Social Financing and Payment by Results: Greater driver in efficiency, innovation, and impact in tackling social problems?

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Social Financing and Payment by Results: Greater driver in efficiency, innovation, and impact in tackling social problems?

By

Erin Mathis

A Thesis Submitted in partial fulfillment of the requirements for the degree of

Master of Science in Science, Technology, and Public Policy

Department of Public Policy

College of Liberal Arts

Rochester Institute of Technology

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Social Financing and Payment by Results: Greater driver in efficiency, innovation, and impact in tackling social problems?

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Masters of Science, Science, Technology and Public Policy
Thesis Submitted in Fulfillment of the Graduation Requirements for the

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Abstract

There is mounting pressure on government to provide funding for social services; however, due to budget constraints and complex social issues, this has become a challenge (Social, 2014). With the increase of poverty, behavioral and mental health issues in America, the status quo in the social sector simply will not hold (Shah, 2013). In 2013, fourteen percent of Americans were living below the poverty line (Gongloff, 2014), with one in five children living in poverty (Shah, 2013, p.2). In 2011, under President Obama, the US government decided to try a different method in assisting the high demand for social services, social innovation financing (Goldmark, 2011). This paper focuses on the technology of social impact bonds, which falls under Pay for Success financing (Shah, 2013). Using a case study design, it is investigated if outcomes-based reimbursement drives great efficiency, innovation and impact in tackling social problems. Through a deeper dive, exploration of reimbursing social programs based on their outcomes is an attractive model to investors and to what extent stakeholders feel that the SIB will lead to great innovation or efficiency. To do this, one of New York States’ Pay for Success awardees was analyzed -- the Intensive Community Asset Program (I-CAP), which creates alternatives for Family Court Judges and Probation officers who seek to avoid placement of youth into high cost institutional settings (James-Wilson, 2014). The changing landscape of government funding of social programming, multi-stakeholder financing strategies are becoming the new trend in nonprofit funding. This report provides a more robust learning on this new funding mechanism.
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Acknowledgement

My thesis has been a journey. There were many learnings and challenges along the way. I learned critical analysis on a fairly new finance mechanism and bridging the theory and practice of the financial model with social impact, and applying research techniques (literature review, collecting data, and analysis). Balancing work and family, and trying meet deadlines I placed for myself proved to be the biggest challenge. To help mitigate this, I tried to meet with my advisor every other week to keep me on target. In addition, it was challenging getting access to the right people, and scheduling interviews around their busy calendars. However, I was able to access the research participants early in the process, and break the lengthy 1.5 hour interviews into smaller segments for some of the participants, making it more manageable for them.

I would like to thank those who helped me a long with my thesis, including: my husband, Erik, and children, Cameryn, Ava, Emma and Sophie, for their patience throughout the process; my thesis advisor, Professor Foltz, who was understanding, and kept me moving forward, even if only to make me feel guilty; my work supervisor, Kat Bassney, who make it possible for me to take time off to complete my thesis, and provided moral support; all the research participants; the many friends and family who encouraged me; and last, but not least, David James-Wilson, who has since passed from cancer, got me involved in the Pay for Success project at Hillside Family of Agencies – with love and remembrance.
1. Introduction

1.1 Background

Pressure is building for government to provide funding for social services. However, due to the complexity of social issues and budget restrictions, this has become a challenge (Social, 2014). With the increase of poverty, behavioral and mental health issues in the United States, the status quo in the social sector simply will not be able to continue this way (Shah, 2013). In 2013, 14 percent of Americans were living below the poverty line (Gongloff, 2014), with one in five children living in poverty (Shah, 2013).

In 2011, under President Obama, the US government decided to try a new technique to assist in providing for social services. The idea was a group of methods called social innovation financing (Goldmark, 2011). This paper focuses on the specific technology of social impact bonds (SIBs), which fall under Pay for Success (PFS) financing (Shah, 2013). In 2013, New York State published its first PFS request for proposals (Governor, 2014).

This paper will explore if the practice of reimbursing social programs based on their outcomes is an attractive model to investors, and to what extent stakeholders feel that the SIB will lead to great innovation and efficiency. An analysis was completed for one of New York States’ Pay for Success awardees -- the Intensive Community Asset Program (I-CAP), which creates alternatives for Family Court Judges and Probation officers who seek to avoid placement of youth into high cost institutional settings (James-Wilson, 2013).

Historically, 35% of this population has been placed into residential treatment with an average length of stay of 328 days (James-Wilson, 2013). In Onondaga County alone, the average annual marginal cost of these placements is $3.4 million¹ (James-Wilson, 2013). The

¹ Marginal cost per placement day = $527. Total annual placement days = 6,433.
economics for I-CAP PFS Project assume a 30% reduction in the number of days spent in detention and placement among the project’s high risk youth target population (James-Wilson, 2013). This results in $19,287 in combined cost savings to the County and New York State per high risk youth served by I-CAP, compared to a $9,045 assumed cost to serve (James-Wilson, 2013).

1.2 Research Problem & Importance

Given the changing landscape of government funding of social programming, innovative, multi-stakeholder financing strategies are becoming the new trend in nonprofit funding. Despite (or perhaps because of) some of these financing strategies being innovative, organizations face challenges when embarking on such contracts. Discussed in the analysis chapter is how SIBs might mitigate the risk for government funders and increase overall accountability for program quality and outcomes. Also discussed is the opportunity for policymakers to commit to creating policies that offer ease within deal negotiation and create a "true market" for investors. The study further investigates if outcomes-based reimbursement drives greater efficiency, creates more innovation and provides a bigger impact in tackling social problems.

PFS combines social services expertise, private investors, philanthropic and capital funders, and evaluation to transform the way government and society respond to chronic social problems (Third, B, 2014). In a PFS initiative,

Funders assume up front financial risk, and taxpayers pay for a program only if a third-party evaluator determines that the initiative has achieved specific outcomes that create benefits to society and generate savings for government (Third, B, 2014, para 2).

As this type of model gains momentum, we need to look at its effectiveness. However, in some cases it is too soon to tell. In the meantime, it is meaningful to investigate if it is a one-size fits all model – a solution for all social sectors. If not, it is helpful to examine those sectors, or
grass roots social service efforts, who are also trying to obtain funding from the same philanthropic organizations (or government) agencies that are deploying their funding towards a pay for results method.

If we understood the answers to these questions, then government could more efficiently provide funding to social service sectors that meet and do not meet the PFS model. The analysis may not provide a definitive answer to the question(s) or a clear-cut solution to the problem. However, it will further educate social services agencies, intermediaries, philanthropic entities and possibly policy analysts.

2. Reflections

2.1 Why is this worth my time and why it should be worth your time?

For the last five years I have worked at Hillside Family of Agencies, one of the oldest family and youth non-profit human services organizations in the United States. The organization deals with some of society’s most complex issues, such as: child welfare, mental and physical health, youth development, juvenile justice, and special education and developmental disabilities services.

Addressing complex issues requires a systemic approach that coordinates a wide range of mutually reinforcing efforts. Hillside Family of Agencies works individually and collectively to help children, youth and families find their pathways to success and break the damaging cycles of poverty, trauma and neglect.

My role at Hillside is to find government and private funding to sustain or create these needed services across central and western NY; and I have seen first-hand government funding being cut and impacting crucial services in our communities. Bringing my work at Hillside together with my public policy degree seemed like a natural fit when Hillside was being vetted
for a Pay for Success project, which would allow us to fund services via private funding/investors to be paid back by the government once the outcomes where met. Luckily, I had the opportunity to listen in on the early vetting process with my colleague, Hillside’s Chief Financial Officer, and the intermediary, Third Sector Capital Partners, Inc. In 2014, Hillside was awarded an opportunity to proceed with a NYS PFS project – the Intensive Community Asset Program (ICAP). As you will see in the document, Hillside did not move beyond the contract stage and the project folded. However, this allowed me a unique opportunity to conduct a deep dive into ICAP’s PFS process – the good and the bad.

Although this is a relatively new model, enough has been done to give us a glimpse of the potential. As a backdrop for the case study analysis of ICAP, I reviewed other established PFS projects in varying degrees of stage and success – in all cases the goal was to reduce recidivism rates, keeping youth out of jail, while using case management.

Examples include the UK’s 2010 pilot project at Peterborough Prison (discussed in greater detail in the literature review section), which has also been touted as the first impact bond in the world (Davies, 2014); the fourth and largest PFS project launched in the country, Massachusetts Juvenile Justice PFS Initiative with Roca, which was also designed to improve outcomes for hundreds of at-risk youth ages 17-23 in the probation system or leaving the juvenile justice system in Massachusetts (Third, D, 2014); and the first social impact bond project in the United States which aimed to reduce readmissions of 16- to 18-year-olds to Rikers Island via an Adolescent Behavioral Learning Experience (ABLE) program (Impact, 2013). Even though these are three juvenile justice programs, they are all a little different in their program design outcomes and payment structure (Archer-Rosenthal, 2016).
In 2012, Adolescent Behavioral Learning Experience (ABLE) Program at Rikers Island Correctional Facility was launched in New York City (Vera, 2015). ABLE used Moral Reconciliation Therapy (MRT), an evidence-based behavioral therapy program and employment (Vera, 2015). The City expected to save $32.2 million if they reduced recidivism by 20%, therefore, the intermediary would have received $11.7 million (investment plus return) for achieving the goal and the City would have saved $20.5 million after the payment to intermediary (Center, 2013). The ABLE program was slated to run four years (NYC, 2015). However, after an independent evaluation conducted three years into the four years, by the Vera Institute of Justice, they found the program to be ineffective of reaching a 10% reduction in recidivism with participants (NYC, 2015). In the first year, Rikers showed a 36% decrease in inmate violence, but it did not correlate into a reduction of recidivism (Center, 2013). As such, the program ended in 2015, and the investors were not paid back by the New York City government (NYC, 2015).

And in 2014, Massachusetts Juvenile Justice PFS Initiative was launched between Roca, Third Sector Capital Partners, and the Commonwealth of Massachusetts (Third, B, 2014). Roca uses a High Risk Youth Intervention model that provides intensive street outreach and targeted life skills, education, and employment programming (job readiness and employment) (Third, B, 2014). Although this project is still in the implementation phase, to end in 2021, it has made great progress to meeting its outcomes (Third, B, 2014).

Data revealed that of the nearly 800 young men released from prison in the state annually, almost 65 percent would return to jail within five years of their release and serve an average sentence of 2.4 years (Rangan & Chase, 2015). A large share of the 3,000 young men on probation each year were also likely to violate their terms and enter prison (Rangan & Chase,
2015). The estimated additional cost of housing each prisoner is $12,500 annually (for food, uniforms, and prison programming), with a total cost (including housing, prison administration, and other overheads) of $47,500 annually, so the state would achieve substantial savings from reducing recidivism (Rangan & Chase, 2015). That task was entrusted to Roca, a community-based nonprofit headquartered in Chelsea, Mass. Roca focuses on helping very high-risk young men stay out of prison, secure jobs, and stabilize their lives (Rangan & Chase, 2015). Its intervention model is data driven, built on nearly seven years of evaluating and coordinating its work with evidence-based practices and programs (Rangan & Chase, 2015). Roca had established that its intervention was able to reduce recidivism rates by 25 to 60 percent (Rangan & Chase, 2015).

Peterborough, Roca, and ABLE continuously assessed their interventions, carefully collecting data and tracking outcomes for each client (Rangan & Chase, 2015). These attributes, along with the continuous adjustment of their service delivery models, make all three of these nonprofits ideally suited to the PFS model, unlike many social service organizations (Rangan & Chase, 2015).

With the Massachusetts juvenile justice PFS, the state will achieve savings from reduced court costs and policing, as well as direct savings to the state Department of Corrections and the county Houses of Correction (Rangan & Chase, 2015). The break-even rate for the Massachusetts PFS is a 40 percent recidivism reduction, which is $22 million in program savings and payouts (Rangan & Chase, 2015). If Roca achieves a 70 percent reduction in recidivism, the payout will be capped at $27 million and the state will save an additional $18 million over the contract period (Rangan & Chase, 2015). At that level of achievement, Roca will receive added payments up to $1 million, Goldman Sachs will be paid up to an additional $1 million, and the
Kresge Foundation and Living Cities will each receive up to an additional $300,000 (Rangan & Chase, 2015).

While the PFS model’s focus on impact measurement is an important step in improving program effectiveness, it also poses a challenge for many nonprofits, few of which are as well-equipped as Peterborough, ABLE or Roca to rigorously measure impact (Rangan & Chase, 2015).

After all, evaluating any nonprofit’s impact is both expensive and necessarily complex, ranging from its outputs (How many high-risk young men stayed out of jail?), to broader outcomes (Are those same young men placed in stable jobs and are they better off financially?), to long-term social impacts (Is the result greater economic and social equality?) (Rangan & Chase, 2015, para 21).

Even though the technical model is not for all social sectors, PFS is relevant because of the changing environment and government budget reductions to some of our most pressing and complex social problems. PFS continues to gain momentum across the nation and is at the forefront on political platforms.

In looking at the major schools of thought to the problem, we must first find out how, or if PFS initiatives tackle social problems. As Jeff Liebman from Harvard University’s SIB Lab indicated, “The goal would be to discuss two or three transformative approaches to each policy problem – solutions that could then be applied nationwide” (Liebman, 2015, p. 3). Because there have only been few completed PFS projects completed, it is too soon to tell if this method can tackle some of our most broad and pressing social problems, in addition to replicate and scalability.
2.2 How and why did Hillside get involved with PFS?

Hillside's interest in innovative financing goes back many years (Interviewee 1). As government funding has become diminished, Hillside, like so many social service organizations, tried to find new ways to fund important services in our communities (Interviewee 1). Per Hillside’s Chief Financial officer,

We recognized long ago that public funding had limitations and that using philanthropy to fill the gap between what government could pay and the full cost of delivering services would limit the scope and reach of our impact. Furthermore, we saw how hard it would be to introduce innovations in our service model if our only source of funding was government contracts (Interviewee 1).

Government contracting has becoming inadequate and looked like it had gotten worse over time. The notion of public private partnership was already out there, but the form in which they would evolve was certainly a question. Then different funding mechanisms started being discussed - ones that would reshape government involvement and be clearly innovative. Although Hillside has many years of experience in pay for performance programs with NYS, it would be a couple more years before they realized an opportunity to put forth a response to a [Pay for Success] request for proposal (Interviewee 1).

Around the time social impact bonds were emerging in the United Kingdom, Hillside collaborated with thought leaders, Deloitte and Touche, Bridge Span, and Rockefeller Brothers Foundation, at a symposium with in the nonprofit sector to explore all the ways in which this might be relevant to and for our work (Interviewee 1). When New York State began thinking about pay for performance, Hillside contributed their knowledge, experience, and encouragement (Interviewee 1). In parallel, they developed relationships with several philanthropic organizations that were frustrated with the limitations of traditional grant making and were wrestling with how to affect real change for the most intractable social problems (Interviewee 1).

The introduction of new opportunities for funding necessitated the need for key organizations to take a leadership role providing sophisticated infrastructure, scalability models and ways to demonstrate impact to funders (Interviewee 1).
Hillside’s history in the space positioned them to move forward in this role (Interviewee 1).

After Governor Cuomo was elected, New York State decided to be on the cutting edge even though they didn’t understand what it [PFS] was all about. [Cuomo] wanted to be first the governor. And part of it was competitive with Bloomberg and the work he was doing on Rikers Island, so they went through some acclamations, did some interviews, research. [Hillside] contributed to the states thinking about what we knew at the time, and we had already experienced in a variety of ways with public private partnerships with New York State, so it gave us some credibility to have that conversation. It ended up with a request for proposal. We had vetted a multitude of ideas, initially try to aim at Hillside Work Scholarship Connection because we thought it was a natural fit. But once the request for proposal process got exposed to state legislature, they decided that education is not where they wanted to dedicate their appropriations…and based on advice from Third Sector we landed on ICAP and the fact that it had the best chance of meeting everyone needs, as a model. So we went through the request for proposal process (Interviewee 1).

The program model and key service delivery elements are drawn from Hillside’s Re-Investing in Youth (RIY) Project—a program in Monroe County that has operated for three years within a “pay for performance” funding paradigm (Interviewee 2). RIY has generated a range of externally-monitored and validated outcome measures, including significant reductions in the number of youth placed into detention and placement, reductions in failures to appear in court, and reductions in rates of re-arrest (Interviewee 2). Although Hillside first sought to replicate and expand RIY to different counties for PFS,

They quickly realized RIY was not going to be an appropriate model because it was too hard to demonstrate the immediate impact. It was not a good model for pay for success. Even though it was an excellent model, we would need to serve the highest in JJ system before we could demonstrate immediately that we would be preventing placement (Interviewee 2).

RIY’s many successes help inform and provide evidence for the impact that ICAP stands to achieve (James-Wilson, 2013).
3. Literature Review

Although PFS is a fairly new funding mechanism in the US, there is a fair amount of literature on best practices, and comparative analysis of the first 10 pay for success projects in the US. However, with only one project actually completed in the US, there is still much more to learn.

PFS promises to better align incentives to improve social outcomes and to diversify risk associated with investing in innovative programs by using private-sector capital (Third, A, 2014). For social service providers, PFS provides secure, long-term funding that alleviates the challenges of one-year budget cycles while supporting investments in evidence-based service models that produce significant social benefits as well as cost savings (Nonprofit, Pay, 2016).

Several sectors seem to be getting the most PFS attention across the country, including: projects aimed at reducing recidivism among those released from prison or jail; services for at-risk youth, such as those aging out of foster care; homelessness prevention, prenatal, early childhood and preschool services; preventive health care interventions such as those for asthma or diabetes; home-based services for the elderly to stay out of nursing homes; employment/workforce development initiatives (Azemati, 2013).

3.1 History

In response to the growing need of funding for social services, the US government responded by creating the Social Innovation Fund (SIF) initiative (Corporation, A, 2015). As of March 2016, the SIF’s private-sector partners have leveraged match fund commitments valued at $627.5 million - more than double the original federal investment of $295 million (Corporation, A, 2015). The SIF has made a total of 43 awards to grantees located in 17 states and the District of Columbia (Corporation, A, 2015). As a result, over 450 nonprofit organizations have been
funded through the SIF to conduct various outcomes based projects and evaluate results through highly thorough models (Corporation, A, 2015). Through the SIF PFS program, more than $12.3 million has been awarded to 65 organizations across 25 states and the District of Columbia (Corporation, A, 2015). Per the National Service, “This investment has the potential to lead to nearly 100 PFS models across the country” (Corporation, A, 2015, para 3). Across both programs, SIF’s public-private partnerships are committed to increasing the impact of evidence-based community solutions to make a change in the lives of more Americans (Corporation, A, 2015). In addition to the SIF initiative, the federal government created another “five innovation and evidence initiatives that prioritize the outcome-based reimbursement model” (Corporation, B., 2015, para 1).

Further, SIF touts itself as an effective approach to changing lives and communities that positions the federal government to be a impetus for impact—activating private resources to discover and expand community solutions (Corporation, A, 2015). Since its inception in 2009, the “SIF and its private-sector partners have invested almost a billion dollars in compelling community solutions through its SIF Classic and SIF Pay For Success (PFS) programs” (Corporation, A, 2015, para 1).

“SIB/PFS isn’t the first in relating financial innovation to social services” (Davies, 2014, p. 2). A variety of financial services (microfinance) offered to the working poor currently signifies a $65 billion market and allows access to loans for borrowers who are trying to reach ample social and economic benefits, while securing additional credit and providing financial return to investors (Davies, 2014). Social impact investing allows governments to access new sources of funding for social programs while using inadequate government resources in an efficient and effective manner (Davies, 2014).
In 2013, the European Investment Fund (EIF) started the Social Impact Accelerator (SIA) (Davies, 2014). In response, the EU set a policy objective to create an appropriate social investing area for public-private partnerships (Davies, 2014). As an alternative, California Endowment, created SIBs that fund interventions backed by business instead of the government (Center, 2013). If the program reaches favorable outcomes, instead of getting paid back by the government, the investors are repaid by private employers (Center, 2013).

