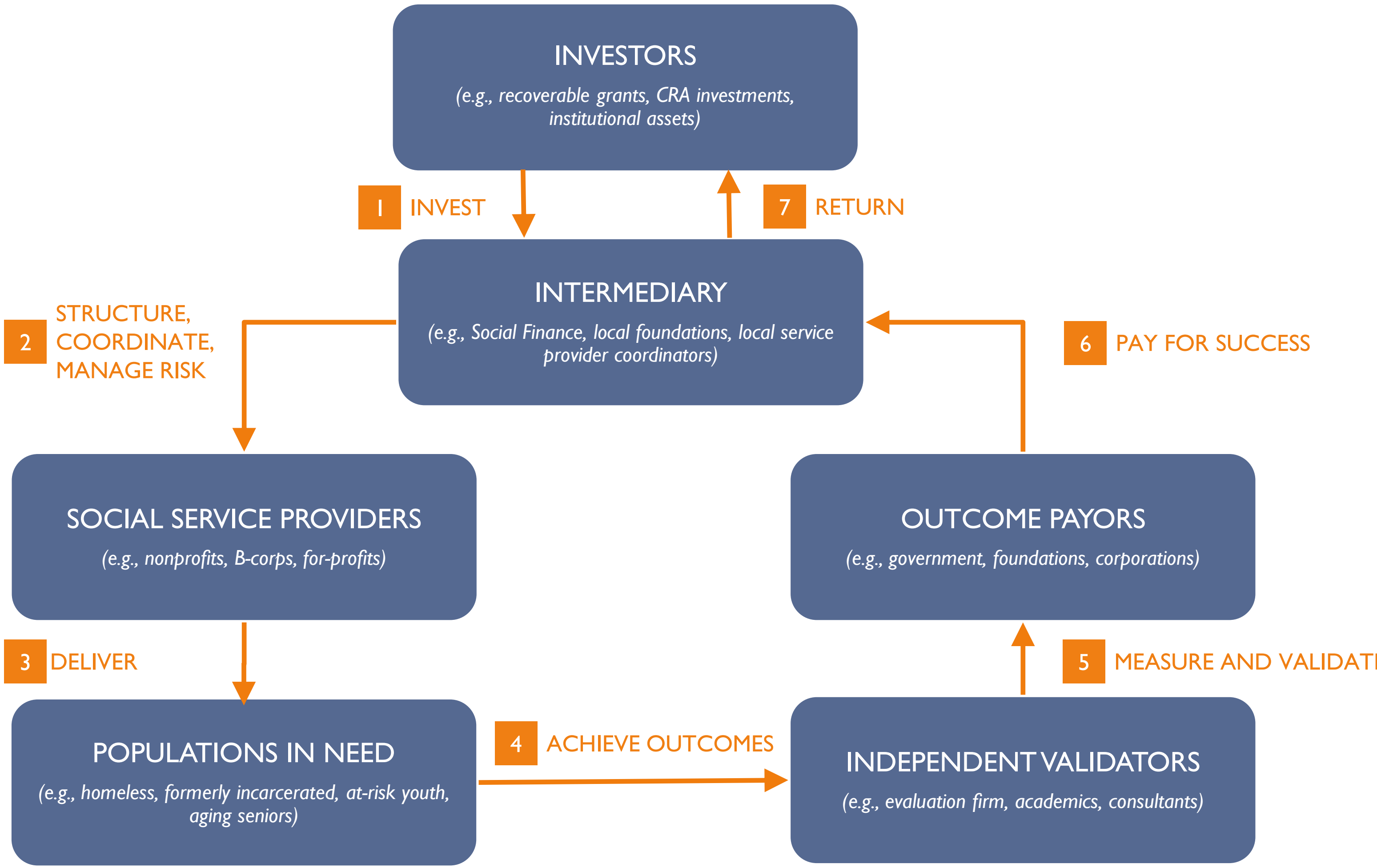
SEPTEMBER 10 2013

Rebecca Leventhal rleventhal@socialfinanceUS.org
617.939.9900 x 26

77 Summer Street, 2nd Floor, Boston, MA 02110

SOCIAL INNOVATION FINANCING OVERVIEW

AN INNOVATIVE MULTI-STAKEHOLDER PARTNERSHIP



SOCIAL FINANCE

KEY STEPS TO LAUNCHING AND IMPLEMENTING SUCCESSFUL SIBS

1 Originate Deal

- Identify government champions & savings opportunities
- Vet proven models of intervention
- Perform nonprofit due diligence
- Conduct financial modeling

2 Secure Government Contract

- Develop & secure government contract
- Secure authorization for multi-year contract
  - Address appropriation risk
- Formulate partnership agreement with metrics & payment terms

3 Structure Instrument

- Develop operating model & structure investment vehicle
- Articulate cash flows, including financial & social returns for target milestones
- Finalize methodology, including metrics & evaluation strategy

4 Raise Capital

- Recruit investors
  - Foundations & charitable trusts
  - High net-worth individuals & family offices
  - Institutional investors
- Issue the instrument & raise investment capital

5 Manage Project Over Instrument's Life

- Provide active ongoing project management and financial intermediation
- Make course corrections as needed
- Coordinate third-party evaluation

Active Risk Management

BUILDING AN INSTRUMENT: SIB RISKS

Nonprofits	1 Intervention Model Risk	• Risk that intervention is not effective in achieving success metrics
Nonprofits	2 Execution Risk	• Risk that program is not effectively implemented by service providers
Intermediary	3 Intermediary Risk	• Risk that program is not well-managed by intermediary, or that intermediary is not well-managed
Investors	4 Investor Funding Risk	• Risk that investors do not meet funding commitments if capital is called over multiple periods

Performance Risk (risks 1–3)

Credit Enhancement and/or Tranched Structure to Mitigate Above Risks

Government	5 Credit Risk	• Risk that government defaults on payments
Government	6 Political Risk	• Appropriation risk

SOCIAL FINANCE

SOCIAL IMPACT BOND ASSESSMENT CRITERIA

Social Impact Bond Application Criteria

Evidence-based programs helping underserved populations
- Service providers with proven track record
- Intervention with measurable outcomes
- Attributable impact to intervention

Potential for significant net savings or value creation
- Policy priority for government or foundation
- Financing needs currently not served
- Acceptable investment time horizon
- Area of interest for investors

Replicable and Scalable
- Provider readiness for scale
- Strong social need
- No harm

PROMISING APPLICATIONS FOR SOCIAL IMPACT BONDS

Preliminary Assessment

		Evidence-based intervention	Sufficient net savings within time horizon	Replicable and scalable
CRIMINAL AND JUVENILE JUSTICE				
Prisoner Recidivism	Post-incarceration programs to reduce recidivism	✔	✔	✔
Juvenile Justice / Disconnected Youth	Post/pre-adjudication intervention services to reduce out-of-home placements	✔	✓	✓
HEALTH CARE				
Aging in Place / Long-term Care	Supportive housing and care coordination to reduce out-of-home healthcare usage	✓	✓	✔
School-based Health Clinics	In-school primary care to reduce medical costs and improve outcomes	✔	✓	✓
Asthma Prevention	Education and home retrofits to reduce asthma-related emergencies	✓	✔	✔
Nurse Home Visiting Programs	Prenatal and early childhood support for first time, low-income mothers to improve family success	✔	✓	✔
OTHER				
Chronic Homelessness	"Housing first" supportive housing to reduce emergency health care and shelter usage	✔	✓	✔
Adult Education	Job training for hard-to-employ populations to fill skill gaps	✓	✓	✔
Early Education	Providing all children with the tools necessary to begin school ready to learn	✓	✓	✔

✔ Aligns with most assessment criteria
✓ Aligns with some assessment criteria
✗ Does not align with assessment criteria

