

Changes in Philanthropy: Emerging Outcomes Based Funding Environment

Presented for:

**Children & Families Commission of Orange County
Annual Planning Meeting**

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NFF as Trusted Advisor – 30+ Years Linking Money to Mission



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|--|--|
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NFF: Supporting Field Development and Investment Readiness for Outcomes Based Funding



Act as an independent, honest broker to the “PFS” field

- Support various PFS approaches and stakeholders as they explore this new “outcomes-based” financing model
- Spread recognition of why and how the PFS outcomes-based financing approaches can be effective
- Identify, disseminate and support PFS structures that can work
- Build and manage structured partnership initiatives for accelerated learning and application of PFS among stakeholders
- Incubate and accelerate providers’ capacity to thrive in an outcomes-based environment

Establish a centralized and interactive education platform for information, best practices sharing and dialogue on PFS – the NFF *Learning Hub*: www.payforsuccess.org

Outcomes-based Finance: The Missing Hub in the Wheel of Systemic Change?



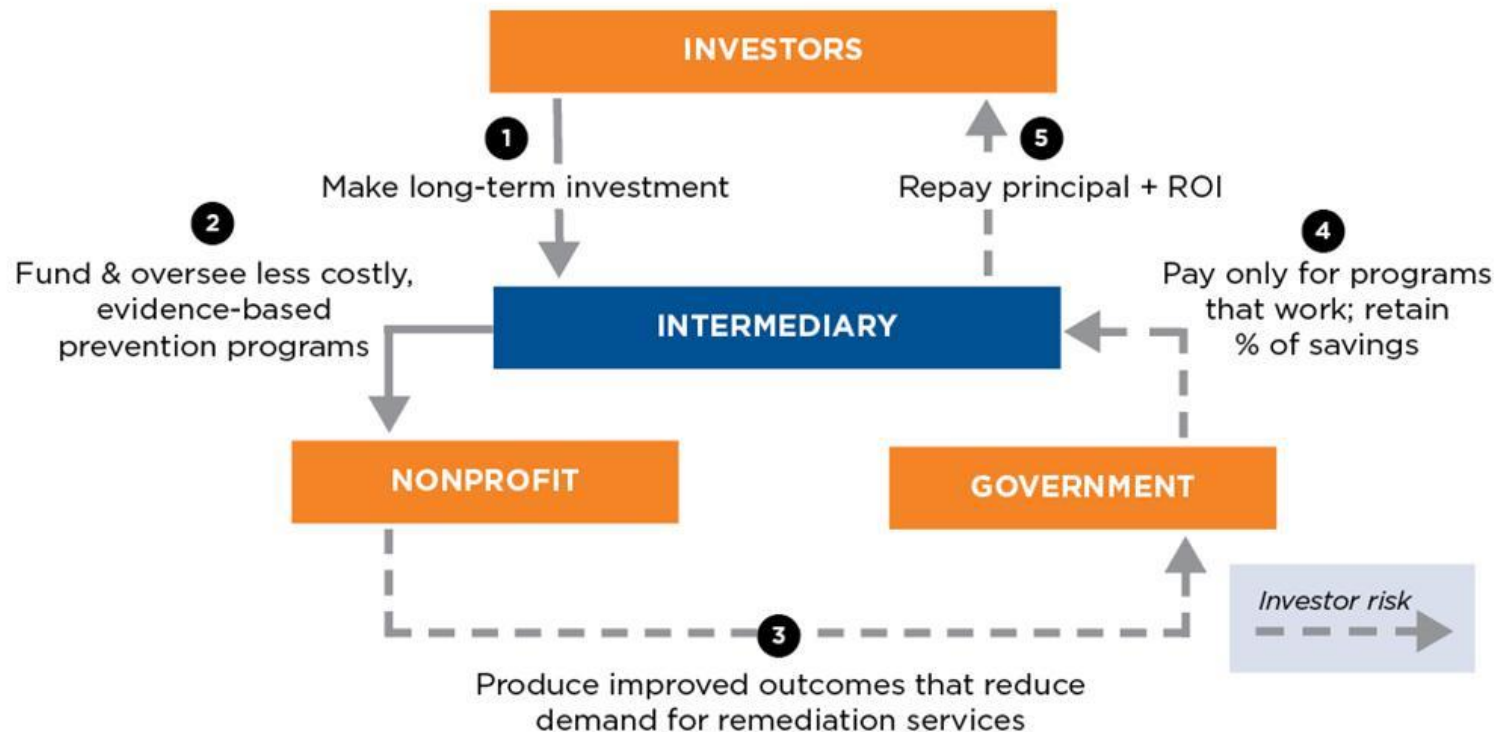
Pay for Success: A Model that Drives Towards Outcomes

