

UNDERSTANDING SOCIAL IMPACT ~~BONDS~~

Partnerships

February 2013

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Preface

Social Impact Bonds (SIBs) are attracting worldwide attention as an innovative form of social service sector investment which encourages cross-sector collaboration and has potential to reward prevention and scale effective social programs beyond the reach of traditional public and philanthropic capital. Bringing governments, not-for-profit organisations and impact investors together with vulnerable individuals and communities, SIBs align the interest of all parties to design, implement and fund preventive and early intervention programs that produce measurable, positive social outcomes. The SIB model does three things well: it focuses existing resources on achieving valuable outcomes; it improves value for money of government expenditures; and it mobilises new capital for the delivery of social services.

The emergence of SIBs comes at a time of significant change in the not-for-profit sector in Western Australia (WA). Nationally, the introduction of the Australian Charities and Not-for-profits Commission in October 2012 will bring regulatory change to the sector. At the same time, the *Putting the Public First: Partnering with the Community and Business to Deliver Outcomes* reforms of the Economic Audit Committee of WA embodied in the collaborative leadership of the Partnership Forum are driving local change. In particular, the move to outcomes-based procurement under the *Delivering Community Services in Partnership Policy* is accelerating cultural and system changes to enable the development of the data, measurement platforms and management information systems required for evidence-based reporting on outcomes. SIBs cannot exist in the absence of such rigorous evidence and the data and measurement that underpins their delivery.

In unravelling SIBs in the context of the dynamic environment in WA, this report does several things. It considers the application of SIBs in WA, acknowledging both the local context and the growing body of predominantly international literature on SIBs. Secondly the report positions SIBs within the WA reform context. At heart, SIBs are a performance-based payment model on the continuum of value-based purchasing options. Finally, the report identifies the potential SIBs hold to increase the pool of capital to fund preventive and early intervention programs, encourage program innovation, provide predictability of funding to not-for-profit organisations delivering effective programs, and align public-sector funding to improved social outcomes.

In coming to understand the workings of SIBs more accurately, it is clear they are much more than a financial instrument and that the term 'bond' is a misnomer. In order to avoid misunderstandings going forward, we recommend they be framed as partnerships, which they are, rather than as bonds, which they are not. Within this report, we adopt the term Social Impact Partnerships (SIPs) for application in WA, although we retain the terminology of SIBs in examining their application elsewhere.

Acknowledgements

This study would not have been possible without the contributions of members of our advisory group, and we thank each one of them for their thought leadership. The views expressed in the paper remain those of the authors of the report alone:

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|---|--------------------------------------|
| ▶ Rebecca Brown, Department of Premier & Cabinet | ▶ Kevin MacDonald, Giving West |
| ▶ Irina Cattalina, West Australian Council of Social Services | ▶ Tim Marney, Department of Treasury |
| ▶ Dwight Clark, JB Were | ▶ Melissa Perry, Mission Australia |
| ▶ Jonathon Leek, Corrs Chambers Westgarth | ▶ Rebecca Tomkinson, Bankwest |

We also acknowledge the conversations held with a number of individuals and organisations that have helped to inform and contextualise the study presented in this report. A list of names and affiliations is provided at the end of this report.

Finally, we are grateful for the support of Lotterywest who embraced the study and identified that the first step was to build an understanding of SIPs within our local operating context.

We trust this report helps to seed and inform conversations about the potential of SIPs as a complementary addition to the tools already available to address our society's most pressing challenges.

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Executive Summary

Social Impact Partnerships (SIPs) are cross-sector collaborations to design, implement and fund preventive and intervention programs that produce positive social outcomes for vulnerable individuals and communities. As an organising structure, SIPs provide a means to engage multiple service providers recognising that most social needs within our communities are complex with no “one-size-fits-all” solution. As a financial instrument, SIPs unlock private capital for social purpose recognising that government and philanthropic capital alone is insufficient to meet the needs within our communities.

In this report, we review the Western Australian landscape for social change, explain how SIPs work, draw on the better established practice of payment-by-results to provide insights into how SIPs can be framed, and explore the potential for SIPs in Western Australia (WA).

Social Impact Partnerships explained

A SIP involves a contractual agreement between an intermediary and government (or other procurer of social services) to improve agreed social outcomes in return for an agreed outcome payment. The intermediary takes responsibility to identify program solutions together with service providers, raise money from impact investors to fund these solutions, conduct ongoing project management, and work with service providers to ensure effective implementation of the identified innovative program. If the agreed outcome is successfully achieved, the intermediary collects the agreed outcome payment under the contract and repays capital with a financial return to impact investors.

While a potentially complex model, a well-designed SIP will encourage a more rational allocation of financial resources towards programs and service providers that deliver improved outcomes for individuals and communities in need. SIPs hold the potential to be a valuable tool to complement the efforts of governments and other existing funders of social programs to achieve better social outcomes for Western Australians.

Potential of Social Impact Partnerships in Western Australia

The shift to outcomes-based contracting under the WA government’s *Delivering Community Services in Partnership Policy* provides a positive environment in which to consider the application of SIPs. Not only does the focus on outcomes lay the groundwork for the establishment of robust measurement systems which are a precondition of SIPs, but it initiates the capacity-building process within service providers and government to transition from paying for activities towards paying for outcomes. Assuming that appropriate measurement systems and contracts for outcomes can be negotiated, the areas for application of SIPs in WA are likely to be similar to those observed in other jurisdictions in which SIBs and like social impact financing models have been implemented. They include alcohol and substance abuse; chronic health problems; criminal justice; early childhood; education and training; homelessness; and mental health. Our research also indicates that there is considerable potential in considering the application of SIPs in addressing Aboriginal disadvantage in these areas.

Implications of Social Impact Partnerships to key stakeholder groups

SIPs represent a new approach that can be added to the suite of tools available to those interested in improving the lives of individuals and communities in need. For government, SIPs can drive achievement of policy objectives and program outcomes and improve effectiveness of public expenditure. Similarly, for other procurers of social services, SIPs provide the opportunity to improve effectiveness of their social or community spend. For not-for-profit service providers, SIPs rewards those who have created effective innovative programs and facilitates access to growth capital. For impact investors, SIPs offer the opportunity of a blended value return. Most importantly, SIPs offer the prospect that better social outcomes can be achieved for vulnerable Western Australians.

1. The Landscape for Social Change in Western Australia

Western Australian context

There are more than 4,000 community benefit organisations operating in WA¹ delivering a wide variety of social programs and services. In addition, more than 250,000 Western Australians volunteer through community organisations each year. In describing the context in which these organisations operate, we highlight four dimensions: unique characteristics of the Western Australian social service delivery landscape; key economic and demographic forces; local policy settings; and the local impact of national policy settings.

Unique characteristics of Western Australia

- The only State to have a public lottery where more than \$100 million is returned to the community via grants to the community-benefit and charity sector.
- Existence of a number of highly endowed Native Title Trusts with assets of more than \$100 million.
- Strong track record of initial public offering (IPO) capital formation (nearly 50% of all listed companies in Australia are based in WA), albeit with underdeveloped financial services, structured finance and private wealth capability (relative to Australia's financial centres of Sydney and Melbourne).
- Mining companies emerging as major actors in the social service delivery landscape in WA through Community Investment Programs with expenditures in excess of \$250 million per year.
- Relatively underdeveloped role of philanthropy in the State, albeit augmented by the recent establishment of GivingWest and major individual gifts by more active donors signalling positive movement in this space.

Economic and demographic forces

- Workforce demand, especially in mining and energy, making housing affordability a growing crisis for many low-income families and individuals.
- Resettlement issues with fast-growing population from overseas and other States.
- Domestic and lifestyle issues related to influx of fly-in fly-out (FIFO) workforce in regional areas, and their absence from family settings.
- Large number of complex needs within Aboriginal communities exhibiting very poor well-being (for example, health, educational attainment, employment) compared to non-Aboriginal population.

Local policy settings

Putting the Public First: Partnering with the Community and Business to Deliver Outcomes, released in October 2009, set an ambitious agenda toward the creation of a more collaborative and innovative public sector. This has included the establishment of the Partnership Forum in 2010 to act as a focal point for building and maintaining the relationship between the public and not-for-profit sectors and fostering collaboration and innovation in policy, planning and service delivery. The Partnership Forum achieves this through bringing together an equal number of senior representatives from State Government agencies and the not-for-profit sector to address issues of mutual concern.

¹ We use the term “community-benefit organisation” to avoid defining the sector by what it is not as in “not-for-profit”. This is a population-share based extrapolation of the national data collected in 2006-7 by the Australian Bureau of Statistics *Not-for-Profit Organisations Australia 2006-7*. A breakdown specifically for Western Australia is being sought.

The Partnership Forum has adopted a set of Partnership Principles and Behaviours, including: a commitment to improve social, cultural and economic outcomes for the WA community; a collaborative approach to decision making and working together recognising the interdependence in the delivery of community services; and a commitment to empowering service users in the design, planning and delivery of community services. These principles engender a focus on community consultation on all significant issues and the engagement of citizens in the ongoing design, planning and delivery of human services. Key initiatives include the initiation of:

- Sustainable funding and contracting reforms, including a move to procurement for outcomes;
- The Social Innovation Grants Program (2011);
- The Social Enterprise Fund (2012); and
- Self-directed services (2011)

Procurement for outcomes by government

The move to outcomes-based procurement entails major cultural shifts and systems change for government agencies and the not-for-profit sector. Measuring outcomes relies on the availability of relevant data at the individual level and the capacity to analyse the data in a meaningful way. This in turn necessitates the establishment of unit record data collection systems and measurement systems that support the assessment of differential impact.

It is early days in the implementation of this major change, and the initial weaknesses observed include: shortfalls in relevant human capital and government agency and community organisation data collection systems to put robust evidence in place in the near term; confusion over language and terms; a lack of coordination between agencies and providers in developing the data-sets and measurement frameworks; and concerns that the skills and flexibility are not yet in place on the purchaser side to reap the benefits of outcomes-based procurement. Naturally, any major system-level change like this one will raise issues that take time to resolve.