Until recently, the majority of social finance and SIBs have been developed in the English-speaking countries of US, UK, and Australia. However, they are now expanding to France, Germany, and Netherlands (Davies, 2014). It is intended that the SIBs will expand quickly over the next five to ten years that the social investments will pay off in the future through greater economic growth (Davies, 2014). In the UK, the market for social investment was estimated at £200 million in 2015 and expects to grow to £1 billion by 2016 (Davies, 2014). “It is easy to measure growth in terms of money, however, it is more challenging to measure growth benefiting society and investors” (Kyriakou, 2013, para 2).

The SIB was first used in the UK in September 2010 (Third, A, 2014). Since then it has been gaining momentum across the United Stated (Third, A, 2014). By 2015, five projects had been launched in MA, NY, NYC, UT, IL and another 21 projects are actively seeking feasibility within an additional seven states (Third, C, 2014). With another 11 states exploring the model (Third, C, 2014). Per Urban Institute, more than 50 PFS projects under development in the United States move closer to launch, stating, “We hope to see a shift toward evidence-based policymaking at all levels of government in 2016” (Urban, 2015, para 13).

As of 2016, many more states picked this finance model as a way to pay for important social issues.
Ten PFS have launch in US. The project timeline [to get to launch] has been about two years, on average. However, assessment and transaction structuring by the Federal Social Innovation’s PFS program in late 2014 should result in many more new project launches in 2016, 2017, and 2018. (Archer-Rosenthal, 2016, p. 3).

3.2 What is Well Understood

"PFS is a tool that should be intentionally used to scale the services and capacity of a service provider. To determine whether a project will accomplish this, one of the first questions we ask is whether it’s serving a significant proportion of the total eligible population" (Neely, E., 2016, p. 9).

Pay for Success (PFS), otherwise known as Social Innovation Financing or Social Impact Bonds, is utilized as a term for performance-based contracting in the social sector (Third, C, 2014). Payment is only provided by the government if results are achieved by social service providers, rather than granting reimbursement payments (Third, C, 2014). Financing is raised by private-sector organizations (philanthropic or commercial) upfront to bridge the gap between government attainment payments and capital needed to run the program (Third, C, 2014).

In the PFS model, depicted in the below diagram, the upfront funding is giving to the intermediary who disperses payment to service provider(s) for delivery of the intervention program (Third, C, 2014). Once the social program is completed, an external evaluator measures success of outcomes, and based on the achieved outcomes, the government makes payments to the intermediary (or special purpose vehicles) to repay funders (Third, C, 2014).
3.2A Contractual process

PFS and SIBs have stakeholders that potentially benefit from this form of payment by results, they include:

- **Government** – a SIB removes upfront costs of service delivery from government and shifts the financial risk to private investors, who lose their investment if interventions do not prove outcomes (Disley, 2011). The government will identify the problem to target and pay for the successful attainment of project goals (Roman, Five, 2014).

- **Services Providers** – unlike other payment by results (PBR) mechanisms, service providers are not paid by results and do not bear the risk of the SIB (Third, A, 2014). Providers are paid upfront which provides possibilities for non-profit and community organizations, which could not carry the risk under traditional arrangements to deliver services (Third, C, 2014). Another way in which SIBs are different from other traditional finance models is that under a SIB, several different providers can deliver services that contribute to improved outcomes (Third, C, 2014).

![Figure 1: PFS Model](image)
• **Investors** – SIBs offer a new investment opportunity with a blended return; investors receive some financial return but also value the social returns on their investment (Roman, Pay, 2014).

• **Intermediaries** – intermediaries structure the financial deal and solicits investors. In some instances the intermediary prices the PFS instrument and oversees implementation (Roman, Pay, 2014).

• **Independent Evaluators** – evaluation looks to see if the project meets its target goals (Roman, Pay, 2014).

• **Society** – SIBs may improve outcome and quality of life by funding service provision where there previously was none (Roman, Pay, 2014). It is claimed that SIBs might be particularly used to fund preventative interventions, or other kinds of service delivery which governments might not priories for funding – especially in a time of limited resources (Roman, Pay, 2014). In a SIB the government is not prescriptive as to the way in which services are delivered; it is hoped this may encourage innovation in service provision (Roman, Pay, 2014). Further, in some of the literature on SIBs it is suggested that private donors and organizations may be willing to consider more innovative and/or risker projects that government is likely to fund (Roman, Pay, 2014). Whether SIBs will encourage innovation has not been identified, and is something which will be explored in later stages of this evaluation (Roman, Pay, 2014).

• **Service Users** – some groups, including offenders, may be less attractive beneficiaries for both charitable giving and government spending (Roman, Pay, 2014). SIBs may raise funding to deliver interventions to these groups (Roman, Pay, 2014).

When Rangan and Chase discussed their findings in the *Payoff of Pay for Success*, they concluded that after studying the initial contracts they believed that the model is appropriate only
for a narrow cohort of nonprofits that meet two related criteria: “They must be able to effectively deliver and measure their social impact; and they must be able to translate that impact into financial benefits or cost savings that are traceable to the budgets of one or more institutions or government departments” (Rangan & Chase, 2015, para 6).

**3.2B Investors**

If expected outcomes are accomplished by the end of the contract period, investors receive back their capital plus a rate of return based on level of results achieved which is negotiated upfront (Davies, 2014). PFS and SIBs have opened social services to large capital markets, should investors want to assume the risks associated with the project/service (Davies, 2014). Traditional contracts or short-term funding can be a barrier to continuity of service in addressing social challenges (Disley, p. 18). The RAND report states, “the stable funding provided under the SIB may be an advantage in terms of organizational sustainability and less disrupted service provision” (Disley, 2011, p. 18).

SIBs are not considered a bond in the traditional sense, as they do not pay out a fixed interest rate once matured (Davies, 2014). According to Davies, they are more like “equity investments” that pay on the results accomplished and pass along a great level of risk because they may lose their return on investment if the project doesn’t prove successful (Davies, 2014, p.4). SIBs are also very involved in the front-end planning, which also differs from a traditional government funding mechanism (Davies, 2014). First a social issue needs to be chosen, followed by the development of the intervention strategy, establishing outcome measurements, budget, and timeframe, along with and financial framework or rates of return (Davies, 2014). The
intermediary assists the social service agency in establishing these components (Davies, 2014). Investors are sought once the bond is set up and often includes those interested in the social benefit, such as grant making trusts and philanthropists, rather than just the financial return (Davies, 2014).

Projects to date have been clustered into three main categories: criminal justice and recidivism, early childhood education; and homelessness. Recidivism and homelessness have emerged as leading PFS issue areas because of the high cost associated with frequent and repetitive use of jail, prison, emergency rooms and shelters, and baseline outcomes which are bad enough that even marginal change would be notable (Archer-Rosenthal, 2016, p. 3).

By attempting to attract investments in the service of impact-driven models, government agencies will learn to quantify the costs of social issues and nonprofits will learn to quantify the benefit of their interventions, leading to a more effective partnership in serving society’s needs (Rangan & Chase, 2015).

The Nonprofit Finance Fund (NFF) published a comparative analysis of the first 10 pay for success projects in the US and has shown a great variation of size of PFS projects (Archer-Rosenthal, 2016). However, according to Archer-Rosenthal, there appears to be solidarity in the field that somewhere between $5-10M is the appropriate threshold for a PFS project (Archer-Rosenthal, 2016). Some of PFS projects have been funded by well-known supporters, such as: Rockefeller Foundation, Kennedy School of Government, McKinsey, New York’s Mayor Bloomberg, and Goldman Sachs (Archer-Rosenthal, 2016).

In response to the SIB movement, the Kresge Foundation committed $350 million to social investing. Per Kresge Foundation’s president and CEO, Rip Rapson,

The language of philanthropy is shifting, from grantmaking and social investing being seen as two disparate strands of investment, to a new model, where all types of social funding work in an integrated way toward the same end. This solidifies the notion that we, as a foundation, cannot solve complex social programs through traditional grantmaking alone. By defining this funding pool, we are extending our
hand to for profit and nonprofit partners alike and are asking them to join us on the front lines to use more innovative approaches to this work” (Kresge, 2015, para 1).

**3.2C Risk & Accountability**

An example of risk and accountability is the UK’s 2010 PFS pilot project at Peterborough Prison, which has also been touted as the first impact bond in the world (Davies, 2014). Between 2010 and 2015, adult male individuals in Peterborough prison received One Service intervention to reduce recidivism (Davies, 2014). In addition, Community Rehabilitation Company (CRC) provided rehabilitation to the prisoners, while an independent evaluator measured whether an outcome payment should be made to investors (Ganguly, 2014).

The investors paid £5 million to social service organizations to provide 3000 male prisoners (serving less than 12 months) with reentry rehabilitation programming, in hopes they will not reoffend and end up in prison again (Davies, 2014). If they are successful in reducing recidivism by 7.5%, investors will receive their investment back plus a return based on a percentage of the cost if they reoffended, capped at £8 million (Davies, 2014). The Peterborough Prison pilot was completed in 2014 (Davies, 2014). Although preliminary data showed a 12% decrease in recidivism in the first year (Center, 2013), actual numbers were at 8.4% decrease, not meeting the 10% target for an immediate outcome payment to investors (Davies, 2014). However, because the recidivism stayed above 7.5% for the final cohort, the Ministry of Justice made payments to the investors (Disley, 2015).

In a report by Rand Europe to evaluate the SIB at HMP Peterborough, stakeholders saw a number of innovations in the pilot, but that these were not necessarily as a result of SIB funding, stating, “There is no compelling reason to believe that SIB funding on its own fosters innovation” (Sharman, 2016, para 4). The also indicated that the Peterborough pilot led to wider benefits such as improved relationships between local agencies, commissioned providers and
HMP Peterborough, and acknowledges that the Peterborough SIB is effective (Davies, 2014). Peterborough’s rehabilitation program delivered a meaningful improvement in life outcomes for ex-offenders, stating, “A more plausible conclusion is that innovations are fostered in projects and initiatives led by committed partners who are able to look at service delivery with ‘fresh eyes’ and with an outcome-focus, question traditional approaches, and who have freedom to make changes and test new ways of working” (Sharman, 2016, para 6). Such features might be more likely to be present within SIBs – because “SIBs are often established to encourage new approaches to service delivery, and require substantial attention to outcomes due to their payment structure – but these kinds of innovations are not necessarily lacking in other funding and delivery models” (Sharman, 2016, para 8).

The SIB finished early due to the introduction of the Transforming Rehabilitation program, which also worked on a payment-by-results basis, and was the first of its kind (Disley, 2015).

Some of the lessons learned from the HMP Peterborough SIB included:

- Developing a competitive market for delivery agents; involving a new commissioning landscape where government has no direct relationship with the service provider; legal structures of the SIB being transferable to future SIBs; SIBs in new policy areas will always pose new analytic challenges; and financial and reputational risks appear to have been transferred (Disley, 2015, p. 37).

Nick Davies, public services manager at National Council for Voluntary Organizations (NCVO), said: “The evaluation is clear that there is no reason to believe that SIB funding necessarily fosters innovation” (Davies, 2014, p. 1). Davies also expressed concerns over the use of SIBs after November’s Autumn Statement revealed that a further £80m would be spent on them. He said:

The key unanswered question is whether a simpler, alternative funding model would have delivered the same benefits, more cost-effectively. What is known is that SIBs are very complex and expensive to set up. We urgently need more research to ensure that the £80m allocated for SIBs in the spending review isn’t
wasted. SIBs are an interesting idea, but currently the hype is vastly outstripping the evidence of their effectiveness (Davies, 2014, p. 2).

Andrew O’Brien, head of policy and public affairs at Charity Finance Group, said that

We know, for example, that it can take a long time to get going and be very expensive, and we know that there can be difficulties in trying to reconcile the needs of long-term change when it comes to service users, with the needs of private finance – they want to make some return as soon as they can. We know there are these weaknesses...but I think the real damning bit is that there is nothing specific about the SIB model that makes it more innovative than any other funding model, as far as I can tell from reading the report. And given that the government has decided to put £80m into SIBs, it should maybe have a rethink about that and see whether it is better to spread that out via a few different funding mechanisms (Sharman, 2015, para 20)

The HMP Peterborough report also concluded that despite providing additional supports for service users, recruitment of volunteers was often challenging (Sharman, 2016). It said that “future initiatives should be realistic about the challenges associated with the use and recruitment of volunteers, and the timescales required for security vetting” (Sharman, 2016, para 10).

It also revealed that because of SIB funding, the One Service was observed to be more adjustable than other interventions (Sharman, 2016). For example, new ways of engagement were executed throughout the pilot and new providers were assigned (Sharman, 2016). It also found that funding of the service was perceived as variable (Sharman, 2016). It said:

Staff reported that it was quicker and easier than in other interventions to access resources to cover, for example, temporary B&B accommodation, phone credit and other consumables. This flexibility could prevent crisis situations (such as homelessness), and incentivize engagement (Sharman, 2016, para 24).

This report was the third and final report from RAND on the Peterborough SIB (Sharman, 2016). The first report, produced in 2011, looked at initial learning from the planning and early implementation of the report (Disley, 2011). The second, produced in 2014, looked at the pilot's operation over the previous four years (Sharman, 2016).
Mark O’Kelly, head of finance at the Barrow Cadbury Trust, an investor in the Peterborough Prison SIB, provided a foundation’s point of view:

The Trust was attracted to the idea of targeting its investments towards interventions that can improve social outcomes. The alignment of shared goals was important to them, as was the flexibility and rigor that the SIB approach brought to the question of how you keep prisoners from reoffending (Perakis, 2013, para 7).

The Rockefeller Foundation supported Peterborough project and in reviewing the first results they stated the following, “The evaluation reveals that the Peterborough SIB is effective, and Peterborough’s rehabilitation program is delivering a meaningful improvement in life outcomes for ex-offenders” (Ganguly, 2014, para 1).

In addition, the Peterborough SIB taught us that future SIBs face the challenge of trying to share outcome payments across the central and local government departments and agencies that accrue savings (Disley, 2011). In particular, SIBs in areas that currently receive statutory provision (act of parliament) will need to measure outcome metrics which will allow government to keep the effect of SIB funded interventions separate from the non-SIB projects (Disley, 2011). The advantage of the SIB is that “It creates an opportunity for the Ministry of Justice to improve rehabilitation outcomes for offenders without risking its own capital and resources upfront” (Disley, 2011, p.8).

It is difficult to correlate impact measures to monetary returns, and many social interventions simply resist the kind of impact measurement and connection to financial savings demanded by the PFS structure (Rangan & Chase, 2015). The measurement will be challenging for those already struggling to fund services, let alone finance the human and technical resources to support complex tracking systems (Rangan & Chase, 2015).
3.2D Policy

The concept of social impact bonds is so popular in many circles that politicians believe that they can gain appeal when they make SIBs part of their campaign platform (Cohen, 2014). Brookings Institution recently concluded,

While there is still much to learn in designing and implementing social and development impact bonds, early experiences are somewhat promising, in that at the very least, they have gotten bureaucrats, the investors and providers of services to the same table and with aligned interests (Cohen, 2014, p.3).

In its fiscal year 2014 budget, the Obama administration proposed nearly $500 million to fund its Pay for Success program, including $300 million for the US Treasury Department’s Incentives Fund to enable cities, states and nonprofits to support outcome based public-private partnerships (Rangan & Chase, 2015). The administration proposed an additional $195 million to support pay-for-success programming through the US Department of Labor, Justice and Education (Rangan & Chase, 2015). Although only $7.5 million was approved by the US Congress, an additional $70 million was earmarked for a Social Innovation Fund (SIF) through the Corporation for National Community Service, of which 20 percent was budgeted for PFS programs (Rangan & Chase, 2015). From that allocation, by late 2014 the SIF has issued grants totaling $11.2 million (Rangan & Chase, 2015).

Congress supported an ongoing appropriations bill to fund PFS and SIF funding at 2014 levels through the 2015 fiscal year (Rangan & Chase, 2015). At roughly $20 million a year, it is a small but definite endorsement of the concept, however, it is less than the initial $695 million proposed (Rangan & Chase, 2015). The state, county, and city governments have shown noticeably more enthusiasm (Rangan & Chase, 2015). An outbreak of activity in 2014 brought to development a total of seven PFS contracts totaling just over $77 million in the United States, along with another 20 projects in various stages of preparation (Rangan & Chase, 2015). The
majority of contract that have been executed and pending are being constructed by Third Sector Capital Partners or Social Finance US, which act as financial intermediaries, secure financing and oversee the contracts’ social service implementation and evaluation (Rangan & Chase, 2015). When all these projects come to completion, almost $300 million worth of private and philanthropic capital will be in circulation (Rangan & Chase, 2015).

3.2E Lessons Learned

Rangan and Chase believe by using PFS contracts, and philanthropic funding to construct a new impact-driven model for meeting social needs, governments and nonprofits will learn to operate more effectively (Rangan & Chase, 2015).

PFS is an important step toward making governments and nonprofits accountable and more effective in serving society’s neediest citizens, and to the extent that PFS employs private capital to serve this end, the money is well spent. The motivations of social impact investors in PFS projects, and investors’ prioritization of social impact over financial returns, could make the critical difference in how the sector develops (Rangan & Chase, 2015, para 33).

Market capital will have a role to play, but return-seeking investors will participate when the financing structure minimizes their risk, as recent contracts have done (Rangan & Chase, 2015).

The Chairman of Big Society Capital, Ronald Cohen, told Financial Times that “sustainable and ethical investment was not just a trend, but could be a game changer” (Kyriakou, 2014, para 1). He went on to say, “Connecting a social performance – such as reducing the likelihood of youths re-offending and re-entering the prison system – to a financial return, social impact bonds have given social enterprises access to the markets” (Kyriakou, 2014, para 1).

Even though there is discussion of an infrastructure funding gap, Macomber disagrees and states, “The world is not short on capital – a startling $43 trillion of assets is currently under management in the US alone. Investor from hedge funds to insurance companies are operating in an environment of low yields, near-zero interest rates, and a glut of savings” (Macomber, 2016,
para 3). He goes on to say that rather than a funding gap, there is a “bankable projects gap”: the projects themselves are not attractive to investors (Macomber, 2016, para 3). The new financial technology of the SIB will assist in area (Macomber, 2016). Social impact bonds were envisioned to tackle social problems that can be objectively measured, such as recidivism; “making them a great candidate for sustainable development, with reliable and objective data” (Macomber, 2016, para 5).

Per Macomber, investors and entrepreneurs interested in PFS financing would be more interested in questions such as, “on a sliding scale of social impact, what do we get if we were to reduce road congestion by 10%?” (Macomber, 2016, para 6) – providing an example incentive to unite with a shared goal in mind (Macomber, 2016).

The ability to attract pure return-seeking capital may be limited for social impact bonds. However, social impact and PFS securities could unlock substantial foundation, philanthropic, and NGO assets to buffer the risk for return-seeking capital. Corporations might even get involved. PFS is a potentially powerful way to mobilize vast pools of global capital toward multi-sector thinking, working toward a common goal that none of the parties currently seems able to finance. (Macomber, 2016, para 8).