CASE STUDIES

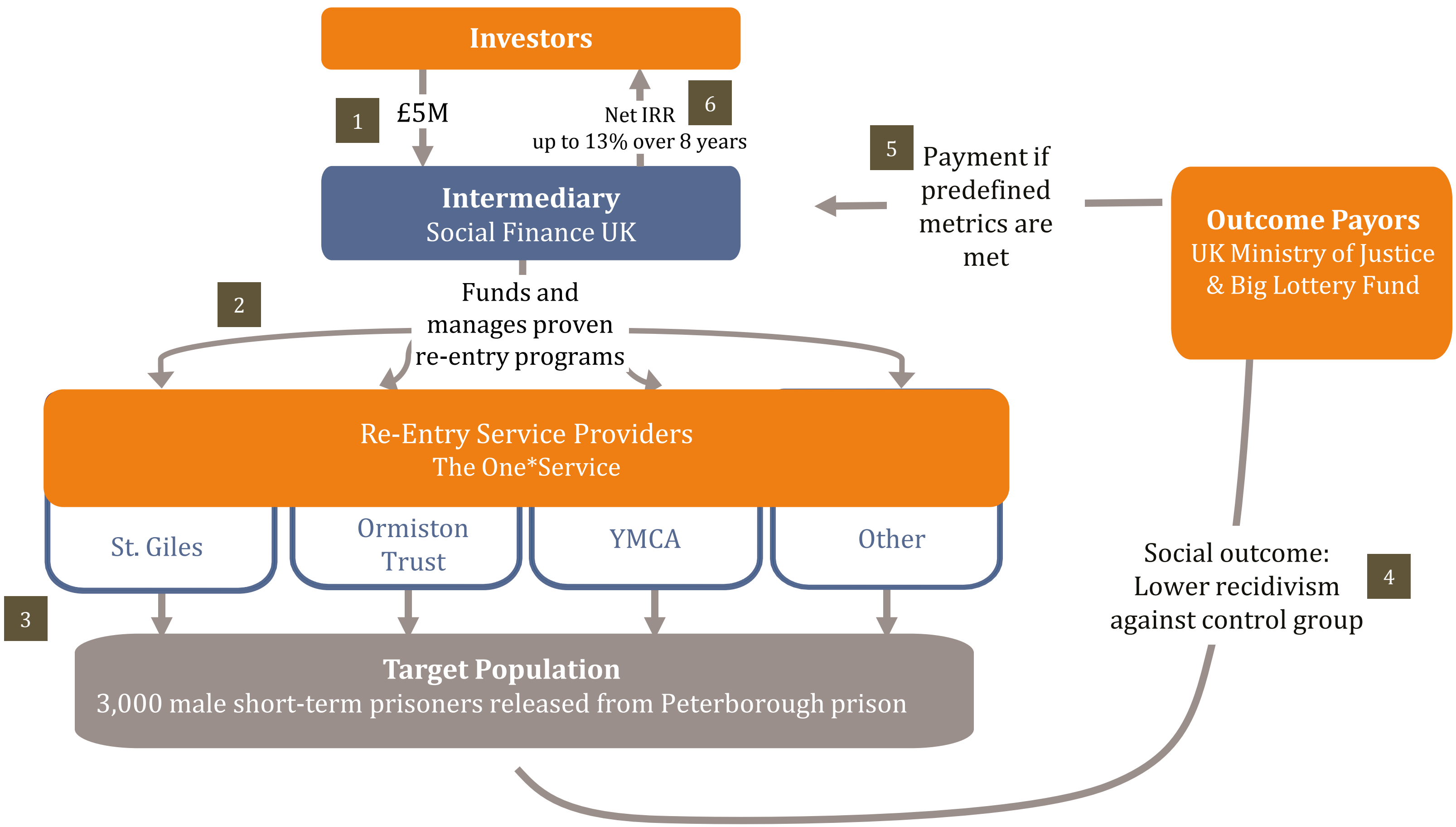
CASE STUDY: OPERATIONAL SOCIAL IMPACT BONDS

Peterborough Social Impact Bond

- Peterborough SIB was launched in 2010; UK Ministry of Justice contracted with Social Finance for a 7.5% reduction in recidivism
- Social Finance developed the concept and worked to structure and implement project
    - Collaborated with government and providers to identify service needs and appropriate metric
    - Designed program that had flexibility to adapt to client needs in real time
    - Implemented data management system to allow for real time collection of data and data driven decision making
    - Brought multiple providers together to coordinate services and align effort towards achievement of common outcome
- Partners felt community confidence in program was key to success
    - Social Finance established advisory committee of leading experts and local stakeholders to provider oversight and credibility to project
- In addition to raising capital and structuring the financing, Social Finance has also played the ‘program intermediary’ role
    - Social Finance has supported the implementation of the project and funded a full time project manager to oversee project and provide course corrections where necessary

THE WORLD'S FIRST SOCIAL IMPACT BOND AT PETERBOROUGH

Funds Flow and Structure



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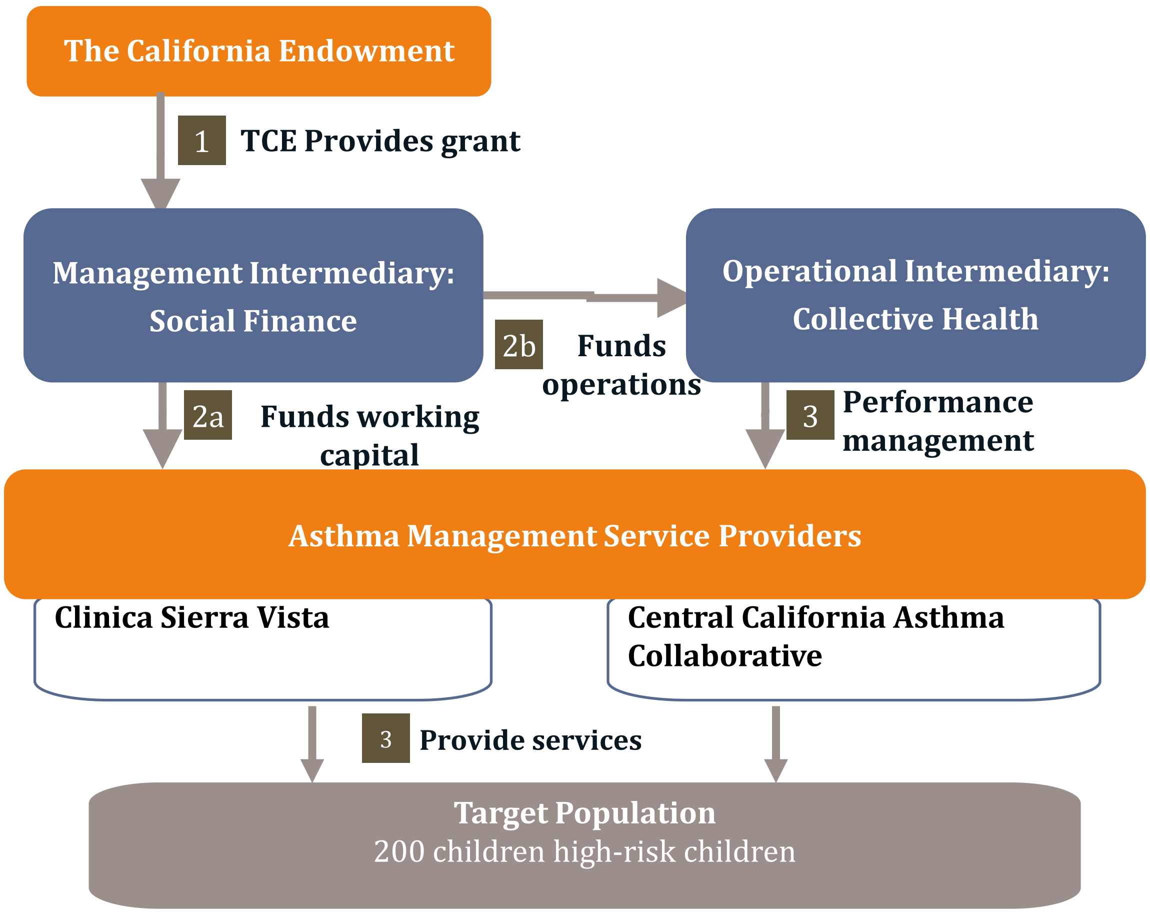
CASE STUDIES: DEMONSTRATION PROJECTS

Fresno Asthma Management Project

- The California Endowment awarded Social Finance and Collective Health a grant to work with proven providers in the Fresno, California area to implement an asthma management and prevention program for 200 low-income children.
  - Goal to improve the health of children living with asthma and reduce the costs associated with emergency room treatments and hospitalizations.
- Social Finance is financial intermediary and Collective Health plays operational intermediary role
- Project is intended to substantiate social and financial benefits of up-front investment in effective asthma management
- Social Finance endeavors to prove cost-savings from asthma intervention can be achieved and quantified.
- If pilot proves successful, partners will launch SIB to serve broader population

