

# Climbing the Pay for Success

## Learning Curve:

How a working group helped South Carolina understand and prepare for PFS financing

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INSTITUTE *for* CHILD SUCCESS

In January 2013, few people in South Carolina had ever heard of Pay for Success financing (PFS), a new approach to funding solutions to difficult social problems. PFS uses private and philanthropic capital to expand successful projects, even when government budgets are strapped.

But by September of that year, the state had expressed interest in using PFS to improve maternal and child health, issuing a “request for information” seeking formal input on how this financing mechanism could be implemented. Foundations, banks, and other groups were excited about the prospect of investing in PFS.

These stakeholders were excited because they were ready. In the intervening months, government officials, service providers, local foundations, academics, legislators, and potential investors had come together to delve into the subject of PFS financing from many angles. They learned about PFS in other jurisdictions, considered how it could apply in their areas, identified challenges and benefits, and brainstormed ways to overcome thorny implementation issues.

The nonprofit Institute for Child Success (ICS) convened the working group that sparked this transformation. This document describes lessons learned from the experience, providing a roadmap for those who wish to convene similar working groups to explore PFS financing.

### HOW DOES PAY FOR SUCCESS WORK?

With PFS (also called Social Impact Bonds, or SIBs), philanthropic funders and private “impact investors” provide the initial capital to scale up successful programs, which are run by nonprofits. Government does not pay for the expansion (private investors do); instead, it pays only for agreed-upon outcomes, which must be verified. PFS projects are typically managed by an intermediary organization.

The PFS model solves a common problem—government’s insufficient resources for expanding proven social programs—by securing capital from private sources. If successful, a PFS project will eventually save government money, which it can then use to repay investors. PFS has the additional benefits of increasing accountability for government spending and advancing partnerships between the public and private sectors.

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(by)

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## (establishing a working group to explore PFS for South Carolina )

The Institute for Child Success (ICS) is committed to improving the systems that serve children from before birth through age five to ensure that all children succeed. South Carolina has implemented programs that improve children's health and well being, but these programs serve only a small fraction of those who need them. Meanwhile, funding that could help expand effective preventive programs is tied up in responding to the very problems that could have been avoided in the first place through these programs. These problems include child abuse, unidentified learning disabilities, and crime.

PFS financing addresses this conundrum by leveraging private funding to bring effective programs to scale and enabling government to pay later, once it has evidence that cost-saving outcomes will be achieved. ICS believed PFS was a promising way to bring much-needed resources to children in their earliest years.

### WORKING GROUP GOALS

1. To educate a wide range of potential stakeholders about Pay for Success financing.
2. To consider the potential of PFS financing to help South Carolina address social problems on a large scale.
3. To get stakeholders started on building capacity for PFS financing and planning PFS projects where appropriate.

Since PFS financing requires the private, public, nonprofit, and philanthropic sectors to work together, ICS felt it would be best for all of the potential stakeholders to explore this new financing mechanism in a single working group. The response to the Institute's invitation to participate was enthusiastic, with 50 people taking part. (A list of members can be found on pages 6-7.)

The Duke Endowment and the Doris Duke Charitable Foundation provided support for planning and meeting expenses. The working group met six times in person and by webinar in 2013. Below we share three strategies that contributed to the working group's success, as well as potential pitfalls other jurisdictions should plan to avoid.

## (three key strategies for a successful PFS working group)

### *1. Include all of the many stakeholders, including senior government officials*

It takes many parties to make Pay for Success work. PFS requires government to pay for outcomes. Thus, the legislature, executive branch, or both must commit funds, an executive branch agency must lead a procurement process and facilitate implementation, and officials at the highest level of government must provide the political leadership needed for a new approach.

In addition, investors, service providers, researchers, and intermediaries need to participate in a transaction. Other experts and community leaders provide important outside scrutiny to make sure any deal serves the community's needs.

ICS included all of these stakeholders in the working group and provided information specific to each one's role. For example, at one meeting, Rick Edwards, partner at the intermediary Third Sector Capital Partners, led an exercise in which participants broke out into groups by sector and considered a hypothetical PFS transaction. The subsequent discussion brought to light multiple perspectives on the same situation and helped participants understand each others' viewpoints.

## STAKEHOLDERS REPRESENTED\*

- Executive Branch (Governor's Office and state agency leadership)
- Legislature
- Service Providers
- Foundations
- Universities
- Banks
- Chambers of Commerce

\*see list of members on pages 6-7

## 2. Analyze real-life examples

Pay for Success financing is terrific in theory, but what does it mean in practice?