- **A *contract* (not necessarily a bond) that:**
 - Connects performance outcomes to financial return
 - Monetizes social impact/outcomes
 - Realizes costs savings (typically for government)
 - Leverages private capital
- **Innovative integration** of evolving practices (i.e., pay for performance, outcomes measurement) in the social sector at an opportune time– ***aligns interests in achieving social outcomes***
- **Social Impact Bond** is one of potentially many ways to *capture the embedded values and linkages of **pay-for-success financing***

Pay for Success: How a Transaction “Flows”

Original and piloted structure (Peterborough) effectively creates and incentivizes mutual interest in achieving outcomes

FIGURE 1 SOCIAL IMPACT BOND MECHANICS



Source: Social Finance USA: Adapted from Jeffrey B. Liebman, "Social Impact Bonds," Center for American Progress (February 2011)

Pay for Success: Embedded Values



Pay For Success: US Market Evolution



Summer 2012

- New York City – launched first fully-funded Social Impact Bond (SIB) transaction in U.S.
- Massachusetts – announced two SIB contracts (*unfunded*)
 - One contract to address recidivism among youth
 - Second contract to address chronic homelessness in Boston area

2013-2014

- First Early Education SIB Pilot Announced (Salt Lake City)
- NY State SIB launched
- MA ROCA transaction launched

Today

- Over 30 State, County and Municipal Governments Assessing Feasibility and Developing Pay-for-Success Projects
 - *Intervention under consideration in Chicago, Philadelphia, SC, MI, CA, CO, IL, OR, VT, NJ*
 - *NFF/Irvine CA PFS Initiative*
- Pay-for-Success being incentivized at the Federal Government Level
 - Federal Budget Proposals
 - Department of Labor - \$20 million
 - Department of Justice - Second Chances Act (recidivism reduction)

Promising Programs & Approaches in the Early Childhood Space



| Programmatic Approach | Organization | Target Population | Outcomes |
|--|--|---|---|
| Pre-school setting with structured data tracking | Voices for Children Utah, Granite City School District | At-risk Preschool – age children | Reduction in need for special education services, education benefits include improved 3 rd grade scores. Longer term benefits include reduced crime, better wages. |
| Home visitation program by RNs | Nurse Family Partnership | Low-income, first time mothers & children | Improved prenatal health, intervals between births, maternal employment, child school readiness Fewer childhood injuries & subsequent pregnancies |
| Triple P (Positive Parenting Program) | Multiple | At Risk Families with children 0-8 | Reduced rates of child maltreatment, fewer foster placements, fewer hospitalization/ER visits for child maltreatment |
| Pre-school setting with structured data tracking | Pre-K Counts (multiple partners) | At Risk Preschool Children in PA | Improved kindergarten readiness |

- Goals of increasing access to preschool, increased school readiness and decreased use of special education services
- **Success payments tied to decreased use of special education services through 6th grade**
- Private capital enables 450-600 3 and 4 yr olds in yr 1 to attend pre-school; potential to reach over 3,5000 over 5 yrs
- Up to \$4.6M from Goldman Sachs and \$2.4M subdebt from J.B. Pritzker Foundation to finance an expansion of the Utah High Quality Preschool Program in Granite and Park City School Districts
- United Way of Salt Lake oversees preschool programs implementation and manages repayments to private investors
- Public funding from County School Districts and State Department of Education provide repayment

Nurse Family Partnership: PFS pursuit as a means to scale delivery



- Targets high-risk (low-income) mothers' first pregnancies
- Home visitation by registered nurses from pregnancy – age 2
- Effectiveness proven in 4 random controlled trials plus > 20 other rigorous evaluations
- Cost-benefit analyses showing positive ROI
- NFP infrastructure supports replication with fidelity to model
- Possible Health Outcomes for PFS Contract:
 - Fewer pre-term births, infant deaths, child emergency department visits, closely spaced second births, subsequent births or subsequent preterm births
 - Increase in children fully immunized
- Possible Other Outcomes for PFS Contract:
 - Child welfare: Fewer incidences of child abuse or neglect
 - Education: Fewer remedial school services through age 6
 - Criminal justice: Fewer youth crimes through age 17
 - Maternal life-course : Increased employment, decreased TANF use