FRESNO DEMONSTRATION PROJECT: GRANT TO SIB MODEL



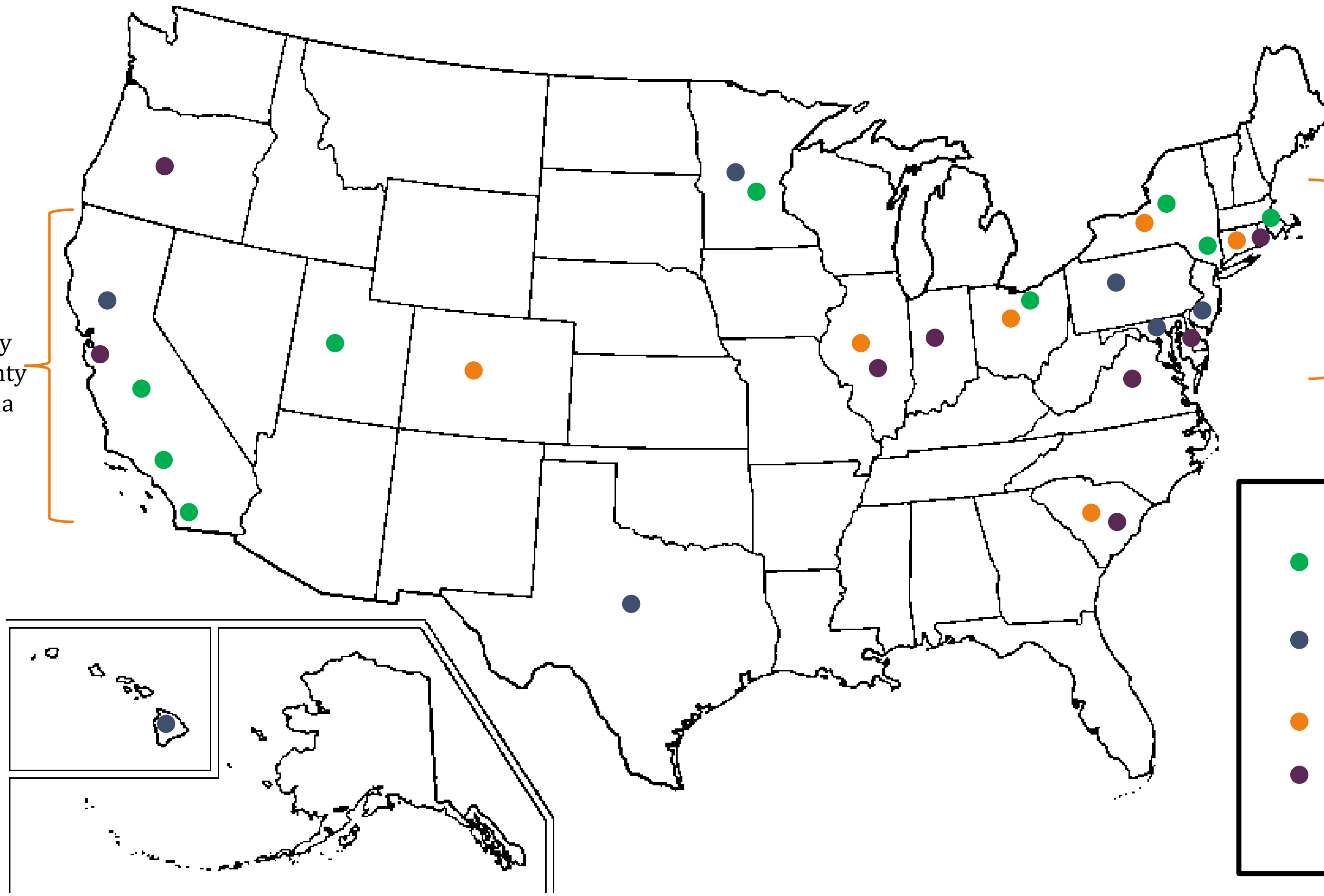
SOCIAL FINANCE

OVERVIEW OF US SIB ACTIVITY

SIGNIFICANT INTEREST ACROSS THE COUNTRY

Active SIB Projects, Legislation, and Technical Assistance Pursued

Fresno
San Diego County
Santa Clara County
State of California



Connecticut
District of Columbia
Maryland
Massachusetts
New Jersey
New York City
New York State
Pennsylvania
Rhode Island

Legend

- Active SIB Projects (Proposed or Launched)
- Legislation (Pursuing or Passed)
- Harvard TA Lab
- Other Interest (Working Groups, Feasibility Studies, etc)

FEDERAL, STATE, AND LOCAL ACTIVITY

Strong Federal Interest

- President Obama's FY2014 budget increased support for Pay for Success, including:
  - $195M in support of PFS in areas of job training, education, criminal justice, housing, and disability services
  - $300M Incentive Fund at Treasury to provide credit enhancement and to supplement outcomes payments (akin to UK's Outcomes Finance Fund)
- Department of Justice and Department of Labor are providing funding for PFS pilots

Increasing Activity at State/Local Level

- NYS General Assembly approved $30M in Pay for Success over next 5 years
- NYS and NYC have both begun procurement processes; IL began RFI process Spring 2013
- New Jersey, Maryland, California, Texas, Hawaii and Pennsylvania are all considering PFS legislation
- 28 jurisdictions applied to Jeff Liebman's Harvard Social Impact Bond Technical Assistance Lab for pro bono assistance

Transactions Moving Forward

- NYC launched nation's first SIB at Rikers Island; focus on youthful offenders
- NYS selected Social Finance as intermediary for SIB financing workforce reentry program
- Social Finance and Collective Health were awarded a grant from the California Endowment to launch a Health Impact Bond demonstration project
- Massachusetts is contracting to launch financings focused on juvenile justice and chronic homelessness
- Early education demonstration project launched in Utah

SOCIAL FINANCE

ABOUT SOCIAL FINANCE

MISSION AND VALUES

We believe that everyone deserves the opportunity to thrive, and that social impact financing can play a catalytic role in creating these opportunities.

Who We Are	***Our mission is to mobilize investment capital to drive social progress*** We structure and manage impact investments that will unlock capital to fund effective solutions and drive an outcomes-focused social sector. Social Finance is a registered 501(c)(3) organization.
History	Our sister firm, Social Finance UK, launched the world's first Social Impact Bond in 2010. We work closely together but are independently funded, managed and governed. • SF US: Launched operations in 2011 • SF UK: Founded in 2007 • Common mission, model and knowledge platform
Core Values	• **People:** People are our mission and our inspiration; we are committed to our team, our partners, and the individuals we serve. • **Performance:** Our work demands rigorous thought, inquiry, and analysis; we pride ourselves on the depth and quality of our endeavors. • **Collaboration:** We build strong, enduring relationships across sectors to align diverse interests and advance our collective mission. • **Integrity:** The highest standards of accountability and transparency underpin all of our work.

SOCIAL FINANCE

OUR SERVICE OFFERINGS

Our Focus is on the Social Impact Bond*

Advisory Work	• Feasibility studies • Development and implementation of proof-of-concept projects
Transaction Execution	• Cost benefit analysis • Financial structuring • Outcome metric selection and evaluation design • Contract development • Capital raising
Post Transaction Support	• Performance and fiscal management • Accounting and compliance • Investor relations
Field Building	• Market education, thought leadership, research and advocacy to support the development of a strong and sustainable Social Impact Bond and broader impact investment market

* Social Impact Bonds are not traditional government issued bond and are also referred to as pay for success, pay for performance, social innovation financing, or outcomes-based financing

SOCIAL FINANCE

WHAT WE DO

Our work spans geographies and issue areas; however, our fundamental approach is consistent.

1) **Assess the Problem:** First, we dive into the problem and ask: a) What is the problem? b) How big is the unmet need? c) Is there an intervention that can improve results? d) Can impact investing play a role?

2) **Identify a Social Outcome Financing Solution:** If a social impact financing strategy is appropriate , we identify promising ways to finance the expansion of programs with a track record of performance, a strong evidence base, and a focus on outcomes.

3) **Shape the Partnership:** We develop performance-based structures that align the incentives of government, investors and providers to achieve shared, measurable goals.

4) **Raise Capital:** We raise capital from impact investors to fund the initiative.

5) **Collaborate through Completion:** We work over the investment life with all stakeholders to ensure that social and financial goals are met.