To answer this critical question, South Carolina's working group plunged into the details of the single PFS transaction that had been announced in the United States (in New York City), as well as other deals that were nearing completion. The working group worked closely with experts in this emerging field.

At the initial meeting, Megan Golden of the NYU Wagner School's Innovation Labs, an authority on new nonprofit financing methods, shared information on the payment terms and parameters of the New York City project, which focuses on reducing recidivism. In a subsequent webinar, the group heard from Liz Gaynes, executive director of the Osborne Association, which is providing the bulk of the services to the teenage boys in the New York City project. Gaynes shared Osborne's experience as the only US organization actually implementing a PFS project, describing challenges as well as benefits.

“The collaboration between funders, scholars, state agency representatives, and service providers demonstrates a solid momentum building between theory and action. Being able to engage with this working group has challenged GEEARS and our partners to accelerate our conversations around the possibilities for PFS in Georgia.”

- Laura Stamm Wagner  
Director of Research  
Georgia Early Education Alliance  
for Ready Students

Nirav Shah from Social Finance, a nonprofit dedicated to promoting private investment in solving social problems, reviewed PFS transactions in development around the country. Rob Dugger of ReadyNation, which brings business support to investments in early childhood, discussed his organization's work applying PFS financing to pre-kindergarten programs. Rick Edwards of Third Sector Capital Partners, an intermediary, presented the project being developed with the nonprofit group Roca in Massachusetts. By the last meeting, working group members were well versed in how PFS financing can apply in multiple settings and how the field was progressing.

## 2013 WORKING GROUP MEETING TIME LINE

- February 7, 2013: Intro to social impact finance (In-person meeting)
- April 15, 2013: The investor's perspective (Webinar)
- April 23, 2013: In-depth analysis of PFS transactions in development and break-out groups by sector (In-person meeting)
- May 22, 2013: The service provider's perspective (Webinar)
- August 27, 2013: Presentation of ICS feasibility study on PFS finance for the Nurse-Family Partnership (In-person meeting)
- October 30, 2013: Progress and next steps in SC and internationally; needs and opportunities for capacity building (Final in-person meeting)

### *3. Encourage challenging questions and creative ideas*

The working group was not a marketing vehicle for PFS financing. In fact, it encouraged participants to bring up any challenges or obstacles they saw to PFS.

And they did. For example, program managers raised the concern that they would not be able to secure data on outcomes that occur after participants complete a program. The facilitators and other working group members acknowledged the obstacles and brainstormed ways around them. In this case, researchers in the group were able to talk about what data is available and suggest ways of accessing it.

It helped that the working group's convener, the Institute for Child Success, was not interested in being a party to any eventual PFS transaction.

### **(potential pitfalls that working groups should consider)**

“As government budgets tighten, it is critical that we develop alternative means of financing important interventions to support our youngest learners. The working group was exposed to real world practitioners of pay for success. We were educated about the value and the challenges of establishing these models.”

- Dave Morley  
Board Member  
Past National Chair  
Parents As Teachers (PAT)

**CHALLENGE:** Pursuing opportunities for PFS funding is time consuming and requires resources.

**SOLUTION:** Set realistic expectations—understand that the working group will lay crucial groundwork, but more time and resources will be needed to evaluate actual potential deals for PFS.

ICS initially envisioned that, after some preliminary education, working group members would quickly begin exploring opportunities for PFS financing and share them with the group.

However, we soon realized that that was too much to expect. Understanding PFS financing and its implications itself takes time. Exploring actual opportunities for implementing it requires resources beyond what working group participants could typically devote.

This experience provides an important

warning: while a working group can lay the groundwork for PFS financing, exploring an actual deal requires detailed analysis that takes time and costs money. If the working group operates on a limited budget, as did the South Carolina group, this work must be done with additional, dedicated resources.

The Institute's study of the feasibility of using Pay for Success financing to expand the Nurse-Family Partnership, an evidence-based early childhood program, is one example of a dedicated effort to evaluate a specific opportunity for PFS financing.

