

INVESTING FOR “IMPACT” OR INVESTING FOR PROFIT? SOCIAL IMPACT BONDS, PAY FOR SUCCESS, AND THE NEXT WAVE OF PRIVATIZATION OF SOCIAL SERVICES AND EDUCATION



Martin Carnoy, Stanford University
Roxana Marachi, San José State University

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National Education Policy Center

School of Education, University of Colorado Boulder
Boulder, CO 80309-0249
(802) 383-0058
nepc.colorado.edu

Acknowledgements

NEPC Staff

Kevin Welner
Project Director

William Mathis
Managing Director

Patricia Hinchey
Academic Editor

Alex Molnar
Publications Director

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Executive Summary

A major new financial phenomenon has appeared within the social services arena, with corresponding legislation poised to change how social services are delivered and who delivers them. While different programs use different terms—including, for example, Pay for Success (PFS) or Results-Based Financing (RBF)—the umbrella term encompassing all such programs is Social Impact Bond (SIB). SIBs are promoted as a way to help fund projects in such areas as health care, homelessness, early education, workforce development, and prison reform. These investments are thought to have potential to cut costs but are nonetheless viewed as too risky for public agencies to directly invest their scarce public funds. In this review, we examine whether SIB financial structures provide all that they promise and whether results so far yield any insights into their future direction and potential pitfalls.

The research literature includes a small but useful set of studies that examine SIBs. We analyze these as well as related findings, including several case studies as examples of SIBs in the United States; further, we assess approaches to social service delivery. While we do not attempt a full-scale cost-benefit analysis of SIB programs, we do explore how such financial instruments operate and their most evident advantages and disadvantages.

Our review finds that SIB projects are designed to promote financial investments in low-income communities while concurrently shifting service delivery, data gathering, and evaluation processes to the private sector. Thus, in the current policy landscape, SIBs are poised to substantially alter how public resources are deployed to address social issues. The newest forms tether success metrics to digital smart contracts designed in ways that allow investors to profit from the social service projects. One layer of such future privatization will involve

contracting with private entities for the actual delivery of public services, eliminating current public oversight. Another will involve allowing data from youth/participants in studies to be siphoned into private tech firms' databases, allowing those firms to sell the data in increasingly valuable longitudinal data markets. By design, such models make social service programs accountable to investors, but not necessarily to the communities ostensibly being served. The new structures are also likely to involve the outsourcing of research to third-party evaluators, who may not have the best interests of the public in mind nor be required to ensure participant protections throughout the research process.

Accordingly, we question the net benefits of SIBs and related performance-based financing schemes, and we raise the possibility that, ultimately, SIBs may be yet another way for the private sector to finance relatively low-risk social projects for private gain. We also consider that like many public-private partnerships framed as providing social solutions, including those in education, SIBs may serve to focus public attention and public sector funding on immediate needs—and away from large-scale solutions to structural issues associated with poverty and social segregation.

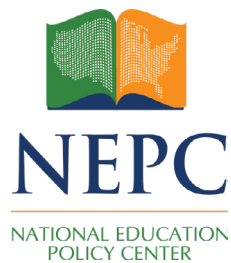
Recommendations

Recent legislation means that education leaders need a good understanding of SIBs: Pay for Success (PFS) financing structures are embedded in the Every Student Succeeds Act (ESSA), and through the Social Impact Partnerships to Pay for Results Act (SIPPRa) millions of dollars are likely to soon be distributed to support SIB arrangements. Therefore, we urge education leaders to recognize that such projects have been designed to: (a) turn public services into centers for the extraction of private profit; (b) view individuals from a deficit lens, as in need of being “fixed” with narrow/short-term metrics of success; (c) amass vast amounts of data that can be used for predictive profiling of targeted communities; and (d) remove community voice and control from governance of public services. In cases where public agencies already have PFS projects under way or are in nascent stages of enacting such projects, we recommend the following:

1. Before contracting out a social impact project, the public agency involved should be able to show that previous experience with the intervention indicates its risk of failure is high enough to warrant spending public money not only on the considerable administrative costs required to develop the SIB contracts, but also to pay off the investor. Otherwise, the public agency should directly execute the intervention.
2. Projects vying for SIPPRa and/or ESSA funding should be required to demonstrate alignment with the Belmont Principles and Guidelines for the Protection of Human Subjects of Research. These include full, informed consent/assent from participants, assurances of data privacy, confidentiality and anonymity, and opportunities to discontinue participation at any time without penalty or harm. Private researchers should adhere to basic research ethics, especially when working with vulnerable populations and extracting public funds for projects that yield both data and profits.
3. If private firms are to collect sensitive social/emotional, behavioral, attitudinal, health,

and/or learning data from youth, and if longitudinal research on the projects are to include predictive analytics of any sort, the firms should make clear to families how data will be used and what type of predictions about participants will be produced. In addition, a clearly communicated opt-out option should be available to families who want to receive services but not participate in data collection.

