



SOCIAL IMPACT BONDS

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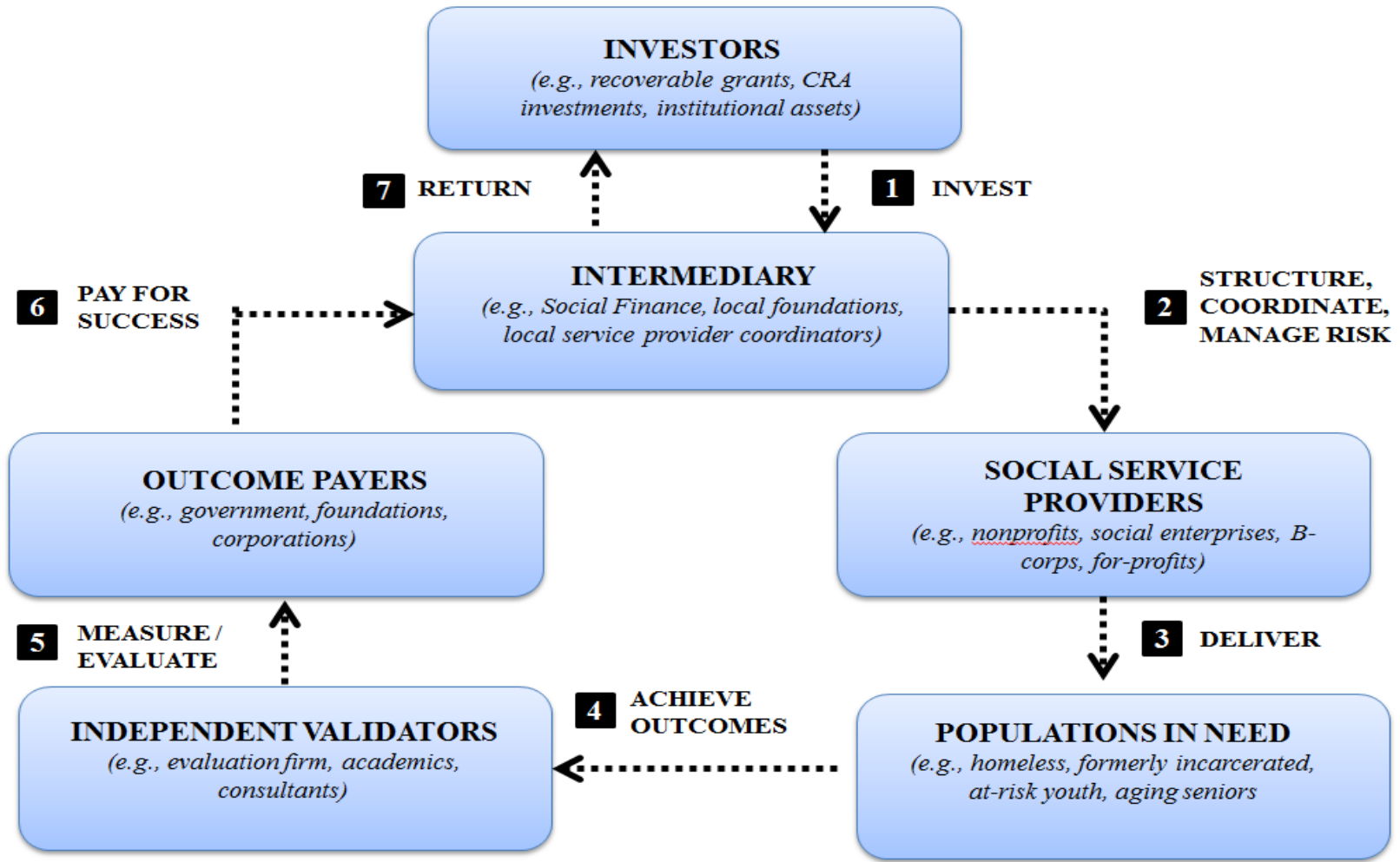


What is a Social Impact Bond (SIB)?