<table>
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<tr>
<th>Benefits</th>
<th>Challenges</th>
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<tbody>
<tr>
<td>-Increase capital available for social interventions via private finance (Davies, 2014). Funds human service programs that may not otherwise obtain funding (Roman, Pay, 2014)</td>
<td>- Investors may be expecting the same rate of return equivalent to the market of equity investments with similar risk (Davies, 2014)</td>
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<td>-Knowledgeable investors bring precision to social services (Davies, 2014). Mechanism for funding regional and state initiatives across jurisdictions (Roman, Pay, 2014)</td>
<td>- Social service needs to provide a measureable outcome, therefore, may be selective in which social activity is chosen (Davies, 2014). In addition, this may limit programs which are evidence based, therefore limiting or discouraging innovation (Roman, Pay, 2014)</td>
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<td>-Private organizations may bring more innovation to the process than public sector (Davies, 2014). Reasonable targets to</td>
<td>-Outcomes are complex and misconstrue the complexities; it can lead to inaccurate conclusions regarding cause and effect</td>
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<tr>
<td>Determine success (Roman, Pay, 2014)</td>
<td>(Davies, 2014). It also requests complex legal, institutional and financial arrangements up front (Roman, Pay, 2014)</td>
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<td>-Government doesn’t have to find capital up front or need to find additional funds to pay the return (if the outcomes are met, the public saves money) (Roman, Pay, 2014)</td>
<td>- Mission driven organizations may find it challenging to enact a business driven model/return on investment to their work due to lack of know-how or values (Davies, 2014)</td>
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<td>-Government’s risk is minimized because it is transferred to private investors (Davies, 2014). Governments transfer risk — it’s a win-win for tax payers (Roman, Pay, 2014)</td>
<td>- Charities may be threatened by social services organizations who receive SIB because it could lead to redistribution of funding to charitable grants (Davies, 2014)</td>
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<td>-Provides a good investment tool for foundations and trusts, who normally see a much lower return (Davies, 2014)</td>
<td>-Providing services with performance-based outcomes, may result inaccurate activity (cream the population for the easier to serve participants in order to meet outcomes) (Davies, 2014)</td>
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<td>-Beneficial when there are limited resources and projects demand large up-front capital (Control, 2013). May increase community-based service infrastructure (Roman, Pay, 2014)</td>
<td>-Many social organizations address local needs and don’t have capacity to scale (Davies, 2014)</td>
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<tr>
<td>-Increases reliance on programs with a track record of success by using evidence to identify programs (Roman, Pay, 2014)</td>
<td>-Financial and investment challenges: lack of knowledge on investors end, concern that SIBs tie up money for long time, there is lack of historical data; may generate lower financial return than traditional investments (Davies, 2014)</td>
</tr>
<tr>
<td>-Allows organizations to collect resources and knowledge (Roman, Pay, 2014)</td>
<td>-Not ideal for every intervention due to the defining nature of the method, along with the measured costs and benefits (Center, 2013)</td>
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<td>-Lack of transparency and regulatory clarity: return on investments are taxed at the full rate, unlike their traditional income investments that are tax-exempt (when funding is given to charitable organizations) (Davies, 2014)</td>
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<td>-Provide difficulty for government appropriations: due to the long-term nature of SIBs, contracts can tie-up future legislatures (Center, 2013)</td>
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### 3.3 Criticism

Although PFS has been met with great hope, there are critics who do not believe in finance
model (McIntyre, 2015). Dr. Schneider is a staunch critic of Pay for Success (McIntyre, 2015). She said,

The lure of Pay for Success is the money. So, in states where market-based education reform has taken hold, Pay for Success is more likely to be heralded as benevolence and the profit motive downplayed-- and it will likely lead to scandal (McIntyre, 2015, para 10).

Some other education advocates agree. Former assistant U.S. education secretary and New York University education historian Diane Ravitch called the initiative an outright “threat,” telling readers of her blog and to “phone lawmakers at once to stop this money-making scheme.” (McIntyre, 2015, para 11).

In 2015, the first set of outcomes in the Utah High Quality Preschool Program in Salt Lake County, Utah was announced (Roman, Pay, 2014). Launched in 2013, the project provides high-quality preschool to low-income three- and four-year-olds (Roman, Pay, 2014). In October, only one of the 110 students targeted for special education and identified as at risk ended up using special education services in kindergarten, causing outcome payments to funders (Roman, Pay, 2014). Some critics have questioned the metrics used to measure the outcome payments, while others focused on lessons learned and the benefits of expanding preschool no matter what the outcomes (Roman, Pay, 2014).

According to Dugger, while educators and evaluators work to improve outcomes for participating kids, they will continue to do so at the expense of the private sector (Dugger, 2015). In fact, he doubts that any type of rigorous evaluation and examination of the results would happen if this were simply a traditional state or federal program (Dugger, 2015).

A central argument of Pay for Success proponents is that they save money by only funding successful programs (Saltman, 2016). However, as the prior sections suggest, if in fact evaluation is not independent and only already successful programs are being selected, and
governments have incentives to continue contracting, then industry development through competition cannot work (Saltman, 2016). Yet, there is additional evidence that Pay for Success adds costs rather than cutting them (Saltman, 2016).

However, some critics have concerns with the two main claims for SIBs: more resources and better results, stating, “They are admirable but speculative” (Pratt, 2013, para 3). The first claim, that SIBs will deliver new resources, is based on the idea that legislative bodies will assume additional funds based on a projection of future savings (Pratt, 2013). If an organization’s services reduce repeat trips to prison, saving the government money, the organization and its financiers deserve to be rewarded with extra payments from that money made available through reduced expenditures in housing these prisoners (Pratt, 2013).

“If your organization’s services reduce repeat trips to prison, saving the government money, your organization and its financiers deserve to be rewarded with extra payments from that money made available through reduced expenditures in housing these prisoners” (Pratt, 2013, para 4). There will be new sets of organizations who are awarded funding with SIB contracts, leading compelling arguments as a comparative edge in the competition for resources (Pratt, 2013). Pratt asks,

Will SIB-financed services produce improved outcomes through the enhanced discipline that’s derived from their participation in the SIB process, with its mandate to pay only for results? It’s an aspiration, to be sure, but there is no evidence to back it up. This high-stakes carrot-and-stick approach is not unlike the expectations inherent to the “No Child Left Behind” education legislation, which had its own heavyweight marketing promotion before dismal unintended consequences set in, including cheating scandals by pressured school administrators throughout the United States (Pratt, 2013, para 6).

Pratt discusses Campbell’s Law (after Donald T. Campbell):

The more any quantitative social indicator is used for social decision-making, the more subject it will be to corruption pressures and the more apt it will be to distort and corrupt the social processes it is intended to monitor (Pratt, 2013, para 12).
In addition, Savedoff states “critics charged that this financial model overstates the program’s success and the payoff to investors” (Savedoff, 2015, para 4). Savedoff goes on to question this stage as it is not whether the impact bond’s success is being overstated, but whether the measure is acceptable to track progress and calculate payments (Savedoff, 2015).

Utah’s experience provides an opportunity to recognize how much we know about choosing the right indicators for SIBs and other payment by results programs (Savedoff, 2015). It also shows the importance of explaining to decision makers and the public why an indicator is the right one and how much risk is associated with the model (Savedoff, 2015). In addition, all parties need to understand what the true objectives of the program are, including: decreasing costs associated with decreased demand and increased outcome improvements (Savedoff, 2015). Utah’s PFS preschool program paid out $260,000 based on the number of students who avoided special education each year through sixth grade (Metrics, 2015). Utah saved $281,000, therefore investors in the program received 95 percent of those savings (Metrics, 2015). However, there were some suggestions of irregularities in how the Utah program’s success was measured (Savedoff, 2015).

Ellen S. Peisner-Feinberg, a senior scientist at University of North Carolina stated,

> To assume that all these children would have gone to special education is kind of ridiculous. The lesson is that before a PFS program is considered again, investors and schools need to find better ways to measure their outcomes. You have to be sure very rigorous ways of measuring the impact to make sure it’s legitimate in terms of the outcomes you get. That didn’t happen here. (Metrics, 2015, para 4).

Further, Liner discussed legitimate concerns about SIBs and other PFS models. “Although they are designed to generate new savings for the government and taxpayers, they also incur new costs and require robust oversight” (Liner, 2016, para 5). The following are a few examples from
Liner of the downsides of SIBs—or arguments against them:

1. **Transaction costs**: “SIBs have higher transaction costs than standard programs because of the number of additional parties involved, such as investors and program evaluators. Economists consider these costs to be wasteful since they would not be incurred under alternative arrangements” (Liner, 2016, para 5).

2. **Accuracy of projections**: “The projected government savings are estimates, which even if a program is deemed successful, will take time to break even. In the end it may not deliver all of the intended financial benefits” (Liner, 2016, para 5).

3. **Acting in good faith**: Since impact targets are projected, it could be gamed so that the payout is easier to make. It is thus, critical for the state or local government to hire an independent program evaluator to make sure a true outcome is achieved (Liner, 2016).

4. **Profit motivation**: Some critics argue that SIBs introduce profit into areas where there shouldn’t be any (Liner, 2016). “They believe that reducing recidivism or helping special needs children should be the work of government and charity and not expected to turn a profit. Many public sector expenditures exist in the public sector precisely because it is impossible to assess their return on investment monetarily; yet, they are still believed to generate positive social returns” (Liner, 2016, para 5).

5. **Service quality**: Because SIBs prioritize the delivery of certain metrics over general activity in order to get paid, “nonprofits may over-focus on one aspect, rather than overall service quality. Furthermore, outcomes may be influenced by factors outside the service provider’s control, such as the home environment of the individuals being served” (Liner, 2016, para 5).
The early termination of the New York City, Rikers Island, PFS in July 2015, after failing to meet its recidivism goals, and Goldman Sachs resulting $1.2 million loss in outcome payments, illustrate why return-seeking investors are unlikely to invest in PFS projects without the cushion of philanthropic risk absorption (Rangan & Chase, 2015). Bloomberg Philanthropies is taking the biggest loss, after all, paying out $6 million to Goldman Sachs’ without receiving any success payments from the city (Rangan & Chase, 2015). It also provides valuable lessons for governments about how to vet service providers for PFS contracting (Rangan & Chase, 2015).

Similar to the Peterborough project, the New York City government will hopefully apply the lessons learned from its PFS project to structure its own recidivism programs (Rangan & Chase, 2015). However, NFF states, “even though Rikers did not meet the metric, doesn’t mean they didn’t show success. It’s an important nuance. It’s important to share these lessons learned with the field” (Interviewee 5).

Considering the fundamental role philanthropic and mission-led investors are playing in PFS and SIB projects around the globe, the future of PFS lies in aligning with impact-seeking investors, not return-seeking investors (Rangan & Chase, 2015). Despite early projections for PFS and SIB instruments to enlist private capital to solve social ills, we are encouraged by its potential to stimulate more foundation investments in the sector, potentially sideling profit-seeking investors (Rangan & Chase, 2015). US foundations, with assets of nearly $700 billion and average annual grantmaking of $40 billion in the past 10 years, have long been criticized for their relatively low levels of program-related investments, only about $500 million a year on average (Rangan & Chase, 2015). Among the country’s largest private foundations, impact-related investing constitutes only about 2 percent of endowment spending and roughly one-half of 1 percent of grant spending (Rangan & Chase, 2015). The emergence of foundations as
leading players in recently launched contracts is indeed encouraging, and we see this—not the engagement of private market capital—as the potential major funding source for the PFS model (Rangan & Chase, 2015). This development, along with improved efficiency and effectiveness of both government and nonprofit social welfare provisioning, will be the real and measurable benefit of the PFS model for society’s neediest citizens (Rangan & Chase, 2015).

### 3.4 The Future of Pay-for-Success

All of the new PFS contracts being negotiated from Connecticut to California will require service providers to demonstrate rigorous data collection and impact reporting (Rangan & Chase, 2015). These projects targeting juvenile and adult incarceration, homelessness, health care access, education, and other social challenges not only will raise the bar for nonprofits to demonstrate robust indicators of their outcomes but also, we believe, will fundamentally change the way governments procure and deliver social services (Rangan & Chase, 2015).

In 2013, New York State budget authorized the state to undertake PFS initiatives in health care, child welfare, early childhood development and public safety (Governor, 2014). Responsibility for this initiative was given to the NYS Division of the Budget (DOB), which issued a PFS request for proposal in August 2013 (Governor, 2014). The 2014-2015 budgets allocated $53 million for the PFS initiative (Governor, 2016).

At this same time, NYS launched a $13.5 million PFS project to increase employment and reduce recidivism in Rochester and New York City (Governor, 2016).

In a press release announcement, Governor Cuomo said,

> New York State’s leadership in Pay for Success is another example of our focus on innovation and performance in making government work for the people of the state. This public-private partnership model is one we see working over and over again and one that saves taxpayers money and improves how we deliver services here in New York (Governor, 2014, para 2).
According to RAND Corp:

Conventional finance markets do not price social value creation; and consequently, there is a lack of comparable performance information (metrics) to support the creation of a new or modified social investment marketplace (Disley, 2011, p. 27)

According to Urban Institute, there are steps to PFS, including: Strategic Planning: drivers of criminal justice system populations and costs, gaps in infrastructure, evidence of intervention, PFS suitability diagnostic; Developing the PFS transaction and infrastructure: identify the population to be served, costs, expected benefits, recoverable benefits, price and performance target; Delivering service and evaluate success: service provision and training and technical assistance and evaluation (Roman, Why, 2014).

Part of the problem is that each pay for success project is unique (Roman, Why, 2014). That means that project designs aren’t easily transferrable from one government body to another (Roman, Why, 2014). “So each project requires a nonprofit to surrender their best talent for great lengths of time” (Roman, Why, 2014, para. 5). There are many other things unknown such as: outcomes, replication (scalability), sustainability, and investor buy-in (Roman, Why, 2014).
4. Methodology

In September, 2014, New York State approved a PFS mechanism for funding a program to assist juvenile delinquents from reoffending (Governor, 2014). The funds would be used to provide youth in NYS juvenile justice system with an alternative to placement that helps create pathways to success in home, school, and community (James-Wilson, 2013). The program was called Hillside Intensive Community Asset Program (ICAP), and would serve youth in 10 counties of upstate New York with intensive care management, specialized services, and connection to neighborhood-based natural supports and community-based resources in order to reduce the number of days spent in placement or jail, thus minimizing the negative long-term impact of incarceration on employment, education and health (James-Wilson, 2013).

4.1 Primary Research Questions

The research framework allowed me to answer the research questions below, will drive secondary questions.

1. What were the strengths and weaknesses of the SIB/PFS contractual model as complemented?
2. What is making the SIB attractive to the investor?
3. To what extent-how and why-do stakeholders feel that the SIB will lead to greater innovation and/or efficiency?

4.2 Data Collection & Analysis Techniques

The research conducted took place over a period of four months. A single-case study research design method, with two comparison cases derived from the literature, was used to explore the research question based on findings from interviews with individuals from the organization involved in the development of the PFS project, ICAP. Interviews were conducted
via phone call or face-to-face, asking both open-ended and closed-ended, semi-structured questions to key players involved in the case study (see Interview Questions in Appendix A). The interview questions were modeled after the RAND report, “Lessons learned from the planning and early implementation of the Social Impact Bond at HMP Peterborough” (Disley, 2011). The general semi-flexible interview guide was used to ensure that the same general areas of information were collected from each interviewee. Set of questions and topics were categorized by defining outcomes, impact, return on investment, policy implications, risk and accountability. Interviews included: Third Sector Capital Partners, Hillside’s CFO, Hillside’s Children’s Center Executive Director, Hillside ICAP Program Manager (Table 2). These interviews were conducted in May 2016 through July 2016 (the interview consent form is included in Appendix B). Some topics/questions were explored more in-depth with some interviewees than with others, according to their role in the development of the PFS program/contract. However, interviewees were encouraged to raise and respond to a range of issues, including those outside their particular role in the development of ICAP. The focus of the research was on experiences and views of a sample of those involved in ICAP.

When the thesis proposal was written, ICAP was still in its infancy stage, with deployment in May, 2015, and would not have available measures for two to three years. However, in August, 2016 the project was still not launched, and shortly following they learned New York State decided to not move forward with the ICAP project. As a result, there was not great detail surrounding the contracting and implementation phase, nor include the perspective of service users. As such, the limitations involved in moving forward were discussed in great detail. In addition, other potential stakeholders were not interviewed due to their lack of involvement in the contract phase, however, may have provided a different perspective.
Table 2: Interview Schedule

<table>
<thead>
<tr>
<th>Interview #</th>
<th>Organization*</th>
<th>Role</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Hillside Family of Agencies; ICAP</td>
<td>Chief Financial Officer; Board member for the corporate Hillside ICAP (assisting in contracting and subcontracting process)</td>
</tr>
<tr>
<td>2</td>
<td>Hillside Children’s Center</td>
<td>Executive Director, Central NY region (led the initial discussions with the counties and project proposal to the state)</td>
</tr>
<tr>
<td>3</td>
<td>Hillside ICAP</td>
<td>Program Director hired to run the ICAP project (coordinated all the players, including: state bodies, counties, intermediary, independent evaluator, and potential investors)</td>
</tr>
<tr>
<td>4</td>
<td>Third Sector Capital Partners, Inc.</td>
<td>Intermediary (provided financial advisory services, including deal construction, economic modeling, fundraising, and assistance in negotiations with the state)</td>
</tr>
<tr>
<td>5</td>
<td>Nonprofit Finance Fund (NFF)</td>
<td>Provided funding for the soft start/ramping up phase of the project</td>
</tr>
</tbody>
</table>

*Contacts changed and evolved over the course of the research.

The interviewees participated in the development of ICAP, and provided their unique experience, and partiality of their involvement. The interviews were audiotaped and fully transcribed. The analysis began with the themes from the key research questions, while looking for issues, ideas, success and concerns raised by the interviewees.

Across the stakeholder groups there was a considerable degree of consensus, both in the accounts of how the SIB was developed and risks and benefits of the PFS.

The findings from the ICAP case study interviews were then compared to existing data on a program in Massachusetts, whose initiative is also to reduce recidivism among at-risk youth (Third, 2014), and the Rikers program in New York City that tried to reduce recidivism among formerly incarcerated individuals and increase workforce readiness (MDRC, 2015). Secondary
research was used in the MA and NYC projects. Views of key individuals were gathered and independently reported, drawing out where possible potential lessons.

Further, the research for this paper relies heavily on previous work of others who have studied this field. There is considerable literature on how the PFS model works, however, very little on the effectiveness of the finance initiative, which is defined in this paper as government paying back the private investors (with or without interest). The collected data, including interviews, document/literature review, reports, including other case studies, was analyzed for patterns and trends and incorporated into this final document. The method used to analyze the data collection was completed through preliminary themes such as: barriers/problems, benefits and impacts.

Due to the time constraints, the case study was limited to the implementation process and negotiations with the service agency, and their experiences with the intermediary, state agency and investors.

Based on existing literature, the qualitative aspect of this method lent itself to finding out how the PFS model has been working since its inception in the US. The case study method helps us understand complex issues and can strengthen what we already know about the existing research/data within a real-life context (Yin, 2014). Qualitative research, in general, is used to explore and understand social and public policy issues (Huberman and Miles, 2002), which is a perfect design method for exploring the proposed problem.

Using the single-case study design, the research findings did not provide for the basis for PFS effectiveness, however, it could still assist policy, investors and social service agencies in understanding this new technique. Although this is a relatively new financing mechanism, there currently are some case studies provided by Social Finance, intermediary for social impact bonds
(Social Finance, 2014), which delve into engagement with PFS. In addition, it helps find the gap between the different participating actors in the PFS process.
5. Findings

5.1 ICAP Overview

The Hillside Children’s Center’s ICAP creates compelling alternatives for Family Court judges and Probation officers who seek ways to avoid the placement of youth into high-cost and developmentally damaging institutional settings (James-Wilson, 2013).

In March 2014, Governor Cuomo announced finalists to NYS DOB’s Pay for Success (PFS) request for proposal (RFP), and indicated that the State would enter into negotiations to launch Pay for Success projects with finalists, including Hillside’s ICAP (Governor, 2014). ICAP was selected from among a number of policy areas under consideration by NYS, including education, children and family in the home, and healthcare (Governor, 2014). “Even though they [the State] didn’t understand what it [PFS] was all about, this RFP came on the heels of Bloomberg’s work/support for PFS program he was doing on Rikers Island”, which was the first deployed social impact bond in the states (Interviewee 1).

While the state was conducting interviews and research, Hillside was able to contribute due to their experience with public private partnerships with New York State, giving Hillside credibility (Interviewee 1). Third Sector, the intermediary, vetted three different Hillside programs (Interviewee 1). ICAP was chosen because they had poor outcomes, which could be improved, and there was clearly potential savings from improving those outcomes (Interviewee 1).

