An Introduction to Social Impact Bonds

Cason Schmit, J.D.
ORISE Legal Fellow

Public Health Law Program
Office for State, Tribal, Local and Territorial Support
Centers for Disease Control and Prevention

April 2014
Disclaimer

The contents of this presentation do not represent official CDC determinations or policies.

The findings and conclusions in this report are those of the author and do not necessarily represent the official position of the CDC.

The contents are for educational purposes only and are not intended as a substitute for professional legal advice.

Always seek the advice of an attorney or other qualified professional with any questions you may have regarding a legal matter.
Innovations in Public Health Financing

INTRODUCTION TO SOCIAL IMPACT BONDS
Presentation Overview

- A social impact bond (SIB) analogy
- What are SIBs and why are they important?
- Considerations in creating a SIB program
- SIBs in progress and new applications
- Laws and proposed laws addressing SIBs
- Concluding remarks
- Questions
The Deal

- **Problem**
  - Cost of 30 new energy efficient bulbs is $120

- **Offer**
  - I replace all of your bulbs for free
  - You give me nothing upfront

- **Catch**
  - If you get energy savings of $200 ($100 per year for 2 years), then you give me $150 after 2 years
  - If not, I get nothing and take my bulbs back and return your old bulbs
The Deal: A Positive Resolution?

- Results if successful
  - For you
    - Total cost: $150
    - Total savings: $200
    - Net benefit: $50
  - For me
    - Total cost: $120
    - Total income: $150
    - Return on investment: 25%

- Result if unsuccessful
  - For you
    - Go back to old bulbs
  - For me
    - Stuck with new bulbs and costs
Pay for Success

- Pay for success (PFS) arrangements
  - Payments are based on program outcomes
    - example: SIBs
Current Problems in Social and Public Health Services

- Limited resources
- Focus on remediation not prevention
- Pay for services
  - Services may not achieve desired outcomes
- Lack of data on effectiveness of programs
Significance of PFS and SIBs

- Social ills and public health problems cost money
  - Example: Homelessness ($6–7 billion)$^1$
    - Shelter costs
    - Welfare
    - Medicaid
    - Etc.
  - Many governments lack the funding needed to address problems

- PFSs and SIBs can transform those costs into potential profit
  - If profitable, PFSs and SIBs can leverage large amounts of private capital into Social and Public Health Programs

- Can create a public policy trifecta
  - Win-win-win for government, private sector, and vulnerable populations

What Are SIBs?

- **Definition**
  - Financing mechanisms used to raise upfront funding for social and public health preventative interventions from private investors
  - Leverage the anticipated savings due to prevention as a source for financial rewards to the investors
  - Rewards due if and only if the intervention succeeds in reaching predetermined benchmarks, thereby shifting the financial burden of success to the investors

- **Definitional problems**
  - Difficulties: novelty, flexibility, complexity, and terminology
### Why Is This Model Attractive?

<table>
<thead>
<tr>
<th>Governments</th>
<th>Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Limited financial risk</td>
<td>Philanthropic investors</td>
</tr>
<tr>
<td>Funds prevention/outcomes</td>
<td>• Performance evaluated</td>
</tr>
<tr>
<td>Potential budget savings</td>
<td>• Opportunity to scale initiatives</td>
</tr>
<tr>
<td>Encourages efficiency</td>
<td>• Program-related investments</td>
</tr>
<tr>
<td></td>
<td>• Fosters collaboration</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Intervention providers</th>
<th>Commercial investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stable multiyear funding</td>
<td>• Promising new market for commercial profit</td>
</tr>
<tr>
<td>Builds relationship with government</td>
<td>• Growth to social services</td>
</tr>
<tr>
<td>Amplify impact</td>
<td></td>
</tr>
</tbody>
</table>

| Intervention recipients | |
|-------------------------| |
| Access to needed programs | |


Promising SIB Applications

- Recidivism
  - UK, NYC, MA, NY
- At-risk youth services
  - UK, NY, MA, Australia
- Homelessness
  - UK, MA
- Workforce development
  - U.S. Dep’t of Labor
- Early childhood services and education
  - Salt Lake City, Utah
- Pre-natal care
  - SC
- Asthma reduction
  - Fresno, CA
- Diabetes
  - Israel
- Elderly services
  - UK, S. Korea
- Others likely in the future

A Structural Example

SOCIAL IMPACT BONDS
An intermediary negotiates with SIB backer for SIB repayment terms
Intermediary seeks initial financing from private investors by issuing SIBs.
To make investment more attractive, intermediary can seek credit enhancement (CE) to lower the risk of failure to investors.
Similar to insurance, CE returns a portion of investment if SIB program fails.
Intermediary/Bond Issuers contracts with Intervention Provider.
Credit Enhancement

Investors/Bond Holders

Intermediary/Bond Issuers

SIB Backer

Provides intervention to target population

Target Population

Intervention Provider
At pre-determined times, independent entity evaluates the program’s success or failure.
If SIB Program Fails . . .
Evaluation reveals that program failed to reach benchmarks for success.
Backer not obligated to reimburse

Program Failure

credit enhancement

investors/bond holders

independent evaluator

intermediary/bond issuers

sib backer

target population

intervention provider
If used, CE partially repays investors, reducing impact of failure.
Investors suffer any additional loss

- Credit Enhancement
- Investors/Bond Holders
- Intermediary/Bond Issuers
- Target Population
- Intervention Provider

Program Failure:
- Independent Evaluator
- SIB Backer
If SIB Program Succeeds . . .
Evaluation reveals that program has reached success benchmarks.