On a positive note, this move to outcomes-based procurement demands the development of robust outcome metrics and performance systems that are preconditions to SIPs. While New South Wales (NSW) has moved ahead to a SIP pilot (or Social Benefit Bond, as they term it), the broader cultural and system change entailed in a whole-of-government move to outcomes-based procurement has not yet commenced there.

Social Innovation Grants Program

In May 2010, the Premier of WA, Hon Colin Barnett MLA, announced the establishment of a Social Innovation Grants Program to promote innovation in the delivery of social and community services. The Program provides for funding of \$2 million in 2010-11 and \$4 million in each of the two years following.

Social Enterprise Fund

The WA Government's \$10 million Social Enterprise Fund (SEF) aims to increase the number, effectiveness and efficiency of social enterprises in WA by supporting not-for-profit community sector organisations to establish new or strengthen existing social enterprises. A consortium, led by Social Ventures Australia and including Social Innovation in WA, the Centre for Social Impact at University of Western Australia (CSI UWA), and the Western Australian Council of Social Services (WACOSS) provides a support service to ensure the effective delivery of the SEF, including pre-investment support to social enterprises preparing to apply, and after-care business support to successful funding recipients.

Self-directed services

Self-directed services design and delivery affords opportunities for individuals, families and communities to have a significant say in how services are designed and delivered, which is a break from the historical model of service provision. There are a range of benefits in heading down the

path of self-directed service design, including providing individuals greater power to make decisions about matters that affect their lives, avoiding the 'learned helplessness' that government intervention can create, and promising improved outcomes for individuals by responsive service provision.

Outcomes expected from the broader adoption of self-directed services include: more effective service delivery that is more responsive to citizen needs; constructive debate in the public sector and in the community as to the understanding of and merits of self-directed service design; extensive discussion in the public sector and in the community as to the application of self-directed service design to different areas of policy and service delivery; the introduction of alternative approaches to service delivery; and financially viable service models for service delivery organisations.

Relevant national policy settings

Nationally, a number of policy settings are in flux influenced by recommendations of the Productivity Commission and Senate Economics References Committee in their respective reports, *Contribution of the Not-for-Profit Sector* [2010] and *Investing for good: the development of a capital market for the not-for-profit sector in Australia* [2011].

The recommendations of the Productivity Commissions focus on a reform agenda centred around five main elements: improved knowledge systems to support understanding about effective social interventions; clearer governance and accountability via a consolidated regulatory framework; more effective sector development; social innovation to develop new and better ways of tackling social problems; and strengthening cross-sector relationships to facilitate improved delivery of government funded services.

The introduction of the Australian Charities and Not-for-profits Commission in October 2012 will set in play a consolidated regulatory framework including the roll-out of a standard chart of accounts for the not-for-profit sector. Although the longer-term vision is for simplicity and portability of information, there is considerable concern that this reform may burden the not-for-profit sector in the short to medium term. It is also not yet evident if the reforms will achieve a move towards measurement of outcomes to allow demonstration of social impact and development of an evidence base to guide social programs.

The recommendations of the Senate Economics References Committee specifically build on Recommendation 7.5 of the Productivity Commission, which observed a need for Australia to develop a sustainable market for not-for-profit organisations to access capital [p. 194]. The central recommendation of the Committee's report is the establishment of a Social Finance Taskforce to 'assess the mechanisms and options in the progress and development of a robust capital market for social economy organisations in Australia' [p. xxiv]. Development of new financial products was also emphasised by the committee, including a recommendation in regard to SIBs (Recommendation 6.3). A summary of the 15 recommendations contained in the report is provided at Appendix I including detail of Government's response in which five recommendations were accepted in principle, eight noted and two not supported. Whilst only Recommendation 6.3 pertains specifically to SIBs, it is important to recognise that the scope and reach of many of the recommendations have potential to influence the supply of capital to social purpose organisations (including not-for-profits, social enterprises, social purpose businesses, etc.).

Also reflecting the recommendations of the Productivity Commission in regard to improved access to capital for the not-for-profit sector and social innovation, the Australian Government has instituted the Social Enterprise Development Investment Fund (SEDIF) and the Community Development Financial Institution (CDFI) Pilot. Under SEDIF three new funds totalling \$40 million have been established by Foresters Community Finance, Social Enterprise Finance Australia and Social Ventures Australia to provide debt financing to social enterprises. The CDFI Pilot provides \$6 million to five organisations to pilot approaches for developing CDFIs in Australia. The five organisations participating in the pilot are: Community Sector Banking; Fair Loans Foundation;

Fitzroy and Carlton Community Co-operative; Foresters Community Finance; and Many Rivers Microfinance.

2. Social Impact Partnerships: Procurement of social outcomes

The case

Governments throughout the world spend billions in public money each year on social service provision. In many cases, funding becomes entrenched and opportunities for innovative solutions designed address the root causes of problems dry up. Not-for-profit organisations constantly struggle to identify and attract sufficient capital to scale innovations that attack the causes of social problems, improve the prospects for communities and individuals in need, and alleviate societal costs. Governments and non-for-profit organisations are thus trapped in a vicious cycle where a lack of resources for social innovation particularly in the context of prevention leaves vulnerable individuals and communities in a downward spiral of missed opportunity.

Where do SIPs fit conceptually?

SIPs have been conceptualised to encourage a collaborative innovative approach between the government, private and not-for-profit sectors to address pressing social problems through the design, implementation and funding of preventive and early intervention programs. For governments, SIPs provide the opportunity to increase effectiveness of public expenditure. For not-for-profit organisations, SIPs unlock a new source of long-term capital to fund effective programs. For impact investors, SIPs are a new product within the emerging field of impact investing to provide opportunity of a blended value return (refer below text box, Impact Investing: Mobilising capital for social change). Most importantly, SIPs facilitate the delivery of effective programs to improve the lives of individuals and communities in need.

In the WA context, SIPs most properly fit within the existing framework outlined by the government in *Delivering Community Services in Partnership Policy*. As can be seen in Figure 1, SIPs fit as a flexible arrangement with a service agreement that provides for payment only on delivery of agreed results.

How are SIBs considered in the literature?

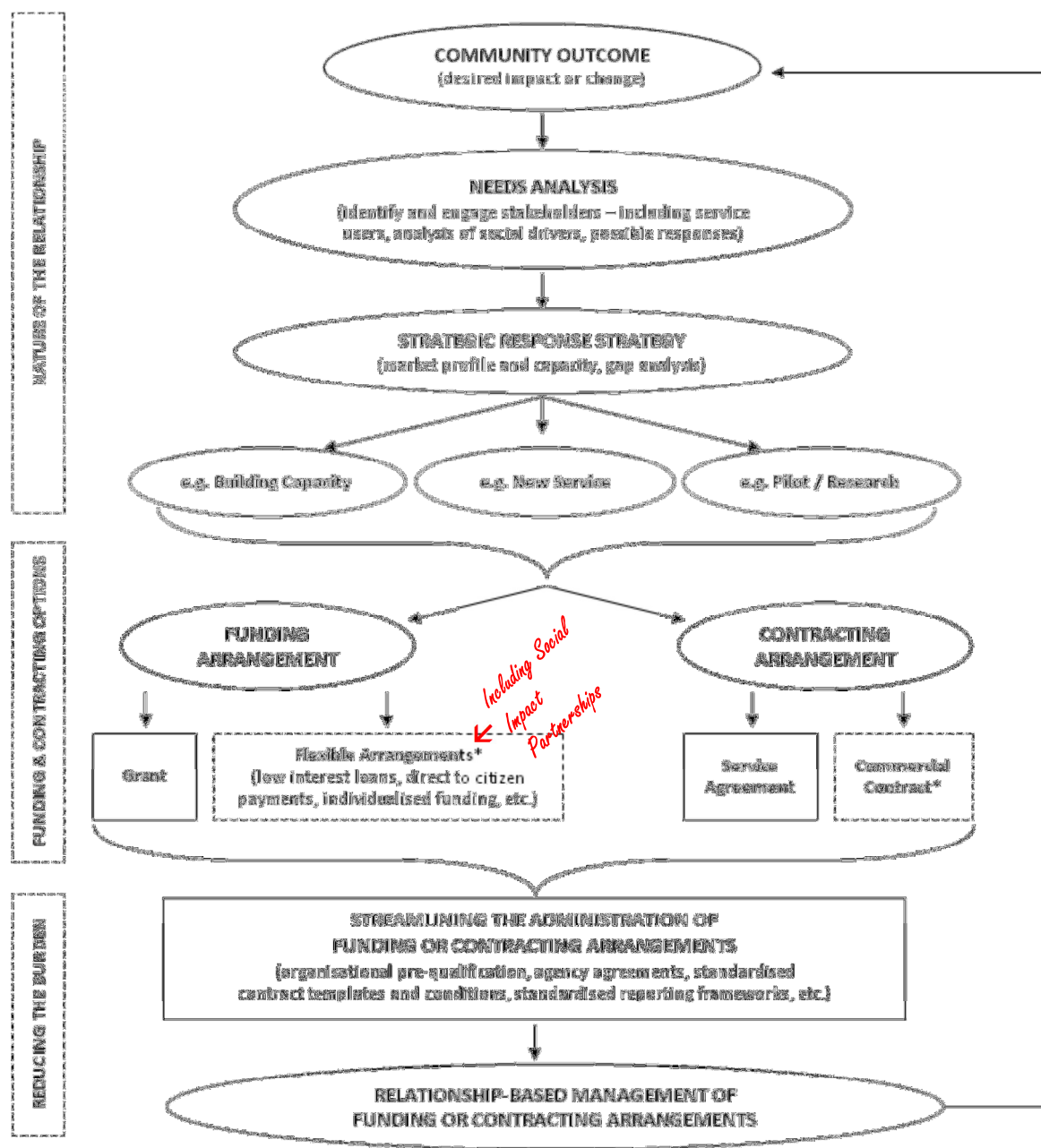
Early literature identified SIBs as a ‘new contracting and financing mechanism...driving significant non-government investment into addressing the causes of deep rooted social problems with returns generated from a proportion of the related reduction in spending on acute services’ [Social Finance Ltd, 2009; p.2]. The definition assigned to SIBs has been progressively refined over time, with emphasis now placed on SIBs being an innovative form of cross-sector collaboration to align all stakeholders’ interests around achieving common objectives for the benefit of poor and vulnerable populations [see Callanan et al., 2012; Social Finance, Inc., 2012]. Hence our adoption of the term SIPs.

