The Next Frontier of Community Development: Pay for Success and Social Impact Bonds

Innovative Programmatic and Policy Responses to Poverty
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Winning Battles But Losing the War

Percent of Total Population below Poverty Level (Annual)

Source: U.S. Census Bureau
### Poverty Worst in Decades By Some Measures

<table>
<thead>
<tr>
<th>Measure</th>
<th>In 2010</th>
<th>Highest...</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share of overall population in poverty <em>(earning below $22,314 for a family of four)</em></td>
<td>15.1%</td>
<td>Since 1993</td>
</tr>
<tr>
<td>Number of people in poverty</td>
<td>46.2 million</td>
<td>On record*</td>
</tr>
<tr>
<td>Share of people below half of the poverty line</td>
<td>6.7%</td>
<td>On record*</td>
</tr>
<tr>
<td>Share of poor people below half of the poverty line</td>
<td>44.3%</td>
<td>On record*</td>
</tr>
<tr>
<td>Share of children in poverty</td>
<td>22.0%</td>
<td>Since 1993</td>
</tr>
<tr>
<td>Share of adults aged 18 to 64 in poverty</td>
<td>13.7%</td>
<td>Since 1966</td>
</tr>
<tr>
<td>Share of people living in suburbs in poverty</td>
<td>11.8%</td>
<td>Since 1967</td>
</tr>
</tbody>
</table>

Source: Center on Budget and Policy Priorities, U.S. Census Bureau
Rebuilding neighborhoods necessary but not sufficient
Human capital development key to solving poverty

Challenge: Current funding sources oriented towards real estate development not human capital development

Solution: Create new funding sources that pay for successful social outcomes (Pay for Success)
Presentation Outline

- What is Pay for Success (PFS)?
- Examples of PFS
- What are Social Impact Bonds (SIBs)?
  - Example #1: Early Childhood Education in Salt Lake
  - Example #2: Supportive Housing in Portland, OR
- Benefits of Pay for Success
- Pitfalls of Pay for Success
What is Pay for Success? Connecting Cash Flows

- Contract and financing structure to capture downstream government savings to fund upstream community investments.
Performance-Based Contracting

- Government commits funding for successful outcomes (i.e., increased graduation rates)
- Independent impact auditor evaluates program effectiveness
- Government only “pays for success”
Service Provider Financing

- Private investors fund service provider operating costs in exchange for a share of the success payment.

- Financing terms are based on:
  1. Difficulty of achieving success
  2. Track record of the service provider
  3. Length of the contract

- Investors bear the risk that success won’t be achieved (and that the government payment won’t be triggered).
Examples of Pay for Success

- Prize-based Philanthropy
- Low Income Housing Tax Credit
- Tax Increment Financing
- Energy Efficiency Financing
- Human Capital Performance Bond
- Social Impact Bond
3,500 low-income 3 and 4 year olds will be enrolled in the Utah High Quality Preschool Program and have their academic progress tracked from K-6 grade.

Children participating in the program will be given the Peabody Picture Vocabulary Test to determine how many, absent high impact preschool, would likely require special education services in the future.
SIB Example #1: Early Childhood Education in Salt Lake

- $4.6 million senior loan from Goldman Sachs to United Way of Salt Lake.
- $2.4 million subordinate loan from J.B. Pritzker Foundation to United Way of Salt Lake.
- United Way of Salt Lake oversees implementation of the project and manages investor repayments.
- Every year of avoided special education generates a success payment of $2,470/child plus 5% interest to Goldman Sachs and J.B. Pritzker Foundation until senior and subordinate debt is fully repaid ($1,040/child thereafter).
Early Childhood Education in Salt Lake: Transaction Structure of the Utah SIB

1. FUNDING
2. LOAN REPAYMENT
3. SENIOR SOCIAL IMPACT LOAN
4. STREAM OF PAYMENTS TO FUND INTERVENTION
5. MEASURES IMPACT
6. DETERMINES SUCCESS PAYMENTS
7. LOAN REPAYMENT
8. SUCCESS PAYMENTS

Source: Goldman Sachs Bank USA and the Federal Reserve Bank of San Francisco
The Bud Clark Commons (BCC) provide apartments and services for homeless residents in Portland, OR.

Offer a full spectrum of services with an emphasis on:
- The integration of health and wellness services within a supportive housing program
- The “harm reduction model,” which prioritizes housing for the most vulnerable applicants and does not screen out residents who are struggling with addiction

Applicants must earn below 35% AMI to qualify.

