



# research

**Social Impact  
Bonds: A  
new way to  
privatize  
public  
services**

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## Social Impact Bonds: A new way to privatize public services

### Summary

Social Impact Bonds are the newest idea to catch the eye of governments attempting to “reform” the public service to save money.

In the 2012 federal budget, Finance Minister Jim Flaherty announced that Social Impact Bonds held “promise” and the federal government was looking at adopting them. As part of his report for the Ontario government recommending major cuts to public services, Don Drummond called for pilot projects using Social Impact Bonds in several different areas. In Alberta, the Progressive Conservatives support them.

The fear is that Social Impact Bonds will become yet another way to privatize and/or cut funding from community and social services. Among the areas where Social Impact Bonds have been proposed as a way of providing services are: developmental services; homelessness; supports for people with developmental disabilities; mental health; justice and corrections; and public health. An added concern is Social Impact Bonds will increase administrative costs and reduce public accountability.

### What are they?

The idea behind Social Impact Bonds is that private investors and the government enter into a contract. Private investors fund services that have the potential to save governments money. Governments repay investors their capital and an agreed-on profit, if agreed-upon social outcomes are met. If the service does not meet the agreed-on social outcomes, investors get nothing back.

An intermediary organization administers all aspects of Social Impact Bond projects including hiring the organization that is actually delivering the service.<sup>1</sup> Proponents of Social Impact Bonds have made it clear that ideally the role of governments would be limited to agreeing on the social outcomes and paying up if the social outcomes are met.<sup>2</sup> All other decisions about how the service will be delivered will be in the hands of the intermediary organization, whose first priority will be making money for its investors.

While Social Impact Bonds are being promoted as a way to fund new services, attempts are already being made to use them to replace public funding. In 2011, the British government announced Social Impact Bonds to fund early intervention services after cutting funding for programs to support young families.<sup>3</sup>

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1 Social Finance, A New Tool for Scaling Impact: How Social Impact Bonds Can Mobilize Private Capital To Advance Social Good

2 Center for American Progress, What Are Social Impact Bonds? An Innovative New Financing Tool for Social Programs. [http://www.americanprogress.org/issues/2012/03/social\\_impact\\_bonds\\_brief.html](http://www.americanprogress.org/issues/2012/03/social_impact_bonds_brief.html)

3 Polly Toynbee, “Who’s in the market for sub-prime behaviour bonds?”, The Guardian, July 4, 2011

## **We don't know if Social Impact Bonds will work**

There's been a lot of hype around Social Impact Bonds, but no one knows if they actually work. Only one Social Impact Bond project is up and running. This is a service to provide support and counselling for inmates released from Peterborough prison in Britain, who served less than one year. The social outcome for the project is to reduce re-offending by at least 7.5%, compared to a control group from other prisons.

It will be 2014 before the project will have been running long enough for people to know if it has succeeded.<sup>4</sup> If the social outcome is met, investors could be making as much as \$12.6 million from an investment of \$7.9 million.<sup>5</sup>

## **Social Impact Bonds create a new layer of bureaucracy**

The need to negotiate contracts on social outcomes, repayment and how to measure social outcomes will eat up a lot of money and staff time. Even for a relatively simple project like the Social Impact Bond in Peterborough, a preliminary evaluation found that getting agreement on the social outcome was, "a time-consuming and analytically complex process."<sup>6</sup>

Under the model used so far for Social Impact Bonds, there is also the cost of the intermediary organizations. That costs includes the efforts of the intermediary organizations to promote themselves – for example Social Finance, the intermediary behind the Peterborough prison Social Impact Bond spent \$52,500 hiring a lobbyist in Massachusetts.<sup>7</sup>

## **Investor profits add to cost**

As mentioned, with the first Social Impact Bond investors could make as much as \$4.7 million on an investment of \$7.9 million. But even this may not be enough. Most of the investment for the Peterborough Social Impact Bond came from charitable foundations. This has led to suggestions that governments may have to provide investors with additional incentives.<sup>8</sup>

Proponents of Social Impact Bonds argue that the profits are still less than what governments would spend in other areas without the additional services. But if government can achieve savings at a lower cost by funding a service directly, why use Social Impact Bonds.

