LEGISLATIVE ANALYSIS AND PUBLIC POLICY ASSOCIATION

Pay for Success Funding Initiative

FEBRUARY 2021

WHAT IS PAY FOR SUCCESS?

Unlike typical funding scenarios for providers of social programs, Pay for Success (PFS) – sometimes referred to as a social impact bond – is a funding initiative that involves, at a minimum, four parties: (1) the service provider/social program; (2) an investor or investors; (3) an independent evaluator; and (4) a traditional funder or "outcomes payor," usually a branch of federal, state, or local government. These four parties enter into a contract that specifies: (1) the amount the investor(s) will invest and how long the investor(s) will fund the program; (2) the outcomes the social program must achieve in order to trigger repayment by the traditional funder; (3) the entity responsible for conducting the independent evaluation and the point(s) at which such evaluation(s) will be conducted; and (4) the terms for repayment by the traditional funder and any return on the investment.

The following is an example of how a PFS-funded program works: Service provider, Early Education Program; investor, PFS Finance; XYZ Independent Evaluators; and traditional funder, ABC County, enter into a contract. Early Education Program is a social program designed to reach children at risk of failing in the first years of school. It gives them a solid educational foundation before entering kindergarten and follows them through fifth grade. PFS Finance agrees to invest $2 million in Early Education Program over a period of ten years. The terms of the contract require that no more than five percent of the children who go through the program require special education in grades K-5. If Early Education Program meets that requirement, ABC County will repay PFS Finance the money it invested plus a modest (three percent, for example) return on the investment. XYZ Independent Evaluators conducts the first evaluation after the first cohort of children completes kindergarten. If the evaluation shows that only two percent of children who completed the program required special education, that triggers the repayment provision, and ABC County will repay PFS Finance whatever funds it invested to date plus the return on investment. ABC County will continue to make those payments each year that Early Education Program meets the requirements. Most likely, PFS Finance will include a stipulation in the contract that allows it to cancel the contract if Early Education Program has not met the requirements triggering repayment by a certain point, for example, after five years, allowing PFS Finance to cut its losses. In some cases, if the social program is successful, the traditional funder will take over funding the program at the expiration of the contract period.

PFS is used across a variety of social programs including, but not limited to, criminal justice, homelessness, at-risk youth, job training, and educational opportunities. Unlike with traditional funding, PFS recognizes that there is no "one-size-fits-all" and does not require that programs use certain prescribed methods. Therefore, programs can adjust their methods to meet the needs of the population and community that they are serving, making them better able to serve different communities within the same service area. PFS is, in essence, a funding opportunity for social programs that passes the risk of failure to investors and away from traditional funders.

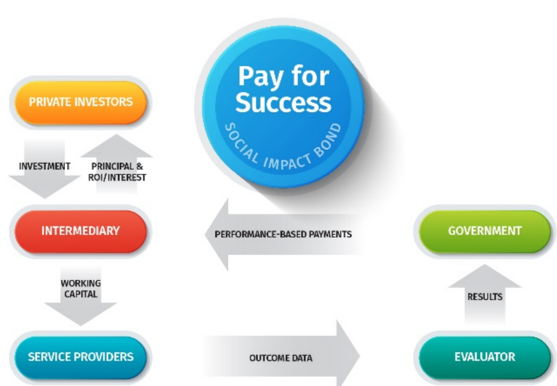
As PFS becomes more commonplace across the country, other funders, including health care systems and insurers, are beginning to take an interest in them and are exploring the opportunities presented by the PFS model.

BACKGROUND

The first program with PFS financing began in 2010 in

Peterborough Prison in the United Kingdom (UK). Using £5 million in funds from trusts and foundations, Social Finance UK – a nonprofit organization that partners with governments, service providers, and volunteers – funded the program through an umbrella organization called One Service which was designed to help offenders stop the cycle of reoffending. The program initially showed an 8.4 percent reduction in recidivism. By July 2017, it showed a nine percent reduction in recidivism compared to the national control group. Per the contract with the UK Ministry of Justice, by maintaining a reduction in the recidivism rate of above 7.5 percent, investors were repaid for the initial investment and recouped a return of just over three percent per annum.