SOCIAL FINANCE

SOCIAL FINANCE BOARD & TEAM BIOGRAPHIES

BOARD OF DIRECTORS

David Blood, Chair, Finance and Investment Committee, is co-founder and Senior Partner of Generation Investment Management. Previously, he spent 18 years at Goldman Sachs including serving as co-CEO and CEO of Goldman Sachs Asset Management from 1999-2003. David received a B.A. from Hamilton College and an M.B.A. from the Harvard Graduate School of Business. He is on the Board of Harvest Power, New Forests, SHINE, Social Finance UK, Social Finance US, The Nature Conservancy, Fondation 1796 and Hamilton College; the Advisory Board of Bridges Ventures and the Harvard Business School Visiting Committee.

Sir Ronald Cohen is Chairman of The Portland Trust , Bridges Ventures and Big Society Capital. He chaired the Social Investment Task Force (2000-2010) and the Commission on Unclaimed Assets (2005-2007). He was a co-founder and chairman of Apax Partners. He was a founding director of the British Venture Capital Association and the European Venture Capital Association. He was also a founder and former Vice-Chairman of EASDAQ and former director of NASDAQ Europe. He is a graduate of Oxford University, and Harvard Business School. He is a member of the Harvard Board of Overseers and the Board of Dean's Advisers at Harvard Business School, a Vice-Chairman of Ben Gurion University and a member of the University of Oxford Investment Committee. He is also a Trustee of the British Museum. In 2007, Sir Ronald published *The Second Bounce of the Ball – Turning Risk into Opportunity*.

Alexander Friedman is the Chief Investment Officer of UBS Wealth Management and chairman of its global investment committee. Prior to joining UBS, Alex was founder and managing partner of Asymmetry LLC, a private investment company, and senior advisor to Lazard, the international investment bank. Previously he was the Chief Financial Officer for the Bill & Melinda Gates Foundation. Earlier in his career, Alex was an investment banker at Lazard and also served as a White House fellow and as an assistant to the Secretary of Defense in the Clinton administration. Alex is chairman of Safeboats International and is a non-executive director of Actis. A member of the Council on Foreign Relations, he serves on the boards of the Seattle Art Museum and the Access Fund. Alex received a J.D. and an M.B.A. from Columbia University and a B.A. from Princeton University.

Luther M. Ragin, Jr. is Chief Executive Officer of the Global Impact Investing Network. Previously, he was Chief Investment Officer of the F.B. Heron Foundation, a national foundation with assets of $250 million. Prior to joining the Foundation in 1999, Luther was the Chief Financial Officer of the National Community Capital Association, a trade association of community development financial institutions that provide access to capital in low-income communities. Other significant experience includes Earl G. Graves, Ltd., and Chase Manhattan Bank. Luther is a member of the Board of Directors of Rockefeller Philanthropy Advisors, ShoreBank Corporation and The Threshold Group. He holds a B.A. and Master of Public Policy from Harvard, and is a graduate of Columbia University's Executive Program in Business Administration.

BOARD OF DIRECTORS

Sonal Shah, Vice Chair, is the former director of the White House's Office of Social Innovation and Civic Participation. She also served on President Obama's Transition Board overseeing the Technology, Innovation, Government Reform working group. Before joining the White House, Sonal was the head of Global Development Initiatives at Google.org. Prior to Google, she was Vice President at Goldman Sachs, Inc. Sonal also co-founded a nonprofit, Indicorps, which offers fellowships for Indian-Americans to work on development projects in India. Prior to that, she worked at the Center for American Progress and the Center for Global Development. From 1995-2002, Sonal was an economist at the Department of Treasury, where she was the Director for African Nations, worked on the Asian Financial Crisis and post-conflict development in Bosnia and Kosovo. Sonal received her M.A. in Economics from Duke University and B.A. in Economics from the University of Chicago. She is an Aspen Crown Fellow and a Next Generation Fellow.

Dana Smith, Chair, Governance and Nomination Committee, serves as Trustee for two active family foundations, including the Richard and Susan Smith Family Foundation. Her past professional experience includes work at the Boston Housing Authority where she was Deputy Director of Services, Boys and Girls Clubs of Boston where she was Director of Operations and the City of Boston where she was a youth outreach worker. Dana is currently the incoming Chair of the Board at the Boys & Girls Clubs of Boston and the Chair of the Board of Trustees of Facing History and Ourselves. She also serves on the boards of the Park School and the Dean's Leadership Council at the Harvard Graduate School of Education. Dana attended Tufts University and graduated in 1988 magna cum laude. After graduation, she received a fellowship to teach in SOWETO, South Africa. She completed her Masters in Education at Harvard University Graduate School of Education with a concentration in Children and Adolescents at Risk.

Bracebridge H. Young, Jr., Chair of the Board, is Mariner's Chief Executive Officer, a Partner and a General Securities Principal for Mariner Group Capital Markets Inc. He joined Mariner directly from Goldman Sachs, where he retired as a Partner, head of European Debt Capital Markets. Brace also headed fixed income and foreign exchange sales in London beginning in 1992. In 1989, Brace moved to Tokyo to run all of the firm's fixed income activity in Japan. Brace first became a Partner at Goldman Sachs in New York City in 1988 where he was the Co-Head of the Money Market Sales and Trading Department. He was the Head Trader for institutional money market funds from 1983 to 1988 and started at Goldman Sachs on the Commercial Paper trading desk in 1980. Brace received a Bachelor's degree from Bowdoin College in 1977 and an M.B.A. from the Stern School of New York University in 1983. He is the Chair of the Board and Trustee of Buckingham Browne & Nichols.

TEAM

Tracy Palandjian, CEO and Co-founder

For more than a decade, Tracy has dedicated herself to building a more impactful and effective nonprofit sector and to re-imagining the role of the capital markets in enabling social progress. Inspired by her work with its sister organization in the UK, Tracy co-founded Social Finance, Inc. in January 2011. Prior to Social Finance, Tracy was a Managing Director for 11 years at The Parthenon Group, a global strategy consulting firm, where she established and led the Nonprofit Practice and worked with foundations and NGOs to accomplish their missions in the US and globally. She is co-author of *Investing for Impact: Case Studies Across Asset Classes*, a report that provides an important view on the evolution of the impact investing industry. Prior to Parthenon, Tracy worked at Wellington Management Co. and McKinsey & Co. She is the Chair of the Board of Directors of Facing History and Ourselves, a member of the Board of Overseers at Harvard University and a Director of Affiliated Managers Group (NYSE: AMG). She also serves on the Investment Committee of Milton Academy. A native of Hong Kong, Tracy is fluent in Cantonese and Mandarin. She graduated magna cum laude from Harvard College, with a B.A. in Economics, and holds an M.B.A. with high distinction from Harvard Business School where she was a Baker Scholar.

Caitlin Fleming, Associate

Caitlin Fleming is an Associate on the Business Development Team where she develops and implements innovative solutions for financing social outcomes. Her portfolio includes investments in outcomes across the "cradle-to-career" spectrum including re-entry, workforce development, child welfare, and education. She crafts investment proposals and conducts benefit-cost analysis and due diligence to assess their feasibility. She also builds the partnerships and infrastructure needed to execute successful projects. Prior to joining Social Finance, Caitlin contributed to the design of successful social service models, growth and capital-raising strategies, and multi-million dollar government contract proposals for a variety of stakeholders including nonprofits, foundations, governments, and businesses. Most recently, she supported the White House Office of Social Innovation and Civic Participation's work to advance evidence-based practices, innovative financing tools, and public-private partnerships to maximize public resources and drive investment toward effective social solutions. She also helped innovative nonprofits develop the capacity to scale effectively as a founding member of AchieveMission's Talent Initiative, a management consulting firm for the social sector. Caitlin is a StartingBloc Social Innovation Fellow, and previously served as a Coro Fellow in Public Affairs and AmeriCorps Resident in Social Enterprise. She graduated magna cum laude from Carleton College with a B.A. in Political Science and Fine Art.

Jonathan Goodman, Senior Advisor

A successful investor and Wall Street veteran, Jonathan advises Social Finance and its clients on complex capital markets issues, business strategy and quantitative methodology. Jonathan started his finance career at Goldman Sachs & Co. where he was part of Fischer Black's original "Rocket Scientist Group" devising quantitative strategies in the currency and commodity markets. He subsequently moved to London where he built and managed Goldman Sachs' European equity program trading, derivatives and risk arbitrage businesses. He returned to New York to join Steinhardt Partners LP where his responsibilities included investments in special situations, mortgage-backed securities, convertible bonds, Japanese warrants, high yield bonds, distressed securities, equity and fixed-income arbitrage, private transactions, insurance derivatives and other esoteric securities. He was named the youngest partner in that firm's history, and after Michael Steinhardt's retirement, he founded Concentric Capital Management LLC, an opportunistic global hedge fund that has managed for the past 15 years. He is a graduate of Yale College and the University of Pennsylvania with degrees in Systems Engineering and Applied Mathematics.