Impact Investing: Mobilising capital for social change

Impact investments are investments made with the intention of generating measurable social and environmental impact alongside financial return and are considered to hold the potential to drive innovative solutions to global challenges [Global Impact Investing Network, 2012]. The form of these investments will vary, including traditional debt or equity for financially-sustainable enterprises that provide a product or service that generates impact, through to more innovative structures, such as Social Impact Bonds that monetise social outcomes [O’Donohue et al, 2010; p.7].

A growing interest in impact investing has been seen in Australia in recent years as evidenced by the emergence of a range of investment opportunities that have mobilised an array of impact investors. An estimated \$250 million has been channelled to impact investing in Australia since 2008 across a wide range of impact areas, including education, job creation, environment, health and financial services (refer Appendix 2). The potential market size for impact investing in Australia is estimated at \$10 billion [Centre for Social Impact, 2010: b.25].

Figure 1: Delivering Community Services in Partnership Policy Flow Chart



*While commercial contracts (with for-profit organisations) and flexible arrangements (such as low-interest loans) do not fall within the scope of the *Policy*, references are shown above to illustrate where they sit in relation to other funding and contracting arrangements

Putting definitions aside, at a practical level, SIPs are collaborative cross-sector partnerships designed to implement and fund innovative preventive and intervention programs that produce measurable, positive social outcomes resulting in improved effectiveness of public expenditures. The overarching feature of the collaboration under SIPs is that it facilitates the channelling of private risk capital from impact investors to fund social programs, with government paying only if the programs succeed. This upfront funding is critical in enabling service providers to roll out programs that are fully funded for the duration of the contract, thus removing the risk associated with insufficient access to capital, optimising the chance of success and allowing service deliverers to focus on service delivery. The mechanics of a SIP along with the key players within a SIP - community, government, impact investors, intermediary and independent assessor - are described at Figure 2.

Despite financing of social programs being a key feature of SIPs, and despite the use of the term 'bond' in nomenclature around the world they differ substantially from traditional bonds. Unlike traditional bonds that offer capital certainty and regular income to investors, the capital and income payments under the current conceptualisation of SIPs are dependent on performance, and thus better likened to equity.

How are SIBs progressing internationally?

The first SIB was launched in the United Kingdom in September 2010 by Social Finance, Ltd. The £5 million One*Service SIB is designed to provide funding for programs which will reduce the rate of recidivism among prisoners serving short sentences at Peterborough Prison. In the United Kingdom, around 60 percent of short-sentenced prisoners are convicted of at least one offense in the year after release. Impact investors will be repaid their capital investment and receive a financial return ranging from 2.5 percent to 13 percent commensurate with a reduction in re-offending of not less than 7.5 percent. If the measured improvement in reoffending is less than 7.5 percent, the impact investors lose their capital. See further detail at pages 18-19, One*Service SIB.

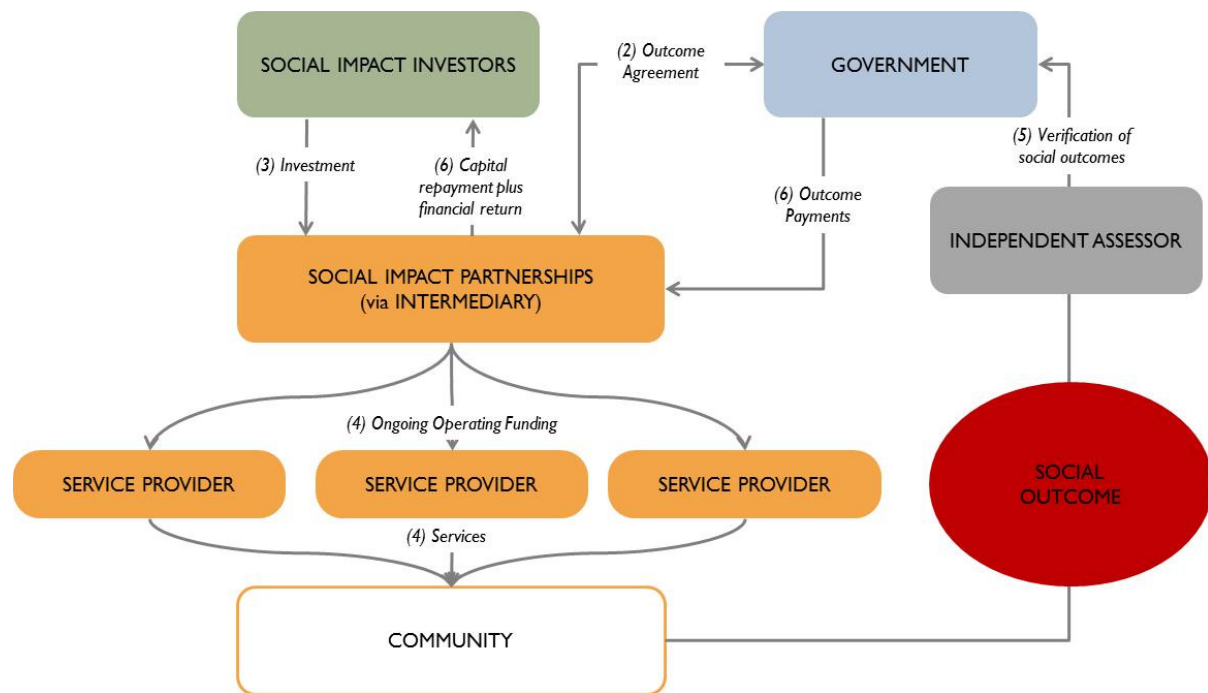
The model put forth by the One*Service SIB has attracted attention worldwide and, beyond the United Kingdom, is being actively explored in Australia, Canada, Ireland, Israel and the United States (refer Table 1). The United Kingdom now has 14 SIBs live or in development to address a range of diverse social including employment pathways for youth, children at risk, homelessness and complex families. A pathway for retail investors to participate in SIBs in the United Kingdom has been opened with the February 2013 launch of Allia's Future for Children Bond. A SIB to address help young offenders in New York has been invested in by Goldman Sachs. Elsewhere in the United States SIBs are being developed to help reduce homelessness and youth crime and undertake preventative healthcare initiatives.

Closer to home, in March 2012 the State Government of New South Wales selected three preferred proponents to commence joint development for Social Benefit Bonds (SBBs) aimed at reducing young adult recidivism and out-of-home care. Also, the Senate Economics References Committee recommended:

'the Office for the Not-for-Profit Sector identify policy areas where social impact bonds could be applied, including intractable problems in Aboriginal communities. The plausibility of creating social impact bonds in partnership with state governments should also be examined. The Office for the Not-for-Profit Sector should work with relevant government departments and agencies and social organisations to implement a social impact bond trial.' [2011; p.157-158]

The Government has noted this recommendation in its response to the Committee.

Figure 2: How do Social Impact Partnerships work?



1. The **community** is the starting point of any SIB as it is social needs of the community, or individuals within the community, that a SIB is designed to address.
2. **Government** enters a contractual agreement (i.e. Outcome Agreement) with an **intermediary** under which the intermediary agrees to deliver an agreed social outcome to a defined community in return for an agreed outcome payment. On the basis of the Outcome Agreement, the intermediary takes responsibility to identify program solutions to address defined social needs of the community, raise money from impact investors to fund these solutions, conduct ongoing project management, and work with service providers to ensure effective implementation. An intermediary may take the form of a program intermediary that arranges and project manages the SIP as well as directly participating in the delivery of programs, or a financial intermediary that arranges and project manages the SIPs and contracts selected service providers to deliver programs.
3. **Impact investors** contribute capital via the SIP to pay for service delivery by chosen service providers, cover the cost of the intermediary and pay for costs of outcome evaluation.
4. The intermediary provides multiyear funding to one or more **service providers** to deliver services to improve social outcomes of a target population. The model encourages innovation and cooperation among service providers whose individual and collaborative endeavours are rewarded for performance (i.e. outcomes, not outputs). The intermediary will monitor performance and work with the service providers to ensure the services successfully deliver anticipated outcomes.
5. An **independent assessor** determines if the pre-agreed social outcomes are successfully achieved.
6. If, and only if, the pre-agreed social outcomes are achieved, government makes outcome payments to the intermediary. In turn, the intermediary repays impact investors according to the terms of the SIP.