### ASSESSING PFS FINANCING FOR A SPECIFIC INTERVENTION: ICS'S FEASIBILITY STUDY OF THE NURSE-FAMILY PARTNERSHIP

While leading the working group, ICS conducted a separate, eight-month feasibility study, on whether PFS financing could be used to scale up the Nurse-Family Partnership, a successful early childhood intervention. Supported by additional funding, this study, *Using Pay for Success Financing to Improve Outcomes for South Carolina's Children*, concluded that PFS could indeed be used to expand early childhood programming such as the Nurse-Family Partnership. It is available at [www.instituteforchildsuccess.org](http://www.instituteforchildsuccess.org).

During the study, ICS sought input from working group members, as well as other interested parties. This input enabled ICS to identify and respond to many valid concerns and solidified our confidence in our finding that PFS is indeed a feasible way to improve outcomes for South Carolina's children.

**CHALLENGE:** Geographic and time restrictions make it hard to attend meetings.

**SOLUTION:** Strategically schedule meetings in locations and at times that make it easy and worthwhile to attend.

ICS held the working group meetings in Columbia, the state capital, which was less than a two-hour drive for participants coming from other parts of the state. Even so, it was difficult to get full attendance at all of the in-person meetings.

This experience suggests that other jurisdictions would be wise to schedule in-person meetings strategically, either planning around other big events that bring people to the meeting location or providing a compelling and substantial-enough agenda to warrant significant travel. Larger states might consider convening regional, rather than statewide, working groups.

“The Mary Black Foundation, like many funders, wants to be able to maximize our impact and leverage other resources for our community. Social Impact Financing or Pay for Success models are intriguing ways for foundations to think about growing successful programs and improving outcomes for children on a much larger scale than we might be able to achieve on our own. It's important for us to participate in conversations, like the Working Group, about new and different ways to do our work of creating community change.”

- Molly Talbot-Metz  
Vice President of Programs  
The Mary Black Foundation

## **(conclusion)**

South Carolina's experience shows that a working group can help a critical mass of stakeholders understand the value and constraints of Pay for Success financing.

That understanding can generate ideas for applying PFS financing to address pressing social problems, speed the time to complete any PFS transactions, and promote collaboration to achieve the best results for taxpayers and communities.

## **(South Carolina PFS working group members)**

Sally Baggett

*Carolina Health Centers*

Wanda Crotwell

*Mike Daniel & Associates*

Tamar Bauer

*Nurse-Family Partnership*

Todd Dalrymple

*The Duke Endowment*

Taylor Beard

*Grace Church*

Leigh D'Amico

*University of South Carolina*

Bonnie Bella

*Trident United Way*

Susan DeVenny

*South Carolina First Steps*

Eric Bellamy

*Children's Trust of South Carolina*

Tim Ervolina

*United Way Association of South Carolina*

Anne Bergin

*Trident United Way*

Mike Fair

*South Carolina Senate*

Chris Bishop

*Nurse-Family Partnership*

Megan Golden

*New York University*

Edie Blakeslee

*Coastal Community Foundation*

Gwynne Goodlett

*USC School of Law - Children's Law Center*

Leigh Bolick

*South Carolina Department  
of Social Services*

Ted Hendry

*United Way of Greenville County*

Megan Branham

*Children's Trust of South Carolina*

Derek Lewis

*Greenville First Steps*

Mike Brennan

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Steven Lize

*Consultant*

Erica Brown

*Harvard SIB Lab*

Rhett Mabry

*The Duke Endowment*

Sam Cook

*Center for Heirs' Property Preservation*

Steve Mann

*University of South Carolina*

Edna Crews

*Coastal Community Foundation*

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*New Carolina*

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*South Carolina Senate Labor,  
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Christian Soura  
*Office of Governor Nikki R. Haley*

Laura Stamm Wagner  
*GEARS (Georgia Early Education  
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Anne Wallace  
*South Carolina Senate Committee  
on Corrections and Penology*

Bunnie Ward  
*United Way of the Midlands*

Joe Waters  
*Institute for Child Success*

Gage Weekes  
*Hollingsworth Funds*

Sue Williams  
*Children's Trust of South Carolina*

Jane Witowski  
*Greenville Health System*

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*Mike Daniel & Associates*

Dan Wuori  
*South Carolina First Steps*

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The Institute for Child Success is a non-profit, non-partisan research and policy organization that fosters public and private partnerships to align and improve resources for the success of young children in South Carolina. A partnership of the Children's Hospital of the Greenville Health System and the United Way of Greenville County, ICS supports service providers, policy makers, and advocates focused on early childhood development, healthcare, and education to build a sustainable system that ensures the success of all children, pre-natal through age five.