TEAM

Jane Hughes, Senior Consultant

Jane drives the organization's thought leadership by helping to craft the Social Finance message and to develop research and analysis that helps fuel industry growth. She has inhabited both the financial world and the social development world, and is dedicated to bringing these forces together for the benefit of all stakeholders. Most recently, Jane was executive director of World Learning's master's degree program in sustainable development in Washington, D.C., where she also created and taught a course on microfinance and impact investment. She spent 17 years as an international finance professor at Brandeis University's International Business School. Prior to her academic career, Jane was a vice president at Manufacturers Hanover Trust Company in New York, in the World Corporate Division. Jane has consulted, lectured, and published widely in the fields of international banking and finance; business, government, and the global economy; and international development. She co-wrote a leading textbook on international banking, and is currently working on a second edition of Separating Fools From Their Money: A History of American Financial Scandals (first edition, 2007). Jane graduated magna cum laude from Princeton University with a degree in French literature; she also has a master's degree from Johns Hopkins University School of Advanced International Studies, and an MBA from New York University

Kate Manning Kennedy, Director of Communications

Kate Manning Kennedy is the Director of Communications where she leads all external communications efforts for the organization including public relations, market education and partnership building. Kate develops marketing collateral to reach the organization's key audiences; maintains the brand and mission, vision, values; and executes multi-media marketing and communications activities in service of the organization's goals. Prior to joining Social Finance, Kate developed and implemented strategic communications campaigns throughout the private, public and nonprofit sectors. Most recently, she was a Director of Strategic Communications at the Glover Park Group, a leading public affairs firm in Washington, D.C., where she developed communications strategies for Fortune 100 companies, private equity firms and their portfolio companies, and other financial services clients. In this role, she specialized in platform development, internal communications, employee engagement, brand development, executive messaging, and crisis communications. Prior to the Glover Park Group, Kate served as a Communications Manager at Fidelity Investments where she focused on internal change management communications, executive communications and employee engagement strategies. Earlier in her career, Kate managed marketing and communications campaigns at TechFoundation, Inc., a nonprofit based in Cambridge, MA. She has also worked in the legislative office of Senator John Kerry and the 2004 Democratic National Convention Finance Committee. A graduate of Fairfield University, Kate majored in International Studies with concentrations in Political Science and Spanish.

Rebecca Leventhal, Director

Rebecca Leventhal is a Director on the Business Development Team where she collaborates with nonprofits and governments to identify and structure innovative ways to expand critical social service programs. She focuses on criminal justice and education financing products where she leads deal teams to structure and develop Social Impact Bonds and other innovative financings by building partnerships, performing due diligence, overseeing benefit-cost analyses and executing transaction negotiations. Additionally, she leads feasibility work to identify areas for future social investment. Prior to Social Finance, Rebecca held various roles in the public and private sector, specifically in government, politics, finance, and the nonprofit field. Rebecca spent 15 months working for Hillary Clinton's presidential campaign, where she cultivated relationships and built partnerships with communities in over 30 states. Previously, Rebecca was an ambassador for President Clinton in support of his political, charitable, and personal work. Rebecca also spent time in Office Management and Budget and the U.S. State Department. Rebecca began her career at Merrill Lynch in the Municipal Finance department where she financed state and local government institutions and nonprofit facilities and later joined the Structured Finance department where she arranged secured transactions. Rebecca holds a JD from Harvard Law School and an AB in Social Studies from Harvard College.

TEAM

Caitlin Reimers, Director

Caitlin Reimers is a Director on the Capital Markets Team where she leads the financial structuring and capital raising activities to drive social impact at scale. She brings investment insight to the Product Development Team to create optimized financing solutions tailored to achieve our public and private partners' desired social and financial outcomes for each transaction. Specifically, she drives the development of outcomes pricing, financial projections and risk/return models, builds relationships with investors, and manages the execution of outcomes-based financing transactions. Prior to Social Finance, Caitlin worked in strategic management consulting and asset management. While at Strategic Value Capital Management, she led due diligence and valuation analysis and made investment recommendations, including timing and portfolio weighting, to the fund manager. During her time at The Parthenon Group, Caitlin drove in-depth market research and best-practice analyses to provide strategic support for prominent education and financial services clients. Committed to supporting enterprise development in low-income communities, she has also had experience facilitating the structuring of offering memorandums for an impact investing fund and assessing microcredit loans for low-income women. From 2010-2012 she served as the pro-bono Director of Finance and Strategy for a start-up fair trade fashion organization. Caitlin holds an MBA with high distinction from Harvard Business School, where she was a Baker Scholar, and a BA with honors from The Woodrow Wilson School of Public and International Affairs at Princeton University.

Jill Scherer, Associate and Grants Manager

Jill Scherer is an Associate and Grants Manager for Social Finance where she oversees the organization's foundation deliverables and grant reporting. Jill also contributes to Social Impact Bond development through research of potential applications, with a particular focus on how outcomes-focused financing can address homelessness. In addition, she plays a key role in the organization's fundraising efforts by researching and writing grant applications. Prior to joining Social Finance, Jill conducted research on how innovative finance can drive community and international development. Most recently, she was a Senior Research Analyst with the Milken Institute, an economic and financial think tank in Los Angeles. She co-authored several reports in support of Milken's Financial Innovations Labs, roundtables designed to identify financial solutions to social, economic and environmental challenges. Her reports spanned the topics of early childhood, health, and small business growth. Previously, she worked in the private sector at Charles River Associates, a business and economic consulting firm. Jill has a Masters Degree in Public Policy from the University of California, Berkeley and a B.A. in Economics from Wesleyan University.

Nirav Shah, Director

Nirav Shah is a Director on the Business Development Team where he leads the organization's efforts to create innovative financing mechanisms to advance healthcare policy and eliminate homelessness. Nirav develops collaborative partnerships with key, multi-sector stakeholders to deliver financial solutions that funnel investment capital into preventative programs, including chronic disease management, permanent supportive housing for the homeless and better coordinated care systems for the underserved. Prior to joining Social Finance, Nirav worked for the Financial Rescue Unit in the Office of Management and Budget within the Executive Office of the President. In this role he examined Federal policy and programmatic initiatives as part of the suite of Federal economic stabilization policies with a specific focus on housing policy. Earlier in his career, Nirav worked with Cambridge Associates as a Senior Hedge Fund Analyst where he analyzed fund performance and created hedge fund manager reviews for foundation, university, and high-net worth clients. Prior to Cambridge Associates Nirav worked at Bank of America where he developed new, innovative credit products to the Bank's retail clients. Nirav holds a Masters of Public Affairs from the Lyndon B. Johnson School of Public Affairs and a Bachelor of Science in Business Administration with a concentration in Finance from Boston University.

TEAM

Stephanie Shieh

Stephanie provides administrative support to the Social Finance team. Prior to joining Social Finance, she worked as an administrative assistant at Open Circle, a Massachusetts-based non-profit working to implement social and emotional learning (SEL) curricula in elementary schools in the New England region and beyond. She has also served as a junior associate with the D.C. Public Schools' (DCPS) Central Office, where she supported summer school operations in the Office of College and Career Readiness. She graduated magna cum laude from Wellesley College with a B.A. in Biology and Education Studies.

Joanna Vanden, Director of Operations

Joanna Vanden is the Director of Operations where she oversees all day-to-day operations of the firm including budget and financial management, human resources, organization development, and general office management. Joanna plays a key role in executing business priorities in support of the organization's goals. Prior to joining Social Finance, she was Director of Operations for the homeless services agency, HomeStart, Inc., and worked in fundraising for prisoner reentry services. In addition to her work at Social Finance, Joanna serves on the Board of Directors for Food For Free, a Cambridge-based nonprofit working to alleviate hunger in Greater Boston. Joanna graduated summa cum laude from Boston College with a B.A. in history, and holds an M.B.A. with high honors from Boston University.