Table 1: International Social Impact Bond Activity

Australia	<p>The NSW Government announced in the 2011-12 Budget its intention to commit \$21 million to establish SIBs (referred to in NSW as “Social Benefit Bonds”) in the areas of out-of-home care and recidivism. An Expression of Interest was launched late September 2011, and in March 2012 three preferred proponents were selected to enter a joint development phase to further develop their proposals with the NSW Government. It is anticipated that the SIBs under development will begin to be formally marketed to investors in the second calendar quarter of 2013. The proposals, reported as totalling \$27 million, are:</p> <ul style="list-style-type: none"> • \$7mm SIB by Mission Australia to assist 500 young adult offenders from Junee and Parklea prisons for up to six years; • \$10mm SIB by Benevolent Society, Commonwealth Bank and Westpac to support 550 families over five years to reduce the number of days children spend in out-of-home care; and • \$10mm by UnitingCare Burnside to work with children up to five years of age and their parents over seven years to reduce the number of days in out-of-home care. <p>Mission Australia and UnitingCare Burnside have both appointed Social Ventures Australia as financial adviser to assist in structuring and fundraising of their respective SIBs.</p>
Canada	<p>Following recommendations of the Canadian Task Force on Social Finance made in its December 2010 report, <i>Mobilizing Private Capital for Public Good</i>, the March 2012 federal budget proposed support be provided to SIBs. In November 2012, the Minister of Human Resources and Skills Development issued a National Call for Concepts on Social Finance with submissions due January 2013. It is anticipated that a review of concepts, including opportunities for SIBs, will be released Spring 2013. The BC Social Innovation Council also lists SIBs within its April 2012 strategy.</p>
Ireland	<p>The Government Program for National Recovery 2011-2016 provides: “We will establish a new model of financing social interventions – called Social Impact Bonds – that share audited exchequer savings with charitable and voluntary organisations” (Department of Taoiseach, 2011: p.3). Clann Credo, a social investment organisation, with the support of Social Finance UK, is undertaking research to identify the high-potential areas for application of SIBs in Ireland.</p>
Israel	<p>SIBs focused on unemployment within the ultra-Orthodox (Haredi) and Arab-Israeli communities are being developed by Social Finance Israel.</p>
UK	<p>The United Kingdom has 14 SIBs live or in development with an approximate value of £280 million:</p> <ul style="list-style-type: none"> • One*Service SIB at Peterborough prison to reduce the rate of recidivism among prisoners serving short sentences at Peterborough Prison (refer “Overview of One*Service SIB at pages 18-19). • Six SIBs have been commissioned by the Department of Work and Pensions (DWP) through its £30 million Innovation Fund aimed at improving employment outcomes for young people not in education, employment or training (NEETs): <ul style="list-style-type: none"> ▪ Private Equity Foundation will launch a SIB to fund Tomorrow’s People’s ThinkForward project to place “super coaches” into ten schools to help 950 disadvantaged young people in Shoreditch ▪ Triodos Bank and Greater Merseyside Connexions Partnership (GMCP) will launch a SIB to deliver a three year program called “New Horizons” to improve the outcome for 3,900 disadvantaged young people in Merseyside ▪ YMCA will launch the first SIB in Scotland to support its work with 300 young people over a three year period ▪ Social Impact Partnerships established by Social Finance Ltd and chaired by Former welfare-to-work manager at Serco, Richard Johnson, will launch a SIB to fund Adviza to deliver a three year training and support programme to 1,500 disadvantaged 14 and 15 year olds in the Thames Valley ▪ Social Impact Partnerships will launch a SIB to fund Teens and Toddlers to roll out a well-established programme for over 1,100 at risk 14 to 15 year olds across the North West of England ▪ A partnership between Third Sector Consortium (3SC) and delivery bodies Dyslexia Action and CfBT Education Trust will launch a SIB to fund its Capitalise programme targeted at vulnerable young people in secondary schools in the Cardiff and Newport areas • Manchester City Council has voted to pilot a SIB to improve the outcomes for looked after children and young people aimed at reducing the number entering into foster care. • Essex County Council has awarded a contract to Social Finance Ltd to deliver Multi-Systemic Therapy (MST) to families across the county with complex needs aimed at reducing the number of young people aged 11-16 years entering care or custody. . Allia’s Future for Children Bond provides for a 20 percent allocation of subscribed investments to the Essex County Council SIB. • The Greater London Authority and Department of Communities and Local Government has awarded SIB contracts totalling £5 million to two providers – St Mungo’s and ThamesReach - to pay for

interventions to address the needs of 800 entrenched rough sleepers in London.

- Consortium of Voluntary Adoption Agencies (CVAA) has developed and is proposing launch a SIB to facilitate and support 300 extra adoptions a year.

Government support for SIBs in the United Kingdom is further evidenced through the launch of a £20 million Social Outcomes Fund and establishment of The Centre for Social Impact Bonds.

USA	<p>New York City launched a SIB in August 2012 to reduce youth recidivism for over 3,400 adolescent men coming out of incarceration from Rikers Island. Preventative education and counselling services financed by the pilot will be overseen by a program intermediary, MDRC, and will be delivered by two non-profit organizations, Osborne Association and Friends of Island Academy. Goldman Sachs is investing in the pilot through a \$9.6 million loan, supported by a \$7.2 million partial guarantee from Bloomberg Philanthropies.</p> <p>The states of California, Massachusetts, Minnesota, New York and Ohio are also pursuing SIBs:</p> <ul style="list-style-type: none"> • The city of Fresno, California and the California Endowment Fund are pursuing a pilot “health impact bond” working with 1,100 low income asthma patients to reduce asthma-related emergencies. • Massachusetts requested proposals in January 2012 for SIBs tackling chronic homelessness and juvenile justice, announcing in August 2012 that it had selected organisations to participate in the launch of two SIBs. The Corporation for Supportive Housing and Massachusetts Housing and Shelter Alliance were selected as program intermediaries for the delivery of preventative services designed to address chronic homelessness, while in one of the pilots. In the second pilot, Roca Inc. will provide job training and counselling services to address recidivism for youth leaving juvenile detention. Third Sector Capital Partners was selected as the financial intermediary overseeing both of these projects. • Minnesota has set aside up to \$20 million to pilot “human capital performance bonds” that blend elements of SIBs and municipal bonds to fund pay-for-performance human services programs. • New York state issued a request for information in September 2012 to identify potential SIB opportunities • Cuyahoga County, Ohio released a request for responses for a SIB pilot in November 2012. Third Sector Capital Partners is acting as technical adviser to the County in the process. <p>At the federal level, in the 2012 budget President Obama set aside \$100 million for pilot programs for SIBs (referred to in the US as “Pay-for-Success” bonds). The areas identified for application of SIBs included recidivism, early childhood intervention to address learning difficulties, summer school for disadvantaged students and elderly care services to avoid unnecessary placements in nursing homes. The administration subsequently announced in January 2012 that the Departments of Labor and Justice would support SIB pilots through the Workforce Innovation Fund and the Second Chance Act grants.</p> <p>In recognition of the potential value of application of the SIB model in the US, the Rockefeller Foundation has provided grants totalling \$1.075m to Nonprofit Finance Fund, Social Finance US and Third Sector Capital Partners to encourage development and support for application of the model, while the Omidyar Network has granted \$1.3 million to Social Finance US.</p>
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What are the key objectives of Social Impact Partnerships?

The key objectives of SIPs are [see Centre for Social Impact, 2011; Clann Credo, 2011; Social Finance UK, 2011a; Von Glahn et al., 2011a and 2011b; Callanan et al, 2012; Social Finance, Inc, 2012]:

- To increase the total pool of capital available for spending on social programs by mobilising private risk capital from impact investors
- To drive innovation and effectiveness by reducing program prescription by government and focusing on social outcomes
- To transfer the risk of program innovation from government to impact investors
- To promote disciplined performance measurement and evidence-based action to identify what works and, in turn, fund what works
- To promote more effective public expenditure.

Early discourse on SIPs emphasised the potential for government savings by facilitating the funding of preventive and intervention programs that reduce the need for government spending on acute intervention. The conversation has progressively moved to highlighting the potential of SIPs to

provide a balanced benefit between social impact and effective public expenditure. SIPs should be evaluated ‘not on their savings potential to government budgets but on their broader benefits to society,’ particularly the cumulative benefit to three groups – constituents, taxpayers and avoiders [Callanan et al., 2012; p.18]. Constituents derive tangible (such as increased earning) and intangible (such as improved well-being and social engagement) benefits from social programs in which they participate. Taxpayers benefit from the reduced need for expensive crisis-driven services that do not address the root causes of the problem. Avoiders benefit from not being subject to an adverse experience (such as being a victim of crime).

Achievement of these objectives is of course premised on a SIP being undertaken in an environment conducive to its application. Preconditions identified for successful SIPs include [see Social Finance, Ltd, 2011; Liebman, 2011; Mulgan et al, 2011; Clann Credo, 2011]:

- There is an unmet and ongoing social need
- There is a desire for a new, extended or more effectively delivered service/initiative to meet this unmet social need
- The outcomes and target population can be defined
- The outcomes can be measured
- Government (or other commissioner) is able to commit to a contract that would provide acceptable terms and conditions to attract investors.

Assuming preconditions are present and the stated objectives for SIPs can be realised, all stakeholders in SIPs benefit from successful SIPs (Table 2).

Table 2: Benefits to Stakeholders of Successful SIPs

Source: Social Finance, Inc. 2011, p.11

STAKEHOLDER	BENEFITS
Nonprofits	<ul style="list-style-type: none"> • Access to growth capital to scale up operations • Access to a stable and predictable revenue stream without labour intensive fundraising • Facilitated coordination with organisations working on overlapping problems
Impact Investors	<ul style="list-style-type: none"> • Achievement of financial return and social impact • Participation in a new asset class with portfolio diversification
Government	<ul style="list-style-type: none"> • Accountability for taxpayer funds • Reduction in the need for costly downstream remediation • Increased supply of effective services for citizens without financial risk
Community	<ul style="list-style-type: none"> • Access to an increased supply of effective social services • Reduction in the need for crisis-driven intervention

Who will invest in Social Impact Partnerships?

The single most important distinguishing objective of the SIP model is that it is ‘explicitly designed to bring in private investors’ [Social Finance, 2011b; p.4] to cover the upfront costs of programs.

The Young Foundation identifies a variety of funding sources for SIPs as described in Table 4. The Centre for Social Impact, in assessing the potential of a pilot in New South Wales, reported that likely investors will include philanthropic investors, as identified by Young Foundation, as well as socially-engaged investors looking for a commercial investment opportunity that provides a social impact [Centre for Social Impact, 2011; p.26].

During a recent segment of the *7:30 Report* on the New South Wales pilot, one of the preferred proponents reported:

'There is a fair bit of interest out there in the investment market for people to invest their money into social programs, investing their money into something that's actually going to make a difference' [Claerwn Little, Unitingcare Burnside, 2012].