Hillside’s ICAP in collaboration with stakeholders would finally settle on serving approximately 800 youth in 10 upstate counties over a five year period (Interviewee 2). In reaching the 800 youth to be served, specific geographic counties would help facilitate in the
delivery of the interventions over a sustained period and tracking the outcomes of those interventions (Interviewee 2). Hillside developed collaborative efforts for ICAP implementation in Albany, Broome, Cayuga, Erie, Herkimer, Monroe, Oneida, Onondaga, Rensselaer and Schenectady counties (Interviewee 2). ICAP hoped to launch a “soft start” in summer 2016 in all participating counties in which a sample of ICAP eligible youth would be served (Interviewee 2). This pilot would ensure that the design was solid and that all program components were functional (Interviewee 2). Any necessary model adjustments would be made prior to the fall 2016 formal full program launch (Interviewee 4).

The soft start was a lessons learned from Massachusetts. We launched Massachusetts and the first batch of referrals that we got was 20% of what the SIB lab had modeled would be there. So, alarm bells went off. We can't do a project with 20% of the kids we thought were there. And at the time Roca hired staff for 100 kids; they would have to lay off staff (Interviewee 4).

5.1A ICAP Project Partners

When the New York State Department of Budget’s Pay for Success RFP was announced, Hillside participated in an informational call hosted by the Alliance for Children and Families in which Third Sector described the PFS opportunity (Interviewee 1). The RFP was for the state’s first Pay for Success (PFS) projects in the areas of health care, child welfare, early childhood development, and public safety (Governor, 2014). The Hillside representative on the call was one of the few participants who understood this model (Interviewee 4). Third Sector learned that Hillside had a proven track record developing and delivering new programs, and, most importantly, possessed expertise in tracking data and monitoring programs for consistent quality (Interviewee 4).

Once NYS awarded Hillside ICAP as a successful bidder of PFS, Third Sector was hired as the project intermediary to provide financial advisory services to the project, including deal
construction, economic modeling, fundraising, and assistance in negotiations with the State (Interviewee 1). Other contractors such as an auditor and fiscal agent would have also been utilized as needed by the intermediary organization (Interviewee 1).

Governance of ICAP would be accomplished via an Oversight Committee comprised of representatives from Government, Hillside, Third Sector and funders (Interviewee 1). Decisions were made in a consensus model, with access to external dispute resolution services if ever required (Interviewee 1).

The creation of a dedicated special purpose project intermediary entity that exists outside of Government was an important requirement among lenders who were concerned about the security of PFS funds and all other parties who will seek the protection of a limited liability corporate structure (Interviewee 1). Hillside created an ICAP subsidiary 501(c)3, nonprofit corporation for financial transactions associated with the project so it could accept the loans and grants from funders (Interviewee 1). It paid HCC and Third Sector for the respective work, and served as the contractor within the state to execute the ultimate pay for performance - formal project intermediary (Interviewee1).

**Third Sector Capital Partners, Inc.** Third Sector Capital Partners, Inc. (Third Sector) is a nonprofit advisory firm whose mission is to “accelerate America’s transition to a performance-driven social sector” (Third, C, 2014, para 2). Founded in 2011, Third Sector has established itself as a leading practitioner of Pay for Success (PFS) in the United States (Third, C, 2014). Third Sector works with governments, social service providers, funders, and other stakeholders to develop and launch PFS projects that improve the lives of people most in need by driving government resources toward proven and effective programs (Third, C, 2014). Part of Third Sector’s mission is to change the way the government works (Third, C, 2014).
Specifically, to make the social sector more outcomes focused. To accelerate America's transition to a more outcomes focused social sector. We think the way to do that is primarily with government, as opposed to with philanthropy, because government spending is more than the available philanthropy. We're working with government to change the way that they contract, since more government spending happens through their procurements. The benefit to us of doing a Pay for Success project is that it is an actual change in the way the government works. It's not a report that somebody issues that says, "Hey you should do outcomes based contracting." It's not a test; it's not something that's small and intangible. It is an actual payment for outcomes by a government.

We think that the more we can get governments to do these types of projects, the more usual it becomes and we will have effectively moved government from paying for inputs and outputs, which is extremely inefficient. If we can do that we think that's our value added, so that's our benefit (Interviewee 4).

Third Sector constructed and manages the Commonwealth of Massachusetts’s $28 million Juvenile Justice Pay for Success Initiative, the largest financial investment in a PFS contract in the country (Third, B, 2014). Third Sector also helped launch the nation’s first county-level PFS project in Cuyahoga County, OH (Cleveland) and California’s first PFS project in Santa Clara County (Third, C, 2014). Third Sector has received a three-year, $1.9 million grant award as part of the Social Innovation Fund’s (SIF) inaugural PFS grant program (Third, C, 2014). The goal of Third Sector’s SIF Award was to accelerate the development of PFS projects across multiple levels of government nationwide and to share lessons learned with a broad community of stakeholders to increase adoption of evidence-based policymaking (Third, C, 2014).

In terms of Third Sectors involvement with Hillside ICAP,

Our work really happens before the contract is signed. Once the project launches, we are just an advisor. We believe it’s really important for Third Sector to have the seat at the table for the management of the projects. But we will not be the quote, unquote “intermediary” once the project launches. That will be held by ICAP. They are both the program delivery here, but also the financial intermediary. They'll take out the loans and for any grants necessary. They'll also manage the project day-to-day once it's launched (Interviewee 4).
**Hillside ICAP:** Hillside was impressed that Third Sector was already leading the development of PFS programs in other states (Interviewee 1). Collaborating with Third Sector, Hillside developed a response to the RFP that involved a new service delivery model (Interviewee 1). Hillside felt they could use their experience in service delivery, supported through a Pay for Success agreement structured by Third Sector, to fill an unmet need in juvenile justice (Interviewee 1). They responded to the RFP at the end of 2013, and in January of 2014, New York State Governor Andrew Cuomo made an announcement in his State of the State address that $100 million would be allocated to support these PFS initiatives (Interviewee 1).

When the status of successful awardee came through, Hillside ICAP hired a Project Director to work with all parties to oversee the operation and governance for the project, including delivery of data to the independent evaluator, managing investor relations, coordinating delivery of service and PFS payments, and any necessary remediation based on ongoing project performance monitoring (Interviewee 1). “We want to have social programs we know work, instead of funding things for inputs, or funding for outputs. The work Third Sector is to move social sector towards funding for outcomes” (Interviewee 4).

**Urban Institute:** Hillside ICAP appointed an independent evaluator, Urban Institute to undertake data analysis in order to determine whether offenders who receive interventions as an alternative to prison are less likely to reoffend than those who do not have access to PFS SIB-funded intervention (Interviewee 2). Although there was not much discussion regarding the vetting process or credentials in selection of Urban Institute from the interviewees, it was undoubtedly one of the most important partners in the PFS process. Urban Institute are self-described as:

An indispensable resource for nearly 50 years because of our intellectual integrity. We are unrivaled in the breadth and depth of our expertise, the thoughtful analysis
we generate, and the cutting-edge tools we develop. We are unique in our ability to simultaneously deliver the objectivity and rigor of academic research with the timeliness and accessibility necessary to inform current debates and imminent decisions.

Today, more than ever, America needs an independent, authoritative source of evidence and insight to ensure that important decisions are rooted in reliable information. Urban is that trusted source for many stakeholders, including the following: philanthropists, national lawmakers, state governments, nonprofits, community foundations, journalists, and individuals and families (How, 2018, para 1,2).

If participants of ICAP are convicted less than offenders in the comparison group, then PFS will have benefits for NYS and wider society in the form of improved outcomes for the offenders and for their communities, which experience less crime. In addition, there would be benefits to the government, by saving money through reduced costs of policing, court cases, and prison placements and so on. If the independent evaluator calculates that reoffending is reduced by 30%, compared with a matched comparison group, New York State will pay back the investors for this improved outcome. In translating research to practice, Urban states,

Our experts translate the facts for diverse audiences; apply them to real-world problems to find solutions, and share them in accessible ways with policymakers at every level, as well as with business and philanthropic leaders, advocates, and practitioners. Our work improves their critical decisions and therefore has a direct impact on families and communities around the country (Urban, How, 2018).

Urban Institute also works with Third Sector and Roca in implementing a statistical evaluation of the Massachusetts Juvenile Justice Pay for Success Initiative.

**Harvard SIB Lab:** The Harvard Kennedy School Government Performance Lab, grown out of the Social Impact Bond Technical Assistance Lab (SIB Lab), “conducts research on how governments can improve the results they achieve for their citizens. An important part of our research model involves providing pro bono technical assistance to state and local governments” (The, 2018, para. 1). Through engagement of students and graduates in the PFS process, the Lab
gains insights into the barriers that governments face and the solutions that can overcome these barriers.

The Lab placed a full time government innovation fellow at NYS offices to provide technical assistance for ICAP. The School received a grant to offer ten consulting opportunities to various governmental entities to assist in setting up the PFS program. One interviewee discussed the quantifying social outcomes became difficult when working government and academic agencies.

They were way too academic, and couldn’t bring their thinking in line with real life. For example, the fellow would raise theoretical problems at every step of the process instead of being accepting of learnings from other PFS projects. Because the Lab was a valued partner to the State, the State would side with the fellow. This became a real detriment to the project, and eventually the fellow moved on to another consulting gig (Interviewee 1).

A differing point of view from Third Sector, “I think because we had the SIB Lab fellow, who had worked on the previous contract, there were some quick answers that she was able to give and bring people up to speed on the team” (Interviewee 4). This wasn’t the first time Third Sector worked with the Harvard SIB Lab. The SIB Lab also assisted Massachusetts in developing the procurement and designing the data analysis strategy for Roca.

**Nonprofit Finance Fund (NFF):** Hillside received funding from Nonprofit Finance Fund (NFF) under a program of the Social Innovation Fund to support project development and participate in a knowledge sharing network of initiatives pursuing PFS projects (Pay, 2016). Although NFF was not officially a part of the ICAP PFS model, they provided $250,000 for the ramp up of the three month soft start (Interviewee 1). In addition, as ICAP PFS was never deployed, NFF provided insight to the investor perspective of PFS for the purpose of this case study.
We scale solutions to social challenges, working with many to provide capital, coordinate resources, explore funding alternatives, and remove obstacles between nonprofits and their missions (About, 2016, para 10).

5.1B Structure & Timeline

Since April 2014, Hillside and its intermediary partner, Third Sector Capital Partners, have worked with key stakeholders within Office of Children and Family Services (OCFS), Department of Budget (DOB), Division of Criminal Justice Services (DCJS), and other State agencies on ICAP deal construction (James-Wilson, 2013). Hillside also has formally involved county level juvenile justice content experts in the design of ICAP via an Advisory Council (James-Wilson, 2013). These ongoing conversations focused on:

- The target population of juvenile justice-involved youth for ICAP;
- The number of counties that might need to be involved to reach the proposed number of youth during a 5-year service delivery period – and the point in the juvenile justice process where referrals will be made;
- The outcome measures that will trigger PFS payments to investors;
- The data necessary for developing the evaluation and the cost model (James-Wilson, 2013)

The design of this program was driven by Hillside’s dynamic, cooperative relationships with key county-level probation officials and grassroots nonprofit leaders (James-Wilson, 2013). These partners were uniquely positioned to provide key information and preliminary data about underserved target groups and unmet needs, along with pragmatic insights into optimal operational procedures and priority outcome measures (James-Wilson, 2013). Their involvement was critical for constructing a program that would fill existing service gaps and would be a good candidate for PFS funding (James-Wilson, 2013).
The interviewees felt the state envisioned a model where the role of the intermediary was pretty broad. The state learned early on that Third Sector brought a lot of expertise in terms of fiscal management and constructing government contracts. However, per a few interviewees, Third Sector’s expertise was not in service contracts or managing accounts payable. Hillside felt they were better at it, in addition, it added unnecessary costs to the project. The funders liked the setup between the Hillside ICAP and Third Sector because it was efficient. “[Funders] want any incentive money to go to them not just go into overhead” (Interviewee 1).

Developing the ICAP PFS model took approximately 2.5 years from the point at which Third Sector initially discussed the concept with Hillside, to its no-go status in August 2016. Once awarded, Hillside started the process of developing ICAP into a viable program. The state set up a committee of about 50 people representing all the relevant agencies inside the state.
Following, the target group was selected and the number of ICAP sites began to be identified. From the time the proposal was submitted until the project ended prematurely, the number of sites and youth to be served were increasing due to the need for a sufficient number of juvenile delinquents (JD), and to recruit a sufficiently large cohort of JD’s in order to detect a statistically significant change, within a reasonable period of time. The more youth being served meant the more funding would be needed from investors to deliver the intervention, so there was deliberation of the need to keep the upfront funding attainable. ICAPs cohort of 800 would be a large enough sample to detect a statistically significant reduction in recidivism of 30% over 5 years.

**Table 3: Timeline**

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>September 2013</td>
<td>Third Sector vetted Hillside and narrowed down to two projects</td>
</tr>
<tr>
<td>December 2013</td>
<td>Hillside, in partnership with Third Sector, submitted responses to the NYS request for proposal on PFS</td>
</tr>
<tr>
<td>January 2014</td>
<td>NYS names Hillside ICAP project and Third Sector as the successful bidder in the procurement for intermediary and service provider</td>
</tr>
<tr>
<td>February 2014</td>
<td>Third Sector develops a preliminary information document for prospective funders</td>
</tr>
<tr>
<td>May 2014</td>
<td>Hillside met with NYS Governor’s office. They wanted Hillside to start working with Third Sector and State offices (OCFS, DCJS, DOB) to plan project together</td>
</tr>
<tr>
<td>Summer 2014</td>
<td>Hillside and Third Sector worked with State parties and partners to develop the evaluation, line of financing and budget 3x/ week</td>
</tr>
<tr>
<td>Summer 2014 -</td>
<td>Trying to find supporting data – figure out the counterfactual</td>
</tr>
<tr>
<td>Fall 2014</td>
<td>ICAP Project Director hired to assist in design of program, evaluation, and investor meetings. At this same time, Hillside found out state requested a randomized control group</td>
</tr>
<tr>
<td>Fall 2014 –</td>
<td>Developed collaboration with 10 counties, Office of Children and Family Services (OCFS), and Office of Probation in each county</td>
</tr>
<tr>
<td>Summer 2015</td>
<td></td>
</tr>
<tr>
<td>Spring (May)</td>
<td>Hillside worked on payment metrics with Third Sector and how it</td>
</tr>
</tbody>
</table>
would be calculated. Hit a lot of road blocks in finding data sets to predict placement

Summer 2015  Hiatus with state, as they were working on other projects and stopped actively working with Hillside

Fall 2015  State reengages; finally state approved bringing on board an external/ independent evaluator;

Late March 2016  External evaluator, Urban Institute, hired to conduct data analysis and determine if project is viable

Summer 2016  Soft Start anticipated start date

August 2016  Soft Start and full program launch stopped

Fall 2016  Full program launch anticipated start date

5.2 Contractual Process

In a traditional government-service provider contract, government would procure contractors through a competitive process. In a PFS model, the service agency provides proof of concept. As such, there were many contract issues and challenges.

5.2A Contractual Complexity

There would be four key contractual relationships with an additional 10 subcontracts:

Hillside ICAP and New York State; Hillside ICAP and the intermediary, Third Sector Capital Partners; Hillside ICAP and private funders; Hillside ICAP and service providers; and Hillside ICAP and the counties (Albany, Broome, Cayuga, Erie, Herkimer, Monroe, Oneida, Onondaga, Rensselaer and Schenectady) (Interviewee 1).

The bulk of the work is really in the contracting phase when we’re doing modeling, and showing folks what different trade-offs mean for different parties…we’re documenting data models, so we create possible projects with different characteristics, and present those to different parties, and facilitate negotiation (Interviewee 4).
It is recommended that the negotiation between the state and Hillside ICAP, and funders and Hillside ICAP should happen at the same time because funders and the state may have different perspectives on the initiative and it’s self-overlap (Interviewee 4).

**Independent Evaluator:** Many felt the PFS model proved the value of services to government with respect to feasibility and suitability; saving money based on the success of the project. Even though it took a bit of convincing to the state, once Urban Institute was connected with the project, ICAP made advances with success metrics of the project (Interviewee 1). “It was crucial an independent evaluator was at the table” (Interviewee 1). The state thought they could have done the evaluation through their research office; especially when it became clear that the evaluator would add to the budget costs (Interviewee 2).

The state thought that the Office of Children and Family Services could complete the evaluation.

We learned that the office [OCFS] is extremely good at what they do but they are not as good at stepping back and developing an evaluation design. More importantly, they are not an independent evaluator. They have a stake in the game... This would have been a conflict of interest, as the state only wanted to pay if ICAP had a high success rate. The investors, on the other hand, wanted to see success so they get paid, they didn’t want to see false negatives. The state did finally agree to [an independent evaluator] late summer (Interviewee 2).

But as another interviewee mentioned:

…the good news is since we have had Urban Institute connected with the project, we have made lots more advances with success metrics of the project than if were without them at the table. The state of course thinks they can do it all by themselves. They [state] have neither the time or expertise, and certainly not the credibility to play that role. Plus, the funders don’t want the payer having the right to say they didn’t succeed if it’s going to be a close call. They [state] have acceded to that now, and I think they see things are running better with an independent evaluator at the table…someone to make the judgment calls quickly (Interviewee 1).
The independent evaluator was fundamental to this model to function properly, and Urban Institute was chosen as ICAPs credible evaluation resource.

Expansion: The state preferred ICAP having a randomized control group, which slowed down the development of the project. Instead of 500 youth, ICAP would need about 800-900 kids identified to be a viable project, and thus, had to expand the number to 10 counties. Although expansion from the original proposed three regions into 10 counties was less insurmountable than the other listed challenges, it was identified as a challenge. ICAP would need five subcontractors for full implementation. ICAP would need five subcontractors for full implementation. However, because of the organizations grass roots infrastructure there was worry about the ability to reach the required outcomes.

With the counties, Office of Probation and Social Services, the project needed to be consistent across the state to prove a strong evaluation design and for investor buy-in. However, this is a problem, as each county needs to have some difference because the JJ department works a little different in each county. ICAP worked with each county to make those design distinctions and developed memorandums of agreement. As such, the neighborhood centers were aligned with the project, as they played an integral part of the design for natural supports and services in their community. Since the contract never came to fruition, one interviewee stated, “if we had it to do over in a perfect world –we would recommend using a model that has already had a proven track record.” At the end of the day, the real issue is if the population is big enough given all the external changes going on like raise the age.

Predicting and Measuring Impact: One of the challenges in launching this PFS project across New York State has been the complexity and diversity of the involved counties. Traditionally, each county’s social service and probation departments oversee different aspects
of the juvenile justice system, including separate funding streams and databases. Therefore, they found that court procedures, service offerings, and tracking of data vary from one county to the next (different data sources didn’t talk to each other). While state agencies work to coordinate and combine data, there are limitations around what data points are collected and variations in the data consistency and availability at different levels and in different regions (Nonprofit, Pay, 2016). When asked if there can be any improvements made in working with government on Pay for Success, Interviewee 4 responded, “In New York, we have some folks that really care about this issue [juvenile justice]. They're working really hard to do these data pulls for us on top of their normal stuff. I don't want to bash it [state] open too much for being risk averse…” (Interviewee 4).

With the lack of reliable and historic data, the predictor of three days in detention was impacted. Therefore, ICAP was unable to find the counterfactual, and the state did not want to pay if the indicator was not in place and confirmed to have had an impact. “We do have really tough data systems in New York. A lot of silo data that takes a long time to match. Even when it does match, it doesn't tell us everything we need to know. It only gets us to some sort of proxy information” (Interviewee 4).

Along those lines, another major challenge was matching the county-identified target youth and the program eligibility criteria to the data housed within state and county systems. All the stakeholders at the state and local level share the same big picture goal, which is to measurably improve the lives of these youth. However, the details of how each stakeholder identifies who these youth are and tracks their needs can be substantially different. For example, from the beginning, Hillside’s partners in county probation departments have a clear idea of who their target youth are based on daily experiences and observations, though the individual nature and
extent of the needs of these youth are often not well-captured or reported. Similarly, the state partners have had clear and striking evidence of the extended and costly involvement of these youth in placement institutions, further supporting the need for ICAP. Some felt the reliance on the counties to execute the project was the weakest part of the design.