Gary Pelissier, Senior Analyst

Gary Pelissier is a Senior Analyst on the Capital Markets Team where he develops market-based approaches to address complex contemporary social issues. Gary works closely with both the Capital Markets and Product Development Teams to structure innovative alternative financing strategies for high-quality, highly effective social service providers. Prior to joining Social Finance, Gary worked as an investment-banking analyst at Morgan Stanley in the Public Finance department. As the quantitative analyst on the Housing group, Gary was responsible for modeling the fixed income and mortgage cash flows for some of the Nation's largest and most sophisticated housing agencies, including MassHousing, Florida Housing, Connecticut Housing Finance Authority, State of New York Mortgage Agency, and New York City Housing Development Corporation. During his time at Morgan Stanley, he helped structure and price over $2.5 billion of debt for his State HFA clients. Gary graduated magna cum laude with high honors from Harvard College in 2011 with A.B. in American History and Literature and a secondary field in Economics.

Alissa Bonneau, Associate Extern

Alissa Bonneau joins Social Finance as an extern from Bain & Company. As an Associate Extern on the Business Development Team, she researches and develops innovative solutions across sectors, with a specific focus on healthcare and homelessness. She conducts investment proposals, diligences new opportunities, and builds relationships with government, nonprofit, and investment partners. While at Bain, Alissa worked with clients across a variety of industries, conducting adjacency evaluation, organization redesign, operational improvement, growth strategy, and private equity due diligence. She also performed nonprofit case work through Inspire, Inc. She has done economic policy research for both the Stanford Institute for Economic Policy Research and the Gaidar Institute for Economic Policy in Moscow, Russia. She received a B.A. with Honors in Economics from Stanford University, and served as the President of Stanford Nonprofits while on campus.

Casey Littlefield, Advisor to the CEO

Casey A. Littlefield is a Harvard Business School Leadership Fellow serving as Advisor to the CEO. Casey leads projects in business development and strategic planning to direct sustainable organizational growth. Committed to supporting efficient scaling and impact in the social sector, she has experience in management consulting, financial services, and the nonprofit sector. Before joining Social Finance, Casey was an Education Pioneers Fellow at Education Growth where she provided support for nonprofit organizations that offered compelling solutions to unmet needs in education. Prior to Education Growth, Casey worked at New Leaders where she was responsible for strategic planning initiatives, including: revenue forecasting; financial scenario development; brand auditing and development; governance management; and communications. Earlier in her career, Casey assisted in the launch of Teach For India in Mumbai, and worked in management consulting at Oliver Wyman Group. Casey holds an MBA from Harvard Business School, and a B.A. in history from Yale University.

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Bringing Social Impact Bonds to New York City

The City of New York

Kristin Misner
Chief of Staff to the Deputy Mayor
For Health and Human Services
& Family Services Coordinator

What are Social Impact Bonds?

- A Social Impact Bond is an investment vehicle designed to encourage private funding for promising social programs
  - Taps into new funding opportunities
  - Private investors fund a program's delivery and operations
- Public sector commits to paying the contractor only if improved social outcomes are achieved
  - Taxpayers only pay for interventions that work
- Third-party evaluation confirms that outcomes have been achieved before investors can be paid

Addressing Adolescent Incarceration in NYC

- **Issue**: those who enter jail as adolescents have a high likelihood of re-entering the system in the years following their release
  - nearly 50% of adolescents who leave Rikers return within one year
- **Program**: Adolescent Behavioral Learning Experience ("ABLE")
  - Provide evidence-based intervention in-jail and post release to 16-18 year olds in DOC custody at Rikers Island
  - The goal is to improve social skills, problem solving, self-control and impulse management.
  - Estimated roughly 3,000 adolescents served each year for 4 years
  - The Osborne Association and Friends of Island Academy will deliver the intervention through trained facilitators working closely with DOE and DOC staff
  - Part of Mayor's Young Men's Initiative and the City's commitment to improving outcomes for young black and Latino men
- **Goal**: to decrease participants' likelihood of future criminal behavior and reincarceration
- **Budget**: $2.4 million annually for 4 years

Calculating the Savings

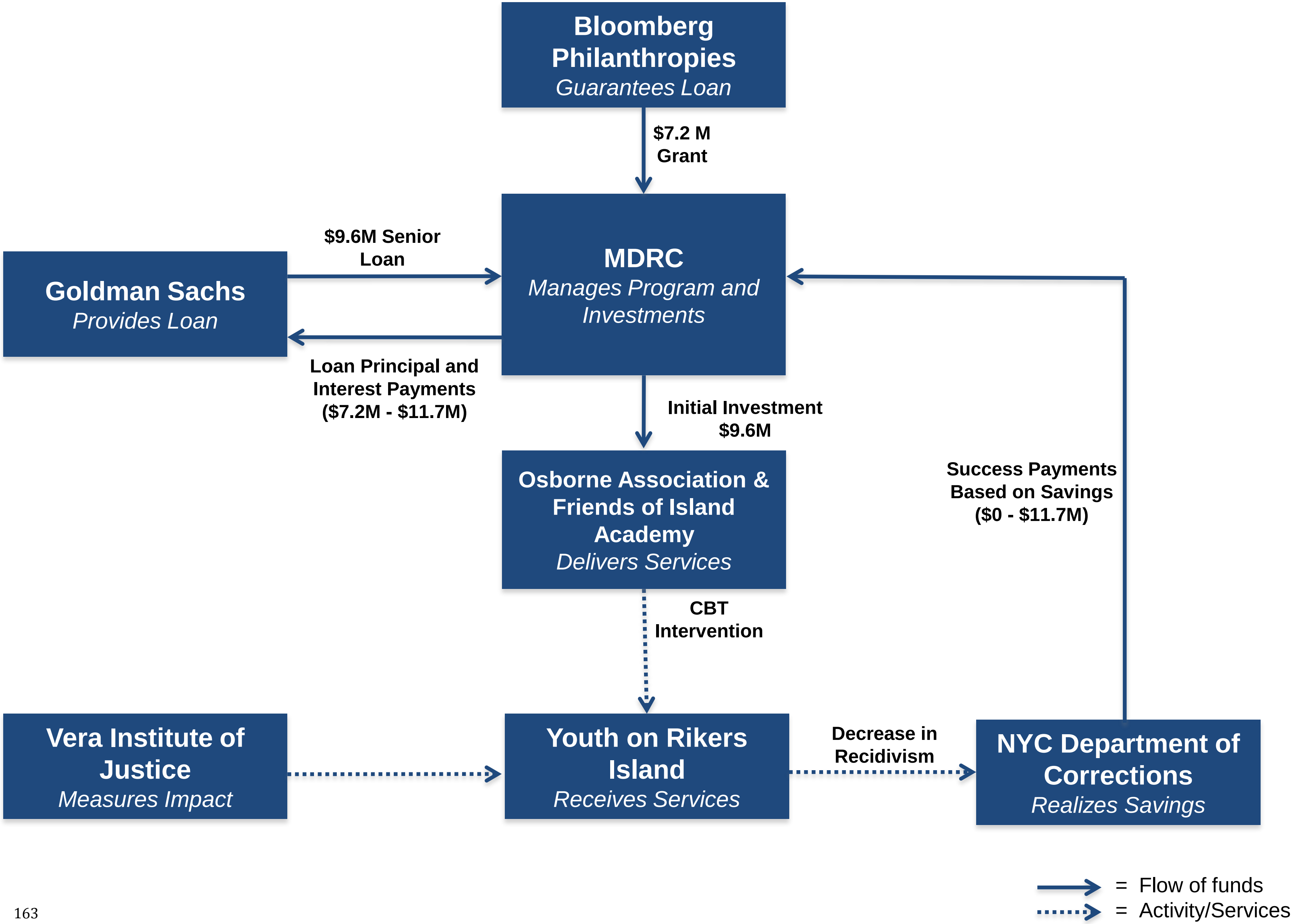
Analysis

- Estimate the number of program participants
- Baseline Bed Days Per Participant
  - Used DOC historical cohort analysis
- Effect of ABLE Program on Projected Bed Usage
  - Calculate projected number of bed usage with and without ABLE (create the counterfactual)
- Turned Bed Day Savings into Cost Savings

Partners

- **Goldman Sachs** funds the project's delivery and operations through a $9.6 million loan to MDRC;
- **Bloomberg Philanthropies** provides a $7.2 million grant to MDRC to guarantee a portion of the investment;
- **MDRC** oversees the day-to-day implementation of the project and manages the Osborne Association and Friends of Island Academy, the two non-profit service providers that deliver the intervention;
- **The Vera Institute of Justice**, an independent evaluator, determines whether the project achieves the targeted reductions in reincarceration;
- **The Department of Correction** pays MDRC based on reduced re-admissions and the associated cost savings and MDRC then pays the private investor.

