SOCIAL FINANCE

A Technical Guide to Developing a Social Impact Bond:

Vulnerable Children and Young People

March 2011

Introduction

This guide aims to set out the steps that are required to assess the feasibility of a Social Impact Bond (SIB) idea. It starts with the identification of a social issue where a SIB might be applicable and examines each factor that must be considered if a SIB is to be effective. The guide is written to assist those developing SIBs to reach a stage where it would be possible to establish a contract between a public sector commissioner and investors.

This guide is one in a series of technical guides. Each document focuses on how a SIB can be developed to address the root causes of a specific social issue.

What is a Social Impact Bond?

- A Social Impact Bond ("SIB") is a contract with the public sector in which it commits to pay for improved social outcomes.
- On the basis of this contract, investment is raised from socially-motivated investors.
- This investment is used to pay for a range of interventions to improve social outcomes.
- If social outcomes improve, investors will receive payments from government.
- These payments repay the initial investment plus a financial return.
- The financial return is dependent on the degree to which outcomes improve.

SIB Objectives

Social Finance has created SIBs - an outcomes-based funding mechanism – to provide new investment to improve social outcomes. SIBs fund preventative and early intervention programmes which tackle the underlying causes of specific social problems. Incentives are aligned across public sector commissioners, external investors and service providers, all of whom are acting to achieve improved social outcomes as defined in a contract.

The main objectives of the SIB are to:

- Increase the pool of capital available to fund early interventions;
- Encourage a broad diversity of service providers and collaboration between providers;
- Create more market discipline and offer predictable revenue streams for service providers to enable those that are effective to thrive; and
- Align public sector funding more directly with improved social outcomes.

The first Social Impact Bond was launched in September 2010 at Peterborough Prison. It funds rehabilitation services for short-sentence prisoners released from the prison, with the express aim of reducing re-offending. Social Finance is currently exploring a number of potential applications of SIBs in areas such as health, drug rehabilitation and Children's Services.

SIBs and Children's Services

Children's Services departments across the country address a range of needs when working to improve the lives of children in their areas. These range from providing Children's Centre services for the early years to accommodating vulnerable children where there are fears for their safety. Many of the activities carried out by Children's Services are statutory – required by law to be provided by the State. Others are more of a preventative nature – trying to address underlying needs before they escalate into crisis.

Social Finance is developing a working hypothesis of how a SIB might fund more preventative services related to the activities of Children's Services, with the objective of improving the wellbeing and prospects of vulnerable children and young people. Over time, if such interventions succeed, they should enable a shift in expenditure away from acute spending towards expenditure on early intervention services – reinforcing cycles of positive spending and outcomes. There will undoubtedly be a range of areas in which a SIB could help to improve social outcomes of children and young people. In this guide we use our SIB working hypothesis as one example to demonstrate how to assess the feasibility of such projects.

In **Box 1**, we set out our working hypothesis for a SIB focused on reducing or preventing time spent in care by adolescents experiencing behavioural problems or family breakdown. The rest of this guide illustrates a SIB feasibility assessment based on this hypothesis.

Box 1 – Vulnerable Children and Young People: SIB Working Hypothesis

- There are significant numbers of adolescents in and at the edge of the care system due to behavioural problems or family breakdown. Typically, over 30% of looked after children are in the adolescent age range.
- For many adolescents entering care there is a strong probability of staying in care long-term.[1]
- Outcomes for looked after children are significantly worse than for children in the population as a whole. One example of this is educational attainment: 14% of looked after children achieve 5 GCSEs A*-C, compared to 65.3% for children overall.
- The financial costs to Local Authorities of young people entering and remaining in the care system are high. The estimated expenditure on looked after children is more than £2 billion per year in England.[2]
- The direct cost of placement for a looked after child is, on average, £40,000 a year. Placement costs range from £25k to £250k per child per year, ranging from foster care to specialist residential care.
- There are interventions which address the needs of vulnerable young people and those of their parents, stabilising the situation and enabling the family to remain together. Such interventions range from those of a practical nature to the more therapeutic.
- A Social Impact Bond could raise investment to fund interventions intended to reduce preventable family breakdowns and the number of young people entering care. A SIB could also fund support for those who have recently become looked after, aiming to swiftly reunite them with their families, where measures are in place to address the underlying needs of the young person and their family.
- A lead outcome indicator may be one linked to reducing or preventing time spent in care which in turn can be linked to "cashable savings" and improved social outcomes. This would need to be balanced by a basket of indicators to reflect the well-being of the child.