One of the alternatives ICAP discussed was to “dump the whole state system all together, and work out a data collection program through the counties and manage it themselves, which would be expensive, but probably a lot more efficient than anything being done by the state” (Interviewee 1).

**Standardizing Data:** As the external evaluator was not brought onboard early in the process, it proved to be a resource and time-intensive effort to synchronize operational evaluation requirements across 10 distinct counties. Standardizing and streamlining the way in which youth are identified required a deep understanding of each county and each department’s electronic databases or paper systems and their respective data reporting protocols, as well as the norms of how each local court system handles and processes these cases. Reaching consensus among all stakeholders and partners around how to structure the collection, tracking, and sharing of critical data, and refining elements such as eligibility criteria and process indicators, required clear and transparent communication and creative, solutions-focused work.

Data sharing is bigger than one agreement. Hillside ICAP showed issues of data sharing, such as: collecting data, data integrity and accessibility. Data needs to be stored for program accessibility. A lot of programs that have been successful have been able to build data systems” (Interviewee 5).

It is important to note that government entities have traditionally tracked outputs, or activities, services, and events. Less information is collected on type of need, details of program
approach, and long-term effect. ICAP, working within the context of PFS, is proposing to track outcomes, or individual results, measurable accomplishments, and overall impact. This is a subtle adjustment, but an important one, and part of what makes ICAP so different and so promising for counties and the state. With an entirely new process for collecting data and proving success, ICAP is a game-changer for local and state agencies.

In order to know what the likely outcomes are gonna be, you have to know how many kids you're gonna treat and how you're gonna evaluate them... We're waiting on that data pull from the state to tell us, "here's how many kids there are," which impacts our budget. Then, also, "here's how negative outcomes there are", which will ultimately affect our modeling of how much success we think we can have with them...They [state] just stare at you with a blank face because they don't even know how they get that information. Very hard to build a project if you can't do it. We want to be data driven. We don't want to engage in a project because we think it's good (Interviewee 4).

**Change in legislation:** The rapidly changing policy landscape made it difficult to predict judicial behavior, complicating the referral process and increasing risk for New York State and potential funders. As a recent example, there was concern that the roll-out of the new pre-disposition sentencing tool (PDRAI) in spring 2017 and proposed Raise the Age legislation-to serve sixteen and seventeen year olds in the juvenile justice system-would change, in unpredictable ways, the number and characteristics of youth headed to placement facilities. (Nonprofit, 2016).

Although the ICAP target group would be composed of youth at least ten years of age at the time of delinquency occurred, the age limit may be amended by state legislation to the age of 12. New York State Governor Andrew Cuomo has announced that he supports legislation to increase the age of criminality. This legislation will potentially both add youth to the target population, as 17 and 18 year olds are phased into the juvenile justice system, but also decrease the target population, as youth that are at the lower end of the risk pool might be newly categorized as
ineligible for placement or may be able to be treated by other, newly created programs funded through Raise The Age (RTA) legislation (Gately, 2015).

**Transparency:** The state wanted to regulate inputs, and although Hillside was willing to share in the interest of being transparent on the budget, they were not willing to share line items when they felt the focus should be on the service. Hillside wanted to be able to do what was needed to make sure ICAP was success and not to be held to the structure they envisioned five years at the beginning. In addition, the state was not willing to give direct data access to an independent evaluator -- they wanted to do all the data manipulation themselves claiming it’s too complicated for anyone else to understand. The interviewees felt the government was worried about losing control – “they don’t want to give up any” and were “more interested in returns than achieving the end state.”

In addition, there was a new evaluative instrument that the state created for the juvenile court judges in order to recommend placement or not, based on existing information. Although, the guidance allows for more consistency across jurisdictions, they felt this would be a barrier to judges because they would be going off an already flawed system.

5.2B  Finance Model

In a PFS contract, intermediary organizations and service providers partner to raise operating funds from third party investors to support the scaling of existing program or the implementation of new program that are evidence-based and cost-effective. As stated in the literature review, government commits to repay third party investors only if agreed upon outcome targets are achieved and are verified through an independent evaluation. If targets are achieved, then investors are repaid, including an agreed upon return on their initial investment to compensate them for the cost of their capital. The payment to investors is based on the estimated budgetary
savings and social benefits occurring to the public sector as a result of the intervention’s performance if the project fails to achieve its targets, NYS will not repay investors, ensuring that tax payer funds are not spent on ineffective programs (Hillside, 2016).

**Budget:** Overall budget and project numbers changed many times. However, when ICAP was first proposed the project, the budget was approximately $11.7 million, requiring $11.7 million of private social innovation financing and calling for a maximum of $14 million of PFS payments to be paid by the State. Hillside anticipated a $5.9 million Senior Loan at 5% annual interest, a $2.9 million program-related investments (PRI) Loan at 3% annual interest, and $2.9 million philanthropic grant.

**Counterfactual Projection:** Annually, the target population within Onondaga County spends 762 days in detention and 6,433 days in placement. Total combined marginal costs to the County and State for the detention and placement of the 284 High Risk Youth in the target population totaled $18.3 million across the five-year period, an average marginal cost of $64,422 per target youth (James-Wilson, 2013).

ICAP assumed a Base Case 30% reduction in the number of days spent in detention and placement among the project’s High Risk Youth target population (James-Wilson, 2013). As shown in Exhibit C, the Base Case 30% reduction avoids 4.0 days of detention and 33.9 days of placement per High Risk Youth when compared to the assumed counterfactual. This would result in $19,287 in combined marginal cost savings to the County and State per High Risk Youth served by I-CAP (overall a $16+ million of marginal cost savings for the State and Counties combined), compared to a $9,045 assumed cost to serve. Baselines for I-CAP’s two main target outcomes were developed using current and historical data about detention and placement rates
provided by Probation staff from Onondaga and Monroe Counties. An impact evaluation would be conducted by the State to determine PFS payment amounts.

**Figure 3: Base Case Detention/Placement Days Avoided and Cost Savings**

<table>
<thead>
<tr>
<th></th>
<th>Assumed Counterfactual (5-Year Average)</th>
<th>Base Case Treatment Group</th>
<th>Impact of I-CAP Program</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Number of Youth</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Juvenile Detainees</td>
<td>177.4</td>
<td>177.4</td>
<td>0.0</td>
</tr>
<tr>
<td>&quot;High Risk&quot; &amp; 7+ Days</td>
<td>56.8</td>
<td>56.8</td>
<td>0.0</td>
</tr>
<tr>
<td>Placed in DHS or OFCS</td>
<td>19.6</td>
<td>13.7</td>
<td>-5.9</td>
</tr>
<tr>
<td><strong>Percent of &quot;High Risk&quot; Placed</strong></td>
<td>35%</td>
<td>24%</td>
<td>-10%</td>
</tr>
<tr>
<td><strong>Average Length of Stay</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In Detention (High Risk Group)</td>
<td>13.4</td>
<td>9.4</td>
<td>-4.0</td>
</tr>
<tr>
<td>In Placement (Placement Group)</td>
<td>328.5</td>
<td>328.5</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Total Days</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Detention</td>
<td>762</td>
<td>533</td>
<td>-229</td>
</tr>
<tr>
<td>Placement</td>
<td>6433</td>
<td>4507</td>
<td>-1926</td>
</tr>
<tr>
<td><strong>Days per High Risk Youth</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Detention</td>
<td>13.4</td>
<td>9.4</td>
<td>-4.0</td>
</tr>
<tr>
<td>Placement</td>
<td>113.3</td>
<td>79.4</td>
<td>-33.9</td>
</tr>
<tr>
<td><strong>Marginal Cost per Day</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Detention</td>
<td>$350</td>
<td>$350</td>
<td>$-</td>
</tr>
<tr>
<td>Placement</td>
<td>$527</td>
<td>$527</td>
<td>$-</td>
</tr>
<tr>
<td><strong>Total Marginal Cost per High Risk Youth</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Detention</td>
<td>$4,690</td>
<td>$3,283</td>
<td>$(1,407)</td>
</tr>
<tr>
<td>Placement</td>
<td>$59,732</td>
<td>$41,851</td>
<td>$(17,880)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$64,422</td>
<td>$45,134</td>
<td>$(19,287)</td>
</tr>
</tbody>
</table>

(James-Wilson, 2013, p.12).

The value of the outcome payment would have been determined by two elements: 1. a cost for each reduced reconviction event – negotiated and agreed between Hillside ICAP and NY State; and 2. the number of reduced reconviction events – based upon the difference in reconviction for those who participate in ICAP and the comparison group. New York State most likely would have placed a cap on the outcome payments, ensuring that its liability is limited.
5.3 Investors

“Given the inherent limitations of public funding and philanthropy, organizations must be willing to commit transparent processes and measurable outcomes, and let go of traditional procurement conventions in favor of funding that can be linked to independently confirmed results” (Richardson, 2016, para 1).

Because there was no final contract, ICAP didn’t complete the investment component necessary to move the PFS project forward. However, since investors are a crucial piece to the PFS model, when ICAP was selected as a finalist, Hillside, Third Sector worked to meet with investors and build interest in the project. The initiative gained local and national attention, as the Corporation for National Community Service highlighted the PFS project with visits to the office of Senators Schumer and Gillibrand, and educational Hill visits. NYS DOB, ICAP, and its intermediary partner, Third Sector Capital Partners, held SIB deal construction conversations with a working group of key stakeholders within OCFS, DCJS, and other state and local agencies. However, per Interviewee 4,

We believe the work for the funders is going to be more cumbersome because the state has said they do not want to talk at all to funders. They want Third Sector to be an intermediary that's completely between the two of them [Third Sector and the funder]. They won't be on phone calls together, which I don’t think we’ve done before. We’ve always had pretty collaborative partners that are willing to talk to each other face-to-face. I think what they know is that there’s a strain on resources, but also I think that they needed some sort of expertise to negotiate on their behalf (Interviewee 4).

Third Sector was charged with securing the capital stack for ICAP, and Hillside was responsible for securing funding necessary for the “soft start” phase. The soft start was necessary to effectively reach scale by program launch and was identified as the three month ramp up phase before project launch. In this phase, Hillside would bring service delivery in all project counties as outlined in ICAP’s Intervention Model and program manual – this reduced potential risk for investors and allowed ICAP to exercise all the processes at least once. The
potential ICAP donors were excited about the soft started because it allowed them to see the success criteria before they provided funding. The investors along with the intermediary discussed having a soft start. To fund the “soft start” phase, Hillside received $250,000 from Nonprofit Finance Fund (NFF) as part of a federal effort powered by the Corporation for National and Community Service’s Social Innovation Fund. Although the soft start never took place, the funds did not need to be paid back due to meeting a matching obligation.

**Investments and their identification:** There are different funding opportunities for investors, for example many of the outright gifts or grants from Foundations do not expect a repayment or return on investment, and at the other end of the spectrum are investment firms, such as Goldman Sachs and Bank of America, who would like a return on their investment on behalf of their client or their organization. “Social investment is distinct from a grant, in which money is given away, in that a financial return, however small, is expected.” (Disley, 2015, p. 24). Many of the potential investors showed interest in the mission-aligned investing rather than making a grant.

The payment to investors is based on the estimated budgetary savings and social benefits occurring to the public sector as a result of the intervention’s performance if the project fails to achieve its targets, NYS will not repay investors.

Third Sector was responsible for the framing of how the capital stack would be constructed and that’s changed any number of times since the first reiteration. They went to 1/3, 1/3, 1/3 senior, junior, philanthropic model. Then Third Sector went to supporting more heavily on philanthropic money versus the capital stack to reduce the risk for the lenders; the bigger proportion of philanthropic dollars provides less risk for lender. “At the end of the day, it would be up to the funders on how they want to set up their support” (Interviewee 1). Because this is a
six year project, the investors and capital stack was open to some negotiations because not all of it was needed on day one. However, this was an issue for the state, as they want all the dollars at the start of the project. The State did not want the investors to change their minds later on. If ICAP had to get all the money up front, then the state might have to be open to paying interest to those investors. Third Sector, however, was adamant that there be local investors. If there was local buy-in, there would be a better chance of obtaining national funders. Although Third Sector was seen as a trusted partner, one interviewee did not find the importance of acquiring local Foundation support to gain national momentum. Additionally, NFF indicated that, “having local foundation involvement is important because they can vouch or bring people in” (Interviewee 5).

Per the interviewees, the failure of Rikers Island to meet their outcomes did not scare away funders, however, they are going to be more selective with who they do business with if you don’t have an experienced intermediary on your team, it’s probably an uphill battle unless you have an in-house funding scheme (Interviewee 1). Goldman Sachs, for example, dealt with Rikers Island not going as planned, so I’m sure there's a little hesitation. Then, on the flip side of that, you also have Pay for Success becoming more visible throughout the nation and some [investors] that are like, ‘Oh! I want to learn more about that.’ Or, ‘I want to get involved in that.’ (Interviewee 4). However, Third Sector states,

How much funding is tied to that interest, I don't know. We'll find out. I think the field's gonna grow really quickly here. I don't know how much capital there is out there to do all of that. So, it'll be interesting to see how many of these [PFS projects] get funded. I think there's a bunch that will be able to go to funders. But they may have pick of the crop here. Say, ‘oh, you know, this deal's better than that one.’ It very well could be that the number of projects being done outpace the number of funders that even just know how to invest. If that's the case that I think we're gonna have to do one of two things: either educate new funders, and bring them on board. Or, convince the funders that know how to do it to allocate a larger share of their investible funds for these projects. I don't know. I think it will probably be a competition (Interviewee 4).
Interviewees claim that there is legitimate interest in people wanting to do social impact investing; many of the potential investors showed interest in the mission-aligned investing. For example, Merrill Lynch was clearly motivated by their existing investor class, many of whom had a desire to take a portion of their existing portfolio and put it towards social investing. Merrill is set up to wait until they get the investors versus front load the money then go after the investors. Goldman Sachs, however, gives their own money, then finds investors. One of the interviewees could envision a future world in which Hillside has credibility with the investors that are behind Merrill Lynch and you can work out private placements on a routine basis for different projects where they would get safety through diversification of the projects they would participate in, but would only work with a handful of players. However, the novelty of the PFS concept scares many of the small to mid-size foundations. “Even the ones who like the idea are scared of it” (Interviewee 1). For example, the local community foundation of CNY was interested, but said it was too far on the edge for them. While others thought it was a wonderful model because they saw it as a vehicle to break loose from their moral obligation to renew long term commitments. After the five year commitment, the Foundation doesn’t have to worry the cycle of continued renewals - they can invest once and still see a successful outcome. Another stated, “We see some philanthropists be issue specific. For them, it’s very, very important that it’s aligned with their mission. But, for commercial lenders, not so much” (Interviewee 4). “Investors, philanthropists, from what we are seeing, continue to be at the table. We continue to see more and more commercial investors and a good amount of enthusiasm from investors for PFS projects” (Interviewee 5). In finding investors for PFS projects, Third Sector put together funder councils.

We sent out invitations to commercial banks, philanthropies - high net worth individuals, other types of lenders and providers of funds. We gave them updates
on what the project looks like during repeatability phase as well as construction. We kind of court them and keep them updated on what we're working on. While that process happens folks will say, ‘Thanks for the invitations. It's been great sitting on this funder council, but you don't need to include me going forward.’ Or, we’ll get some folks that are really interested in that geography, and ask to be kept up-to-date on everything we’re working on.

As we're going through the process, they [investors] have different preferences or how they feel about the project. Once we get to sort of a ‘hey let's fund this thing we have all the bidding done.” Then, we put together that first meeting on the project and say, "who's in, who's out? Who's gonna sit at the negotiation table?" (Interviewee 4).

As already discussed, the state pays upon meeting the outcome metric. However, investors stated that five years is a long time for a return (more risk), therefore, Third Sector recommended a payback option to receive a certain percentage after each year. Overall, the funders understand risk better than government does, and are willing to allow for risk but don’t want to get caught up in government scoring of success or failure. The investors are watching and learning as the field is evolving. Below is the funder grid for ICAP separated out in lending sections.

**Figure 4: ICAP Funder Grid**

<table>
<thead>
<tr>
<th>Funding Level</th>
<th>Funders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senior</td>
<td>Goldman, QBE, Bank of America/ Merrill Lynch, Prudential</td>
</tr>
<tr>
<td>Junior</td>
<td>Living Cities, LISC</td>
</tr>
<tr>
<td>Philanthropy</td>
<td>Farash Foundation, Barclays, Edna McConnell Clark Foundation, Hecksher Foundation, FB Heron Foundation, Ford Foundation, Oishei Foundation, Tow Foundation, Ralph Wilson Family Foundation, Next Street, Soros Foundation, Kellogg Foundation</td>
</tr>
</tbody>
</table>

**Securing investment:** At 30% impact, the best case, the Senior Lender would be repaid $6.7 million, THE PRI lender would be repaid $3.3 million and the grantor would be repaid $2.9 million (James-Wilson, 2013). The Senior Lender’s principal would be completely repaid at 12% impact and the PRI lender’s principal would be completely repaid at 18% impact (James-
Wilson, 2013). Above 30% impact, the lenders would share an additional maximum payment of $1.1 million (to be negotiated), as currently modeled (James-Wilson, 2013).

**Financial Risk Mitigation:** The proposed financing structure is designed to mitigate a range of risks (James-Wilson, 2013):

- If impacts are “only” 18% rather than the Base Case 30% assumption, all lenders experience a return of principal and all philanthropists experience a “replenishment into the project” of their grant capital.
- If impacts are “only” 15%, all lenders experience a return of principal.
- If impacts are “only” 11%, Senior debt lenders experience a return of principal.
- If impacts are “only” 5%, the project nevertheless remains solvent throughout the five-year project period, thus avoiding early shut-down.

(James-Wilson, 2013, p. 7).

**Figure 5: Base Case Project Cash Flows (in millions, except new enrollees)**

<table>
<thead>
<tr>
<th>New Enrollees</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
<th>Windup</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Starting Cash Balance</td>
<td>77</td>
<td>77</td>
<td>227</td>
<td>227</td>
<td>227</td>
<td>0</td>
<td>835</td>
</tr>
<tr>
<td>Senior Debt Financing</td>
<td>$ -</td>
<td>$ 5.77</td>
<td>$ 4.76</td>
<td>$ 2.95</td>
<td>$ 7.77</td>
<td>$ 9.17</td>
<td>$ 3.00</td>
</tr>
<tr>
<td>Subordinate Debt Financing</td>
<td>$ 2.00</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ 2.00</td>
</tr>
<tr>
<td>Grant Capital</td>
<td>$ 2.00</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ 2.00</td>
</tr>
<tr>
<td>PFS Payments</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ 7.15</td>
<td>$ 3.98</td>
<td>$ 2.87</td>
<td>$ 14.00</td>
</tr>
<tr>
<td>Interest Earnings</td>
<td>$ 0.01</td>
<td>$ 0.01</td>
<td>$ 0.01</td>
<td>$ 0.01</td>
<td>$ 0.01</td>
<td>$ 0.00</td>
<td>$ 0.05</td>
</tr>
<tr>
<td>Service Payment to Hillside</td>
<td>$ (0.43)</td>
<td>$ (0.69)</td>
<td>$ (1.54)</td>
<td>$ (2.06)</td>
<td>$ (2.31)</td>
<td>$ (0.51)</td>
<td>$ (7.55)</td>
</tr>
<tr>
<td>Intermediary Expenses</td>
<td>$ (0.66)</td>
<td>$ (0.13)</td>
<td>$ (0.09)</td>
<td>$ (0.09)</td>
<td>$ (0.09)</td>
<td>$ (0.07)</td>
<td>$ (1.13)</td>
</tr>
<tr>
<td>Interest Payments on Senior Debt</td>
<td>$ (0.11)</td>
<td>$ (0.15)</td>
<td>$ (0.15)</td>
<td>$ (0.15)</td>
<td>$ (0.15)</td>
<td>$ (0.04)</td>
<td>$ (0.75)</td>
</tr>
<tr>
<td>Principal Payments on Senior Debt</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ (3.00)</td>
<td>$ (3.00)</td>
</tr>
<tr>
<td>Interest Payments on Sub. Debt</td>
<td>$ (0.03)</td>
<td>$ (0.04)</td>
<td>$ (0.04)</td>
<td>$ (0.04)</td>
<td>$ (0.04)</td>
<td>$ (0.01)</td>
<td>$ (0.20)</td>
</tr>
<tr>
<td>Principal Payments on Sub. Debt</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ -</td>
<td>$ (2.00)</td>
<td>$ (2.00)</td>
</tr>
<tr>
<td>End of Period Cash Balance</td>
<td>$ 5.77</td>
<td>$ 4.76</td>
<td>$ 2.95</td>
<td>$ 7.77</td>
<td>$ 9.17</td>
<td>$ 6.41</td>
<td>$ 6.41</td>
</tr>
</tbody>
</table>

Less Grant Capital Stake: $ (2.00)

"Upside" Residual: $ 4.41
Hillside has a long history of partnering with business and philanthropy partners to focus scarce resources on the most promising, data-driven practices that have societal impact. PFS advances ICAP to be the catalyst for bringing the best services to scale, optimizing public resources, and actually addressing the challenges overwhelming our communities. However, most interviewees felt bringing investors on board was difficult, one stated, “a bit of a chicken and egg scenario” (Interviewee 1). Because the data was unreliable, ICAP was unable to discuss numbers with investors. There were discussions with Goldman Sachs, Bank of America, and others (Interviewee 1). However, they recommended ICAP go back to them when the data was finalized. In addition, Third Sector Capital Partners wanted to see philanthropy as lead instead of lag, siting that the “appetite has changed for philanthropic and capital investors” (Interviewee 1). With Philanthropy as the lead, there would be less risk to pay back the money should ICAP not meet their outcomes, although the funding would be more challenging to accrue than capital investors (Interviewee 1).