More generally, policymakers and others should be skeptical of the hype that SIBs are a win-win for all concerned and without downsides. Such claims are often made by private investors, and even by NGOs legitimately seeking more funding to engage in social interventions. We should be sincerely skeptical about bringing the private sector further into the areas of social services and education. No matter how well-intentioned private investors may appear to be, they are ultimately governed by private interests. No matter how easily and often those private interests can be rationalized as aligning with public interests, that is unlikely to be the case.



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Introduction

In the past decade, a new financial phenomenon has appeared within the social services arena, with supporting legislation potentially transforming how social services are delivered and who delivers them. The umbrella term for such arrangements is the Social Impact Bond (SIB), although specific programs employ other names, including Pay for Success (PFS) or Results-Based Financing (RBF). However named, SIBs are promoted as a way to allow private firms to fund public projects in health care, homelessness, early education, workforce development, and prison reform; they can be repaid with interest, providing a profit to funders if a project produces specified cost savings for the state. SIBs first evolved in the United Kingdom’s labor government, when the Prime Minister’s Council on Social Action initiated discussions about alternative funding models for social investments. Sir Ronald Cohen, widely known as the “father of British venture capital,” had chaired the Social Investment Task Force (SITF) for the British government since 2000; in 2007, he co-founded Social Finance UK, a London-based advisory organization working to create a UK social investment market. In the US, the Obama administration first introduced funding for SIB pilot schemes in its 2012 budget,¹ and PFS provisions were written in to the 2015 Every Student Succeeds Act (ESSA) in 2015.²

The motivation in the UK, the US, and other countries for promoting SIBs appears to be twofold: First, they serve to legitimize seeking private, for-profit investments to reduce the social costs of poverty because these investors assume the initial financial risk of such initiatives; and second, they also serve to rationalize such partnerships and investments because they ostensibly save taxpayers money. Although SIBs certainly reflect moves to privatize

public responsibility for investing in the poor and solving social problems associated with poverty and limited access to public services, their history indicates they did not originate in conservative governments. Rather, they appear to have emerged from a widening gap between increasing demands for public solutions to social problems associated with low-income communities, and the decreasing willingness of legislators to support tax programs that would allow funding for public sector efforts to solve those problems directly.

In this review, we examine whether PFS initiatives or other SIB arrangements actually provide all that they promise, and whether results so far yield any insights into their future direction and potential pitfalls. A number of studies have already explored such questions. We analyze their arguments, provide several case studies as examples of SIBs in the US, and assess the SIB approach to social service delivery. Rather than a full-scale cost-benefit analysis of SIBs, we provide an investigation into how such financial instruments operate and their most evident advantages and disadvantages.

Our review finds that, however labeled, SIB initiatives are designed to promote investments in projects intended to support low-income communities while concurrently shifting services, data gathering, and evaluation processes to the private sector. We question the net benefits of SIBs and related performance-based financing schemes and raise the possibility that, ultimately, SIBs may be yet another way for the private sector to fund relatively low-risk social projects for private gain. We also consider that like many public-private partnerships designed to solve social problems—including those in education—SIBs and PFS projects may serve to focus public attention and public sector funding on immediate needs—and away from large-scale solutions to structural issues associated with poverty and social segregation.

We examine whether PFS initiatives or other SIB arrangements actually provide all that they promise.

The way that societies approach social problems has an unavoidable political dimension. While on the surface there may appear to be nothing inherently wrong in addressing social problems with public-private partnerships, it is a political choice to limit investments in poverty-related social services to interventions that can show cost savings—

while additionally giving private firms access to valuable data on already disenfranchised members of society. As an important political choice, the promotion of SIBs requires, at least in part, a political critique.

Few SIBs directly fund education projects; to date, only 13 of 137 SIBs in 11 countries involve education projects. However, it is important that all education stakeholders understand what SIB initiatives represent as an approach to social issues: They reflect the trend toward increasing accountability practices tethered to impact evaluations that use “what works” criteria to judge investments in education and other social services. SIB and PFS structures are essentially the financial driver of impact evaluation and, in that sense, may eventually appear in many aspects of education sector financing. This is true even though, as we show, the relative difficulty of definitively linking short-term monetary benefits with educational interventions makes education a particularly complex sector for SIBs. Nevertheless, SIB/PFS programs may function as the next phase of policy shifts that have already allowed for the privatizing of public education via charter schools. Given the importance of these trends,

two of the three examples of SIBs/PFSs we examine in detail are education-related projects in the US.