- **Credit Enhancement**
- **Investors/Bond Holders**
- **Intermediary/Bond Issuers**
- **Target Population**
- **Intervention Provider**
- **SIB Backer**
- **Independent Evaluator**
SIB backer pays intermediary the cost of initial investment plus any agreed upon premium.
Intermediary repays SIB holders plus any due premium.
CONSIDERATIONS FOR CREATING A SIB
Considerations for a Successful SIB

- Definitions
- Evaluation
- Risk
- Potential savings
Considerations for a Successful SIB: Definitions

- The elements of the SIB should be carefully defined
  - Who is the target population?
  - What does success look like?
    - Outcome performance goals need to be
      - Clear
      - Objective
      - Measurable
      - Non-debatable
      - Achievable
  - What can be “saved”? 


Considerations for a Successful SIB: Evaluation

- Independent evaluators
  - Intermediary may have own evaluators
- Reliable and valid methodology is crucial
  - Measurable evaluation criteria
- Evaluation critical to fair outcomes
Considerations for a Successful SIB: Risk

- Available data helps define the risks
  - Model – effectiveness of the intervention
  - Execution – effectiveness of the intervention as provided

- Proven v. promising
  - Focus on proven interventions minimizes the model risk
  - Promising interventions may still attract investors if potential return is significant
  - Some suggest SIBs use proven interventions until the SIB concept demonstrates success

- Credit enhancement
  - Strategies to improve the risk-benefit outlook for investors, e.g., insurance
Considerations for a Successful SIB: Potential Savings

- Significant potential savings are crucial to attract investors
- Important that SIB deliver savings in excess of cost
- Savings should be identifiable and supported by data
- Savings justify bringing interventions to scale
Illustration of Bankable Savings for Recidivism SIB

**SIB Considerations**

- **Legal issues**
  - Appropriations
  - Government “silos”

- **Standardization**

- **Other critiques**
  - Shifting attention and resources away from other important problems
  - Possible investor influence over intervention delivery
  - Inherent inefficiencies
Current State of SIBs

SIBS IN PROGRESS AND NEW APPLICATIONS
United Kingdom – Inmate Recidivism

- World’s first SIB started in Peterborough in 2010
  - $8M initial investment raised by Social Finance
- Goal
  - Reduce inmate reoffending rate by 7.5%
  - Interim results (Nov. 2013)
    - 12% decrease recidivism in contrast with 11% increase nationally
- Intervention
  - Social services to 3,000 short-sentence male inmates
- Evaluation period
  - Outcomes evaluated years 4, 6, and 8


Nicky Stubbs, *Peterborough social impact bond seeing positive results*, Blue & Green Tomorrow (Nov. 2, 2013), available at 
New York City – Juvenile Recidivism

- In 2012, New York City launched the first SIB in the US
- Goals
  - Graduated benchmarks (8.5% to 20.0% recidivism rate reductions)
  - Payment range: $4.8M (8.5% reduction) to $11.7M (20% reduction)
- Intervention
  - Social services to 3,000 adolescent men per year through 2015
- Investment
  - MDRC raised $9.6M from Goldman Sacs
- Credit enhancement
  - Bloomberg Philanthropies providing $7.2M guarantee

Massachusetts – Homelessness

- **Goal**
  - Reduce costs associated with chronic homelessness, specifically costs associated with mental and physical health, jail use, and shelter use

- **Intervention**
  - Supportive housing for the chronically homeless

- **Evidence Supporting Intervention Model**
  - 2009 program found mean annual Medicaid costs dropped from $26,124, to $8,500 after supportive housing, estimated $1.7M in Medicaid savings


Fresno, California – Asthma Emergency Prevention

- Nongovernmental SIB arrangement
  - Financial stakeholders back the SIB

- Problem and intervention
  - Estimated $87M in annual costs associated with asthma emergencies
    - ED visits, hospitalizations, and lost worker productivity
  - Targeted home based interventions to reduce asthma triggers

- Costs
  - Intervention expected to lower healthcare costs of target population 41%

- Estimated financial savings to backers
  - Medi-Cal ($3M), local employers ($2.3M), healthcare providers ($1M )


South Carolina – Early Childhood Services

- 2013 study suggests that a PFS is a feasible mechanism to improve early childhood outcomes