**5.4 Risk & Accountability**

Although PFS has not shown value quite yet, there is consensus that PFS transfers financial risk away from government and onto investors. However, interviewees identified that there are still perceived risks on the government side. ICAP and intermediaries took considerable effort to make sure of the appropriateness of the outcome metrics to ensure financial risk was limited. In addition, a couple of interviewee cited a reputational risk stating: “the risk is that we fail, not that we lose money, not a legal risk, it is our reputation. Reputation is important and we owe it to the
counties” (Interviewee 2). “Our reputation is the most important thing for our work. You can’t do these projects if folks think that they don’t work. So, it’s very much in our interest to ensure that they work” (Interviewee 4). Another risk identified is the up-front cost to the organizations,

There is a cost risk to Third Sector if you're engaged in building one of these projects. There's a high risk that it won't complete because of the inability for government to engage in these kinds of contracts. Now, that's not really a risk in and of itself, but it is a risk when you tie completing a project to the funding of Third Sector's work. In New York and Massachusetts Third Sector only gets paid for the work that they're doing if the project closes. I think they get paid out a closing fee, essentially, from the project. When you spend two, two and a half, three years building a project and, it hasn't happened to us, but it could where a project doesn't launch. We wouldn't get paid. That's a huge risk to Third Sector (Interviewee 4).

PFS is not a one size fits all model solution for all social sectors. For some grass roots social sectors efforts, who are also trying to obtain funding from the same philanthropic organizations or government agencies, they may be at risk of not getting funding because it has been allocated towards PFS projects/ outcomes-based reimbursement model – organizations that are more sophisticated.

However, interviewees suspect there will be a lot of evolution of the fundamental model once government accepts the fact they can improve promising practices and save money, thus providing heavy motivation to keep funding PFS projects. Further, this opens an opportunity for government to use PFS as a mechanism to prioritize – government can generate interest on the part of private funders to experiment with best practices.

Although PFS takes a long time to reach implementation, interviewees thought that reducing cycle time will happen after it is done right a few times, and the government will receive good information around quality data collection. There is the ability to standardize the process.

[PFS] still requires a big leap of faith around the funders and government and the willingness of a provider…this it’s not insignificant” and a small organization would not be able to make it happen (Interviewee 1).
5.5 Policy Implications

The interviewees saw policy playing a role in Pay for Success programs in different ways, such as:

**Procurement Rules:** One person stated, “It’s a case of thousands. Millions of representatives from every agency in the state of NY participated [in the contract phase] because everyone sees themselves as the center of the universe” (Interviewee 1). Although that was an overstatement, several layers of contracts are relevant to this project. The most important contract is with NYS to be the ultimate payer. Hillside needed to satisfy the Office of Family and Children Services at the Division of Budget, and the Office of the State Controller. However, Hillside found that it was high bound with procurement rules. “As I talk with folks around the country, working on other projects, that is their major hurdle as well. The government has so many rules that make no sense in this context” (Interviewee 3). One example is the time wasted getting bids for intermediary services when there is only one or two sources around the country. Some feel the procurement rules need attention and need to be modernized with pay for success in mind.

Again, PFS is a relatively new model, New York State has only done one of these before, so they are trying to learn from it and unfortunately it’s not just a simple overlay of what they did with Rikers Island. Normalization would be one of the advantages to get PFS projects up-and-running. This would allow the state to take what works and emulate it.

**Appropriation Cycle:** Because the state cannot commit more than two years in advance, there is some apprehension if a six year project will continue to receive payments. Massachusetts solved that problem by having legislation enacted that codified the problem and the solution.
However, in NYS they are not willing to do that, but are willing to manage the appropriations cycle, which allows the state to reappropriate the money every two years to make sure it is available. Many mention that this gives some insecurity to the funders should there be a change in leadership.

**Standardization**: Standardization would help in the PFS process; prove what works and what doesn’t work. One interviewee recommended a nongovernmental model to impact the process of deal negotiations and creating a true market for investors. Some critics argue that PFS is more expense than direct government contracting. Policy can also play a role in getting some program/human services to the top of the priority list that they would not otherwise get through the traditional government contract.

**Service Provision**: Because data shows us that kids who are incarcerated do not have good outcomes, one interviewee recommended having policy around improvement outcomes, such as: staying in school, job retention, access to health care, to prove what works and what doesn’t work. A few respondents indicated that policy in this area is intimately tied to the projects.

“If they're not successful you need to shut 'em down. If they're mildly successful, but maybe not paid back all the funders, you might want to do a second round and change the model or add more to your budget. If they are very successful, I think you get to whether we do policy. I think that that along with the evidence of PFS project, it will help the social service sectors to replicate and, has much more innovation in the space than if we had written the laws. So, the role of policy, I think, is to find a really good program, then write a law and support it (Interviewee 4).

Ultimately, this is about policy to change and produce a vehicle for change. PFS is a tool for creating change and nobody should do it for the sake of doing it, but creating change. PFS is opportunity for ‘proof in the pudding’ then go beyond that. Timeline is promising as most [PFS] project are five to seven years of implementation; PFS is implementing in such a way that it effects reform – it opens a policy window for PFS to take a stand (Interviewee 5).
5.6 Innovation

All interviewees felt PFS drives, or should drive, innovation to some of our society’s most pressing issues through experiment and scalability (replicating in communities across the country), however, this may depend on the stage of the intervention. Interviewee 5 states, “Nobody sees [ICAP not moving beyond the contract phase] as a failure, but lessons learned…this project is innovative in that it will create an alternative to detention and placement for youth in the juvenile justice system. This alternative has not existed before, for this population, in the region” (Interviewee 5).

There are several main benefits of ICAP as a PFS project. Interviewee 3 states,

First, it can be rapidly deployed because of Hillside’s longstanding service delivery partnerships; ICAP is well-positioned to operate across the state, seeking to serve youth in 10 target counties in Western, Central, and Upstate New York in the next five years. Second, it can be adjusted to meet local needs and complement existing community resources. Third, it focuses on clearly measurable outcomes, including reductions in detention and placement days, and improvements in wellbeing for youth and families (Interviewee 3).

Interviewee 1 felt that the ICAP project is innovative because it uses unique local partnerships to provide community-based, intensive wraparound services that are truly individualized to meet the needs of these vulnerable youth (Interviewee 1). Further Interviewee 2 stated, “ICAP’s collaborative, strengths-based, culturally competent approach works to stabilize youth and their families—within their own neighborhoods—by meeting immediate needs, strengthening connections within the community, and developing tools for coping with challenges and creating positive change” (Interviewee 2).

In the end, ICAP didn’t proceed past the negotiation phase, not even making it to the contract phase after almost three years. Per Interviewee three,

Our exploration of Pay for Success will have lasting implications for our organization and clients. Not only have all of us at Hillside learned a tremendous
amount about the application of the Pay for Success model, but it has strengthened our resolve to continue to pursue means to provide solutions to these youth in the juvenile justice system. While the current project will not move forward through PFS, we value the lessons reinforced throughout this process.

When asked the Hillside interviewees if they would try it again, they all said yes, “the concept is worth the lift” (Interviewee 1).
6. Analysis

6.1 Lessons Learned

As mentioned in the methodology section, it was the intension of this thesis to prove the hypothesis that, despite the challenges organizations face in embarking on such contracts, Social Impact Bonds mitigate risk for government funders and increase overall accountability for program quality and outcomes. As such, it will behoove policymakers to commit to creating policies that offer ease within deal negotiation and create a "true market" for investors. From the findings, the following challenges were reviewed: (a) development of outcomes-based reimbursement payment structures, (b) defining outcomes, and (c) predicting impact, through different phases of the model.

6.1A Collaborative Relationships

Transparent and collaborative relationships with external partners are key (Nonprofit, 2016). The process moved fastest and most successfully in areas in which we had strong, pre-existing relationships with judges, county and state officials, and partnering Neighborhood-Based Organizations. (Nonprofit, When, 2016). Building strong relationships with our intermediary and evaluation firms was also critical, as was clear communication and shared understandings of goals and timelines (Nonprofit, When, 2016). “It’s important to invest in a team that is very collaborative. There is an element of social capital…having a great working relationships are crucial” (Interviewee 5). In addition Third Sector states, “we don't work with nonprofits directly without a government partner. So, we prioritize what outcomes the government wants to work on. But, what that looks like is always different. It just depends on the government jurisdiction” (Interviewee 4).
In all of the PFS projects, there are multiple layers of partners from government to the number of service providers (Nonprofit, When, 2016). Interviewee 1 described Roca as having a consortium of organizations trying to deliver the services, which introduces a whole level of complexity and creates internal challenges. Whereas ICAP, however, only had to contend with 10 subcontractors, which they are very familiar with, and themselves as the lead service provider.

Although the different project had different players, the project partners did not seem to be the issue for ICAP not moving forward. However, Interviewee 4 alluded to the fact that the State of MA was easier to work with than the State of NY.

6.1B Building Buy-In

Inclusion, beginning at project conception, of those closest to the work is critical to building buy-in (Nonprofit, When, 2016). The relationships that were built through the PFS process, and the investment made by ICAP partners, were extremely valuable (Nonprofit, When, 2016). Per Interviewee 3, “because county and nonprofit partners were invested in ICAP from its infancy and had been an active part of our ongoing contracting efforts, they were better able to withstand the ebbs and flows of the process and showed greater patience and flexibility than they might have otherwise” (Nonprofit, When, 2016, para 4). Of course, their investment of time and resources and relationships was willingly made in the context of a PFS project coming to fruition and being able to reach more youth in need (Nonprofit, When, 2016). With ICAP no longer moving forward in a PFS model, costs were felt more deeply (Nonprofit, When, 2016). “We will continue to invest significant time in “processing” the frustration associated with the termination of the effort and hope to identify additional ways to leverage the work that has been done” (Nonprofit, When, 2016, para 4).
After reviewing the literature and findings, PFS/ SIBs show they mitigate risk for government and increase overall accountability for program quality and outcomes.

The federal government should become a strategic partner with state and local governments in establishing PFS projects by helping to establish PFS projects in areas where state and local activity has the potential to achieve important federal policy objectives or produce significant federal budget savings” (Liebman, 2013, para. 16).

However, as discussed in the findings, this is not a one-size fits all model – not a solution for all sectors. Not all organizations have the infrastructure set up to conduct complex and heavy front-loaded projects like PFS.

6.1C Long Process

This process takes longer than anticipated, at all points of development (Nonprofit, 2016). PFS projects are difficult to negotiate and require a significant investment of time and resources from all parties (Nonprofit, When, 2016). Interviewee 3, stated,

Variance in staff resources, schedules, and competing priorities always exist when working with multiple state and local governments and multiple nonprofit agencies across multiple regions. To some extent, Hillside Children’s Center had anticipated that because of our strong partner relationships, we would be an exception to the time it was taking other agencies to bring this type of project to execution. We learned, however, that even with our organizational expertise and capacity we were not immune to many of the most common PFS challenges (Nonprofit, When, 2016, para 5).

Although ICAP didn’t complete the contractual process, deal negotiations proved to be long and cumbersome. In every case the upfront work for a PFS project is more inclusive than a traditional government funding contract, more community partner involvement, and more exhaustive (Nonprofit, When, 2016). Each FPS project set up their service contracts differently and each indicated a ramp up period of two – two and half years. As Interviewee 2 mentioned there was some loss of motivation on the states part, as they were ready to move on to another project. All Interviewees were well aware that PFS projects do take an average of two years
before the project has been launched and an additional three – ten years before the project finishes. Interviewee 4 is also involved in the Massachusetts Roca project and indicated a ramp up period of two to two and half years. As indicated in the findings section, ICAP never made it past deal negotiations.

However, governance was a crucial and necessary step for the projects to be successful. As seen with NYS ICAP, NYC ABLE project and MA juvenile justice project, building a PFS initiative is a collaborative endeavor. ICAP had regular meetings with key stakeholders, including: representatives from OCFS, probation in various counties, DOB, and Third Sector (Nonprofit, When, 2016).

6.1D Expertise & Human Capital

Pay for Success projects require an incredible depth and breadth of expertise and a serious investment of organizational time and resources during the project construction phase (Nonprofit, When, 2016). Sharing the lesson learned with their peers, and Nonprofit Finance Fund subgrantee community, proved helpful in navigating this unfamiliar PFS territory (Nonprofit, When, 2016). Per Interviewee 3, “we were also lucky to be able to draw, on a weekly basis, from internal staff with the necessary programmatic, marketing, fundraising, budgeting, HR, legal, and evaluation expertise. Even with all of this support, Hillside also hired additional staff, prior to contracting, in order to manage the PFS negotiations and lay the groundwork for program launch” (Nonprofit, When, 2016, para 6). These team members needed not only expertise in their field, but also required a great deal of optimism and flexibility around shifting timelines and program modifications (Nonprofit, When, 2016). Hillside had to build flexibility to accommodate the associated staff and manage morale for a project that was visible in the public eye, when it was delayed and then didn’t move forward (Nonprofit, When, 2016).
Hillside understands that meeting outcome targets involves maintaining fidelity to a core service intervention with a proven track record of positive outcomes, while at the same time having the adaptive management capacity to innovate and modify interventions in partnership with Probation Officers and Family Court Officials to meet the needs of referred High Risk Youth (at a cohort or sub-group level) (Nonprofit, When, 2016). “This focus on outcomes, and capacity to adapt, are hallmarks of Hillside’s overall organizational culture as well as its institutional structure” (Nonprofit, When, 2016, para 6). Hillside’s senior leadership have provided a consistent vision for Hillside as being a regional leader in translating research into effective practice solutions (Nonprofit, When, 2016); and have shown Hillside’s ability to transform its programs to meet the changing needs of the children, youth and families it serves, and the public and private organizations with which it partners (About, 2015).

6.1E External Evaluators

Involve the independent voice of the external evaluators from the beginning - Everything does hinge on the outcome and baseline from which they will receive payment from the government (Nonprofit, When, 2016). PFS project hinges on accessing the pertinent historical data, understanding what the available data allows us to predict, and determining what kind of evaluation best fits the program and population (Nonprofit, When, 2016). Per Interviewee 3, “moving a project to contract quickly is in everyone’s best interest, it is important to discuss concrete evaluation specifics as soon as possible, as many of the parties involved had significant research expertise, our partners at Urban Institute brought a new and different perspective that substantively advanced our thinking and planning and could collaborate to build the strongest research design removed from any hint of bias” (Nonprofit, When, 2016, para 7). Additionally, it would have been most efficient to have the evaluators closely involved in the process from the
onset so that they fully understood the system constraints, were able to make their requests more focused, and because data from different external state sources can be time intensive to compile and clean up. (Nonprofit, When, 2016). ICAP brought their independent evaluator, Urban Institute, late in the negotiation process; albeit most interviewees describing it as due to the states hesitancy. Without this data, ICAP was not able to identify the cost/final return on investment (Nonprofit, When, 2016). Per Urban Institute, “the volume and integrity of the data isn’t here” (Nonprofit, When, 2016, para 7).

One Solution was to push data aggregation to the county. However, the county data provided unreliable, and to build a new cohesive database would take a lot of time and energy in which the state didn’t want to spend – although this was an issue from the very beginning, it was the state’s inability to make a final decision. Due to limitations in state data, project partners had not yet been able to pinpoint uniform eligibility criteria that would have allowed Hillside to objectively identify all appropriate youth for ICAP. Because eligibility was predicted on a high risk of incarceration, Hillside was dependent upon historic state data to project future risk, and resulting sample size could not support a sufficient rigorous randomized control trial (Nonprofit, When, 2016, para 8).

As we see in ICAP’s lack of sufficient and measurable data across counties in Upstate NY, juvenile justice has suffered glaring gaps between best practice and common practice (Nonprofit, 2016). In the social policy report for juvenile justice, the authors state, “researchers will likely need to be more involved in the translation process and its evaluation if they want juvenile justice policies to better support the use of effective interventions”, and that is exactly what PFS initiatives push in order to become effective (Henggeler, 2011, p. ).

ICAP discussed using a quasi-experimental design to do this evaluation, comparing historical groups who passed through the jail before the program was established (Interviewee 2), as the randomized control trail was not feasible, much like the ABLE project (Vera, 2015).
6.1F External Factors

Despite the need for an intervention and a clear value proposition, external factors outside of an agency’s control can simply make a project’s timing unfavorable (Nonprofit, When, 2016). Ultimately, limitations in data/information systems, as well as a rapidly changing policy landscape, had the most impact on the timeline in which ICAP could have been operationalized and the degree of outcome consistency that could have been predicted (Nonprofit, When, 2016). As Interviewee 3 stated,

In retrospect, bringing the evaluation partners into the conversation earlier would have moved the work forward with enough speed to make some of these issues surmountable. Nonetheless, despite the skill and the commitment of all parties involved, we were not in a position to orchestrate or even confidently predict the timing or content of likely legislative changes, let alone the way in which individuals and systems might respond (Nonprofit, When, 2016, para 8).

6.1G Investor Buy-In

Third Sectors Capital Partners was instrumental in two areas, for the complexity of framing the budget, and connecting Hillside to its already existing capital investors (Interviewee 4). ICAP did not receive capital or philanthropic support for the initiative (Interviewee 4). However, it was made clear the importance to start the conversations early with the potential funders (Interviewee 3). Unlike MA Roca and NYC ABLE projects, Third Sector, wanted to move forward with obtaining the bulk of the funds from private philanthropy/foundations versus capital lenders – due to less risk should the outcome measures not be reached (Interviewee 1). However, this may not have been the best approach, as it would have taken much more time and effort to get $10 million in Foundation funds. In addition, there was a need to get local Foundation buy-in (Interviewee 4). Although, Third Sector saw this as necessary, it would not have deterred large national foundation or capital lenders from supporting the project.
Although the interviewees I spoke with had identified “perceived social return on investment” as a very important factor in the decision to invest or not, time will tell if this remains as other PFS projects are completed. NYC ABLE failure to meet their outcomes may have residual effects for investors. Because the PFS projects are averaging seven years per project, which is needed to make a systemic impact within a sector, investors are funding one sum for the PFS projects over a length of time instead of consistent annual funding – this would be appealing to some if not all Foundations.