- An innovative financing mechanism in which government and/or commissioners enter into agreements with social services providers and investors and pay for the delivery of pre-defined outcomes (Social Finance 2011; OECD, 2015).
- Implemented as well in developing countries as **“Development Impact Bonds (DIBs)”**
- Also known as **“Pay-for-Success”** contracts (USA) or **“Social Benefit Bonds”** (Australia)



The mechanism



Source: OECD (2015) adapted from Burand (2013)



Main Stakeholders & their Role

- **Government or Commissioner:** Commissions the SIB (although not exclusively) and is the ultimate outcomes payer. It may also determine the outcomes metrics and payments terms.
- **Investors:** Provide funding for the intervention.
- **Intermediary:** May acts as a convener of all stakeholders involved in the mechanism in order to reach an agreement on the SIB contract. May be responsible for raising capital, structuring, managing, and/ or initiating the deal.
- **Service provider:** Responsible for the delivery of the social services, the attainment of agreed outcomes, potentially the provision of data related to them.
- **Evaluator:** Assesses whether the agreed outcomes have been attained. It could be an independent evaluator or an advisor for setting up the outcome metrics
- **Legal advisors:** Provide legal advice and help to structure the SIB deal



SIBs Models & Structures

1. The SIB model

- Individual transaction SIB
- SIBs Funds (for multiple outcome payment contracts- oftentimes around the same issue)
ex. Innovation Fund, Fair Chance Fund (UK)

2. The structures for SIBs contracts

- Direct
- Intermediated
- Managed



SIB Structures

1. Direct

- The delivery contract signed between the outcomes-payer and service provider or a services provider-controlled Special Purpose Vehicle (SPV).
- Service provider is responsible for the implementation of the deal & the performance management.
 - He holds the greatest amount of responsibility.
- Intermediary is responsible for raising capital, structuring the deal and determining its feasibility.

2. Intermediated

- The delivery contract is signed between the outcomes payer and the investor or an investor-controlled SPV or an intermediary
- Intermediary identifies and contracts the service provider, supports the performance management process and refines the financial model
 - In some instances, the intermediary can also invest in the SIB



SIB Structures (cont.)

3. Managed

- Delivery contract signed between the outcomes-payer and the prime contractor (usually an intermediary) or an intermediary-controlled SPV.
- Intermediary (or its SPV) manages the entire SIB development process.
 - The process is similar to the intermediated SIB, in terms of the activities of the intermediary.

* Main difference with the intermediated structure seems to be that under the managed structure the intermediaries have not invested in SIBs directly so far.

➤ *Yet, these are only 3 structures. There is enormous flexibility in the way an impact bond can be structured and wide variation in the roles of the various stakeholders.*



SIBs Geography & Scope

- **60 SIBs** are at the implementation stage in various countries
- **61 SIBs** are at the design stage
- **Policy areas:**
 - Homelessness, crime & recidivism, youth unemployment & NEETs, early childhood development, child welfare, workforce development, foster care, refugees, reduction of drop-outs from school, supporting single mothers at risk, family support



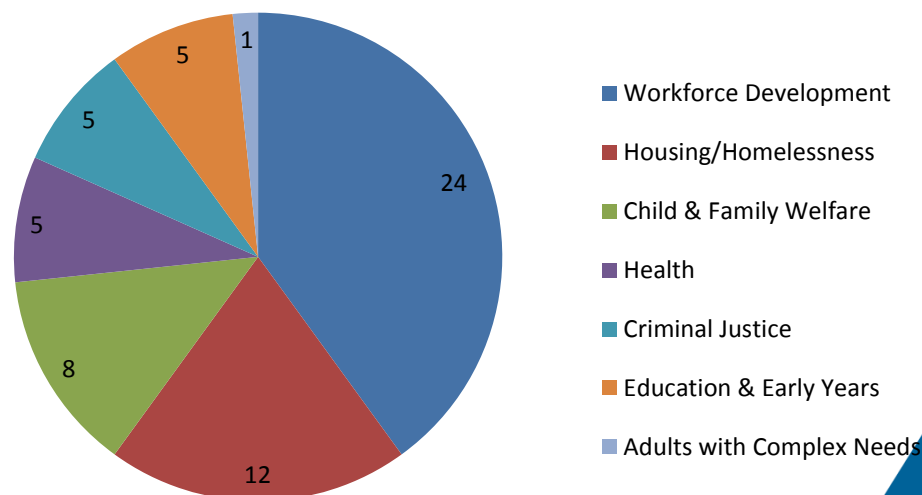
SIBs Implemented per Country & Policy Area