Westpac, in its role as banker to The Benevolent Society, another of the preferred proponents, has identified appetite amongst big corporations and ethical investors commenting:

'Whilst this won't be a transaction that will be a high yielding investment, I think it will be secure, but it actually also delivers that - call it the warm inner glow of actually having an investment that delivers a broader social benefit to the community' [Craig Parker, Westpac, 2012].

Ultimately the assessed risk profile of a SIP, in regard to both its expected impact and financial return, will be what determines the universe of investors. SIPs structured to emphasise impact with a financial return that is considered 'below-market' for the perceived financial risk (that is, the risk of loss of capital) will appeal to 'impact-first' investors. 'Financial first' investors can be expected to only uptake SIPs if the financial return adequately compensates for the perceived financial risk, a risk that most will find difficult to ascertain until a successful track record can be established for SIPs or the risk of non-payment is sufficiently mitigated by Outcomes Agreements that, as discussed later in this report, incorporate a blend of output and outcome payments or acceptable credit enhancement techniques.

Table 3: Potential sources of investment capital for SIPs

Source: Adapted from The Young Foundation, 2011

SOURCE OF FUNDING	DESCRIPTION	ADVANTAGES
PHILANTHROPIC	Funds are raised from philanthropic investors and the government is contracted to pay based on achieved outcomes.	Can generally accept higher levels of risk, thus increasing scope for experimentation and innovation in service delivery.
PUBLIC SECTOR	A state or local government borrows from the existing market or uses its own resources to finance an innovation with a guarantee from the Federal Government to pay if particular milestones are reached.	Relatively few players and low transaction costs means public-sector SIPs are easy to design and implement.
COMMERCIAL	Funds are raised from commercial investors and the government is contracted to pay based on achieved outcomes.	Suitable where there is a proven model of successful intervention. Can be used to fund scale ups of successful pilot programs.
HYBRID	Funds are raised from two or more of the above sources.	A benefit of the hybrid model is the ability to introduce differing risk tranches for investors with complementary motivation for participation and risk-return appetite.

What are the risks of Social Impact Partnerships?

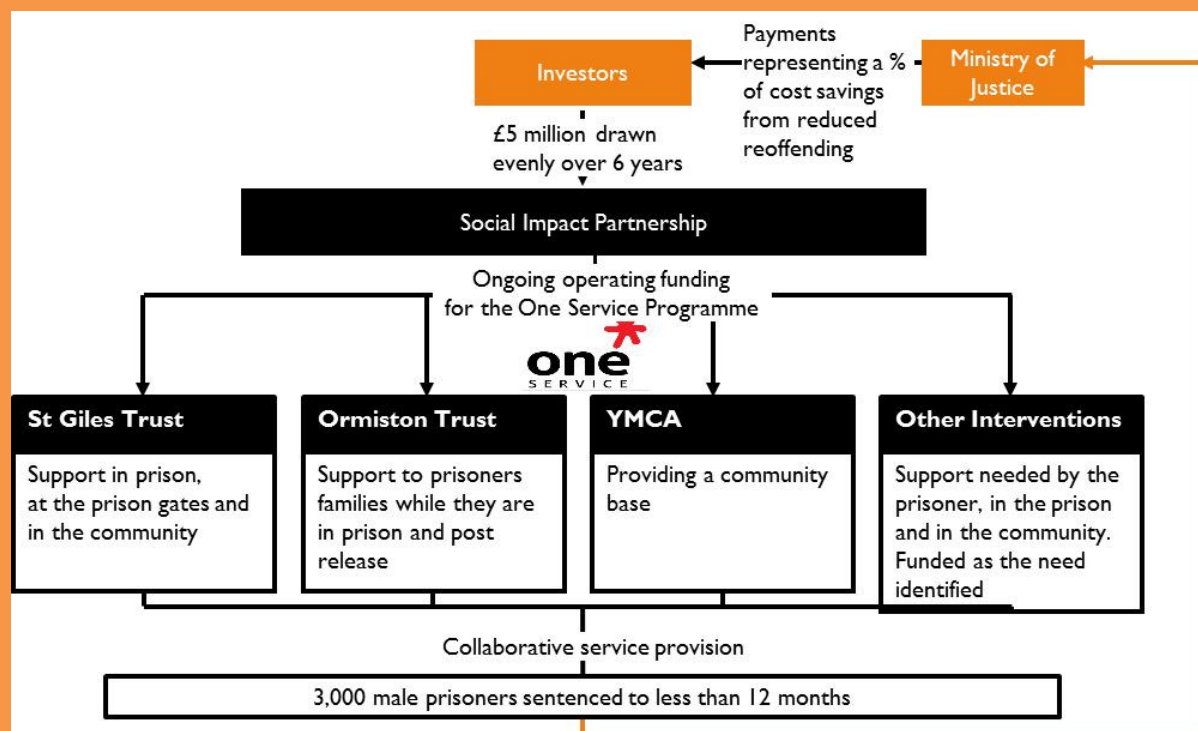
As with any cross-sector partnership involving contractual arrangements coupled with financial transactions, SIPs carry inherent risks. These risks include, but are not limited to, program, execution, beneficiary, intermediary, political, financial and reputational risk [refer Social Finance, Inc. 2012].

- **Program Risk:** The ability of SIPs to produce the desired social outcome for the target population depends on effective program design, coupled with strong delivery capacity of the service provider.
- **Execution Risk:** The multi-stakeholder relationships within any SIP are complex and must be well managed to ensure that the responsibilities of all parties are clearly defined and each has

capacity to deliver upon these responsibilities. Strong knowledge management and communication across all parties will be essential to ensure effective collaboration.

- **Beneficiary Risk:** Provisions must be in place to ensure that the community does not suffer harm should the SIP fail to deliver the agreed social outcomes.
- **Intermediary Risk:** Intermediaries must have the capacity and long standing commitment to add value throughout the lifecycle of a SIP. They must be able to deliver diverse expertise from capital structuring and raising to investor relations to cross-sector relationship management. Importantly, they must also have access to and be able to effectively manage and optimise input from subject-matter experts in regard to program design and implementation.
- **Political Risk:** Government must be able to provide impact investors with a secure commitment to make timely payment of agreed amounts upon successful delivery of agreed social outcomes. Such commitment must be capable of withstanding the vagaries of government budget and political cycles.
- **Financial Risk:** Impact investors bear the full risk of non-payment should the social programs supported by the SIP fail to deliver the agreed social outcomes. It is possible that SIPs may adopt risk mitigation techniques that alleviate, at least partially, investors' financial risk. Risk mitigation techniques may include credit first-loss provisions, capital reserves, capital guarantees, credit-wraps and other like techniques. The recently announced pilot in New York to address youth recidivism includes a partial guarantee from a philanthropic foundation (refer Table 1). It may also be that in order to achieve an acceptable risk transfer to impact investors and economic value for commissioners that Outcome Agreements incorporate a mix of output and outcome payments.
- **Reputational Risk:** Unsuccessful SIPs pose reputational harm to the service providers that have failed to deliver the agreed social outcomes. Such failure can be expected to lead to adverse implications for these service providers in future fundraising efforts. Government also faces reputational risk should it fail to honour any of its contractual commitment to make outcome payments despite timely achievement of the agreed social outcome.

Overview of One*Service SIB



The world's first social impact bond, One*Service SIB, was launched by Social Finance Ltd. in September 2010, aimed at reducing re-offending by short-sentence male prisoners leaving Peterborough Prison. Social Finance is a financial intermediary established in 2007 to help build a social investment market in the UK through devising financial structures and raising capital to enable organisations successfully tackling social problems to access the investment they need to innovate and grow. The SIB model had been conceptualised in 2007 and, following nearly three years of research and design, including extensive consultation with potential relevant stakeholders within government, the social sector and private investors, the product was launched.

The key elements of the One*Service SIB are [Social Finance UK 2011c]:

- ▶ A contract was entered into with the Ministry of Justice to address the reoffending behaviour of 3,000 short-sentenced male prisoners leaving Peterborough prison over a six-year period. The Ministry of Justice, in combination with the Big Lottery Fund, agreed to make outcome payments if the number of reconviction events among Peterborough prison leavers, measured by offences committed within a 12-month period following release, is successfully reduced by not less than 7.5 percent as compared to the offending behaviour over the same period of a “control group.”
- ▶ One* Service SIB, issued by Social Finance, raised £5 million from 17 investors, primarily from the UK and two from the US, with proceeds being made available to provide upfront funding for the provision of intervention services to be provided under One* Service. The majority of investors in the One* SIB are charities or foundations, along with some high-net-worth individuals.
- ▶ A set of interventions delivered by four not-for-profit organisations – St Giles Trust, Ormiston Children and Families Trust, YMCA and Supporting Others through Volunteer Action (collectively One* Service) – provide tailored, individual service to three cohorts of 1,000 unique short-sentenced male prisoners from Peterborough prison. Coordination across the four not-for-profit organisations is managed via a common case management system used for all members of the cohort while in prison, passing through the prison gates, and at post-release, while the overall delivery of One*Service is the responsibility of a full-time project director.

- ▶ Investors receive an increasing return if the number of reconviction events among Peterborough prison leavers falls by not less than 7.5 percent, with the return to investors commensurate to social outcomes and ranging from 2.5 percent to 13 percent.
- ▶ An Advisory Group provides Social Finance, on behalf of investors, with a wide range of expertise in implementing the SIB.

In a report commissioned by the Ministry of Justice to examine the lessons learned from the planning and early implementation of the One* Service SIB, it was observed that the majority of the investors in the One*Service SIB are charities or foundations, along with some high-net-worth individuals [Disley et al., 2011; p. 25]. The charities and foundations include the Barrow Cadbury Trust, Esmée Fairbairn Foundation, Friends of Provident Foundation, The Henry Smith Charity, Johansson Family Foundation, LankellyChase Foundation, The Monument Trust, Panahpur, Paul Hamlyn Foundation and the Tudor Trust [Social Finance, 2010a]. Some investors elected to fund their investment through grants, while others used endowment capital [Disley et al., 2011; p.26]. Interviews conducted with investors as part of the report revealed ‘trust in Social Finance and the providers, the desire to support an innovative, emerging funding mechanism, and alignment with a criminal justice mission, attracted investors’ [Disley et al., 2011; p.32].

