PUBLIC HEARING ON

"Bill 20-125, Social Impact Financing Amendment Act of 2013"

Before the
Committee of the Whole
Council of the District of Columbia

The Honorable Phil Mendelson, Chairman

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Good morning, Chairmen Mendelson and Members of the Committee of the Whole. My name is John Ross, Senior Advisor and Director of Economic Development Finance for the Office of the Chief Financial Officer (OCFO). I am pleased to testify for the Office of the Chief Financial Officer on Bill 20-125, the Social Impact Financing Amendment Act of 2013. We have been asked to speak to the Council more generally about social impact bonds.

In 2009, The Rockefeller Foundation gave a grant to Social Finance UK to develop a new financing tool, which came to be known as social impact bonds. Although the name includes the word "bonds", the issuance of debt is not typically part of the process. Rather, social impact bonds are an alternative procurement method that makes payment of contractors contingent upon performance.

The idea behind social impact bonds is to use private sector investment to experiment with, implement and grow government social programs. Often these programs have been previously funded by the government, on a smaller scale. The goal of the private investment is to expand the government program to reach a wider set of clients and to minimize financial risk to the government of uncertain results.

There are usually at least four entities involved in a social impact bond program – the government agency, the service provider, the investor, and the evaluation organization. The execution of the government program is often outsourced to a third-party organization with a proven track record in a specific type of service provision.

The program is initially funded by the investor. If the program is successful, the government will pay back the investor with interest. If the program does not reach its goals, the government does not pay the investor or pays the investor a limited sum. As a result, payment is based on achievement rather than process or work performed.

To determine what has been achieved by the program, the outcomes must be defined prior to the start of the program, and they must be measurable. In order for the investor to ensure that success and failure of the program is being accurately measured, a third party evaluator is often brought in to measure the baseline and then to measure any changes in outcomes based on the service being provided.

Generally, the public sector enters into a set of contracts with the service provider, the investor and the evaluator. The proposed bill would amend the District's contracting process to allow the District to enter into these kinds of procurements. The risk to the District of this service delivery system is primarily determined by the District's ability to negotiate the contracts with its partners. The financial advantage of a social impact bond program is that the risk of failure is shifted to the investor.

To date, there are two widely discussed social impact bond programs in the world. The first was implemented in Great Britain at Peterborough Prison. In this case, payments are contingent upon whether or not the program lowers the rate at which prisoners reoffend. More than 17 investors invested over $5 million to fund a number of nonprofit organizations to work with prisoners after they are released to reduce their reoffending. The success of the 8-year program is measured by the decrease in convictions.

In New York City, Goldman Sachs invested $10 million to expand a program with the goal of reducing the likelihood of re-incarceration of 16, 17 and 18 year olds. Goldman Sachs will be repaid based on the success of the program. However, their investment is partially protected by a grant from Bloomberg Philanthropies.

The success of social impact bond programs begins with choosing the right social service program. The program must be scalable and measurable within a defined period of time. In order to choose the right program, many cities have opted to perform a feasibility study to determine the suitability of various programs for a social impact bond investment.

In addition to choosing a program, a city must also choose reliable partners with a proven track record to both implement the program and to measure the outcomes of the program. Finally, a city must find an investor or investors who are willing to fund a program without requiring a backstop or guarantee from the city itself. Often the investors are socially motivated investors such as foundations, who are willing to risk an investment in a new or expanded social service program in order to prove its effectiveness on a larger scale.

Social impact bonds have the potential to foster and expedite social programs within the District of Columbia. The OCFO would be happy to work with your office on the process of implementing such a program.

Thank you for the opportunity to testify. This concludes my testimony and I am happy to answer any questions you have at this time.