With initial support of **\$2.5M from the James Irvine Foundation**, NFF is implementing a California PFS initiative

- The core initiative goal is to **close 3 PFS deals in CA in 2 years**, and to create a cohort of PFS leaders to capture and disseminate knowledge about the process
- ~\$2M of the grant will be used to offer **technical assistance** to leaders aiming to close PFS deals in their communities
- NFF will manage the provision of technical assistance to the leaders through **qualified intermediaries**
- NFF will also manage the creation of an **Funder Interest Group**, which will give feedback to leaders on deal structure and potentially offer investments for PFS deals
- NFF will create a **community of learning** among cohort leaders to accelerate the sharing of lessons learned and disseminate those lessons more broadly within the PFS field in CA

Framework for Considering Stages of PFS Project Development



| Stage 1: Exploration | Stage 2: Pre-Structuring | Stage 3: Transaction Structuring | Stage 4: Shovel Ready |
|--|--|--|--|
| <ul style="list-style-type: none"> • Conversation among local stakeholders is occurring • Education efforts have been undertaken/ are under way • Initial ideas for suitable PFS projects are being discussed, considered, prioritized • Government officials have expressed interest in PFS | <ul style="list-style-type: none"> • Informed consideration or due diligence of effective interventions/ programs that could be right for PFS in a community is underway • Evidence to support the efficacy of such high-impact programs is being collected and evaluated by stakeholders • Governments are undertaking (or engaging third parties to undertake) feasibility assessments and/or cost benefit analyses that look at the relative merits of scaling or implementing programs in a community • Such feasibility assessments or cost benefit analyses determine the potential cost savings generated by projects under consideration | <ul style="list-style-type: none"> • Governments (or the back-end payors in a non-governmental transaction) have reviewed the due diligence completed for a potential project and committed to moving forward with structuring a PFS transaction • A third party is engaged to structure a transaction, refine the program design and consider the delivery implications of a scaled project • A procurement process (or direct engagement) of involved parties (providers, evaluators and intermediaries) takes place • Potential investors are engaged | <ul style="list-style-type: none"> • Most, if not all, stakeholders (providers, evaluators, intermediaries, government agencies) have committed to the project • The transaction has been substantially structured; Exact program design elements may need to be finalized • Investors, investor terms or specific project design elements may remain outstanding/ need to be negotiated • Contracts need to be negotiated |

Barriers to Systemic Adaptation

Gaps in
Data,
Evaluation,
Evidence
Base

Early
Stages/
Proof

Flawed
Funding
Systems

Organization
& Funder
Readiness


Uncertainties
over cost of
measureme
nt

Scaling/
Replication
challenges

**Challenges for Building an Outcomes
Based Financing Environment**

Inflection Point in the Systemic Shift from “Outputs” to “Outcomes”


The Appeal and Possibilities of PFS Embedded Values And Linkages



Promotes
more
efficient and
effective
outcomes-
driven service
delivery:
programs
that work




Monetizes
the positive
social impact
of prevention
& early
intervention



Cost savings
or revenues
plus lower
risk to
governments
compared to
current
practices



Aligns
interest
of investors,
providers &
governments
on positive
social
outcomes



Integrates
social &
financial ROI
for the
private
impact
investor pool
and suggests
scalability





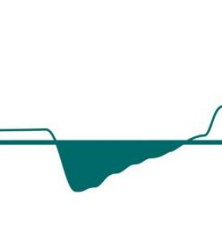



More
productive
allocation
of risk
among
investors,
governments
& service
providers

Considerations for Assessing Service Provider “Right Fit” and Readiness



- **Deliver preventative or early intervention programs**
 - Government funding provides a substantial percentage of support for these programs
 - Program provision can provide financial benefit to government funders
- **History of evidence-based outcome metrics to evaluate performance**
 - Track record of success in achieving outcome targets in reasonably compact timeframe (1 to 6 years)
- **Organizational capacity to:**
 - Reach population needed for statistical significance
 - Collaborate with other providers
 - Ability to track capital investment (and perhaps create business models)
- **Governing body supportive of PFS participation, capacity demands and reputational risk involved**
- **Financial health and durability required for participation**