Country	SIBs
Australia	2
Austria	1
Belgium	1
Canada	1
Finland	1
Germany	1
India (DIB)	1
Ireland	1
Israel	2
Netherlands (the)	5
Portugal	1
South Korea	1
Switzerland	1
UK	31
US	10

54 SIBs have been implemented to date in 15 countries (including 1 DIB)

***At least 61 new SIBs are at the design stage**

SIBs per policy area



Source: Instiglio & Social Finance databases, 2016



Opportunities/Advantages

- **Finance**
 - **Capitalise on private funds targeting social outcomes** in times of budgetary constraints (and not only).
 - **Transfer outcome performance risks & upfront costs** to investors.
 - **Provision of upfront capital to social services providers** and multi-year revenue stream.
- **Social Outcomes & Measurement**
 - Nurture a **culture of monitoring & evaluation**.
 - Possibility to **focus more on preventive interventions** and not only on remedial ones.
 - **Build the evidence base on what works** and potentially take it to scale.



Opportunities/ Advantages (cont.)

- **Social Services Delivery**
 - **Stimulate innovation** in social service delivery without using immediately the public finances.
 - **Shift the policy focus** for social services from outputs to outcomes.
 - **Transparency, accountability and cost-effectiveness** of public spending for social service delivery.
 - **Foster collaboration** among diverse stakeholders & government levels (national, regional, local).



Challenges/ Disadvantages

- **Finance**
 - Unexpected **transaction costs**
 - **Annual budget cycle** constraints
 - **Wrong pockets** issue (vertically, horizontally)
 - Determining **payment schedules & outcomes pricing**
 - **Risk allocation & guarantees**
- **Social Outcomes & Measurement**
 - Identify **measurable outcomes & target groups**
 - Design a rigorous **measurement methodology**
 - Avoid **perverse incentives** (“cherry picking”, “cream skimming”)



Challenges/ Disadvantages (cont.)

- **Social Services Delivery**
 - **Engagement of large social services providers quite** often rather than small ones
 - Existence of **enough of social services providers** that are tender ready
- **Regulation**
 - Eventual **regulatory reforms** may be required in terms of procurement, taxation, investment regime.
 - Capacity of social services providers to actually deliver public services
- **Political considerations**
 - **Political impetus & long-term commitment** is needed regardless of electoral cycles or government fluctuation.
 - Reserve **“step in rights”** in order to ensure social service delivery continuity in case of a SIB failure.



When you design a SIB keep in mind that..

- SIBs are :
 - fairly **new financial instrument** with limited evidence regarding their results: **further analysis is needed in order to develop a robust evidence base**
 - **complex instruments**, involving multiple stakeholders from different sectors. **Time, technical expertise and commitment to collaborate are indispensable**
 - **costly instruments** so far with significant transaction costs (expected to drop). Policy makers should **evaluate carefully the value added to implement a SIB compared to a more traditional approach.**



When you design a SIB keep in mind that.. (cont.)

- Providing **a conducive ecosystem and a sound regulatory framework** are essential steps in the establishment of SIBs as they need to work into specific national contexts.
- The level and **depth of experience in payment-by-results contracts and performance management methods** by all stakeholders need to be considered. This expertise seems to be more specific to some countries than others.
- SIBs seem **more appropriate for policy areas** in which there are **target groups that can be easily identified**, when there are **measurable outcomes**, and when **investors are familiar with non – profits, social enterprises and social policies**.
- Although there is a strong emphasis on the role that SIBs can play in preventive interventions, it remains important for the public authorities to address them directly as well.



When you design a SIB keep in mind that.. (cont.)

- SIBs may be a **risky endeavour** due to lack of precedent and may entail “failures” in financial and social terms. Still, “failure” can be a relative term.
- The government may need to step in and ensure the continuity of social services in case of a SIB failure. Therefore, it may be more appropriate to view **SIBs as complementary rather than a core mechanism for social services delivery.**
- While SIBs have achieved interesting results in some policy areas and triggered debates that can help reflect on how social services are being financed and delivered, **additional knowledge and sound evidence need to be generated in order to reduce controversies around SIBs.**



Budgetary considerations

- Conduct a costs and benefits analysis of the project
 - This is required to confirm **whether the proposed SIB makes sense for the government.**
 - This analysis also informs decisions about **how much to pay at different levels of performance** since governments will generally want payments not to be greater than the benefits produced.



