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House Committee on Ways and Means, Subcommittee on Human Resources
Hearing on Social Impact Bonds and Families in Need

Chairman Reichert, Ranking Member Doggett, and Members of the Ways and Means Subcommittee on Human Resources, good afternoon. Thank you for the invitation to testify today from the perspective of a local government on the potential of social impact bonds, which I believe have great potential to advance the effectiveness of government services.

I am Linda Gibbs, a principal at Bloomberg Associates, a non-profit consultancy created by Michael Bloomberg to support mayors in achieving their visions for the citizens of the cities they serve. We apply our expertise across eight practice areas and are now working in nine jurisdictions around the world, at no cost to the Mayors we advise. Before joining Bloomberg Associates, I served for thirty years in New York City government, and in the final eight years as Deputy Mayor for health and human services.

Working in City Hall with Michael Bloomberg we focused closely on the current causes and potential solutions to poverty In New York City. The Young's Men's Initiative was a key component of this work, in response to the Mayor's request that we identify strategies to reduce disparities for young men of color in the city. The nation's first social impact bond in New York City was born of that initiative, as we searched for funding sources to help commissioners launch innovative strategies to meet the Mayor's challenge.

Social Impact Bonds (SIB) are a type of Pay for Success (PFS) contract, but with a public-private partnership financing model that funds tested preventative programs at no cost to the taxpayer, improving social outcomes and ultimately saving taxpayer dollars. Private investors fund a program's delivery and operations (often administered by a nonprofit intermediary) under a contract in which government commits to paying the investors back with interest if and only if improved social outcomes are achieved that generate taxpayer savings. A reliable third-party evaluation determines if the program has achieved prescribed outcomes before government makes any "success payments."

This unique financing model is gaining momentum, and there's widespread interest among governmental bodies across the USA and internationally, largely due to the fact that it represents a new way to bring private sector capital to advance social change. However, I believe the potential benefits from SIBs to advance the effectiveness and efficiency of government services is much larger. The first SIB was implemented in the United Kingdom and recent results announced the initial success of the Peterborough SIB in meeting the threshold target by reducing recidivism rates by 8.4%, exceeding the threshold target of 7.5%. The NYC project which began in 2013 was the first in the United States.

The goal of the NYC project is to reduce future jail time among adolescent inmates who are held in our jail on Rikers Island. The reduction in future jail time is associated with savings to the city's Department of Correction, in the form of shutting down unneeded housing units. After negotiations among all parties, projections of impact were established based on the national research of programs akin to the one we adopted, adjusted based on local population data. Specific "success payments" are tied to different levels of impact and associated government savings.

Allow me to explain the program. At the time we began, we estimated there would be approximately 3,400 youth who would experience a stay at Rikers in a single year. We know from historical data that this population has a shocking one-year recidivism rate of nearly 50%, a mean length of stay of 65.3 days, and an average of one prior incarceration at the DOC.

Our goal in the Young Men's Initiative was to make a significant difference in this outcome. The question was what might work to improve their chances when they left our custody? While several programs have been adopted as part of the Young Men's Initiative, one in particular captured our imagination. What if we fundamentally restructured their experience while they were in our custody, strengthening their social skills and assisting their ability to make more responsible decisions when they returned home? Providing a group program in a jail setting, we believed, had the potential to improve group dynamics and counteract the negative effects of incarceration on later criminal behavior.

We started with research on what programs have evidence of succeeding in this goal, with this population. Most therapeutic programs like what we had in mind are operated in prison settings, for populations that already have been sentenced. We differ in that the vast majority of our youth are held pending the outcome of their trial. And they are young, just 16-18 years of age.

We settled on an evidence based cognitive behavioral therapy called Moral Reconation Therapy. The term "cognitive behavioral therapy" (CBT) is a general term for a range of therapies with similar characteristics. These therapies emphasize changing negative patterns of thinking as a way to reduce harmful, self-destructive, and antisocial behavior. CBT has been found to be effective in decreasing substance abuse and reducing criminal behavior. It has been tested in prisons across the country and shown to reduce recidivism rates and improve participant behavior. There is a large evidence base for cognitive behavioral therapies. The Vanderbilt Institute for Public Policy Studies conducted a meta-analysis of 58 experimental and quasi-experimental studies on the effects of CBT on the recidivism of adult and juvenile offenders. The study found that in a 12-month follow-up period individuals in the treatment group experienced an average reduction in recidivism of 25%.