From a structural perspective, investment in the One* Service SIB occurs through a limited liability partnership. A limited liability partnership is a generally acceptable legal structure used in mainstream private equity and provides a transparent tax structure under English law (i.e. investors are responsible for paying tax on their share of the income and gains arising from the partnership, as per their individual tax status). UK resident taxable investors invest directly in the partnership, whereas UK tax-exempt investors that qualify as charities invest through a charity feeder instrument which allows outcome payments to be received by charities as donations.

While the early evidence from the pioneering SIB indicates an unmet social need is being addressed by One*Service – clients reporting better control over lives and local police conveying lower incidences of reoffending [Social Finance, 2011c; p. 10] – the ultimate test of its success for impact investors will only be answerable at the final maturity of the SIB when the level of financial return will be able to be fully determined. An indication of the financial return will begin to emerge commencing year 4, which marks the first potential instance when the performance of One*Service may qualify for an outcome-based payment by the Ministry of Justice.

In the one year since the launch of the One*Service SIB, David Hutchison, CEO of Social Finance, observes that they have ‘learned that the flow of money influences the level and efficiency of delivery’ [Social Finance, 2011c; p. 2]. By providing flexibility of funding the SIB model enables funding to be directed to best meet the needs of the targeted user population rather than, like many existing programs, flow to the provision of a particular service irrespective of need or outcome. The stable funding provided under the SIB model may also be considered an ‘advantage in terms of organisational stability and less disrupted service provision’ [Clark, et al., 2009 as cited in Disley et al., 2011; p. 21].

3. Taking lessons from the practice of payment-by-results

A fundamental component within the SIP model is the Outcome Agreement that provides for payment of an agreed amount for successful delivery of an agreed social outcome. This Outcome Agreement can be likened to a payment-by-results contract, an approach which has evolved over many decades since the middle of the last century.

Payment by results has been described as ‘performance management with teeth.’ Government commissioners and private procurers focus their choice and performance management against ultimate program or policy objectives and set the incentives and rewards against achievement of these. There are a number of reasons why governments and private procurers seek to move to this way of funding services. These include the desire to: encourage a more rational investment of capital and non-capital resources; transfer performance risk to providers; drive innovation and front-line empowerment; provide for greater security and longevity of funding enabling better planning management and rational capital investment; integrate several funding streams; and integrate service delivery components/teams.

Successful contracting and procurement for outcomes is an activity which relies upon: knowledge of the particular social service operating environment; excellent data sources; and a generous amount of thoughtfulness and judgment. There are no silver bullets or simple formulas. There are often tensions between goals.

A number of principles useful for guiding the development of Outcomes Agreements to be leveraged in SIPs can be gleaned from the work of Sturgess, Cumming, Dicker, Sotiropoulos [2011] *Payment by Outcomes – A Commissioners Toolkit*, 2020 Public Services Trust, London:

- Commissioners must understand that good outcomes based commissioning is not formulaic and will be the result of a somewhat iterative process of learning and discovery between providers and purchaser/commissioners.
- Genuine alignment of the provider and purchaser/commissioner interests is critical and drives outcomes better than any specifics of contracting.
- Know where payment for results works best and where it is not suitable. Evidence suggests it is best applied where commissioners have some confidence in the service models that are likely to work, and want to improve service delivery chains to deliver better outcomes. Knowledge of all the linkages between inputs, outputs and outcomes need to be gained. Payment for results should never be a default option. Environments where the outcomes have very long delays before they are measurable, for example, may not be appropriate for pay-for-results payment regimes.
- Disciplined thinking about outcomes is required for definition of appropriate outcomes is one of the most difficult challenges in public administration. The authors caution that outcome measurement works best where: the nature of the outcome is relatively uncontested; it can be easily captured in operational performance measures; an indicator of the outcome can be secured reasonably soon after the intervention; the outcome is attributable to the subject intervention rather than external factors; and there is a need for judgement as to the most appropriate intervention. Sometimes, for these and other reasons, outputs will be a more appropriate proxy. Other times outputs or inputs may be the better course.
- Understand the full dynamics and design of the system in which you are operating recognising performance contracting relies on measures, standards and incentives that give full regard to the human dimensions of performance regimes. Successful performance contracting has been shown to draw not only on financial incentives, but also on a wide range of non-financial incentives.
- The human capital playing the commissioning role needs intensive training and development and sometimes new leadership. Often coming from a tight compliance background, development of the nuance and judgement required to design and implement the type of successful partnerships that underpin great outcomes over time is not in everyone’s capacity.

4. Potential for Social Impact Partnerships in Western Australia

The successful application of SIPs in WA, as in any jurisdiction, requires careful design and implementation, taking full account of the context of the local environment. Consideration needs to be given to how SIPs fit within the myriad of regulation that governs the delivery of social services and financial products. Government policy pertaining to contracting for social services, together with budget allocation processes, often complicated by multiple funding streams (cross-agency and cross-jurisdiction), must also be understood. This is additional to the challenge of assessing whether the core building blocks for a successful SIP exist, and can be configured to improve the lives of individuals and communities in need.

SIPs complement the reform agenda

As discussed earlier in this report at Section 1, there is a raft of reform underway in the not-for-profit sector in WA right now. In addition, the sector is facing national regulatory reform following the introduction of the Australian Charities and Not-for-profits Commission in October 2012. New modes of operating are being encouraged by the shift towards outcomes-based contracting under the WA government's *Delivering Community Services in Partnership Policy*, an increased focus on innovation, and the need to develop alternative revenue streams under the Social Enterprise Fund and Social Innovation Grants Program. These changes are creating intense pressure on individual not-for-profit organisations and the sector as a whole to be nimble and responsive, while simultaneously ensuring continued and expanded support is provided to individuals and communities in need.

SIPs, as a collaborative outcomes-based partnership, fit well within the continuum of purchasing options laid out in the *Delivering Community Services in Partnership Policy* and which centres upon achieving better outcomes for Western Australians. The policy recognises that not-for-profit organisations play an important role in the wellbeing of communities and are often able to provide flexible and innovative responses superior to those of government. Not dissimilar to the process for development of a SIP, the policy provides for articulation of community outcomes – social, cultural and/or economic – and development of a strategic response strategy following a needs assessment of services required for delivery of the desired community outcome. The policy also recognises that the funding arrangements to enable implementation of the strategic response strategy may be multiple (including grants, loans, direct citizen payments and individualised funding), albeit includes only traditional government grants within its scope with alternative funding arrangements, such as those that may arise under a SIP, left subject to other relevant government policies. Contracting arrangements for the purchase of services from not-for-profit organisations by government are also included in the policy. Emphasis is placed on specifications for such contracts to be on outcomes sought and avoid prescribing inputs, and recognises that sustainable service delivery and ongoing viability of not-for-profit organisations requires consideration be given where appropriate to long-term arrangements.

One of the challenges likely to be faced by not-for-profit organisations under the policy is how to unlock funding sources to supplement government grants and meet working capital needs prior to receipt of payments under contract arrangements. This is precisely the funding challenge that SIPs are designed to address. SIPs raise funds upfront from impact investors for use by not-for-profit organisations to fund selected preventive and intervention programs designed to deliver the agreed social outcome specified within an Outcomes Agreement. It is encouraging that the approach to contracting articulated in the policy, specifically in regard to a focus on outcomes and long-term arrangements, is at a conceptual level consistent with that needed for Outcome Agreements under a SIP to unlock alternative funding.

A further benefit of SIPs, complementary to recognition within the policy to develop strategic response strategies to community needs, is they inherently acknowledge that most social needs are complex and a “one-size-fits-all” solution is rarely effective. Thus in contrast to traditional outcomes-based contracting arrangements with single providers, SIPs, via an intermediary, provide

for engagement with a flexible portfolio of locally-tailored interventions from multiple service providers to optimise the target outcome.

What are the social needs to which SIPs may be applied?

It is reasonable to believe the potential areas for application of SIPs in WA will be similar to those being considered in other jurisdictions around the world.

Criminal justice, out-of-home care, homelessness, complex families and youth-at-risk are areas for which SIPs have been or are currently being designed and implemented (refer Table 1). Commentators also believe SIPs may be applied to address a range of other societal challenges, including chronic health problems (such as management of diabetes), mental health difficulties, drug and alcohol abuse, and aged care [see Social Finance UK, 2011b, p.6; Young Foundation, 2011, pp 23-27; Moynagh, 2011, pp 14-15].

While no explicit criteria or framework for identification of areas for application of SIPs has yet been developed, it would seem they are 'well suited to scale interventions focused on behaviour change' [Callanan et al, 2012; p.12]. Additional guiding factors include government policy priority, societal benefits and investors' appetite or empathy for the targeted social outcome.

Table 4 identifies potential vulnerable populations in WA that may benefit from SIP-funded preventive and early intervention programs. There would appear to be high potential for SIPs to be considered for programs driving social outcomes for Aboriginal communities throughout WA.

Are the essential elements for SIPs present in Western Australia?

As has been discussed, outcomes data and robust evidence gathering mechanisms and systems are required in order that SIPs, which pay on delivery of outcomes, can realistically be put in place. At present the WA social service delivery sector is responding to the procurement reforms being driven by Government and the *Putting the Public First* reform process initiated by the Economic Audit Committee. This is an early stage of generating a knowledge base to inform the cultural change involved in a true shift to an outcomes focus. The next stage will involve the development of the stand-alone, shared and 'ecosystem' measurement systems to underpin outcome measurement. This will all take time, but the journey has at least begun.

