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The Rise Of Social Impact Bonds.

The social impact bond or pay for success program ("PFS program") is an alternative private financing model used to test social impact programs before governments step up to finance such programs. In these programs the government contracts with a private sector intermediary to obtain social services. The intermediary obtains funds for the services by raising capital from private commercial and/or philanthropic groups. The intermediary uses these funds to pay a service provider to deliver the social services. Over a set period of time, performance of the social services is measured, usually by a third party consultant, based upon up-front established criteria. After the review period, the government pays the investors only if the performance targets are met.

As of the end of 2015, there were eight (8) established PFS contracts in the United States and more in the pipeline. The Corporation for National and Community Service through its Social Innovation Fund launched a PFS program and selected eight (8) initial grantees through which 43 programs are receiving technical assistance. Banks such as Goldman Sachs, Northern Trust, Bank of America, Merrill Lynch and Santander Bank have invested capital in PFS programs. In addition, federal legislation, known as the Social Impact Partnership Act, has been introduced to help establish PFS programs, and six (6) states (Colorado, Idaho, Massachusetts, Oklahoma, Texas and Utah) have passed PFS enabling legislation. Other states are considering legislation or participating without legislation.

Despite the trend toward expanding PFS programs, there are some criticisms. PFS programs can be more expensive than direct government funding due to costs of legal services, program administration and loan management. There are also questions about how outcomes are measured, since the "success" of most programs is measured in a relatively short time frame considering the deep-rooted social problems that are being addressed. In addition, data suggest that investors want to minimize risk and back programs where there is more evidence of possible success. Detractors of PFS programs argue that governments should finance these programs themselves based upon the probability of success. Despite the questions and criticisms, it appears from the significant increase in PFS programs that this type of investment tool is here to stay, at least in the short-term.

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