Following the initiation of that program, organizations like Nonprofit Finance Fund® (NFF®), Urban Institute, and Social Finance US began working to bring PFS to the United States, with an initial focus on funding programs to reduce recidivism, reduce homelessness, and expand access to early education. Beginning in 2012, and with bipartisan support, the federal government began providing PFS funding, with almost $100 million paid out during the period 2012 to 2016. In 2018, Congress enacted the Social Impact Partnerships to Pay for Results Act (SIPPRA; discussed in more detail below) which supports outcomes-based financing and provides funding for social impact partnerships, including PFS-funded projects. Since their inception in 2011, there have been more than 26 PFS-funded projects in the United States which have met varying degrees of success. However, one of the benefits of PFS financing is that, even those projects that do not reach their expected outcomes provide lessons for others in the field, these lessons can be passed on without the cost of that failure being borne by a governmental entity (ultimately passing it on to taxpayers).



The NFF (discussed in more detail below) issued a report in 2018 that took an in-depth look at the 25 PFS-funded programs operating in the United States at that time, a copy of which can be found here: https://nff.org/report/pay-success-first-25. The programs address issues across the spectrum, including those aimed at reducing recidivism, increasing school readiness, supporting new mother and infant health, achieving housing stability for individuals who are chronically homeless, reducing family involvement with the department of family services, and helping individuals find sustainable employment. PFS financing for the programs ranges from investments by entities like Goldman Sachs to foundations like the Laura and John Arnold Foundation with investments by a single entity or organization ranging from a high of $13.5 million to a low of $435,000. Outcomes payors/traditional funders for the projects encompass a variety of state and local entities including the New York City Department of Corrections; Cuyahoga County, Ohio; Santa Clara County, California; the Commonwealth of Massachusetts; and Salt Lake County, Utah to name just a few. The report also sets forth the maximum amount of funds required to be repaid by the traditional funder/outcomes payor; the name of the evaluator; the contract period; and the circumstance that triggers repayment. Anyone interested in participating in PFS funding in any capacity should review this report.

SOCIAL IMPACT PARTNERSHIPS TO PAY FOR RESULTS ACT (SIPPRA)

As is indicated by the name, SIPPRA addresses social impact partnerships, which include PFS projects. As defined by the Act, the "social impact partnership model" means a method of financing social programs in which: (1) federal funds are awarded to a state or local government if agreed-upon outcomes are reached; and (2) the state or local government partners with service providers, investors, and an intermediary to identify: (a) an intervention expected to produce the desired outcomes; (b) a service provider to deliver services to the desired population; and (c) investors to fund the initial start of the program.

The Act requires that projects produce "one or more measurable, clearly defined outcomes that result in social benefit and [f]ederal, [s]tate, or local savings…" Projects can be designed to produce results in areas related to: increasing employment and earnings, improving rates of high school graduation, reducing dependency on federal benefits, reducing unplanned pregnancies, improving conditions for children across various fields and services (*e.g.*, early childhood education, improving health, foster care, and the like), reducing homelessness, increasing financial stability for low-income families, and "other measurable outcomes defined by the [s]tate or local government that result in positive social outcomes and [f]ederal savings."

State or local governments interested in SIPPRA funding must file an application (available through a Notice of Funding Availability (NOFA) at https://www.grants.gov/).

The Secretary of the Treasury must grant or deny an award within six months of the application. The Act will also award funds for the purpose of conducting a feasibility study to determine if a proposed project is more likely than not to achieve the desired outcomes.

The Act appropriates $100,000,000 to be apportioned over a ten-year period for the purpose of funding accepted projects and other expenditures authorized by the Act.

NONPROFIT FINANCE FUND® (NFF)®

Founded in 1980 as the Energy Conservation Fund, NFF was one of the forerunners in the field of PFS funding of social programs in the United States. Throughout its 40-year history, NFF has helped nonprofits by providing funding, technical assistance, and insights gained through its presence in the industry. In 2011, shortly after the start of the Peterborough Prison program, NFF developed and launched its Pay for Success Learning Hub which helped spread the word about this new funding approach. NFF owned and operated the hub for nine years. During that time, NFF provided consultations to, and invested in, PFS-funded programs across the country. Per its website, NFF "conducted more than 250 PFS trainings, presentations, webinars, workshops, and convenings … for service providers, governments, and investors." Since its foray into the PFS arena, NFF has worked with the James Irvine Foundation, the Corporation for National & Community Service, the Social Innovation Fund, and the Laura and John Arnold Foundation to provide funding, technical assistance, and help launch PFS-funded programs by organizations seeking to reduce recidivism, support the homeless, improve child and maternal health and welfare, and provide job opportunities to people re-entering the workforce. NFF has a number of resources and helpful videos on its website, which can be found here: https://nff.org/invest-in-results.