Potential areas of applications of SIPs are circumscribed by this unavailability of data and lack of provider readiness. Once candidate areas with these requisite attributes are identified, the challenge becomes identifying engaged government agencies along with the collective of programs, service providers, intermediaries and impact investors that could come together under the collaborative partnership of a SIP to deliver measurable social outcomes to the identified community. A confluence of capable stakeholders that are highly motivated to work within a collaborative partnership to solve a given social need for a defined community is fundamental to any SIP.

Table 4: Potential Application of SIPs in Western Australia

Target Population	Prevalence in Western Australia	Example Programs	Societal Benefit
Adult and Juvenile Offenders [ABS, 2011; Loh et al, 2007]	<p>ADULTS</p> <ul style="list-style-type: none"> The prison population in Western Australia reached 4,648 people (92.4% male; 38.1% Aboriginal) in 2011 representing a 16% increase over the past decade Over half (54.1%) of all prisoners have been previously incarcerated Four out of five prisoners (80%) were unemployed at the time of imprisonment Aboriginal people account for 3.3% of the state's overall population but represent 38.1% of people in jail recording a rate of arrest 8.1 times the rate of non-Aboriginal people <p>JUVENILE</p> <ul style="list-style-type: none"> The juvenile detention rate of Western Australia is the third highest in the country at an average of 200 young people on an average night and has recorded an increase of 33% over the four years from 2007 to 2011 Aboriginal juveniles are detained at a rate of 555.3 per 100,000 which is some 44 times greater than non-Aboriginal youth and a rate that is almost double the national rate 	<ul style="list-style-type: none"> Community-based re-entry programs Multi-systemic, multi-dimensional, or functional family therapy 	<ul style="list-style-type: none"> Lower recidivism rates Avoided corrections, probation, parole and facilities expense Reduced crime victimisation
Out-of-home Care [AIHW, 2011]	<ul style="list-style-type: none"> 2,737 children aged 0-17 years (45% Aboriginal) were in out-of-home care as at June 2010 representing an increase of 90% over the past decade Aboriginal children are over-represented in the out-of-home care system being 13 times more likely than other children to be placed in care 	<ul style="list-style-type: none"> Multi-disciplinary assessment, decision making and joint working teams 'around the child and family' 	<ul style="list-style-type: none"> Avoided out-of-home care costs Functional individuals, families and communities
Early Childhood [AEDI, 2009]	<ul style="list-style-type: none"> 25% of all children preparing for primary school in Western Australia are developmentally vulnerable on one or more domains of the Australian Early Development Index (> 50% for Aboriginal children) 	<ul style="list-style-type: none"> Improved access and quality of early childhood education Integrated child and family centres Parenting resource centres 	<ul style="list-style-type: none"> Functional families and communities Breakdown long-term cycles of deprivation and dependency
Chronic Health Problems (e.g. diabetes) [Diabetes WA, 2009; AIHN]	<ul style="list-style-type: none"> 28,138 people diagnosed with diabetes were admitted to hospital in Western Australia at least once in 2008-9. This represents approximately 30% of people currently living with diabetes. Aboriginal people are 3 times (adjusting for age differences) more likely to report living with diabetes 	<ul style="list-style-type: none"> Systematic and coordinated service delivery Self-management support 	<ul style="list-style-type: none"> Improved health outcomes leading to increased wellbeing and productivity Reduced burden and cost associated with chronic conditions (e.g. reduced hospitalization)
Alcohol and Substance Abuse [DAO, 2011; DAO and DoHWA, 2011; AIHN]	<ul style="list-style-type: none"> In 2010 22.7% of Western Australians reported to consume alcohol at a level that placed them at a risk of lifetime harm Between 2005 and 2009, there were almost 67,000 alcohol-related hospitalisations in the state The proportion of the Aboriginal population who drink at a risky/high risk levels is more than twice that of the non-Aboriginal population 	<ul style="list-style-type: none"> Integrated programs including consumer education, peer group support, counselling, family education and case management 	<ul style="list-style-type: none"> Improved health outcomes (e.g. reduce hospitalization) leading to increased wellbeing and productivity
Homeless [DCP, c.2010]	<ul style="list-style-type: none"> Every night in Western Australia there are over 13,000 people without a stable place to sleep, with one third being between 12 and 18 years old and almost 10% under the age of 12 Aboriginal people make up 11.2% of the total homeless population 	<ul style="list-style-type: none"> Permanent supportive housing 	<ul style="list-style-type: none"> Decreased use of acute medical care, shelter and incarceration

Like the rest of Australia, the 'ecosystem' for SIPs within WA lacks qualified intermediaries with the breadth of skills and expertise to raise investment capital and provide long-term project management. In the New South Wales pilot, the lack of specialised intermediaries has evidenced itself in that none of the preferred proponents involve an intermediary. All are pursuing a lead delivery structure [refer Social Finance, 2011c; Mulgan et al, 2011; The Centre for Social Impact, 2011], in which they assume the responsibility for sourcing and managing the investment capital as well as delivery of social services. The Benevolent Society has teamed with Westpac Banking Corporation and Commonwealth Bank to access financing capability, while Social Ventures Australia is financial adviser to Mission Australia and UnitingCare Burnside.

Recognising the field of impact investing is nascent in Australia, the depth of impact investors in the ecosystem is also lacking. A focused strategy to engage potential impact investors, including charitable foundations, high-net-worth individuals and socially engaged corporate and institutional investors, will be required for any SIP in WA.

For government and service providers within the not-for-profit sector, SIPs necessitate a culture shift and willingness to embrace a new collaborative approach. Government must be willing to collaboratively design outcomes-based contracts that, as discussed in Section 3, will take a form quite different to traditional government-vendor contracts. The shift required to move from prescribing services to contracting for social outcomes should not be underestimated.

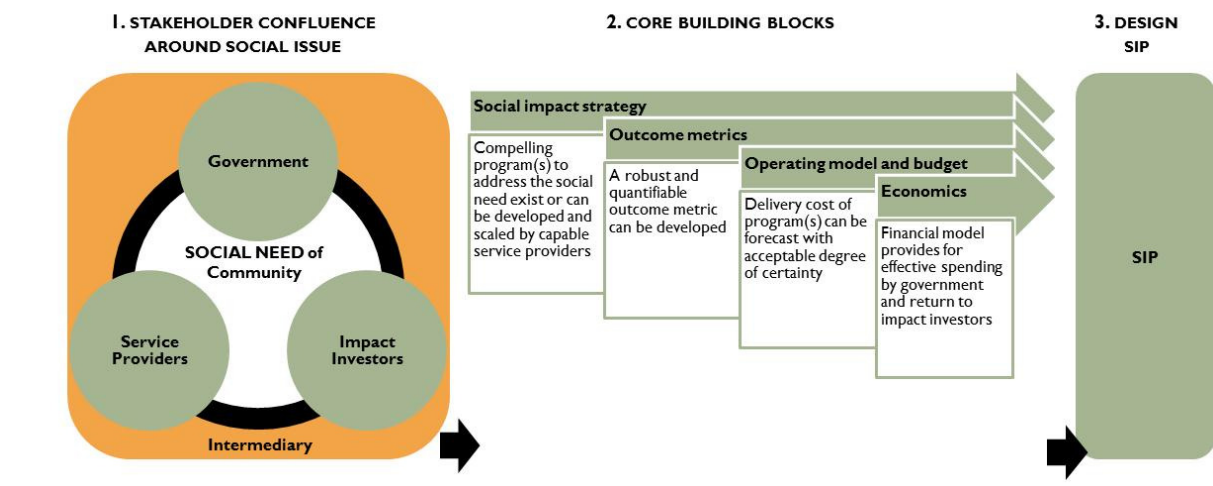
Beyond willing collaborators any SIP requires four core building blocks [Social Finance, Ltd, 2011a]:

1. **Social impact strategy:** A compelling social impact strategy that all SIP stakeholders are confident will address the social need and deliver pre-agreed social outcomes. Confidence will largely rest on the strategy being supported by solid evidence-based research and a highly capable and stable not-for-profit organisation, or multiple not-for-profit organisations working collaboratively together, being committed to delivering the services articulated in the strategy.
2. **Outcome metrics:** A robust and quantifiable outcome metric that is operationally feasible for the service providers, acceptable to impact investors, and an appropriate and acceptable trigger for payments by government under an outcomes-based performance agreement.
3. **Operating model and budget:** A comprehensive operating model and budget that takes account of all costs associated with delivery of the social impact strategy by the not-for-profit organisation(s), project management by the intermediary and outcome measurement and evaluation.
4. **Viable economics:** The value of the social outcome to government as determined by total societal benefit must provide for effective government spending and an acceptable financial return to impact investors.

A high level of iteration can be expected to occur throughout the process of identifying the core building blocks. Ultimately it is essential to have engaged SIP stakeholders committed to tackling the target social issue, compelling programs and capable service providers to solve the social issue, robust and measurable outcome metrics, and total societal benefit that allow effective public expenditure together with financial returns to impact investors. See Figure 3.

Figure 3: Social Impact Partnerships: Essential Elements

Source: Adapted from Social Finance, Inc. 2011



What adaptations of the SIP model can be expected in Western Australia?

Being a new innovation there is no precise script as to how SIPs will develop in different markets and it can be expected that nuances to the basic model will arise to accommodate local factors. Our research indicates that in WA, changes to the model are most likely to centre on who makes payment under the Outcomes Agreement. For while government is and will most likely remain the biggest purchaser of social services in WA, it is possible that other social service purchasers may assume the role of counterparty to the Outcomes Agreement. These may include philanthropists, community foundations, corporations and native title trusts. For instance, there may be preventive programs that generate positive social outcomes for which an entity beyond government may agree to pay for if the outcomes are beneficial to them [refer Social Finance, Inc., 2012]. Basically any entity, or group of entities, that has financial capacity to pay outcome payments and the desire for social outcomes may think about how to utilise the SIP model.

Take for example, a mining company may find it attractive to participate in a SIP that generates social outcomes addressing social needs within Aboriginal communities consistent with those contemplated in Mining Benefit Agreements. Alternatively, in a mature market place, not-for-profit organisations themselves may purchase results and outcomes in some areas from other service providers. Furthermore, in a self-directed service environment, individuals may pool resources and enter the market for pay for result outcomes (i.e. collective purchasing).