Overview of the NYC SIB



Payment Terms for Final Evaluation (4 Years of Investment)

Reduction in Reincarceration	Projected Long-Term City Net Savings ($)*	City Payment to MDRC ($)
≥20.0%	$20,500,000	$11,712,000
≥16.0%	$11,700,000	$10,944,000
≥13.0%	$7,200,000	$10,368,000
≥12.5%	$6,400,000	$10,272,000
≥12.0%	$5,600,000	$10,176,000
≥11.0%	$1,700,000	$10,080,000
≥10.0% *(breakeven)*	$ ≤ 1,000,000	$9,600,000
≥8.5%	$ ≤ 1,000,000	$4,800,000

** Excludes city savings used to continue funding program delivery for youth at Rikers*

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What are the Benefits?

- Investing in outcomes to improve the lives of those in need
- Government is able to preserve public resources for successful interventions while still encouraging innovation in a time of fiscal constraints
  - Savings can be recaptured and reinvested into a permanent funding stream for the program
  - Accelerate adoption and implementation of promising programs
  - Brings added discipline to measuring outcomes for government programs because there is an upfront agreement on how to measure success
- Nonprofit providers receive a committed funding stream not subject to budget cuts
- Can produce financial returns for private investors, who assume the risk while achieving a public good

APPENDIX D: October 7, 2013 Social Impact Bond Meeting

- October 7, 2013 Social Impact Bond Meeting Agenda
- October 7, 2013 Social Impact Bond Meeting Notes
- October 2013 Survey Results

Social Impact Bond Summer Study 2013

Monday, October 7, 2013
9:00 am to 12:30 pm

The Institute for Innovation & Implementation, UM SSW
306 W. Redwood Street, Baltimore

Workgroup Meeting #3 Agenda

Workgroup Goal: Report to the House Appropriations Committee on the merits of Social Impact Bonds (SIB) and their relevance and applicability to Maryland.

Meeting Goals: To wrap up with an overview from a foundation involved in SIBs. The work group will review and share comments on the first draft of the report.

9:00-9:30 am	Welcome. Discuss results of the second participant survey (Michelle Zabel)
9:30-10:15 am	Mr. Jeff Schoenberg is an advisor to The J.B. and M.K. Pritzker Family Foundation, a Chicago-based philanthropy. Mr. Schoenberg principally advises members of the Pritzker family on grant making for The Children's Initiative, a project of the J.B. and M.K. Pritzker Family Foundation which seeks to enhance the early learning capabilities of infants and toddlers, with a special focus on at-risk children. Mr. Schoenberg is a former Democratic member of the Illinois Senate, from 2003 to 2013, and prior to that served for 6 terms beginning in 1990 in the Illinois House of Representatives. Mr. Schoenberg will present on the role of foundations in SIBs, and provide specific information on the Salt Lake City PreK SIB.
10:15-10:30 am	**Break**
10:30-12:30pm	The work group will react to the first draft of the report (sent out by staff prior to the meeting), and list out final recommendations for the report to legislature.

Comments/changes to the first draft due to Roann by Wednesday, October 14, 2013.

SIB Summer Study Contact: Roann Tsakalas, rtsakalas@msde.state.md.us , (410)767-7802

Social Impact Bond Summer Study 2013

Monday, October 7, 2013
9:00 am to 11:00 am

The Institute for Innovation & Implementation, UM SSW
306 W. Redwood Street, Baltimore

Workgroup Meeting #3

Workgroup Goal: Report to the House Appropriations Committee on the merits of Social Impact Bonds (SIB) and their relevance and applicability to Maryland.

Meeting Goals: To wrap up with an overview from a foundation involved in SIBs. The work group will review and share comments on the first draft of the report.

Meeting Notes:

Members in Attendance:
Michelle Zabel, The Institute for Innovation & Implementation, *Chair*
Nathan W. Bowen, Department of Budget & Management
Nancy Fitzgerald (for Marcella Franczkowski), Maryland State Department of Education
Kathy Oliver (for Jeanne-Marie Holly), Maryland State Department of Education
Farid Keshavarz, Department of Public Safety & Correctional Services
Stephen Schrieber-Stahl (for Dan Feller), Governor's Office for Children
Angela Lagdemeo Cabellon, Director of Policy and Planning, Department of Human Resources
Miriam Shark, Annie E. Casey Foundation
Margaret Williams, Maryland Family Network
Terry Staudenmaier, Abell Foundation
Rolf Grafwallner, Maryland State Department of Education
Maura Dwyer (for Ilise Marrazzo), Department of Health and Mental Hygiene

Observers: Caroline Boice, Louise Corwin

Staff: John Spears, Roann Tsakalas, Deborah Harburger

Welcome: Michelle welcomed the members to The Institute and introduced Mr. Jeff Schoenberg

Mr. Jeff Schoenberg – Mr. Pritzker is interested in superior outcomes and is frustrated about the lack of resources available to change the life trajectories of disadvantaged children and their families. In order for programs to be candidates for a SIB, the program must demonstrate hard data that justifies cost avoidance for government. The total SIB transaction is a test of patience. The Salt Lake SIB started working years ago with the Kellogg Foundation and the Voices for Utah Children nonprofit to see if there was an alternative financing model available to fund PreK for at risk children.

Kellogg funded several years of research tracking of 3 and 4 year olds in high quality PreK programs. See http://www.utahchildren.org/issues/early-care-and-education and open "Summary: High Quality Preschool Closes the Achievement Gap and Reduces Special Education Costs for At-Risk Children." If at risk children received high quality PreK experience, then approximately 25% were not tracked into special education. Over 5 years, there was a savings of $1.7m in special education costs. The research demonstrated quantifiable cost avoidance. With this evidence the partnership began, and counted as its members:

- The Kellogg Foundation
- The Voices for Utah Children – provides the research
- The United Way of Salt Lake- oversees the intervention, and
- The Granite County School District – provides training for PreK providers

Private investors were brought to the SIB table - Goldman Sachs provided $4.6m loan, Mr. Pritzker provided $2.4m, the United Way provided $1m, and Salt Lake County Government invested $350k. United Way is the holder of the investment and acts as banker/financial intermediary. At first the state of Utah was going to be banker for the transaction. However, the Utah Legislature did not pass the bill to do this. The SIB project is providing high quality PreK to 3500 at risk children that otherwise would be on a PreK waitlist. United Way also oversees the project as an intermediary, and provided $90k in capital. Salt Lake County also has a financial stake in the project.

The intervention is high quality and evidenced based. As a result of this project, there will be a greater focus on metrics to ascertain whether social interventions are working. The SIB contractual agreement creates a higher standard of data analysis. Utah State University is the research arm of the project and determines if the next quarterly payment should be made based on research demonstrating fidelity to the model and progress.

There will be an estimated savings of $2700 per student in special education savings to the state of Utah. The expectation is to prove the project successful in year 1 and hope that the Utah legislature would pass the law to act as banker. For school year 2013-2014, Granite County enrolled a little shy of 600 at risk (defined as below the federal poverty line) children in PreK. The Granite Schools were ready to welcome these students.

Goldman Sachs gets a success payment when the project is successful. Payment to Goldman Sachs is 90% of the avoided cost, and Mr. Pritzker gets a base interest rate. The success payment is paid after each child enters 6th grade and has avoided special education service. Goldman Sachs and Mr. Pritzker pay in quarterly based on the research intermediary reporting that the program is working satisfactorily. Administrator cost for the SIB is minimal because the school district is expanding an existing service. There was no cost for an intermediary to pull the financing of the SIB together in this model. Also, in other SIB models, there can be another intermediary to act as the banker for the project and oversee the researcher. Mr. Pritzker is in for 12 years. Mr. Schoenberg recommended speaking with Janis Dubno, the lead developer of the Salt Lake City pre-kindergarten project from the Voices for Children Utah, to learn about how measures were set for quarterly success.

Michelle thanked Mr. Schoenberg for participating in the meeting via teleconference.

The minutes were reviewed silently and a motion was made to accept the minutes as written, and the motion carried.

Deborah reviewed the summary report of the survey taken after the September 17th meeting.