Nonprofit Finance Fund®

SOCIAL FINANCE US

Social Finance US is the sister corporation of Social Finance UK, the original PFS funder in the Peterborough Prison project. Founded in 2011, Social Finance US has spent the last ten years working with projects across the country in five main areas: (1) economic mobility; (2) health (3) children and families; (4) criminal justice; and (5) education. Since its inception in the United States, Social Finance US has launched social impact bonds across the country and paid more than $150 million toward outcomes.

In October 2020, Social Finance US, along with the city of Anchorage, Alaska, the United Way of Anchorage, and more than 20 other government, nonprofit, and philanthropic organizations, began collaborating on a three-year project to help 150 residents of Anchorage with chronic homelessness. People who suffer from persistent homelessness tend to also have mental health issues and are high users of emergency services. The goal of the program, named Home for Good (HFG), is to improve housing stability, improve the physical and mental health of the participants, and reduce interactions with emergency services and the criminal justice system. The program is designed so that investors provide the initial capital, and the United Way of Anchorage and other service providers furnish the services. If the outcomes are achieved as determined by a third-party evaluator, the city of Anchorage will make payments which will then be used to continue the services. More about the project can be found here: https://socialfinance.org/project/home-for-good/.

URBAN INSTITUTE

Although the Urban Institute does not provide PFS funding of social programs, it has been instrumental in studying the initiative and promoting it as a viable option for social programs in need of funding. Its website dedicated to PFS, https://pfs.urban.org/, includes multiple sources of information for projects and communities considering PFS funding, including evaluation and early childhood education toolkits. It also provides guidance on developing a team, collecting data, and performance-based strategies. Although the site is no longer updated, it still contains a wealth of information for parties interested in PFS funding.

CONCLUSION

Although the PFS funding initiative is still relatively new, being just over ten years old, it has a presence in 32 countries and has helped fund more than 180 programs to address social issues worldwide.

RESOURCES

Found in the White House Archives for President Barack Obama, [Pay for Success: An Opportunity to Find and Scale What Works] includes an overview of PFS programs and an extensive list of additional resources, including the Office of National Drug Control Policy Resource Guide, [Deploying the Pay for Success Model to Help Address the Opioid Epidemic in the United States: An Opportunity for State and Local Action].

The U.S. Department of Treasury [website] includes information on SIPPRA including an FAQ section and information regarding funding availability.

Other resources include:

"Pay for Success: The First 25," Nonprofit Finance Fund, last modified May 2019, www.nff.org/report/pay-success-first-25.

"Invest in Results," Nonprofit Finance Fund, accessed February 9, 2021, www.nff.org/invest-in-results.

"What is pay for success (PFS)?" Urban Institute, accessed February 9, 2021, www.pfs.urban.org/pfs-101/content/what-pay-success-pfs.

"What is Pay for Success?" Social Finance US, accessed February 9, 2021, www.socialfinance.org/what-is-pfs/.

Amanda Silver and Aishatu Yusuf, "The History and Future of the Pay for Success Field," last modified February 17, 2016, www.evidentchange.org/newsroom/nccd-blog/history-and-future-pay-success-field.

"Peterborough," Social Finance UK, accessed February 9, 2021, www.socialfinance.org.uk/peterborough-social-impact-bond.

Brinda Ganguly, "The Success of the Peterborough Social Impact Bond," The Rockefeller Foundation, last modified August 8, 2014, www.rockefellerfoundation.org/blog/success-peterborough-social-impact/.

ABOUT LEGISLATIVE ANALYSIS AND PUBLIC POLICY ASSOCIATION

The Legislative Analysis and Public Policy Association (LAPPA) is a 501(c)(3) nonprofit organization whose mission is to conduct legal and legislative research and analysis and draft legislation on effective law and policy in the areas of public safety and health, substance use disorders, and the criminal justice system.

LAPPA produces up-to-the-minute comparative analyses, publications, educational brochures, and other tools ranging from podcasts to model laws and policies that can be used by national, state, and local criminal justice and substance use disorder practitioners who want the latest comprehensive information on law and policy. Examples of topics on which LAPPA has assisted stakeholders include naloxone laws, law enforcement/community engagement, alternatives to incarceration for those with substance use disorders, medication-assisted treatment in prisons, and the involuntary commitment and guardianship of individuals with alcohol or substance use disorders.

For more information about LAPPA, please visit: https://legislativeanalysis.org/.