The other area where we would anticipate adaptation is in regard to the payment mix within the Outcome Agreement. The SIP model as demonstrated in One*Service SIB and considered in the literature is based on a contract arrangement between government and the intermediary (i.e. the Outcomes Agreement) where payment is completely performance based. That is, government pays only if the targeted social outcomes are achieved, with impact investors taking the risk that the chosen not-for-profit organisations and selected programs deliver these outcomes. It is clear from discussions undertaken as part of the research for this report, that Outcomes Agreement that incorporate a combination of output and outcome based payments may be necessary to attract a wide array of impact investors. The greater the proportion of outcome payments in the Outcomes Agreement, the greater the risk transfer to impact investors thus the greater the challenge of attracting all but philanthropic investors to SIPs.

Finally, we note that it is possible that the first mover in WA to initiate SIPs will range from government, not-for-profit service providers and impact investors. Our research has indicated that for some larger clinically focused not-for-profit organisations, for example, the investment for

savings case is so strong that they will consider advocating for a trial SIP in their delivery service areas. Also some not-for-profit organisations with well-evidenced programs are eager to explore how SIPs may unlock an alternative source of funding for expansion of their work.

5. What SIPs mean for key stakeholder groups in Western Australia

This report has presented the potential for SIPs in the WA context. We have presented SIPs as both collaborative outcomes-based partnerships and a performance-based payment model on the continuum of value-based purchasing options. We have also considered the potential for SIPs to encourage program innovation across multiple service providers and a means by which to increase the pool of capital to fund preventive and early intervention programs. Finally, we highlighted that SIPs are a complementary addition to the suite of tools available to improve the lives of individuals and communities in need.

The findings of this report, in summary, have the following implications for key stakeholder groups in WA:

Government	SIPs are a tool that can be used, in the right circumstances, to incentivise achievement of ultimate policy objectives and program outcomes. This enables government to: encourage a more rational allocation of resources including towards early intervention and preventive programs; transfer risk to impact investors; drive innovation and front-line empowerment; provide for greater security and longevity of funding, enabling better planning, management and rational investment in capital; integrate several funding streams; and integrate multiple service deliverers.
Other procurers of social services	As with governments, other procurers of social services could use SIPs as a means of achieving far more effectiveness from their social spend through the more rational allocation of resources, innovation, capital investment, focus on effective prevention and better research planning and management enabled by more secure and correctly incentivised funding streams.
Not-for-profit service providers	For not-for-profits, SIPs could do several things: provide growth funds for successful service delivery models and teams enabling them to scale locally and nationally (and potentially even internationally); provide rewards for research, development and innovation that result in improved outcomes; increase resources to effective early intervention and preventive programs; enable more flexible payment models for human capital enabling recruitment of a different mix of skills and expertise; and streamline funding arrangements across multiple government agencies.
Philanthropists High-net-worth individuals Impact Investors	SIPs become a category in which philanthropists can diversify their funding activities and maximise the impact of the funds they have available to support the causes they are passionate about. More businesslike opportunities to make a difference may, in fact, attract a different type of impact investor than traditional philanthropy/charity donors. Overseas experience suggests the younger, more entrepreneurial philanthropists are particularly attracted to SIPs given the models more venture capital like characteristics.
Finance professionals	Over time, a market for impact investing, debt and equity-type investments in social service projects could emerge. Early indications from interstate and overseas are that this market will take some time to build, but will eventually become another asset class and be a set of products that private wealth clients, in particular, will expect major financial service providers to offer. SIPs would comprise one product within this asset class.

APPENDIX 1: Recommendations of the Senate Economics References Committee

Source: Senate, p. xxiv –xxvii

ESTABLISHING A SOCIAL FINANCE TASKFORCE

Recommendation 2.1

Government establish a Social Finance Taskforce to assess the mechanisms and options in the progress and development of a robust capital market for social economy organisations in Australia

Recommendation 4.3

The proposed taskforce consider the potential for philanthropic trusts and foundations to invest a percentage of their corpus in social investment options

Recommendation 4.4

The proposed taskforce consider the potential for superannuation funds and other institutional investors to invest in emerging social impact investment products

Recommendation 5.2

The proposed taskforce consider possible options to develop Community Development Financial Institutions in Australia

EDUCATION, AWARENESS AND CAPACITY BUILDING

Recommendation 4.5

Professional organisations develop materials and professional development workshops to inform the corporate sector of investment opportunities in the social economy

Recommendation 5.1

Philanthropic and financial advisory services promote and encourage opportunities for social investment and engagement with the sector

Recommendation 6.1

Programs and workshops relating to social impact investment be developed by investment organisations to encourage investors to engage in social investment projects and opportunities

PROMOTING SOCIAL INVESTMENT PRODUCTS

Recommendation 4.1

The Australian Tax Office, in consultation with the Australian Charities and Not-for-Profits Commission and other relevant stakeholders, issue explanatory material for Private Ancillary Fund trustees providing guidance on engagement in social impact investment

Recommendation 4.2

The Commissioner of Taxation, Treasury and the Office for the Not-for-Profit Sector work to create benchmarks and standards for financial returns on social investment classes, in order to help trustees and fund managers make informed decisions in this area

Recommendation 6.2

The Department of Treasury and Finance and Deregulation examine ways to create incentives to invest in a social bond market, including the feasibility of tax incentives and government guarantees

Recommendation 6.3

The Office for the Not-for-Profit Sector identify policy areas where social impact bonds could be applied and work to implement a social impact bond trial

STRENGTHENING SOCIAL ENTERPRISE

Recommendation 8.1

The Office for the Not-for-Profit Sector identify relevant current and future government programs that could be extended to offer specialised support for social enterprises, cooperatives, employee share ownership plans and employee buyouts

Recommendation 8.2

The Department of Finance and Deregulation, Treasury and the Office for the Not-for-Profit Sector review the competitive tendering and contracting framework and examine the costs and benefits of social tendering and inclusion of a community/social benefit criterion in competitive tenders

DEVELOPING A MEASUREMENT FRAMEWORK

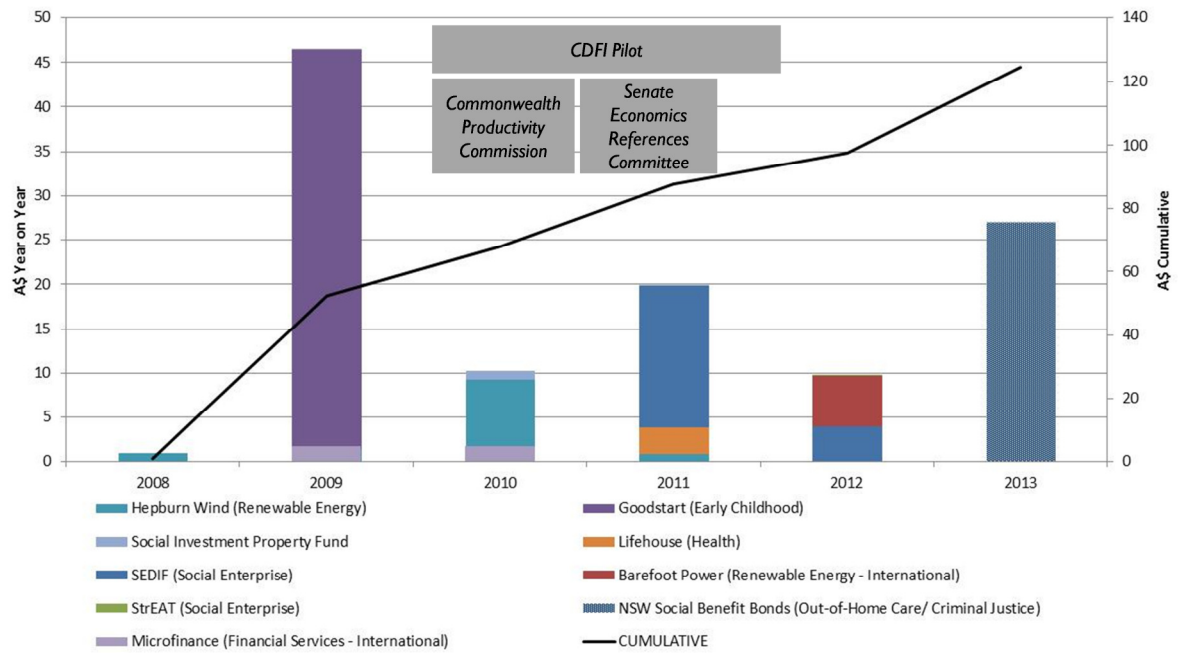
Recommendation 7.1

The Department of the Prime Minister and Cabinet develop a robust measurement framework for social economy organisations in Australia

Recommendation 7.2

The Office for the Not-for-Profit Sector prepare a guide for social economy organisations to assist in the evaluation of their performance

APPENDIX 2: Emergence of Impact Investing in Australia



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Acknowledgements

Jocelyn Bell, The Benevolent Society

Sue Bergersen, Yamatji Marlpa Aboriginal Corporation

Julian Butler, Myer Family Office

Christina Colegate, Yamatji Marlpa Aboriginal Corporation

Justine Coyler, Hills Community Support Group Inc

Coralie Flatters, Hills Community Support Group Inc

Kristin Giantris, Nonprofit Finance Fund (US)

Stephen Goldberg, Social Finance Inc. (US)

Steve Hawkins, The Benevolent Society

David Hutchison, Social Finance Ltd (UK)

Adam Jagelewski, Centre for Impact Investing (Canada)

Roger Kennedy, Mission Australia

Dan Minchin, Head of Strategy, Silver Chain & RDNS (SA) Group

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Peter Taplin, Westpac Banking Corporation

Christopher Thorn, Evans & Partners

Robert Walsh, Sustainability Advisers

Jonathon Wolfe, Social Finance Limited