Apartments are independent living and include full kitchens and baths.
# Bud Clark Commons: Health Care Costs Savings

## Cost Savings to Medicaid

(Per Person, 2013)

<table>
<thead>
<tr>
<th>Services Billed to Medicaid</th>
<th>Year Before Move-In</th>
<th>1st Year After Move-In</th>
<th>2nd Year After Move-In</th>
<th>3rd Year After Move-In</th>
<th>TOTAL SAVINGS AFTER 3 YEARS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inpatient Behavioral Health</td>
<td>$816</td>
<td>$132</td>
<td>$204</td>
<td>$168</td>
<td>$1,944</td>
</tr>
<tr>
<td>Inpatient Physical Health</td>
<td>$6,924</td>
<td>$3,696</td>
<td>$5,976</td>
<td>$2,256</td>
<td>$8,844</td>
</tr>
<tr>
<td>Outpatient Behavioral Health</td>
<td>$2,292</td>
<td>$1,884</td>
<td>$1,968</td>
<td>$2,004</td>
<td>$1,020</td>
</tr>
<tr>
<td>Emergency Department</td>
<td>$2,520</td>
<td>$1,044</td>
<td>$696</td>
<td>$300</td>
<td>$5,520</td>
</tr>
<tr>
<td>Outpatient Primary Care</td>
<td>$828</td>
<td>$732</td>
<td>$384</td>
<td>$348</td>
<td>$1,020</td>
</tr>
<tr>
<td>Outpatient Labs &amp; Radiology</td>
<td>$1,356</td>
<td>$648</td>
<td>$348</td>
<td>$384</td>
<td>$2,688</td>
</tr>
<tr>
<td>Outpatient Specialty</td>
<td>$6,096</td>
<td>$684</td>
<td>$684</td>
<td>$996</td>
<td>$15,924</td>
</tr>
<tr>
<td>Pharmacy</td>
<td>$1,380</td>
<td>$1,260</td>
<td>$912</td>
<td>$1,308</td>
<td>$660</td>
</tr>
<tr>
<td>Other</td>
<td>$1,872</td>
<td>$708</td>
<td>$792</td>
<td>$396</td>
<td>$3,720</td>
</tr>
<tr>
<td><strong>TOTAL ANNUAL COST</strong></td>
<td><strong>$24,084</strong></td>
<td><strong>$10,788</strong></td>
<td><strong>$11,964</strong></td>
<td><strong>$8,160</strong></td>
<td><strong>$41,340</strong></td>
</tr>
</tbody>
</table>

Source: “Integrating Housing & Health,” Center for Outcomes Research and Education (2014)
Bud Clark Commons: PFS Project Cost/Benefit Analysis

Illustrative Three-Year PFS Project
(Serving 59 People)

- Total Savings to Medicaid: $2.44M
- Total Service Cost (59 Adults): $2.05M
- Cost of Impact Evaluator: $103K
- Net Savings Generated by SIB: $290K
- Investor Return (7%): $145K
- Net Savings to Taxpayers: $145K

Principal repaid to investors: $2.15M

Source: “Integrating Housing & Health” (2014) and Federal Reserve Bank of San Francisco
Benefits of Pay for Success

Encourages Social Sector Innovation
- Outcomes-based payments mean nonprofits “sell” success
- Entrepreneurship necessary to compete in the marketplace

Promotes Evidence-based Policy
- Moves us from inputs/outputs to outcomes
- Government only pays for what works

Builds on Success ofExisting Public/Private Investment Model
- $80B in CRA capital, public programs, and private funds
- Low Income Housing Tax Credit example

Supports Holistic Community Development
- Success of community quarterback model but no investment vehicle
- Harlem Children’s Zone, Purpose Built, Strive, Neighborhood Centers Inc., Magnolia Place, LISC New Communities Program
Pitfalls of Pay for Success

Legitimacy of Data Collection and Use
- Pressure on all sides to fudge data

Tying Savings to Payments
- Hard to extract savings from public budgets (may reduce prison overcrowding but hard to close prisons)
- Continuing need to fund prevention

Government Capacity and Appropriations Risk
- Is government ready for this?
- Underwriting appropriations risk may make deals impossible

Ethical Considerations
- The most savings may not equal the most good
- Perverse incentives, careful oversight needed
Thank You!

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