What you need to know about pay for success

- Pay for success (PFS) financing harnesses philanthropic or other private capital to fund evidence-based programs, with government repaying investors only if the programs achieve specified outcomes.
- As of 2016, there have been 11 PFS deals in the United States targeting a range of social outcomes, from early childhood education to chronic homelessness to recidivism.
- PFS has the potential to expand evidence-based policymaking by incentivizing the use of research when selecting programs and expanding our knowledge of what works and what doesn’t through rigorous evaluation.

What is pay for success?

Pay for success (PFS) is a social impact financing mechanism for evidence-based interventions that shifts financial risk for scaling social services from government to private investors. The concept originated in the United Kingdom (where it’s called social impact bonds) and has since expanded around the world. As of 2016, 11 PFS projects have launched in the United States in areas such as early childhood education, chronic homelessness, and recidivism.
Here’s how it works: A funder, typically a private investor or philanthropic organization, commits up-front capital for a proven social intervention with the potential to achieve better outcomes. If that intervention achieves preset outcomes, as determined by an independent evaluator, the government repays investors with interest. The finances of the project are often managed by an intermediary, an organization that specializes in the complex PFS deal structure.

PFS has the potential to expand evidence-based policymaking at all levels of government. By incentivizing governments to use evidence when selecting an intervention and use rigorous evaluation designs when examining results, PFS can set policymakers on a path to more comprehensively consider how funding achieves outcomes. Most American PFS projects are employing randomized controlled trials or other rigorous evaluation approaches to determine the outcomes. These strong evaluations allow stakeholders to build evidence about what works, regardless of individual project outcomes.

PFS works especially well as a vehicle to fund preventive social interventions. Preventive programs often have the potential to generate savings for government by avoiding negative social outcomes and associated service costs (e.g. preventing crime can reduce future criminal justice costs).

### Where has pay for success been used?

As of 2016, 11 PFS projects have been launched in the United States (table 1). In addition, many jurisdictions have launched studies to assess the feasibility of using the PFS model to address a social problem in their community. Nearly 60 such studies have been funded by the Corporation for National and Community Service’s Social Innovation Fund.

### SUCCESS STORY

**South Carolina Nurse-Family Partnership Pay for Success Project**

In 2016, South Carolina partnered with Nurse Family Partnership (NFP) to launch a maternal and child welfare home-visiting intervention for 3,200 low-income first-time mothers. The project’s target outcomes are to reduce preterm births and child hospitalization while increasing healthy spacing between births.

The project leveraged NFP’s 40 years of rigorous evaluation to scale their intervention to thousands more mothers in South Carolina. Philanthropic funders and the federal government, via a Medicaid waiver, will commit $30 million to this intervention over four years.
Three projects have produced results thus far and illustrate some of the preventive interventions that PFS can help catalyze. They also demonstrate the promise of—and challenges involved in—PFS projects:

- Two early childhood education programs in Chicago and Utah have yielded preliminary results. These programs provide preschool to high-need children, with success payments tied to the prevention of more costly special education enrollment. The Chicago program also ties additional success payments to measures of improved kindergarten readiness and an increase in third grade literacy. Both projects have demonstrated positive outcomes and made initial success payments. However, some limitations of their evaluation designs have sparked discussion about how programs should evaluate outcomes.

- The first project launched in the United States was designed to reduce recidivism among incarcerated youth at Rikers Island jail in New York City. The project was funded by Goldman Sachs through a $9.6 million investment offering a maximum outcome payment of $11.7 million if the project reduced recidivism enough to shut down a wing of the prison. Bloomberg Philanthropies served as a guarantor on the project, committing to cover the first $7.2 million in costs if outcome goals were not met. An independent evaluation of early results showed that the intervention had no effect on reducing recidivism, and Goldman Sachs exercised its option to end the project early. Through the PFS deal, the government was able to test a new approach without spending public resources on the program.
What design choices should be considered?

Each PFS project is unique, and there is extensive flexibility within the model when constructing a PFS deal. The launch process itself can be adapted based on the type of organization putting a project together. A local government may engage in a more traditional contracting process, often assisted by an intermediary. Service providers can begin deal development by shopping their services to local governments that may be interested in PFS. Intermediaries often act independently as well, pulling together organizations in a local context to launch a project.

If a project is scaling an existing intervention in a new context, that context will influence the design of the intervention. What works in one place may not work the same way in another, so the service provider will need to work closely with the project partners to adapt a chosen model that best serves the local population.

Government also faces important decisions when designing the funding structure for success payments. Because a PFS project can outlive the administration that launched it, the deal must guarantee payments from a fund that a future administration would be unable to use for any other purpose.