The draft report was reviewed by Deborah. It was requested that a chart with elements necessary for a SIB across the top and current projects (MA, UT, NYC, etc.) down the side be completed for the appendix of the report. The chart should be divided into Tier 1 (operating SIBs), Tier 2 (pre SIBs). Members wanted to be sure that report stressed the SIB negotiations process. It was suggested that more information on SIBs could be found at the National Finance Nonprofit Fund. One member shared that Minnesota has implemented a human capital performance bond. Funds to repay bond came from the State's general obligation fund. This is a bond. The intermediary gets paid upfront by the State.

One member requested that the report provide a positive view for any entity that wants to move forward with a SIB, and that the surveys give a true sense of things right now. Both surveys showed that workgroup members fall to the positive side on SIBs in Maryland. It was requested that the report mention Baltimore City's application to Harvard to begin a SIB. It was requested that it be made clear that the Steps on page 5 of report do not have to happen in that order.

Members took final survey and turned them in.

The meeting adjourned at 11:00 am.

The minutes were emailed out to the workgroup on October 8, 2013 for comments, and members emailed in changes. The minutes became final on October 17, 2013.

Social Impact Bond Summer Study 2013

Participant Survey Results

October 7, 2013

This survey was issued to all Social Impact Bond (SIB) Summer Study Workgroup members and designed to serve as a check-in with all participants to identify current thinking about and questions regarding SIBs in general and in Maryland. A similar survey had been administered in prior to the September SIB meeting, and this survey will be re-administered after the October SIB Workgroup Meeting.

Did you attend the second meeting of the SIB Summer Study Workgroup (Tuesday, September 10, 2013)?

There were 11 respondents; 9 attended the second meeting of the SIB Summer Study Workgroup on Tuesday, September 10, 2013. (All participants have received materials regardless of attendance at the meeting.)

What information about SIBs (either from the meeting or the resources shared) have surprised you or challenged your ideas about SIBs? (Comments in italics are from the October survey; non-italicized comments are from the September survey.)

- *I thought Steve Liebman's checklist of what makes a "ripe" opportunity to consider a SIB was very useful.*
- *Extent to which SIBs are being used or studied across the country*
- *I have a better understanding that a project must really be a good fit for a SIB. Not all projects would lend themselves to SIBs because of a variety of factors such as the timeframe being too soon to show impact results before the funding ends. The example of Rikers Island was a good one as it does take time to change the culture of a person.*
- *I was surprised at the short time horizon for an ideal SIB (presenters stated it to be about 4-5 years), as many social programs have a much longer time horizon for realizing benefits. I also had not considered the fact that SIB could be a way to work around policy/budget silos in departments.*
- *The broad range of issues that people want to address through SIBs; the fact that private investors are interested in investing in social programs; the complicated financing mechanisms; Prof. Liebman's statement that there is a lack of solid evidence of effectiveness for most prevention programs.*
- *(1) It's good to have a large bond because of all the work it takes to put it together. (2) A lot of SIBs do not fund evidence-based practices and therefore are riskier. (3) Private and/or public subsidies or guarantees are essential.*
- Presentation by Dr. Salamon about the variety of new financing options through the private market
- The fiscal analysis done by the Department of Legislative Services is sobering.

- I was surprised to discover the breadth of literature in this area as it is relatively new to me. I was also interested to learn of the existing SIBs and their structure.
- I like the model in concept, am still trying to understand the complexities of the financing mechanism and am concerned about what sound like high legal and transactional costs of creating a SIB. Also, if an investor requires a guarantee, as in the NYC Rikers Island SIB, that would make it more expensive and more difficult to put in place.
- It was a wonderful learning experience for me. I was only vaguely familiar with social impact bonds and I learned a lot about the types of initiatives around SIB. The resources provided a great background.
- There is often significant private capital spurring development like the Bloomberg example in NY

Questions about SIBs: I have questions about SIBs in relation to:

Answer	September Response	**October Response**	
Determining the population focus	3	**3**	No Change
Organizing the financing for the SIB	7	**7**	No Change
Recouping savings from the SIB	8	**5**	Decreased
Challenges to developing and implementing a SIB	4	**5**	Increased
Benefits of implementing a SIB	4	**1**	Decreased
Other (please state):	4	**1**	Decreased
	Understanding what the best use of a SIB is in Maryland -- which agency/foundation would be interested in funding which intervention, and how the savings would be counted and the repayment made. I'm interested in a specific possible case for Maryland		

(11 respondents in September; 9 respondents in October)

Based on the information you have received to-date, on a scale of 1-10, do you think a SIB could work for Maryland in the next few years? (1=SIBs are not at all feasible or realistic for Maryland in the next few years; 10=SIBs could definitely be implemented in Maryland to implement in the next few years)

September Responses:

Min Value	Max Value	Average Value	Standard Deviation	Responses
3.00	8.00	**5.22**	1.86	9

October Responses:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.27**	1.35	11

The October survey asked respondents whether they were employees of a State Agency (DBM, DHMH, DHR, DJS, GOC, MSDE). Six (6) respondents said that they were State Agency employees.

October Responses for State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	7.00	**4.83**	1.17	6

October Responses for Non-State Agency Employees:

Min Value	Max Value	Average Value	Standard Deviation	Responses
4.00	8.00	**5.80**	1.48	5

Please explain your rating.

- All the technical aspects are doable. The question is leadership. Also, whether there is the will and capacity to tackle problems with enough room to reduce costs to put the costs and benefits in balance.
- If one or more agencies is interested in funding a program that has not been funded in the state operating budget, this is an opportune way to do so.
- If Maryland decided to go with SIBs for specific, well-defined projects, I would suggest that it be a pilot or two first.
- In a time of budget constraints, it will be difficult to convince either the Administration or Legislature to provide funding to such a new concept that has few examples and no proven track record. I think that legislation might be passed to enable the State to enter into SIB contracts, but a significant amount of study will be needed in a given project area before a SIB could be conceived of in Maryland.
- It is evident that part of the success of SIBs has to do with leadership. Given that we are on the cusp of election season and that this is a very new initiative, I can foresee that timing would be key.
- Still too many moving parts and actually developing the legislative financing vehicle are barriers

- A clear plan would need to be developed with clear outcomes. Also, staff would need to be designated for this implementation - this isn't something that can be added to someone's job duties.
- With the collaboration of agencies on a focused population it appears to be very possible.
- I think the model has good potential but there doesn't seem to be anyone championing this in any state agency, we don't have a specific target population or specific intervention identified, and other priorities are likely to consume the attention of the agencies and the legislature next session so it may be difficult to get anyone to focus on this. If it is going to move forward we need someone at a high level who is an advocate for a specific SIB.
- The mechanisms that allow for this type of innovation take time
- While SIBs are clearly doable, they are employed to fund projects that government should be undertaking anyway, with private inducements if necessary, and they are expensive and difficult to assemble. I sensed that our budget and legislative colleagues recognized that, too, and their backing would be helpful, if not essential, to get a SIB off the ground.

What specific programs and initiatives might be relevant for a SIB or pre-SIB? (Think about specific projects, populations, and grant activities, including those that are within one agency and those that are interagency.) *No examples were provided in the survey. The following list is generated from the free response section of the survey.*

Early Childhood/Pre-K/Home Visiting: 8

Child Health (e.g. Early Childhood Mental Health Expansion, Pediatric & Primary Care Integration, Asthma): 3

Juvenile Justice: 5

Prisoner Re-Entry/Recidivism Reduction: 2

Child Welfare: 1

Elder Care: 1

Hunger: 1

Housing First: 1

Other Comments:

- It sounds like programs with clear objectives and 'fast' outcomes are better than longer term goals.
- I was intrigued by Dr. Zachik's thought that we try a multi-disciplinary, comprehensive, integrated intervention (perhaps geographically focused?) targeted to very young children and their families. Though complicated to plan and implement, and the big pay-off coming only over time, something big and bold like this might be fitting for the tremendous complexity of the instrument itself.

What additional information would you like to receive to assist with the development of the recommendation to the General Assembly?

- Where would this rank on the Governor's priority list?
- Thank you for what you have provided so far. I have learned much about this topic.
- I think the development of a few proposed project areas would be highly useful. As would be more analysis of what specific Legislation will be needed to enable the creation of SIBs in Maryland.
- Ways that SIBs are used to enhance or augment existing services- without cutting traditional funding mechanisms
- What if any state agencies are interested in pursuing a SIB, and what specific population do they want to target and what outcome do they hope to achieve?
- I know we don't have to come up with a specific recommendation, but that would be MOST helpful to my thinking!