The ABLE project is the only completed project. As a result of them not meeting their outcomes, the New York City Government didn’t have to pay back the project manager, MDRC; leaving the burden of funding to the private investors, Bloomberg Philanthropies and Goldman Sachs (MDRC, 2015). Over the three years, Goldman Sachs loaned $7.2 million (MDRC, 2015). However, the termination of the program meant that Goldman lost $1.2 million and Bloomberg Philanthropies lost $6 million (MDRC, 2015).

NYS ABLE project announced that the evaluation of the first cohort of youth served at Rikers Island jail showed no difference from historical data in their rates of recidivism over the two year period following their enrollment in the PFS funded program. As a result, no success payments were made to Goldman Sachs, the sole investor, which triggered the use of a 75% guarantee by Bloomberg Philanthropies, acting as the guarantor. Goldman Sachs decided not to continue funding for a fourth year of services, a right defined in the project contract (Archer-Rosenthal, 2016, p.3).

Massachusetts is willing to repay the loan with interest to investors because it saves even more money by keeping young people out of prison (Interviewee 3). Investors are willing to put their capital at risk because they believe that Roca’s program works, and because philanthropic funding is mitigating that risk. And Roca is eager to be a part of this complex scheme because it is a way to scale up its work with at-risk youths and young adults. (Rangan & Chase, 2015)

The Massachusetts project, which launched in late 2014, rounded up more than $20 million
from investors. But the time and cost it took to design the project exposes a major, potential deterrent to other nonprofits interested in developing a pay for success project for a government.

To help with the burden, Roca was able to utilize $250,000-worth of free legal aid to help with the negotiating. Still, Roca ended up devoting more of its top staff time than it bargained for when it started. (Farmer, 2015).

Because ICAP did not finish the contract phase, no repayment structure was solidified. However, included is an example of what was originally proposed to the State. In addition, below is a table of Roca and ABLE to show the different ways in which a repayment structure can be achieved.

Although, ICAP did not move past the negotiation phase of PFS, therefore unable to determine savings to New York State, the RAND report from the first SIB pilot at HMP Peterborough indicated that “a small scale SIB will not deliver substantial cashable savings”. (Disley, 2011, p. 2). As discussed in the literature review, the PFS model is based on the premise that the intervention funded will deliver cashable savings to government within the period of the bond. (Disley, 2011). And just like the SIB at Peterborough, Rikers Island did not result in substantial cashable savings to the government departments, which would have been achieved through a significant reduction in the recidivism.

6.2 Importance of PFS Research

Although there is much in the literature review regarding the inner working of PFS/SIBs, it is a relatively new financing mechanism with very little proven outcomes. More and more states are setting aside budget funding for PFS model, allowing for policy implications. “Currently, there is no track record investors can use to achieve return on investment” (Disley, 2013, p.27).
Innovation: Even though the Peterborough RAND report found the SIB not an innovative model, SIBs provide a new idea that could become a significant source of funding for a variety of social services. Further, more importantly than the innovation of the SIB is the innovation of the project or idea which can make a systemic difference for some of the nation’s most pressing needs. The promise of SIBs stems from their ability to advance new social interventions with a new source of financing, bounded by measurable markers of success. It also may be the case that SIBs, because of their complexity and downsides, work best only in a narrow set of cases that have robust scientific evidence and quantifiable results (Liner, 2016).

Even though ABLE did not meet their stated outcomes, MDRC, ABLE’s technical assistance provider, stated that,

While it is disappointing that the program did not meet its goals, the Social Impact Bond financing arrangement worked as it was supposed to...The program provided the therapy to more than 4,000 youth over three years– a positive outcome for the city and taxpayers” (MDRC, 2015).

Additionally, the Osborne Association, service provider in the ABLE project, said they were

Disappointed but not surprised by the Vera evaluation... However, while the outcomes of this program aren’t what we or anyone else would have hoped in terms of recidivism, the program lead to major progress in working with youth on Rikers (Osborne Association, 2015).

Efficiency and Impact in tackling social problems: Many government projects funded the traditional way often do not meet outcome measures, or prove rigorous in the evaluation or scalability. Performance of social programs is rarely assessed, and the measurements that do exist seldom focus on how these policies improve outcomes for those affected. The lack of evidence-based practices has profound economic, fiscal and social consequences (Liebman, 2013). However, it is also important to keep in mind that PFS funding cannot replace general public funding. We still need federal, state, and local governments to fund the operating costs of
school systems, public health care, and safety net programs—services that do not necessarily generate tangible financial returns but are essential for daily life. The only way to find out the ultimate role for SIBs is to push the experiment further. Doing so appears to be worthwhile, because even when SIBs fail, important knowledge can be gained about what techniques do and do not work in addressing social needs (Liner, 2016).

6.3 Limitations of the design

There are some limitations of the design, including validity issues with selection bias, and researcher bias, as I am associated with Hillside and was involved in the beginning vetting and RFP phase of ICAP. In addition there may be some influencing in the collection and/or interpretation of data by the questions that were chosen; and subjectivity on the interviewees part (Qualitative Research Methods, 2010). The main limitation is the lack of time in collecting all the data and transcribing the interviews – additional interviews with NYS state, MA Roca and NYC ABLE would have enhanced my findings and evaluation of the program. In addition, some may perceive the lack of timeliness of the research as a limitation - with ICAP not moving past the contract phase. However, I think it is interesting to analyze a project not deployed, a project which has been implemented, and a project completed, but not reaching its outcomes. Even if ICAP was deployed, because of the length of PFS projects, I would be unable to show effectiveness of the program or return on investment at this time.
7. Conclusion

7.1 Implications & Improvements

Although it is too soon to tell if the PFS projects will meet their stated outcomes, a new mechanism to fund social services on a larger scale is imperative.

At every level of government, policymakers are facing the same challenge: How do we continue to innovate and make additional progress in addressing our nation’s problems when budget cuts are making it difficult, if not impossible, to hold onto the gains we have already made? If our goal is to make significant progress in addressing our most serious social problems, simply expanding the use of these strategies is unlikely to be enough to produce the results we require (Liebman, 2013).

When asked Hillside’s CFO if he would invest the time and resources into another PFS project, he stated, “We would do it again. The concept is worth the lift. It channels to interesting potential” (Interviewee 1). In addition, it is interesting to share Gruminski’s take,

Although most PFS programs have not produced definite results yet, psychological research tells us that even introducing outcome measurement in government contracting can positively influence the behavior of social service providers…transparency alone can create accountability, even in the absence of explicit rewards and sanctions (Guminski, 2016).

As Jon Pratt, Executive Director, Minnesota Council of Nonprofits phrased it, “if SIBs can deliver more resources and better results, what public official or tax payer wouldn’t be for it?” (Pratt, 2013, para 14). Today we have many evidence-based solutions to social problems, however, these solutions focus on a limited population (Roman, 2014). Many times government (policy makers) is looking to create broad solutions for large populations (i.e. reduce all recidivism), however, there is no one solution (Roman, 2014). In order to serve a larger population, there would need to be a combination of evidence-based solutions, but we do not have experience since social scientists tend to focus on narrow groups (Roman, 2014). With SIBs, we can examine different combinations and how they interact (Roman, 2014). In addition,
“For some of our most at risk populations, dozens of government programs are created – spending billions of dollars and delivered in a highly broken manner. For example, one program may provide services for job training, while another provides housing services, and still another provides mental health services. However, no one is making sure that the individual in the community achieves successful outcomes” (Liebman, 2013, p.3)

As with most government spending, we have no idea how effective it is. Performance is rarely assessed and measurement tends to focus on tracking the number of people served and the amount of service provided, rather than the outcomes that are achieved. Although some local governments and federal agencies have improved their measurement of outcomes in recent years, most programs have never been rigorously evaluated. Just as problematic, most agencies lack sophistication in coding and analyzing the date they do collect so they fail to spot patterns and variations in performance that might point to promising or problematic practices. When a government contract with multiple service providers, it almost never puts systems in place to compare their relative performance so that future funding can be allocated to the best performers. There is no systematic ranking of the cost-effectiveness of different programs (Liebman, 2013, p.4).

SIBs or PFS projects is one initiative designed to overcome fragmentation; working with service providers, community partners, government, private business, and private funders.

With that said, there are opportunities for improvement with PFS financial model which need to be overcome, such as: federal and state governments needs to take a larger role in making sure policies are in place to build more infrastructure and make deal negotiations more stream lined, and consider how to appropriately share risk between parties; reallocate funds from less effective programs to more effective programs; make sure that disclosure and transparency are key for the success of the market; scale the innovation fund model to other organizations; make transparent the use of impact evaluation data from existing PFS projects; and consider how to appropriately share risk between parties (Liebman, 2013).
Investments are only paid back if the goals have been met and proved successful, therefore shifting financial burden to investors (Center, 2013). However, without any real history of success, it may prove difficult to keep investors excited about SIB opportunities when they take all the risk and the government does not. SIBs that are successfully established, a “public policy trifecta”, will benefit private investors, social service organizations, and taxpayers (Center, 2013, para. 2).

Some feel SIBs are an innovative way to ensure better outcomes while reducing risk exposure for the taxpayers of the district. (Investing, 2014). Regardless, it is a long process that takes up many resources, and agencies need to have the infrastructure to be evaluable - PFS-funded interventions must have: measurable outcomes, available data, rigorous evaluation method, definable costs, evidence base, and transparency with all stakeholders involved (Liebman, 2013).

When initially diving into the PFS and SIB models, it was a thought that the main mechanism was to find private funding up front to support the program. But, the model is much more than that. Per George Overhoser of Third Sector Capital Partners, “if done correctly, it is a way for private funding/capital to be paid back in full to allow for recycling” (Overhoser, 2015, p.37). Following the conclusion of the PFS intervention, the state will take what works and apply to other RFPs for other social programs (Overhoser, 2015). “It will raise the bar for nonprofits to demonstrate robust indicators of their outcomes but also, will fundamentally change the way governments procure and deliver social services” (Overhoser, 2015, p.37). The problem with this is that it takes years for a PFS project to go through the contract phase, then another set of years (3-10 years) for the project to be completed and identified as a success. This is a long cycle.
Third Sector has a successful history of securing philanthropic funding for PFS projects, and in 2015 was working on a PFS project which needed upfront funding of $92 million (Third, C, 2014). The CEO of Third Sector was quoted as saying,

> With billions of dollars now flowing from the coffers of sophisticated giving-pledge philanthropists, we are bullish that the PFS model will attract the philanthropic capital it needs to catch on and become a mainstay of how government spends its money on programs…(Overhoser, 2015, p. 37).

However, this was not the case for Hillside’s ICAP project. In fact, the findings show they had a lot of difficulty securing philanthropic interest. The local and national philanthropic organizations either didn’t feel their boards wanted to take on the risk of such a costly endeavor or weren’t familiar enough, but still were not interested in investing. Questions are still looming, such as: how much pliability do these philanthropic organizations have with the largest organizations already tied up in several multi-million dollar PFS projects?; and, can this be sustained?

However, George preaches hope. Third Sector is currently working on projects that use a “partial PFS approach” have 20% of government payment once the project is completed and 80% of government payments will be made with an “immediate reimbursement model” (Overhoser, 2015, p.37). George further states that “the need for upfront financing can be removed all together” (Overhoser, 2015, p.37). This would happen by the social service provider using their own financial resources as start-up funding, foregoing “additional private capital markets” (Overhoser, 2015, p.37). However, from a certain perspective, and dependent on the cost of the project, this seems a little too high risk for many social service agencies.

As mentioned many times, PFS is still relatively new and unproven, allowing for much ambiguity for funding streams. First-time projects are expensive and very time consuming due to
learning curve. However, it is our hope that replicated projects should be cost less money and need less capital funding.

7.1A Questions I would pursue further

There are a number of questions that this research raises that could be pursued further given the opportunity and the resources:

1. Can government procurement rules be changed to allow for PFS?
2. How will governments manage pay for success contracts across political administrations?
3. How will governments replicate and scale pay for success contracts that work? [Based on success of outcomes, how does government play a role in deploying evidence-based model to other parts of the country/world?]
4. Can investment of PFS be sustained?

7.2 Policy Recommendations

We have failed to develop effective policy solutions to some of our most pressing social issues, or failed to scale widely the solutions that do work. Budgets should include funding for evaluation of programs and ability to look at new approaches. As Interviewee 1 stated, “We need policy to assist in standardization [of PFS initiatives] and long-term appropriations” (Interviewee 1). The government is used to being the lead role in negotiations (including program development), and as we learned in ICAP, the state put forth roadblocks at every corner, yet didn’t have the time or resources to take on a PFS project.

There may be an opportunity for policy impact on the process of deal negotiations and creating a true market for investors. As the growth of PFS builds momentum across the states, it is important to create policy for a mechanism that could potentially have great impact on complex social changes such as homelessness, chronic health conditions, poor school
performance, and criminal recidivism. It is the US governments’ moral obligation or responsibility to focus on achieving results.

**Tax Relief:** Experts call for “new regulatory framework and tax relief” to entice investors to enter into a social impact bond versus traditional investments (Davies, 2014, p.7). UK parliament enacted legislation in 2014 to address this issue (Davies, 2014). Currently, return on investments from SIBs are taxed at the full rate, unlike their traditional income investments that are tax-exempt (when funding is given to charitable organizations) (Davies, 2014). Government could provide investment incentives to be conducive to charities that wish to invest from their endowment (i.e. mission-aligned investing), rather than by giving a grant” (Disley, 2015, p 28).

**“Full Faith” Contracting:** In 2012, the Massachusetts Legislature authorized the Secretary of Administration and Finance to enter into PFS contracts, with up to $50 million in success payments backed by the full faith and credit of the Commonwealth. This legislative act created the Social Innovation Financing Trust Fund. (Center, 2014).

**Federal and State Governments:** Congress needs to act to ensure that the federal government can take a more active role in shaping the social impact bond market. Create a $300 million Pay for Success incentive fund in the Department of the Treasury (Shah, 2013). Some have suggested that directing even a small percentage of the $43 trillion of assets under management in the United States would unleash a huge flow of return-seeking capital in the service of public good (Rangan & Chase, 2015).

In addition, creating disclosure and transparency on the state level is crucial (Shah, 2013). To date, the decentralized, state-by-state process of social impact bond negotiations in the United States has allowed for natural experimentation in how the deals are set up and financed, but it also means that too many jurisdictions new to impact bonds have had to start from scratch (Shah,
By setting up state departments that specialize and drive PFS projects, it will assist other state departments in understanding the complexities of the process in an already strained infrastructure (Shah, 2013). Per Shah, policy can play an important role in PFS. She stated,

In catalyzing impact investing vehicles that need longer to develop or may offer low rates of return. The G-8 working group (refers to the group of eight highly industrialized nations) should look at the potential for Community Reinvestment Act rules to include impact investing, consider urging more widespread adoption of B Corp legislation, and offer possible changes to the rules for pension-fund investors. All of these policies could significantly increase the amount of money available for impact investing (Shah, 2013, p. 17).

**Evidence-Based Programming:** In addition to policy for the PFS process, there is a clear fiscal policy imperative for evidenced-based policymaking (Liebman, 2013). Smart decisions need to be made about which government activities to continue, which to expand and which to eliminate (Liebman, 2013). “For most social-policy objectives, we have no proven solutions. To rectify this, we need to reform the way government does social spending so that we produce more experimentation, perform more rigorous evaluation of innovative ideas, and pay more attention to performance in funding decisions” (Liebman, 2013, p. 3).

**Scale the Innovation Program Model:** It would be interesting to see a policy in support of Jeff Liebman’s idea of the ten-year challenge; solve ten problems in ten places in ten years to answer our most pressing social issues.

Congress and the president should work together to identify ten social-policy problems where it is a national priority to find solutions. For these ten problems, policymakers and communities must have the ability to identify specific individuals in the population to be served and the ability to measure the population outcomes; these two factors will provide an observable baseline against which improvements can be measured. Then, through a SIB mechanism ten communities would be selected...in an effort to transform outcomes for specific populations within five to ten years (Liebman, 2013, p. 5).
“The goal would be to discover two or three transformative approaches for each policy problem – solutions that could then be applied nationwide” (Liebman, 2013, p. 3). Although it is a great idea, there are some issues, such as the difficulty of implementation across different regions who may not be set to take advantage of such transformative programs – improvements could take decades (Liebman, 2013).
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Appendices

Appendix A: Interview Questions

[Thesis questions: What is making the SIB attractive to the investor? To what extent-how and why- do stakeholders feel that the SIB will lead to greater innovation and/or efficiency?]

The interview questions were modeled after the RAND report, “Lessons learned from the planning and early implementation of the Social Impact Bond at HMP Peterborough” (Disley, 2011, p. 62-67).

**Open Questions:**
Q1.1: Could you tell me about your own involvement in the development of the SIB initiative and its operation for far?
Q1.2: Could you describe your organization’s role in the SIB?
Q1.3: What is your view of the SIB?  
- In terms of the organizations involved, their roles and responsibilities, the benefits and costs.  
- The Feasibility and suitability of the SIB model?

**Overall of contractual processes:**
Q2.1: What was your involvement in the contractual negotiations/discussions?  
- For example, were you involved in negotiations, reviewing, attending meetings?
Q2.2: Who else was involved in negotiations/discussions for the PFS?
Q2.3: Who, or which organization(s), would you say were the main drivers in the contractual process?
Q2.4: Were there any sticking points or challenges in drawing up the contracts?  
- If so, how were these overcome?
Q2.5: Were any aspects of the contractual process easier than expected?

**Meaning/implications of the contracts**
Q2.6: What are your organization’s/agency’s contractual responsibilities under the PFS?  
- To check understanding, clarity and identify accountability under the PFS model?
Q2.7: Do you feel your organization/agency is carrying any risks (contractually)?
Q2.8: Do you feel your agency is receiving any benefits, contractually?  
- For example, [for providers] long-term funding, [for investors] might get a return on investment where wouldn’t have previously, [for Ministry of Justice] service being provided where none was previously.
Q2.9: Do you feel there are any particular strengths and weaknesses of the final contracts, and if so, what are they?  
- For example, in terms of reporting, the time spent in negotiation, the level of risk?

Assessing services delivery
Q2.10: Have any changes been made to the planned intervention model since the start of the PFS?

**Investors:**

Q3.1: Were you involved in any way in developing the investment model for the PFS?
   - If no, do you feel able to comment on the development of the investment model?
   - If no, move to section 5. If yes, continue to next questions.

**Amounts of investment desired and secured**

Q3.2: Do you know how the overall amount of investment needed for the SIB at was decided?
Q3.3: Do you know how much investment was actually secured?

**Investors and their identification**

Q3.4: Are you able to comment on the list of investors in this SIB?
   - Who are they?
   - Are they appropriate?
   - What are their relative contributions?

Q3.5: Are you able to say anything about how potential investors were identified?

**Securing investment**

Q3.6: What are the challenges in demonstrating a fiscal return on investment?
Q3.7: What are some of the challenges trying to get investors on board? How do you get the investor to buy-in?
Q3.8: Were there any challenges in securing sufficient investment?
Q3.9: Do you know if there were any organizations/individuals that considered investing and chose not to invest?
   - Would you be able to tell us anything about them?
   - Do you know, or could you speculate on, their reasons for not investing?

Q3.10: Do you know whether potential investors were given information about the intervention, and if so, what information?

**Factors relevant to investment decisions**

Q3.11: What would you say were the likely factors which influenced decisions about whether or not to invest?
Q3.12: There are a number of factors which they think may have played a role in decisions to invest or not. If I read out this list, perhaps you could score each on how important you think it is – where 1 is not important at all, and 10 is very important, a ‘deal breaker’:
   a. Speed of process
   b. Length of time until outcome payment
   c. Criminal justice setting
   d. Nature of the intervention being delivered
   e. Financial return on investment
   f. Perceived social return on investment
   g. Being involved in an innovative scheme
   h. Profile for participating organizations
   i. Other: *Please specify*

**Ongoing information**

Q3.13: How much ongoing information about the initiative is provided to investors?
If you are able to comment on this, could you give us a rough estimate of how long it takes to provide that information?

Closing question
Q3.14: Do you have any other comments to make in relation to investors or the investment process?