The specific version of CBT being implemented at Rikers is known as Moral Reconation Therapy (MRT). Moral Reconation Therapy (MRT) has a particularly strong evidence base that offers the unique advantage of being an "open curriculum" well suited to the Rikers environment. Unlike other CBT models, MRT offers a lot of flexibility in delivery. For example, groups are open-ended, which means that new clients can enter a group at any time and be meaningfully incorporated. Youth can also move at their own pace through the curriculum. Finally, while the full program is designed to be completed in about 10 weeks, benefits accrue in as little as three weeks. Given that youth move in and out of Rikers frequently and that many inmates will leave before a course is complete, enter after a class has started, or need to switch to other another class, this flexibility of the MRT program is critical.

There is also a strong evidence base for moral reconation therapy specifically. Of the thirteen studies reviewed for us by MDRC, out intermediary partner in the project, seven showed positive and significant effects (others showed either positive but non-significant effects or had design flaws). The Cognitive-Behavioral Treatment Review published a 1994 experimental study on the effectiveness of the MRT model. The five-year recidivism rate for MRT participants was 41% compared with 56% for non-participants (a 15% percentage point difference – that is, 27% lower than without the program). Program participants had lower levels of criminal involvement at all follow-up periods on all indicators of recidivism. The Portland State University's Division of the Administration of Justice released an evaluation on the outcomes of MRT for juvenile offenders in which three percent of MRT participants were re-indicted compared with 13 percent of non-participants.

Based on this research, we adopted the MRT model, and worked with the program founders to formulate its application in the adolescent housing on Rikers. We named the program ABLE (the Adolescent Behavioral Learning Experience). To deliver the program, we worked with a non-profit organization with deep ties to work on Rikers Island, the Osborne Association, and supported them with technical assistance from MDRC.

MDRC is a research and demonstration intermediary organization. Under one roof, it houses the capacity to design, develop, and oversee the implementation of new and existing approaches to complex social and behavioral problems, as well as the capacity to rigorously evaluate the effectiveness of these initiatives. In this project, they will only be exercising their programmatic proficiency in designing and overseeing ABLE.

It is not a guaranteed outcome however. This intervention has never been implemented in a setting as large and complex as Rikers. And as mentioned earlier, this is largely a pre-adjudication population, not one serving time for crimes for which they've been convicted.

The Vera Institute for Justice, serving as an independent evaluator contracted by the city, will be monitoring the success of the program. Vera will be assessing the program service delivery, examining factors related to program enrollment and level of participation in MRT, and determining whether the program has been effective at reducing future jail time. Program payouts will be based on those independently verified outcomes.

The financial terms are key to social impact bond arrangements. In our case, the intermediary, MDRC, working on behalf of the investor, will be reimbursed through a pay-for-success reimbursement system that has been established in contract negotiations. The payout terms in the contract require that payments be made only when Vera validates that performance outcomes associated with future jail time savings have been met.

Here are the terms of the agreement. Goldman Sachs fully funds the project's interventions by advancing a $9.6 million loan to MDRC. If recidivism, meaning return to Rikers, for the group receiving the service, drops by 10%, the investor will be repaid the full $9.6 million investment. At the 10% breakeven point, the city is assuming a reduction of around 560 beds (from cohorts 1-4 over a 7 year period) which translates into anywhere from 4 to 6 housing units. This breakeven point was identified as the amount necessary to be saved to both repay the investment and to have sufficient savings to pay for the continuation of the program.

The loan is secured by a Bloomberg Philanthropies grant of $7.2 million, which is held by MDRC in a guarantee fund. Consistent with the manner in which many foundations make program-related investments, Bloomberg Philanthropies is helping to reduce the risk for a private investor to participate by establishing this guarantee fund. If the reduction is less than 10%, the grant dollars in the guarantee funds will be used to repay a portion of Goldman Sachs' initial investment. Ultimately, $2.1 million of the Goldman investment is at risk, 25% of its principal, if the full guarantee fund of $7.2 million from Bloomberg Philanthropies is depleted. If the guarantee fund is not needed, those funds will be available to support further social impact investments. But any return on the initial investment – triggered by cost savings from reductions in the recidivism rate – will go exclusively to Goldman Sachs or remain in the fund for future social impact projects in NYC; Bloomberg Philanthropies receives no financial return on its investment.