Beginning the process

Social Impact Bonds will not apply in all circumstances. In many areas, traditional funding streams will remain the most appropriate. To determine whether a SIB could apply to tackling a specific social problem, a number of factors must be considered. We set out below the various stages of the feasibility assessment process and a series of key questions to be addressed.

Figure 1 summarizes the key components of the feasibility assessment process based on the hypothesis outlined above.

1 Sinclair, I. *et al.* (2007) *The Pursuit of Permanence: A Study of the English Child Care System*. The research shows that the chance of leaving care is greatest in the first 50 days of the child being in care. After that, the rate of leaving decreases rapidly.

2 The NHS Information Centre (2008*) Personal Social Services Expenditure and Unit Costs England*.

Figure 1 – Feasibility Assessment Process

Define the social issue

Key Questions

- What is the social issue you are trying to solve?
- Which population should this target?
- What age range?
- What geographical area?

Activities

- Assess stakeholder engagement
- Assess the feasibility of measurement with each target population

Key Question:
Is there an engaged commissioner interested in tackling the social issue?

Develop social intervention strategy

Key Questions

- What are the needs of the target population?
- What is the intervention point?
- What are the gaps in service provision?
- What services will meet the needs of the target population to improve the outcome?

Activities

- Analyse research reports
- Consult with public and voluntary sector organisations that work with young people in the local area
- Focus group with young people
- Develop hypothesis on the most appropriate intervention strategy

Key Question:
Are there compelling intervention programmes to solve the social issue?

Develop operating model / Estimate budget for service / Develop outcomes metrics and control / Value outcome

Key Questions

Operating model and budget

- What are the programmes that could be funded as part of a SIB?
- Do these programmes have a track record of improving outcomes?
- What do these programmes cost to deliver?
- How do programmes operate alongside each other?

Develop metrics and control

- Which metric should be used to evaluate the outcome?
- What size of population is needed for measurement to be statistically significant?
- How do we structure a baseline/control against which to measure the impact?

Value of outcome

- Which departments generate cost savings from an improved outcome?
- What is the value of the cost saving?

Activities

- Mapping landscape of potential providers
- Reviewing quantitative evaluations of programmes that meet young people's needs
- Reviewing budgets of service providers to understand cost of service delivery
- Working with Local Authority and independent researchers to evaluate the range of alternatives
- Ensure that the proposed metric is operationally feasible
- Ensure that the proposed metric will meet investors' needs
- Working with the Local Authority's analytical team to estimate the cost saving from an improved outcome

Key Question:
Can a robust outcome metric be developed?

Develop financial model

Key Questions

- Can the SIB financial model work?
- What proportion of cost savings will need to be shared with investors?

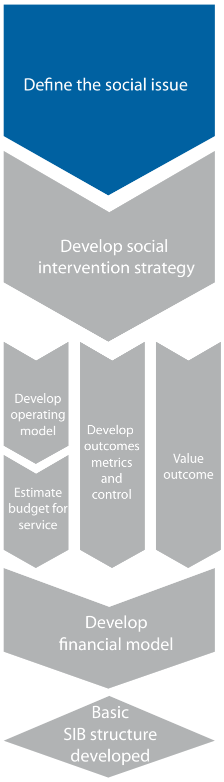
Activities

- Build a financial model and run a range of scenarios

Key Question:
Does the financial model generate savings to the Local Authority and a return to investors in an acceptable time frame?