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4 Policy & Representation Partnership Policy Forum Event Report, Social Impact Bonds – What are they and will they work?, 24th February 2012

[http://www.vonne.org.uk/z\\_includes/inc\\_getasset.php?srcpath=.%2F.%2F&type=file&id=2899](http://www.vonne.org.uk/z_includes/inc_getasset.php?srcpath=.%2F.%2F&type=file&id=2899)

5 Ministry of Justice, Minister Launches Social Impact Bond Pilot, September 11, 2011.

[http://www.socialfinance.org.uk/sites/default/files/SIB\\_Launch\\_PR.pdf](http://www.socialfinance.org.uk/sites/default/files/SIB_Launch_PR.pdf)

6 Ministry of Justice, Lessons learned from the planning and early implementation of the Social Impact Bond (SIB) at HMP Peterborough pg 38. <http://www.justice.gov.uk/downloads/publications/research-and-analysis/moj-research/social-impact-bond-hmp-peterborough.pdf>

7 Marie Szaniszlo, "Pay-for-success' firm taps Robert Travaglini", Boston Globe, April 2, 2012.

<http://bostonherald.com/business/general/view.bg?articleid=1061121538&position=0>

8 Sara Lyons, "Social Impact Bonds May be Coming To Ontario: Celebration and Cautions".

<http://socialfinance.ca/blog/post/social-impact-bonds-may-be-coming-to-ontario-celebration-and-cautions>

### **Determining whether a project is a success will be a long and difficult process**

With Social Impact Bonds, governments and investors have to agree on what social outcomes will be used to determine if the project is a success, how one determines whether it was the Social Impact Bond that produced those outcomes and what rate of return investors should receive. Even though something like how many former inmates re-offend is relatively easy to measure, it took 18 months to complete the work needed for the Social Impact Bond at Peterborough prison.<sup>9</sup>

For other planned projects like services to help troubled families, it will be far more difficult to measure outcomes. Do you measure school attendance or whether the parents found employment? If you measure both, what weight is given to each measure? How do you account for other factors, like an increase in unemployment or improvements to local schools?

### **Like other types of privatization, transparency and accountability are limited**

According to supporters, Social Impact Bonds require, “Government to place few, if any, controls on the way that the external organization accomplishes the outcome.”<sup>10</sup> As the first priority of the organization managing the Social Impact Bond is making a profit for investors, no government controls means no opportunity for the public to have a say in how services are run. And as with P3s, details about costs and service levels are likely to be kept secret on the grounds of “commercial interest.”

### **Need to make money will exclude the most vulnerable**

If the social outcomes for services funded through Social Impact Bonds are not met, the investors lose their money. That means investors will not be interested in providing funding for projects to help those most in need where the severity of the problems means success is uncertain. If governments rely on Social Impact Bonds to fund new services, those most in need of assistance will fall through the cracks.

### **Like P3s, Social Impact Bonds provide the illusion of money for nothing**

Even though they often increased costs P3s spread rapidly, because they enabled governments to borrow money without it showing up on their books as debt. Now, as auditors are catching up with P3s, Social Impact Bonds offer a chance to repeat that shell game.

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9 Ministry of Justice, Lessons learned from the planning and early implementation of the Social Impact Bond (SIB) at HMP Peterborough, pg 9. <http://www.justice.gov.uk/downloads/publications/research-and-analysis/moj-research/social-impact-bond-hmp-peterborough.pdf>

10 Center for American Progress, What Are Social Impact Bonds? An Innovative New Financing Tool for Social Programs. [http://www.americanprogress.org/issues/2012/03/social\\_impact\\_bonds\\_brief.html](http://www.americanprogress.org/issues/2012/03/social_impact_bonds_brief.html)

## **For community agencies the long-term costs of Social Impact Bonds outweigh the benefits**

It's understandable that community agencies seeing the impact of government under-funding are tempted by Social Impact Bonds. Unfortunately, based on the experience to date, Social Impact Bonds will add to the problems caused by funding cuts.

In Britain, the attention given to a few million dollars worth of Social Impact Bonds is helping the government draw attention away from billions of dollars of cuts to services the most vulnerable people in the community rely on. Social Impact Bonds may also result in smaller agencies being squeezed out. To achieve significant savings Social Impact Bonds projects have to be on a large scale and that could lead to large for-profit companies being favoured over community-level non-profit agencies.

## **Even if social outcomes aren't met governments could still be on the hook**

Like P3s, Social Impact Bonds are meant to transfer risk to the private sector. The problem is that who is investing and challenges measuring social outcomes mean that, like P3s, it is very likely that governments will end up having to pay even if a project doesn't work.

With charitable foundations and pension funds seen as the most likely sources of investment, a Social Impact Bond failing will mean charities or people's pensions losing money. Because of the difficulties measuring the success of social services with precision and the amount of money investors stand to lose if social outcomes are not met, we can expect costly court cases whenever a project is judged to be unsuccessful.

## **The larger picture**

For more information on the value of public services, potential threats to them, and how we can respond, please visit the following links:

[www.nupge.ca](http://www.nupge.ca)

[www.publicservicesfoundation.ca](http://www.publicservicesfoundation.ca)

<http://alltogethernow.nupge.ca>