As the program works, the Department of Correction's savings accrue and that money is used to make the payout to the intermediary. Lowering Rikers' recidivism rates will yield significant savings for the city since these costs are all borne by the city without state or federal participation. Drops in excess of 10% produce increasing returns to the investor, as well as additional savings to the city, capping for the investor at a payment of $11.7 million if recidivism drops by 20%. For Goldman, this return on its investment is comparable to returns on its other community development loans. At that point the city will also be saving over $20 million from the improved outcomes from the young people involved, again beyond the savings sufficient to pay the investor and continue payment for the service on Rikers. Any drop beyond 20% and savings that accrue are retained exclusively by the city.

I believe this model has great potential for a number of reasons. It:

- Unleashes creative potential. Innovation in government can be challenging, particularly when there is little prospect that funding is not available to support new approaches. The possibility for SIB funding can free the creative thinking process and stimulate innovation;
- Shifts risk for funding new programs from government to private investors. Government can be risk averse. This financing model transfers risk to private investors so that taxpayers have no liability if a program does not reach successful outcomes – in other words, taxpayers pay nothing if the tested program does not work. The City only pays for programs that result in positive social outcomes and cost savings. In order to incentivize private funders to take the upfront risk, the city is willing to pay a return, similar to bond investments to build bridges and tunnels;
- Brings private capital forward to fund social programs. Government dollars are tied up in programs that represent the consequences of poor outcomes – jail, shelter, remediation. Funding for strategies to prevent those outcomes is scarce and there is reluctance to raise taxes to cover those costs, particularly without strong confidence the preventive strategy will work. SIB financing bridges that gap. SIBs also direct a flow of capital to areas that the current private markets typically do not serve. The charities and NGOs who implement the work receive funding to work in neighborhoods where people do not have the liquid access to private markets seen in the more mature or affluent neighborhoods;
- Advances promising new strategies. There is often reluctance in adopting new practices imported from the experience of others, on the belief each jurisdiction is nothing but unique. SIBs heavy reliance on evidence can help evidence based projects being tested in one place to more easily jump governmental boundaries;
- Creates opportunities to scale up programs. Similarly, pilots with strong research results often have trouble spreading and going to scale. SIB investors can facilitate the spread of what works in support of programs that have evidence to back them up;
- Elevates the tenor of outcomes based management in city halls and state houses, advancing skills in defining clear outcomes, measuring for results, and assessing governmental costs and benefits. There are many reasons government managers will give for not moving to evidence based practices – "It's too complex, we don't have the skills to do that, we don't have the data to do that, you can't measure social outcomes, what you can measure are not the right outcomes, etc, etc, etc. Shifting the focus of government management from "this is how it's always been done", to 'this is how to get the best results" needs focused and forceful advocates, and SIBs can be a powerful inducement to that goal;
- Invests in skill development for government program managers. In many ways I believe SIBs greatest potential for government is that it is bringing to the table expertise in data management, evaluation, evidence based practice and cost-benefit assessments. Particularly for small jurisdictions without the ability to invest in large research capacities, the field of SIB practice is making straightforward tools more broadly available, and the investment in this knowledge development will have benefits well beyond SIB project management; and
- Aligns all parties around a set of clearly defined, measurable outcomes with payment only for success. SIBs have a greater degree of accountability for actual results, driven by the contractual terms for repayment. While many programs government invests in are done of the promise of great future benefits and returns, except for academically leaning research studies, none have the same sharp focus on precise outcome assessment. This again is an area where SIBs have the potential of advancing social program management beyond the SIBs themselves, as this skill level develops broadly.

But SIBs are not a panacea.

- They only work where government is willing to pay investors for their risk. And this is best where cost savings accrue. That will not be true in many circumstances. Many urgently needed social programs will continue to need to be done because it is the right and smart thing to do, despite the fact they produce no savings.

- Other programs that produce savings which take too long to be realized to satisfy an investor's timeframe, or are too dispersed to be easily recouped, are not suitable for SIB financing, although I would note that HR 4885 would solve part of that problem by making it easier to recoup the federal savings that accrue.
- Without good data and management systems, evidence cannot be produced to satisfy the rigor of the model. Over time I would expect this will improve as government agencies become more adept at data management and systems are more widely available at reasonable costs. Great expertise is developing in structuring programs to be administratively simple, and increasing well-structured to avoid practitioner bias. But this is also an emerging expertise and design considerations are significant.
- The effort is in its infancy, and transaction costs are still high, prohibitively high, for many. Again, as skills develop and tools proliferate, these barriers should drop, making the practice more widely available.

In sum, I am optimistic that SIBs offer great potential to move the field of sound social service practice forward, providing well beyond the sort term benefits of new investment dollars, to providing sound outcome based management.