Basic SIB structure developed

Defining the social issue



Social Impact Bonds raise investment to alleviate social problems. The SIB funds interventions which address the needs of a target group when there is either no existing provision or the existing provision is inadequate.

Illustration of social issue: adolescents between the ages 10-15 make up the largest age group entering the care system. This group is more likely than other age groups to remain in care and not return home.[3] Their needs are often complex and could involve significant breakdown in family relationships. Those who stay in care long term often experience poorer outcomes in health and education.

On the basis of the stated social issue, it is necessary to clearly define the target population. It is this group for whom interventions will be funded and outcomes improved. There must be clear criteria against which the target population can be identified and a process through which referrals can be made into the SIB-funded interventions.

Illustration of target population and referral point: adolescents aged 10–15 years old, with behavioural problems, who are referred to the Children's Resource Panel of a Local Authority. Examples of eligibility criteria of such adolescents might include: siblings already looked after, family subject to other services, prior history of being looked after, at risk or record of youth offending.

If the definition is not sufficiently focused the interventions may be too diffuse to have a significant impact on the target outcome. If the definition is too narrow, the target population may be too small to demonstrate a statistically significant effect.

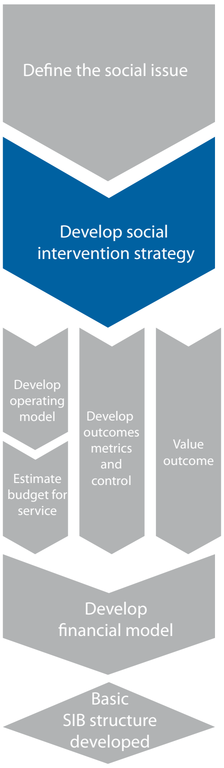
A Social Impact Bond requires an engaged commissioner who is open to outcomes-based contracting where payments are made if agreed social outcomes are achieved. It is important to work in conjunction with an engaged commissioner, through access to data and discussion, in order to develop outcome metrics and target population definitions.

Social Finance is currently working with three Local Authorities – Essex County Council, Liverpool City Council and Manchester City Council. We have embarked on 6 month feasibility studies to investigate the potential for a SIB to fund services targeted at vulnerable children, young people and their families.

Key Question:
Is there an engaged commissioner committed to tackling the social issue for a defined target group?

[3] Sinclair, I. *et al.* (2007) *The Pursuit of Permanence: A Study of the English Child Care System*.

Development of the social intervention strategy



We are looking to develop SIBs that tackle the underlying needs of vulnerable children and young people. Given that these individuals often come from a family environment in which multiple risk factors are present, we recognise that no single intervention is suitable in all cases. Therefore, SIB funding aims to bring together a suite of interventions that are tailored to address the needs of both the young person and his/her family members, and which reflect the local circumstances in which the programme operates.

A first step is to identify the underlying needs of the target group, which the selected interventions will tackle. Once the profile of needs is understood an intervention programme can be developed. To do this, there needs to be a review of both national and local service providers to identify where complementary interventions could best meet the needs of the target population and achieve the desired outcome. The SIB funding structure encourages all service providers to work collaboratively towards achieving the target outcome.

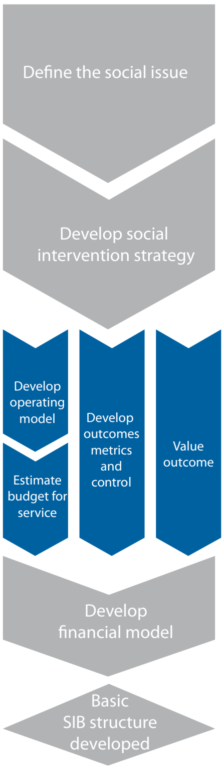
To determine the feasibility of the intervention programme for SIB funding it is necessary to establish the impact the programme is likely to have on the target outcome.