Outcomes:
Q4.1: This is still a fairly new financing model in the US. What do you see as the biggest challenges in developing outcome-based reimbursement payment structures? Specifically for ICAP?
Q4.2: Could you describe and comment on the outcome measures used in the SIB for ICAP, and how these were selected?
  - How is effectiveness or success measured?
  - Could you describe and/or comment on the cohorts of offenders used in the measurement of outcomes?
Q4.3: What were the challenges in defining outcomes? How do you know when a social service agency has well-defined outcomes with PFS potential? Are some outcomes easier defined based on social issue trying to achieve? Specifically for I-CAP?
Q4.4: What are the challenges with predicting and measuring impact?
Q4.5: Are there any particular strengths and weaknesses of the outcomes and payments arrangements, and if so, what are they?
Q4.6: Do you think these measures and payment levels work equally well for all parties?

Stakeholder opinions on the intervention model being used
Q4.7: Were you involved in any way in the development of the intervention model for the SIB?
Q4.8: Do you know how the intervention model and the providers were selected?

Policy Implications:
Q5.1: Where do you see policy playing a role? Could policy fit in insofar as impact on the process of deal negotiation and creating a true market for investors? If so, how?

Risk & Accountability:
Q6.1: What are some of the challenges working with the government on a PFS model? Could it be improved? If so, how?
Q6.2: Does this model reduce risk for government?
Q6.3: What does the PFS model do for government-side investors’ risk accountability?
Q6.4: Is it a one-size fits all model – a solution for all social sectors? If not, what happens to those sectors or grass roots social service efforts who are also trying to obtain funding from the same philanthropic organizations or government agencies who are deploying their funding towards a outcomes-based reimbursement method?
Q6.5: Do you think we will continue to see more government funding deployed for PFS projects?
Q6.6: In what respect does it encourage government efficiency?

Overall:
Q7.1: Do you think PFS drives innovation to some of our society’s most pressing issues? If so, how? Examples? In what respect does it drive impact?
Q7.2: Would you say that there are any lessons learned in terms of the PFS so far?
Q7.3: What would success in the PFS look like for your organization?
Q7.4: There seems to be various organizations being awarded PFS contracts in juvenile justice, but all have slightly different objectives. Do you have any views about rolling out a wider PFS model in juvenile justice?
Q7.5: Have you any other observations to make about the PFS that have not yet been mentioned in our discussion?
Appendix B: Consent Form

Study of Social Financing and Payment by Results in tackling social problems.

Informed Consent

You are invited to join a research study of social financing in tackling social problems. The changing landscape of government funding of social programming, innovative, multi-stakeholder financing strategies are becoming the new trend in nonprofit funding. We are looking for people who are actively involved in social impact bonds or pay-for-success mechanisms, in order to find if the practice of reimbursing drives greater efficiency, innovation and impact on social problems. We hope this will shed light on reimbursement based outcomes - is it an attractive model to investors and to what extent stakeholders feel that the SIB will lead to great innovation or efficiency?

The principal researcher is Erin Mathis, a graduate student at the Rochester Institute of Technology (RIT). Dr. Franz Foltz is supervising this study.

The decision to join, or not to join, is up to you. Please take whatever time you need to discuss the study with anyone else you wish to.

We are surveying individuals involved in three SIB/PFS projects -- the Intensive Community Asset Program (I-CAP), which creates alternatives for Family Court Judges and Probation officers who seek to avoid placement of youth into high cost institutional settings; Roca, also designed to improve outcomes for hundreds of at-risk youth in the probation system or leaving the juvenile justice system in Massachusetts, and the Adolescent Behavioral Learning Experience (ABLE) program, which aimed to reduce readmissions of 16- to 18-year-olds to Rikers Island.

WHAT ARE WE ASKING YOU TO DO?

Participation will consist of answering open and closed-ended questions over a period of an hour and twenty minutes, either over the phone or in-person.

Based on your answers, I may ask you to participate in a hour follow-up interview.

I will investigate questions regarding overall contractual processes, including: What are the challenges in developing outcomes-based reimbursement payment structures/models, specifically from defining outcomes, estimating the potential impact of measuring change and demonstrating a fiscal return (return on investment)? Further, how can policy play a role? Could policy better help facilitate the process of deal negotiation and creating a true market for investors? Does this model reduce risk for government or drive government accountability for program quality and outcomes (in other words, what does the PFS model do for government-side investors’ risk accountability)? What are the lessons learned from the planning and early implementation of PFS? In the end, the report will briefly review findings.

INTENDED BENEFITS

It is reasonable to expect the following benefits from this research:

* Provide a more robust evidence-base on this relatively new funding mechanism.

We cannot guarantee that you will experience benefits from participating in this study. Others may benefit from the summary of the information you share. You may stop participating at any time you choose.

RISKS AND CONFIDENTIALITY
The researchers will take precautions to protect any personal or sensitive information. We recommend you not share information that is proprietary or would otherwise put you at legal risk. We will not use your name in publications that result from this study. We will make every effort to keep your personal information confidential. We will take the following steps to keep information about you confidential:

1. We will keep any recordings or notes in a repository accessible only to the researchers.

2. We will file any paper notes in a locked drawer in an office accessible only to the researchers.

3. Any email communications will be via the researchers’ password-protected RIT email accounts. We will never include personal or sensitive information in online communications.

4. Any quotes used from interviews will be de-identified by the use of an anonymous identifier.

YOUR RIGHTS AS A RESEARCH PARTICIPANT

Participation in this study is voluntary. You have the right not to take part at all, or to leave the study at any time. Choosing to leave will not result in any penalty or loss of benefits. Choosing to leave will not harm your relationship with the research team or with RIT.

If you decide to leave the study, notify Erin Mathis. We will cancel all pending appointments and we will not send you further communications.

If you have questions about the study, any problems, unexpected discomforts, or think that something unusual or unexpected is happening, contact Erin Mathis (at +1-585-233-9895 or exm2929@rit.edu) or Dr. Franz Folz (+1-585-475-5368 or fafgsh@rit.edu)

If you have questions or concerns about your experience as a research participant, you may also contact Heather M. Foti, Associate Director of RIT’s Human Subjects Research Office at +1-585-475-7673 or hmfsrcs@rit.edu
Appendix C: Service Provider Background Information

Founded in 1837, Hillside Family of Agencies is a Rochester, NY based nonprofit provider of family-led and child/youth guided human services, including child welfare, mental and behavioral health, youth development, juvenile justice, special education and developmental disability services. With an annual operating budget of $140 million, extensive programming in the Rochester, Syracuse and Buffalo metropolitan areas and across numerous counties in Upstate New York, Hillside is a “regional leader in translating research into effective practice solutions.” (Hillside, 2016, para 2). Hillside has five affiliates: Snell Farm Children’s Center, Hillside Work-Scholarship Connection, Hillside Children’s Center, Hillside Still Water, and Hillside Children’s Foundation. Together, these five affiliates serve more than 11,000 families annually via 2200 staff members (Hillside, 2016).

There exists a distinct cohort of high-risk juvenile justice involved youth for whom no current community-based option is seen to be credible (James-Wilson, 2013). This is due to a variety of factors, including:

- Challenges in fully engaging youth and their natural supports via existing services due to issues of culture, language, along with a perceived lack of understanding, respect, and accessibility (James-Wilson, 2013).
- Pervasive constraints to participation in existing diversion and alternative to placements serviced due to (i) a lack of stable housing options, (ii) unmet mental health needs, (iii) truancy and runaway behaviors (James-Wilson, 2013).
- Regular adjournments of family court proceedings due to (i) non-appearance, (ii) re-arrest, and/or (iii) lack of family participation, and perceived “buy-in” (James-Wilson, 2013).
However, youth sent to placement often have negative outcomes (James-Wilson, 2013). The patterns of abuse and violence in facilities mean “not only do youth leave facilities without having received the support they need to become law-abiding citizens, but many are also more angry, fearful, or violent than they were when they entered.” (Vera, 2009, para 4).

As youth are removed from their families and communities, institutionalized placement has been associated with a number of negative outcomes, including increased recidivism (James-Wilson, 2013). Youth released from state custody between 1991 and 1995, 75 percent were re-arrested, 62 percent were convicted, and 45 percent were re-incarcerated within three years of their release (James-Wilson, 2013).

ICAP would provide a range of supports that will divert participants from lengthy and repeated stays in detention and eventually placement (James-Wilson, 2013). The overall ICAP model includes:

- Proactive placed based supports, delivered through a neighborhood based Community Asset Navigator, to strengthen participants’ supports and links to community assets;
- Specialized placed-based services to address key risk factors for ongoing detention and placement by delivering services not currently available or accessible in the neighborhood;
- 24/7 crisis support for participating youth people and their families;
- Care management that maintains a strong collaboration with probation services, the community asset navigator, service providers, family court judges and other stakeholders;
- Six months of individualized specialized services;
- An additional year of outcome monitoring (James-Wilson, 2013).
(James-Wilson, 2013)
Appendix D: PFS Comparison

To assist in the review of the challenges, it is helpful to compare ICAP with NYC ABLE Project for Incarcerated Youth and Massachusetts Juvenile Justice PFS Initiative. The tables below show the overview and project partners needed in such an undertaking. They set the stage for discussion.

**Overview:**

<table>
<thead>
<tr>
<th></th>
<th>ICAP</th>
<th>NYC ABLE Project for Incarcerated Youth</th>
<th>Massachusetts/ Roca Juvenile Justice PFS Initiative</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Contract Negotiations</strong></td>
<td>Never made is past contract negotiations. 2013-2016</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Year Launched</strong></td>
<td>Never Launched</td>
<td>2012</td>
<td>2014</td>
</tr>
<tr>
<td><strong>Service Delivery terms</strong></td>
<td>5 projected</td>
<td>4 projected 3 actual</td>
<td>7</td>
</tr>
<tr>
<td><strong>Project Need</strong></td>
<td>45 percent of young adults were re-incarcerated within three years of their release</td>
<td>Nearly half of all adolescents incarcerated at Rikers Island jail will return within one year of being discharged</td>
<td>55% of young adults who age out of juvenile justice system or are on probation will return to prison at least once within three years</td>
</tr>
<tr>
<td><strong>Project Objectives</strong></td>
<td>Reduce recidivism by 30%</td>
<td>Reduce recidivism by at least 10 percent</td>
<td>Reduce incarceration by 40% and increase job readiness and employment</td>
</tr>
<tr>
<td><strong>Individuals Served</strong></td>
<td>Age: 10-16 depending on Raise The Age 835 youth</td>
<td>17,287 (projected) 4,000 (actual) Ages: 16-18</td>
<td>929 Ages: 17-23</td>
</tr>
<tr>
<td><strong>Geography</strong></td>
<td>10 counties in Upstate NY</td>
<td>New York City, NY</td>
<td>Boston, Chelsea and Springfield MA</td>
</tr>
<tr>
<td><strong>Issue Area</strong></td>
<td>Recidivism</td>
<td>Recidivism</td>
<td>Recidivism</td>
</tr>
<tr>
<td><strong>Initial</strong></td>
<td>$14M</td>
<td>$9.6M</td>
<td>$21.7M</td>
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</table>
### Investment Status

<table>
<thead>
<tr>
<th>Status</th>
<th>Never made it past contract negotiations</th>
<th>Completed. However, didn’t meet the outcomes outlined in the contract</th>
<th>Still ongoing. To be completed 2021</th>
</tr>
</thead>
</table>

(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p.4)

### Project Partners

<table>
<thead>
<tr>
<th>Service Providers</th>
<th>ICAP</th>
<th>NYC ABLE Project for Incarcerated Youth</th>
<th>Massachusetts Juvenile Justice PFS Initiative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payors</td>
<td>Hillside Children’s Center</td>
<td>Friends of Island Academy</td>
<td>Roca, Inc.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>The Osborne Association</td>
<td></td>
</tr>
<tr>
<td>Payors</td>
<td>New York State: Office of Children and Family Services (OCFS)</td>
<td>New York City Department of Corrections</td>
<td>Commonwealth of Massachusetts and US Dept of Labor</td>
</tr>
<tr>
<td>Transaction Coordinators</td>
<td>Third Sector Capital Partners; Harvard SIB Lab (contractor working on behalf of the state)</td>
<td>MDRC</td>
<td>Third Sector Capital Partners</td>
</tr>
<tr>
<td>Evaluator</td>
<td>The Urban Institute</td>
<td>Verna Institute of Justice</td>
<td>Sibalytics, LLC The Urban Institute</td>
</tr>
<tr>
<td>Validator</td>
<td>none</td>
<td>none</td>
<td>Public Consulting Group</td>
</tr>
<tr>
<td>Project Manager</td>
<td>Hillside/ ICAP</td>
<td>MDRC</td>
<td>Third Sector Capital Partners</td>
</tr>
<tr>
<td>External Legal Council</td>
<td>Internal general council</td>
<td>Debevoise</td>
<td>Goulston &amp; Storrs PC, Nixon Peabody LLC, Goodwin Procter LLC, and Ropes &amp; Gray LLC</td>
</tr>
<tr>
<td>Technical Assistance Providers</td>
<td>State received assistance from SIB Lab; Third Sector; and Urban Institute</td>
<td>MDRC and Correctional Counseling, Inc.</td>
<td>Government Performance Lab and Chapin Hall</td>
</tr>
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(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p.8)
## PFS Project Contracting and Governance

<table>
<thead>
<tr>
<th>Operational Oversight Structure</th>
<th>ICAP</th>
<th>NYC ABLE Project for Incarcerated Youth</th>
<th>Massachusetts Juvenile Justice PFS Initiative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational Committee includes project manager, OCFS, service provider; intermediary</td>
<td>Operational Committee made up of project manager and service providers’ staff</td>
<td>Operating Committee includes representatives of project manager, Commonwealth Department of Youth Services, and Executive Office of Administration and Finance; service provider; intermediary; evaluator by invitation</td>
<td></td>
</tr>
</tbody>
</table>

| Frequency of Meetings | Weekly when discussing program design and predictors | Every 1-2 weeks | Monthly in the first year, quarterly thereafter |

| Executive Oversight Structure | Oversight committee includes: project director, intermediary, HCC executive director, OCFS, Hillside CFO | Program monitoring committee made up of New York City Department of Corrections and Mayors office, service providers and project manager | Oversight committee includes representatives of project manager, intermediary, service provider executive director, commissioner of dept of youth services and secretary of Executive office of administration and finance |

| Frequency of meetings | Monthly | Monthly | Quarterly |

| Investor role in project governance | None (although, ICAP didn’t get that far) | None | Can attend quarterly meetings of oversight committee and up to two meetings of Operating Committee, as non-voting member |

| Frequency of reporting to Investors | N/A | Monthly reports; Quarterly meetings | Quarterly |

| Non-standard contract termination events | N/A | Non-performance by service provider or intermediary | Commonwealth and senior lender have termination rights if cumulative program attrition exceeds Roca historical baseline by 350% or more at end of year 2 or 3 |

| Appropriations Risk Mitigation | None | None | Success payments backed by full faith and credit of |
(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p.21)

### Investors

<table>
<thead>
<tr>
<th></th>
<th>ICAP (initial plan)</th>
<th>NYC ABLE Project for Incarcerated Youth</th>
<th>Massachusetts Juvenile Justice PFS Initiative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senior Investor/ lender and total senior investment ($MM)</td>
<td>$5.9</td>
<td>Goldman Sachs ($9.5)</td>
<td>Goldman Sachs ($9)</td>
</tr>
<tr>
<td>Subordinate Investor/ Lender and Total Subordinate Investment ($MM)</td>
<td>$5.8</td>
<td>None</td>
<td>Kresge Foundation ($1.5) Living Cities ($1.5) ($3 total)</td>
</tr>
<tr>
<td>Deferred Fee Source and Total ($MM)</td>
<td>N/A</td>
<td>None</td>
<td>Roca Inc. ($3.27) Third Sector Capital Partners, Inc. ($0.05) ($3.76 total)</td>
</tr>
<tr>
<td>Recoverable Grant Source and Total ($MM)</td>
<td>N/A</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>Non-Recoverable Grant Source and total ($MM)</td>
<td>N/A</td>
<td>None</td>
<td>Laura and John Arnold Foundation ($3.7) New Profit, Inc. ($2) The Boston Foundation ($0.3) ($6 total)</td>
</tr>
<tr>
<td>Guarantor and Guarantee ($MM)</td>
<td>N/A</td>
<td>Bloomberg Philanthropies ($7.2)</td>
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(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p. 25)

### Repayment Structure

<table>
<thead>
<tr>
<th></th>
<th>NYC ABLE</th>
<th>MA Roca</th>
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<tbody>
<tr>
<td>Initial investment</td>
<td>$9.6</td>
<td>$21.76</td>
</tr>
<tr>
<td>Max Repayment funds committed by payer</td>
<td>$11.7</td>
<td>$27.0</td>
</tr>
<tr>
<td>Full service delivery</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>term</td>
<td>Full repayment period</td>
<td>3 (actual)</td>
</tr>
<tr>
<td>-----------------------------------------------------------</td>
<td>-----------------------</td>
<td>------------</td>
</tr>
<tr>
<td>Interim outcomes reported? Tied to payments?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sustainability of Funds</td>
<td>Any unspent portion of guarantee to be used by intermediary to facilitate future transactions</td>
<td>State could serve an additional 390 individuals if the project is successful, using federal grant funds; and any repaid philanthropic support will be invested in future PFS projects and/or service provider scaling</td>
</tr>
<tr>
<td>Interest</td>
<td>None</td>
<td>5% (senior) and 2% (subordinate) base annual rate</td>
</tr>
<tr>
<td>Trigger for initial repayment of principal</td>
<td>8.5% reduction between control and treatment</td>
<td>Jail bed-day outcome: 5.2% decrease in days incarcerated; job readiness outcome: participant engaged with worker &gt; 9 times in one quarter; employment outcome: participant earnings &gt; $1,000 in one quarter</td>
</tr>
<tr>
<td>Threshold for full repayment of principal</td>
<td>10% reduction between control and treatment</td>
<td>40% reduction incarceration days</td>
</tr>
<tr>
<td>Threshold for full repayment of principal plus maximum success payments</td>
<td>20% reduction between control and treatment</td>
<td>70% reduction in incarceration days</td>
</tr>
<tr>
<td>Repayment timing</td>
<td>Year 3 (final)</td>
<td>Incarceration outcome: bi-quarterly starting in year 5; Job readiness outcome: bi-quarterly starting at Q7; employment: bi-quarterly starting in year 5</td>
</tr>
<tr>
<td>Return to investor</td>
<td>11% to 22%</td>
<td>11% maximum (senior lenders); 18% maximum (subordinate lenders)</td>
</tr>
<tr>
<td>Success payments to other stakeholders</td>
<td>No</td>
<td>Yes: service provider and project manager</td>
</tr>
</tbody>
</table>

(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p. 29)

**Evaluation**

<table>
<thead>
<tr>
<th>ICAP</th>
<th>NYC ABLE</th>
<th>MA Roca</th>
</tr>
</thead>
</table>

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<table>
<thead>
<tr>
<th>Evaluation Design Methodology</th>
<th>Quasi-experimental: using historical baseline</th>
<th>Quasi-experimental: regression using historical baseline</th>
<th>Randomized control trial</th>
</tr>
</thead>
<tbody>
<tr>
<td>Data Sources for Evaluation</td>
<td>Source of problem</td>
<td>NYC Dept. of Corrections</td>
<td>MA unemployment insurance database</td>
</tr>
<tr>
<td></td>
<td></td>
<td>NYC Office of Mgt. and Budget</td>
<td>Service provider</td>
</tr>
<tr>
<td>Outcomes tied to Success Payments</td>
<td>Number of jail/prison bed-days avoided</td>
<td>Number of participants served and total jail days avoided</td>
<td>Number of jail/prison bed-days avoided; job readiness; and increase in employment</td>
</tr>
<tr>
<td>Outcomes tracked but not tied to success payments</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Length of period evaluation</td>
<td>5 years</td>
<td>4 years (projected)</td>
<td>7 years</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3 years (actual)</td>
<td></td>
</tr>
</tbody>
</table>

(Information for NYC ABLE and MA JJ was retrieved from Archer-Rosenthal, 2016, p.16)