- Intervention: nurse–family partnerships (NFP)
  - House visits and services to first-time, low-income mothers

- Measurable outcomes
  - Measurable improvements possible in health, education, and family prospects
  - Pre-term births suggested as a “bellwether” index

---

Israel and Type 2 Diabetes

- Proposed intervention
  - One-year intensive intervention and two-year follow-up
    - Healthy living and personal fitness programs to high-risk pre-diabetics

- Measurement
  - Number of type 2 diabetics relative to a control group
  - Number of healthy states produced relative to a control group

- Outcome payments
  - Reduction in medical expenditures
  - Reduction in disability expenditures
  - Increase in economic productivity

EXISTING AND PROPOSED LAWS
Examples of Existing Laws

- **California**
  - *Cal. Welf. & Inst. Code* § 14127.4
    - Enables state to “enter into risk-sharing and social impact bond program agreements”

- **Connecticut**
    - Authorizes use of “social investment vehicles”
    - Creates social innovation account

- **Massachusetts**
    - Pay for performance obligations constitute “general obligations” backed by “the full faith and credit of the commonwealth”
Examples of Existing Laws (Cont.)

- **Minnesota**
  - Pay for Performance Act – MINN. STAT. ANN. § 16A.93 et al.
    - Pilot program to test “feasibility and desirability of using state appropriation bonds to pay for certain services based on performance and outcomes for the people served”
    - Creation of special appropriation bond proceeds account

- **Pennsylvania**
  - Innovate in PA Fund – 72 PA. STAT. ANN. § 8811-F (c)(2)
    - Enables consideration of “impact investments based on performance”
Examples of Proposed Laws

- California Senate Bill No. 593 (2013)
  - Requires director of the Office of Planning and Research to identify at least three proposed social impact partnerships to the Legislature each year.

- California Senate Bill No. 594 (2013)
  - Workforce Development Bond

- Hawaii House Concurrent Resolution No. 119-13 (2013)
  - Requested feasibility study for SIBs to fund early learning programs
Examples of Proposed Laws (Cont.)

- **Maryland Senate Bill No. 434 (2013)**
  - Request for proposals

- **Maryland House Bill No. 517 (2013)**
  - State Board of Education – Request for Proposals for SIBs

- **Nebraska Legislative Resolution No. 279 (2013)**
  - Requires the legislative Judiciary Committee to conduct an interim study of SIBs

- **New Jersey Assembly Bill No. 3289 (2012)**
  - Five-year SIB pilot program and study
Examples of Proposed Laws (Cont.)

- Texas Senate Bill No. 1788 (2013)
  - Requires a prevention committee to advise on use of SIBs to finance child abuse prevention programs

- Rhode Island Senate Bill No. 2196 (2013)
  - Five-year SIB pilot program

- Vermont House Bill No. 625 (2011)
  - Authorizes committee to determine whether SIB opportunities exist

- Washington House Bill No. 2337 (2013)
  - Establishes social investment steering committee

  - Social Impact Financing Amendment Act of 2013
Alberta, Canada
- 2014 – Bill 1 creates $1B Endowment for Social Innovations

2014 Bill 1, Savings Management Act, Second Session, 28th Legislature, 63 Elizabeth II (2014)
Announcements: Putting Alberta’s growing savings to work for our future, (Mar. 4, 2014) (avail.
Social Impact Bond Viability

CONCLUDING REMARKS
Market Viability of SIBs

From the McKinsey & Co. United States SIB market analysis

“Our research suggests that SIBs have specific benefits and that the right conditions are in place today to implement SIBs: evidence-based social interventions already exist, there is sufficient stakeholder capacity, and there is real interest and momentum to make SIBs a reality. But turning potential into action will require a clear choice to move ahead and concerted effort to implement this new tool: stakeholders must overcome several challenges, a number of proof points must be demonstrated, and making SIBs more widespread will require some standardization.”

Early Evaluations

UK Justice Secretary Chris Grayling reacting to an interim report suggesting positive outcomes from world’s first SIB in Peterborough

- “The message is clear – our reforms are the right approach and will help us end the pernicious cycle of reoffending, keeping our communities safer.”

Selected Resources

- **CDC Public Health Law Program Research Anthology**

- **Descriptive**

- **Technical guides**

- **Commentary**
QUESTIONS?
Thank you!

Cason Schmit

Cschmit@cdc.gov

(404) 498-2387

For more information, please contact CDC’s Office for State, Tribal, Local and Territorial Support

4770 Buford Highway NE, Mailstop E-70, Atlanta, GA 30341
Telephone: 1-800-CDC-INFO (232-4636)/TTY: 1-888-232-6348
E-mail: OSTLTSfeedback@cdc.gov Web: http://www.cdc.gov/stltpublichealth

The findings and conclusions in this presentation are those of the authors and do not necessarily represent the official position of the Centers for Disease Control and Prevention.