Budgetary considerations (cont.)

- **Build a model of payment schedule options**

Potential features:

- No payments until a minimum performance threshold is reached.
- A range where payments increase with better performance.

*Because payments for performance payments may be capped, by the budgetary authority, it is important to establish a point at which the maximum payment is reached and above which payments no longer rise with performance.

➤ **Good practice**

In preparing for negotiations with private sector partners, it is useful to augment the payment schedule model with a probability distribution of outcomes in order to understand how the expected payment to investors varies under different payment schedules.



Budgetary considerations (cont.)

- **Build a model of project cash flows incorporating**
 - The number of people to be served each year and the cost of that service.
 - The timing of the investor payments that finance service provision.
 - The timing of government performance payments.

➤ **Good practice**

Governments will generally want to insist that the full funding commitment necessary to provide service for the duration of the project be in place at the beginning, so that there is no risk that the project will be shut down mid-stream because of lack of funds.



Budgetary considerations (cont.)

- **Obtain authority from the legislative body**
 - In most governments, appropriated funds must be spent within the current fiscal year.
 - Pay-for-success contracts span several years and governments need a mechanism to commit to making the success-based payments in the future. The specific mechanism to accomplish this will vary depending on the country.



Budgetary considerations (cont.)

Example

- In Massachusetts, USA, legislation was enacted that **gives the Secretary of Administration and Finance the authority to enter into up to \$50 million in pay for success contracts (SIBs)** backed by the “full faith and credit” of the Commonwealth.
- In addition, the legislation establishes a **sinking fund** and requires the Secretary to request appropriations in each year equal to the maximum performance payments that may ultimately be needed based upon the services delivered in that year.
- **This helps ensure that funds are available when performance payments are due, and avoids the need for large one-time appropriations in payment years in one fiscal year.**