This is dependent on two considerations:

- The degree to which interventions are well understood and can be evidenced.
    - *Illustration of intervention development*: Social Finance is undertaking a review of the interventions relevant to the defined target group. This involves investigating qualitative and quantitative evaluations, interviewing service provider staff members and analysing how these interventions meet the needs of the target group and improve their outcomes.
- Whether there is a gap or scarcity of service provision to the target population such that SIB investment is likely to lead to a significant change in the target outcome.
    - *Illustration of intervention development:* If there were little existing support for families of young people who are at risk of entering or who have entered the care system then investment in this area is likely to yield higher social returns and consequently financial returns to investors.

Key Question:
Is there a compelling intervention programme to solve the social issue?

Building the business case



Developing the business case for a SIB comprises several parallel work streams which are set out below.

Developing the Operating Model & Intervention Costs

Given that SIBs are likely to fund a consortia of service providers, it is necessary to have a robust understanding of the total programme delivery costs, including infrastructure and overhead costs. The development of an indicative budget for the proposed suite of services will determine the level of funding that will need to be raised from investors through the SIB.

It is important at the feasibility stage to consider the practical implications of how the SIB can operate. Engagement with a commissioner is helpful to understand how the portfolio of SIB interventions could sit alongside the local authority's "business as usual" processes.

Illustration of Operating Model: discussions with the local authority commissioner may result in an agreement that referral to the SIB occurs at a point when cases are taken to review at the Children's Resource Panel. An agreed set of eligibility criteria would be required so that social workers reviewing the cases could easily identify those who should be considered for the SIB intervention. There would need to be a plan in place for systematic monitoring of performance and collection of data through a case-management system dedicated to the SIB. A system of governance would need to be outlined for the SIB.

Determining the Outcome Metric & Control Group

The outcome metrics form the foundation of the SIB contract between the public sector and investors. All stakeholders need to trust that there is an objective mechanism for assessing and agreeing the degree to which social outcomes have been achieved. Such a metric needs to be linked to cashable savings on the part of the public sector commissioner. Whether or not suitable metrics can be identified is a key determinant of whether or not a SIB is the appropriate instrument for addressing an identified social issue. Care should be taken that the selected metric avoids perverse incentives. In order to measure the direct impact of the SIB-funded interventions on outcomes, a baseline or control group is required. Whether a historical baseline can be used or a comparison group is required depends on the stability of historical data and the availability of a suitable comparable population.

Illustration of outcome metrics: the outcome metrics against which success can be assessed are likely to include a combination of objective and subjective metrics. The basket of metrics might include an objective indicator linked to cost savings such as a percentage change in those entering care or a percentage reduction in the number of care weeks. Alongside this there might be a robust index of target population well-being. The inclusion of a well-being measure in the portfolio of outcome measurements would help guard against perverse incentives whereby a young person was prevented from becoming looked after when it was in the best interests of that young person to be looked after. Another outcome metric to consider is that of school attendance. This is an indirect outcome metric but one which could be linked to better long-term outcomes for the young person. Social Finance is undertaking a detailed study of potential outcome metrics and associated comparison group design for a SIB based on our hypothesis above.

Outcome Valuation

The outcome valuation for a SIB is the average public sector cost saving resulting from an improvement in the outcome. It should be noted that for the purposes of analysing the potential returns to investors, the outcome value is narrowly defined in terms of the cost savings accruing to specific public sector budgets.