How does pay for success promote evidence?

PFS incentivizes stakeholders to choose interventions backed by evidence, increasing the likelihood that projects will meet their outcome goals and investors will be repaid. Not all programs suitable for PFS will have existing rigorous evaluations, but a program with some past evaluation or, at a minimum, a clear and compelling plan to achieve its target outcomes and a project design informed by context presents a stronger case for funding. Existing evidence is used to ‘price the outcomes,’ a form of cost-benefit analysis that estimates the cost savings to government if all outcomes are successfully achieved.

In addition to using evidence on the front end, PFS projects also generate evidence on the back end. As noted above, PFS projects use independent evaluations to determine if programs meet their outcome goals. When these evaluations are rigorously designed, they give stakeholders confidence that the program itself caused the results, expanding the evidence base about what works in social policy.

What makes a pay for success partnership successful?

The capacity and other characteristics of stakeholders involved in a PFS project are critical determinants of that project’s success.

- **Capacity and commitment to plan and execute.** PFS project development typically involves a government feasibility study, a request for proposal, and contract negotiations between the project’s many partners that may last up to two years. Successful projects require committed stakeholders with the capacity to solve problems, identify areas of alignment and comparative
strength, and allocate or find the resources necessary to cover the time and expenses of this planning process.

- **Ability to collect and share data.** Local governments will need data systems to monitor programs and track outcomes. This is even more critical when projects seek to measure outcomes from multiple agencies or governments (e.g., health and criminal justice), which may require data sharing and linking.

- **Commitment to strong evaluation.** Perceived issues with the cost or complexity of a rigorous evaluation design may dissuade stakeholders from including one in a project’s design, so partners should understand the importance of strong research in a PFS project.

- **Receptiveness to collaboration.** PFS projects often require a new level of partnership between government and providers. Clear, constructive, and responsive communication and collaboration are essential to forging strong relationships between these partners. This will support program selection, enrollment, referral, performance management, and other critical tasks that ensure programs have the best chance of success.

### What is the federal government’s role?

The federal government can assist PFS projects at the state and local level by acting as a partner at multiple stages of a deal. In addition to the feasibility studies funded by the Social Innovation Fund, several agencies have already provided funds to support PFS projects:

- The Department of Labor committed a total of **$24 million** to New York and Massachusetts to fund employment services designed to reduce recidivism.

- The Department of Justice awarded an **implementation grant** to Cuyahoga County, Ohio in 2012 to support its Cuyahoga Partnering for Family Success Program.

- The **Every Student Succeeds Act** recently made funding available for PFS projects through the Department of Education, with implementation details forthcoming.

- The Department of Housing and Urban Development announced an **$8.6 million** PFS funding opportunity to help local governments implement permanent supportive housing, an evidence-based model that provides permanent housing and supportive services to the chronically homeless. Grants have already been awarded to the state of Massachusetts; Santa Clara County, California; and Denver, Colorado.

These federal investments can help catalyze PFS deals by reducing the amount of additional third-party investment needed for each project. The federal government has the opportunity to further develop the PFS model through several strategies:

- Supporting feasibility studies and pilot projects.

- Updating grant regulations to make PFS an eligible use where appropriate, particularly for flexible funds like block grants.
• Convening stakeholders to discuss potential future applications of PFS.
• Designating agency experts to stay informed on developments in the PFS field, facilitate sharing of best practices for projects currently under way, and serve as a resource for program staff interested in how PFS might help their programs achieve better outcomes.

Where can I learn more?

• The Urban Institute’s Pay for Success Initiative has developed a suite of resources to support a wide range of stakeholders interested in PFS.
• The Brookings Institution has published a comprehensive report on social impact bonds worldwide.
• The Nonprofit Finance Fund, a PFS funder and intermediary, has developed a website with resources on PFS, including a map with fact sheets for existing projects and PFS legislation.
• Several federal offices are engaging deeply with PFS:
  o The Corporation for National and Community Service.
  o The White House Office of Social Innovation and Civic Participation.
With support from the Laura and John Arnold Foundation, researchers from the Urban Institute, Brookings Institution, American Enterprise Institute, and the Pew-MacArthur Results First Initiative have formed the Evidence-Based Policymaking Collaborative. The Collaborative brings together researchers from organizations across the ideological spectrum to create tools to support evidence-based policymaking at the federal level. The Collaborative’s work is assisted by an Advisory Group consisting of stakeholders throughout the evidence-based policymaking field. The opinions expressed in this brief do not necessarily reflect the views of all members of the Evidence-Based Policymaking Collaborative.