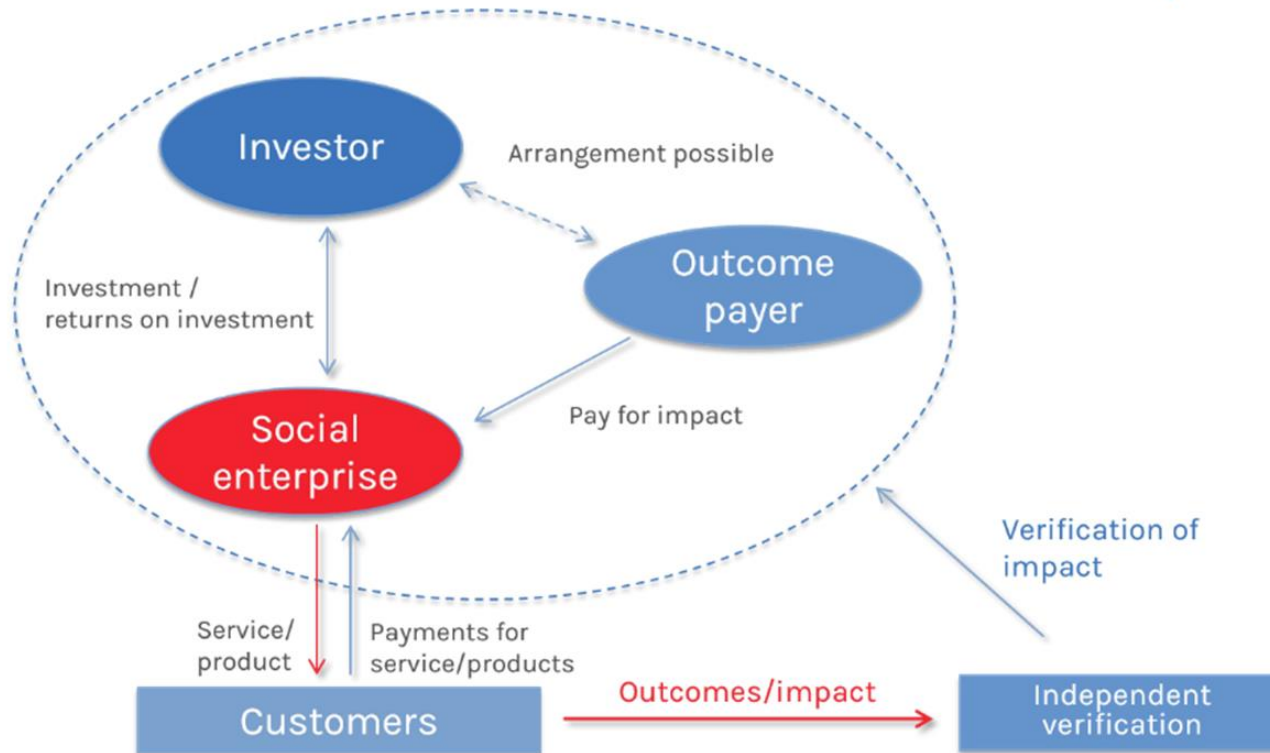
Alternatives to SIBs

- Direct government funding to tackle a social challenge
- Public procurement/ outsourcing to social services provides
- Payment- by-Results contracts directly with social services providers without involving investors
- Community Bonds (Canada)
- Social Impact Incentives (Siinc) (Switzerland and developing countries)



Social Impact Incentives (SIINC)