Illustration of outcome valuation: Local Authority social care cost savings due to a reduction in care placement costs. This potentially could be combined with other sources of savings where the relevant

Figure 2: Illustrative Outcome Valuation – average placement cost of a young person

Type of placement	Probability of admission into placement (Column A)	Average cost per care week (Column B)	Estimated average length of stay in care for 10-15 year olds (Column C)
Fostered (In-House)	40%	£400	60 weeks (based on the estimation that majority will stay in care for less than 2 years)
Fostered (External)	20%	£900	
Residential	20%	£3,500	
Placed with parents	3%	£200	
Kinship	15%	£200	
Secure accommodation	1%	£5,000	
Other	2%	£200	

Calculation:
Step 1 - Column A x Column B = Average cost of placement per person per week
Step 2 - Average cost of placement per person per week x length of stay in care (Column C)

Average placement cost throughout individual's care journey = £68,000
(excluding social services and legal costs)

outcomes were achieved as a direct impact of the SIB-funded interventions. Some examples include:

- a reduction in local youth offending costs if the SIB-funded interventions reduce offending behaviour amongst adolescents in the target group.
- a reduction in costs of places at Pupil Referral Units if school exclusions were reduced amongst the target group.

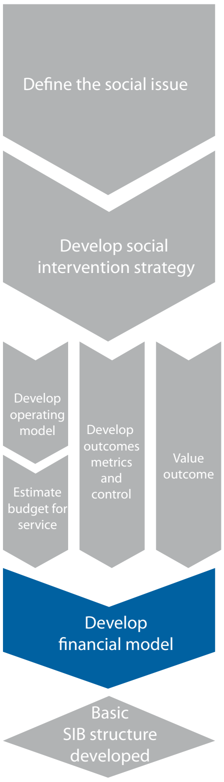
The calculation set out in **Figure 2** illustrates how one might start to value the outcome of preventing a young person from entering care.

A quantification of broader social outcomes (e.g. safer communities due to reduced antisocial behaviour, improved school attendance leading to better qualifications) reflect important social benefits, but do not release cash from public sector budgets that could be used to make outcomes-based payments to investors in a realistic time frame. This may change over time.

Key Question:

Does the financial model generate savings to the Local Authority and a return to investors in an acceptable time frame?

Developing the financial model



The financial model aims to reflect the economics of the SIB. It estimates the costs of interventions, overheads and other fixed costs which together determine the level of investment required over the period of the SIB. Set against this will be the share of the cost savings agreed by the commissioner to be distributed to investors should a sufficient improvement in outcomes be achieved.

The financial model requires consideration of three factors:

- Intervention costs
- Outcome values
- Time horizon to realise investment returns

SIBs work when the costs of achieving the target outcome (intervention costs plus overheads and fixed costs) are substantially lower than the level of the resulting public sector savings (outcome value).

This is essential to developing a financially viable investment proposition on which to raise capital.

A reasonable time horizon for the investment is critical. Investors would prefer to see a SIB that matures within a time horizon of around 5 years. Therefore there needs to be a tight timescale between intervention, measurement of impact and payment on outcomes achieved. This is a consideration particularly in examples such as early years intervention (0-5 year olds). If the outcome metric is educational attainment, but it is necessary to wait 11 years (age 5 to 16 years old) to measure GCSE results for the target population, this will not make for a feasible SIB. For such a model to work, an earlier measure regarded as a reliable predictor of future performance is necessary.

The focus on adolescents (aged 10–15 years old) provides a relatively compact time frame over which to measure outcomes. For this age group, research shows that if a young person remains looked after for more than a short time period (e.g. 3 months), the likelihood of remaining looked after on a long-term basis increases. Outcomes for the young person become much worse with long-term care. Therefore one approach could be to measure placement-related outcomes at 3 or 6 months post-intervention.

Key Question:

Does the financial model generate savings to the Local Authority and a return to investors in an acceptable time frame?

Next steps

We hope the process outlined above is helpful in developing a feasible SIB model. Social Finance would be delighted to engage with you in order to support progress towards implementation. As a first step we would ask you to submit your responses to the key questions set out in the appendix.

For more information please review our publications:

Towards a New Social Economy – Blended value creation through Social Impact Bonds (March 2010).