Different Kinds of Capital Address Different Needs

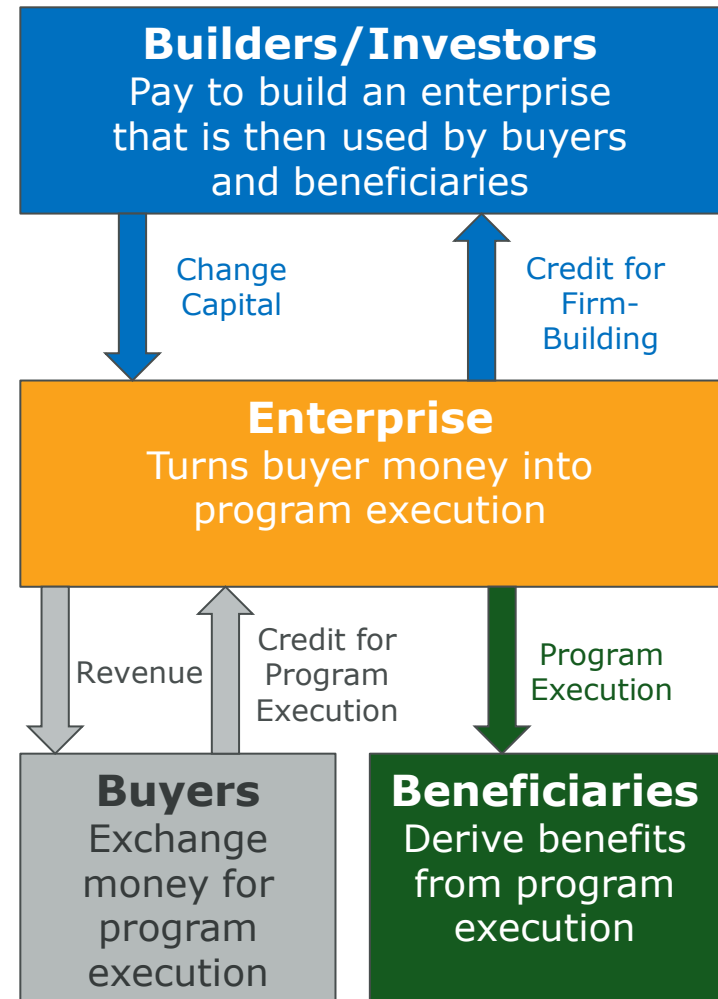
| | Capital Types | Function of each | Addresses: |
|---|------------------------|---|--------------------------|
|  | Working | Allows the organization to bridge revenue timing gaps | Liquidity |
|  | Risk & Opportunity | Absorbs unforeseen funding losses or unexpected, extraordinary expenses | Adaptability |
|  | Change | Funds investments in infrastructure and capacity associated with changes in business model, may cover deficits until programs and operations can support themselves | Adaptability, Durability |
|  | Recovery | Allows an organization to address a historical mistake or chronically undercapitalized operations | Durability |
|  | Facilities & Equipment | Supports acquisitions or upgrades, or can be used to accumulate reserves to meet future facility and equipment needs | Durability |
|  | Endowment | Provides ongoing operating funds through investment income | Durability |

Change Capital (not revenue!) Promotes Adaptability & Durability

There are two kinds of funding:

- **Revenue from “Buyers” provides regular revenue**
 - Covers annual costs of programs & operations
 - Ticket sales, membership fees, program grants, contracts, etc.
- **“Change” capital from “Builders”**
 - Funds the enterprise: to transform what it does
 - Tends to be episodic in nature
 - Can enable growth and experimentation, or provides for risk reserve or deficit coverage

Nonprofits need both revenue and capital to thrive!



General Lessons Learned (to date)

- **Local Context Matters:** Recent US PFS/SIB activity has organized differently according to local conditions-- initial champions have varied, as have resulting structures. One size will not fit all.
- **Independent & Trustworthy Voice Needed:** Given different interests and natural tensions between government, service providers, intermediaries, and investors, maintaining trust among all parties as an objective broker is essential to mobilizing the effort.
- **Catalysts Can Drive Timing:** Government processes and approvals differ. Even with MA/NYC experiences to draw from, RFPs and contracting can still require extended time periods. Moving aggressively through the process requires an incentive.
- **Targeted Technical Expertise Will Be Required:** Depending on capacity of local players, stakeholders will likely need tailored modeling structuring and facilitation support.
- **Broad Stakeholder Engagement is Essential:** Government champion is critical, but not independent of the stakeholder group, including capable intermediaries, strong service providers and evaluators, and engaged investors.

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