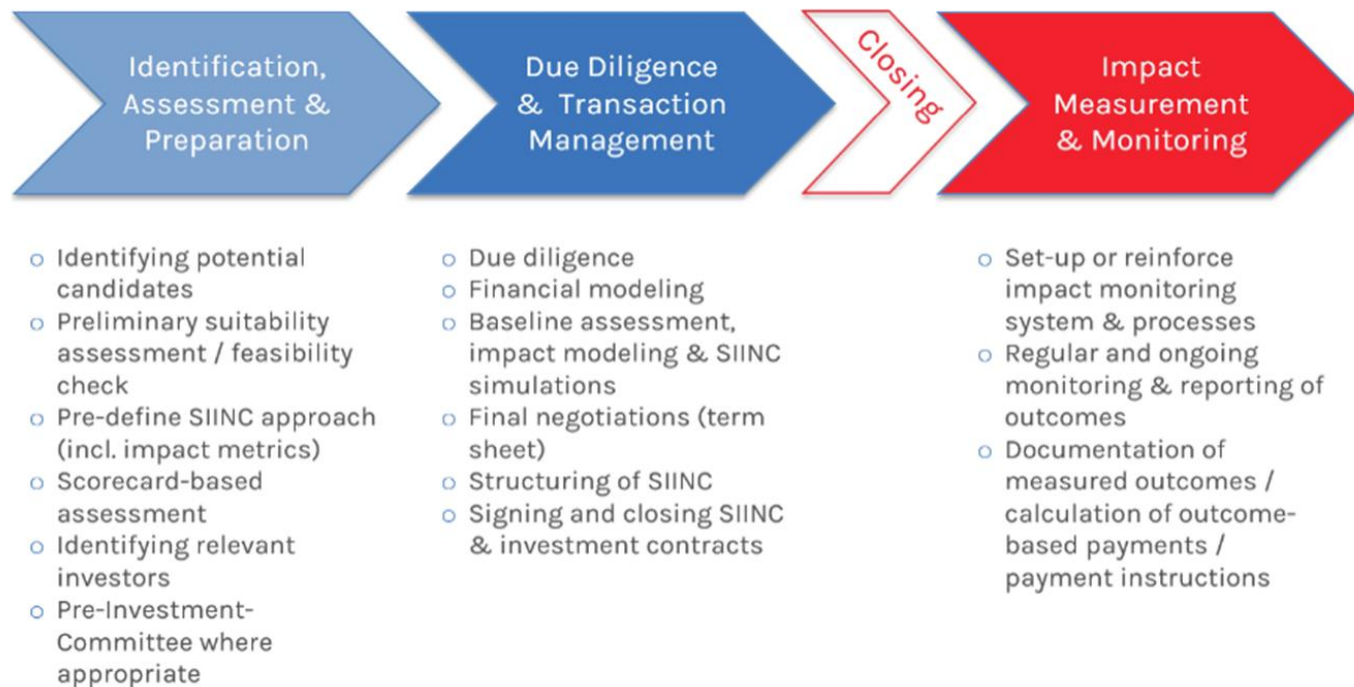
The SIINC Model





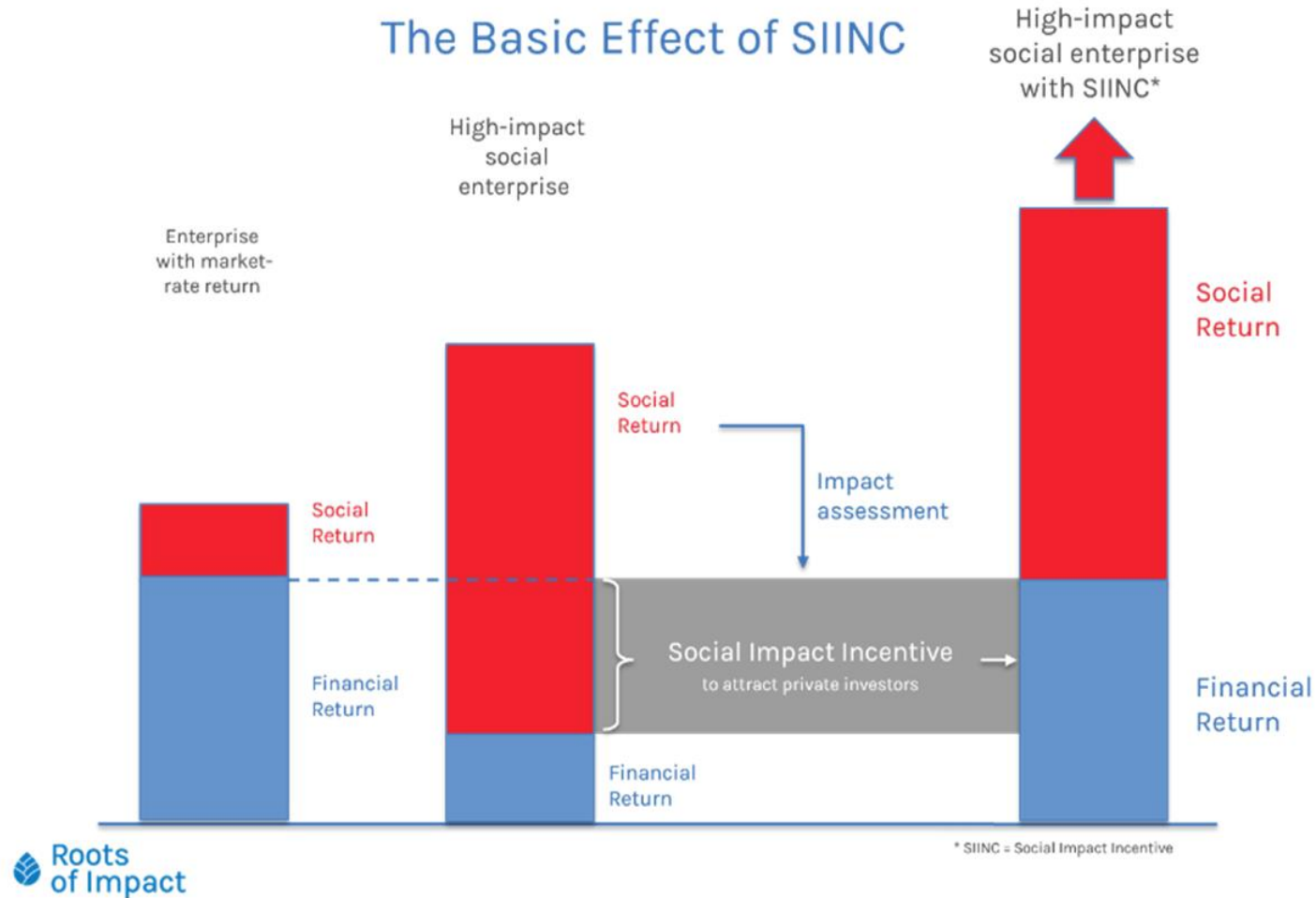
Social Impact Incentives (Siinc) (cont)

SIINC Implementation Steps (Example)





Social Impact Incentives (Siinc) (cont)





For more information

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