Social Impact Bonds – Unlocking Investment in Rehabilitation (September 2010).

We invite you to join the Social Impact Bond forum to connect with other interested stakeholders, or participate in our ongoing series of webinars.

www.socialfinance.org.uk/forum

We wish you all the best with your SIB development and look forward to working together.

Appendix: Key SIB Questions

1. Social issue	
What is the social issue you are trying to solve?	*e.g. Improve outcomes for vulnerable young people in and on the edge of care*
What are the systemic causes of this issue?	*e.g. under-provision of services that address both the needs of young people at risk and their families*
Are there interventions that have been shown to improve this issue?	

2. Outcomes	
What would the desired outcome of the social impact bond be?	*e.g. Reduced entry into care or number of care weeks; improved social outcomes for young people*
How would the improvement in the social outcome be measured?	*e.g. Comparison data from other Local Authorities, distance travelled*
Are there existing objective measures of the outcome?	*e.g. Government data on looked-after children population numbers and outcomes; National Indicators reflecting social outcomes*
What is the current outcome for the target group?	*e.g. 10-15 year olds make up more than 30% of those entering care; poor health and education outcomes*

3. Target population	
How would you define the target group who would receive services funded by a SIB?	*e.g. 10-15 year olds with behavioural problems referred to a resource panel in a particular Local Authority*
Can you define the target group objectively?	*e.g. 10-15 year olds, referred to particular panel*
What criteria would you use to define the target group objectively?	
How do we identify people who are in the target group?	
How many people are in the target group?	
What are their needs?	*e.g. Behavioural and emotional problems, domestic violence, offending behaviour, mental health problems, drug/alcohol abuse*
How does the support need vary across the target group?	

4. Interventions	
What are the proposed interventions to be funded by a SIB?	*e.g. Adolescents or family support services, counselling services, drug/alcohol services*
What are the proposed organisations to be funded through a SIB?	
Is there evidence that these interventions are effective at achieving the desired social outcome?	
Is there a quantitative (statistically significant) evidence base?	
Has an independent evaluation of the intervention been undertaken?	
How have these interventions improved the outcome	
How much do these interventions cost to deliver per person who receives them?	*e.g. £5000 per family over 6 months*

5. Value of the outcomes	
Which government department(s) will financially benefit if the social outcome is achieved?	*e.g. Local Authority Children's Services*
How will these cost savings be achieved?	*e.g. Reduced placement costs*
How much will the government save if the outcome is achieved?	*e.g. Average placement cost per young person per year around £40,000*
Are these cost savings cashable?	*i.e. Can the savings be realised (e.g. placements that are spot purchased are easily cashable)*

About the authors

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Lisa is a Director at Social Finance. She joined Social Finance from Bridges Ventures where she was an Assistant Director. She focused on making private equity investments which would yield both financial and social returns. Prior to this, Lisa founded an e-government software business and worked as a strategy consultant for Marakon Associates. Lisa started her career as a public policy advisor focusing on Treasury, Transport and Employment policy areas. She was a Special Advisor at the Department for Education and Employment. Lisa holds a BA in Social and Political Sciences from Cambridge University and a MBA from London Business School.

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Social Finance is building a pioneering organisation to develop financial products that marry the ambitions of investors and the social sector. We support social organisations to raise and deploy capital; we work with government to deliver social change; and we develop social investment markets and opportunities.

Many charities and social enterprises face serious financial challenges that stop them from carrying out their work effectively. We believe that, if social problems are to be tackled successfully, organisations seeking to solve them need sustainable revenues and investment to innovate and grow. Our role is to devise the financial structures and raise the capital to enable this to happen.

Social Finance injects market principles into funding in a way that stands or falls on results – both social and financial. Our financial products forge essential links between the market, government and society.

In these times more than ever, there is a pressing need to harness social investment to make a long term difference to society. This is our ambition.

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