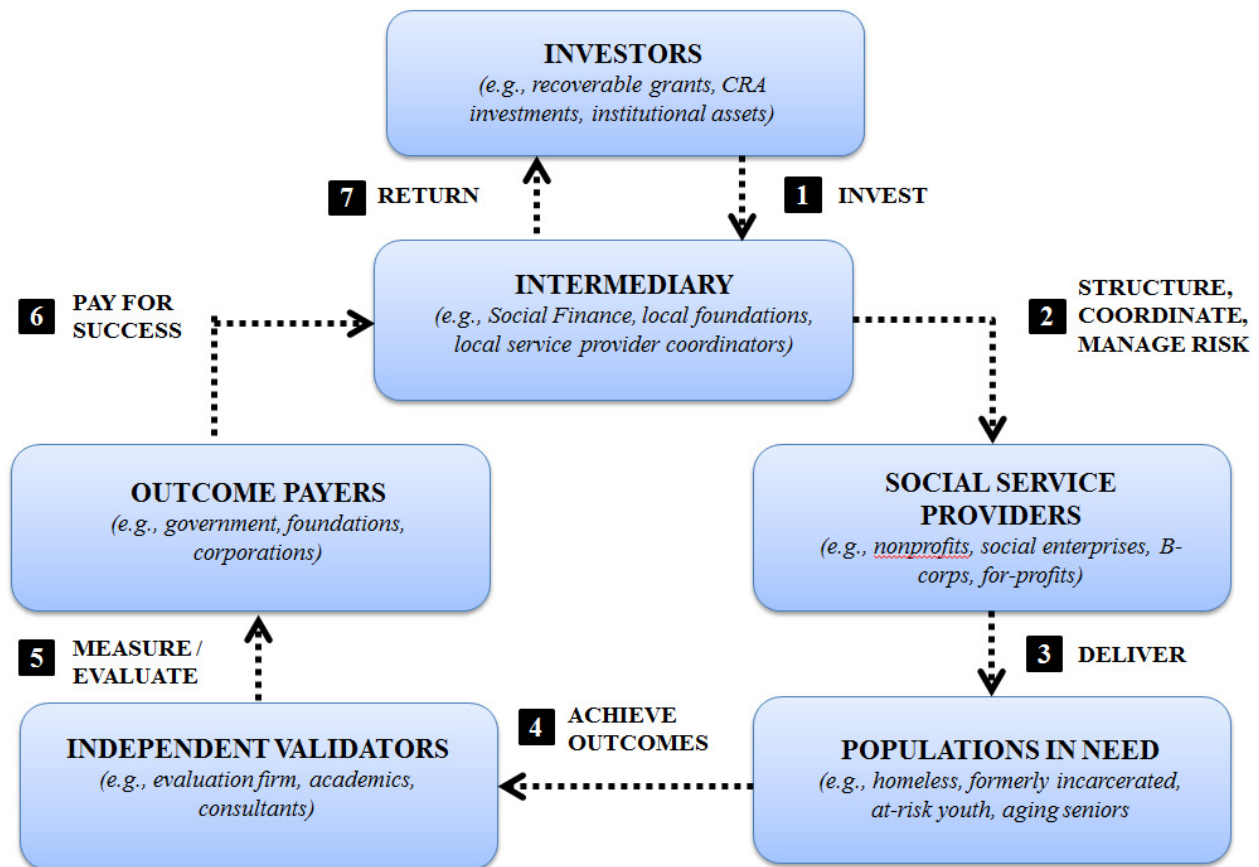
How Social Impact Bond and Pay for Success Structures Function

SIB and PFS financial structures are orchestrated by an intermediary organization, usually a private nonprofit specializing in particular social services, that makes a proposal to both private investors and a government agency. When a proposal is successful, the investors agree to fund an intervention, and the government agency agrees to accept particular criteria for determining success—as well as to repay the investors with interest if the criteria are met. The intermediary organization may administer the intervention or subcontract it. In addition, a third party is hired to design the evaluation and measure the intervention's effectiveness. More formally stated:

A SIB is an innovative financing mechanism in which governments or commissioners enter into agreements with social service providers, such as social enterprises or non-profit organisations, and investors to pay for the delivery of pre-defined social outcomes. More precisely, a bond-issuing organisation raises funds from private-sector investors, charities or foundations. These funds are distributed to service providers to cover their operating costs. If the measurable outcomes agreed up-front are achieved, the government or the commissioner proceeds with payments to the bond-issuing organisation or the investors. In reality, the term “bond” is more of a misnomer. In financial terms, SIBs are not real bonds but rather future contracts on social outcomes. They are also known as Payment-for-Success bonds (USA) or Pay-for-Benefits bonds (Australia).³

Whereas the government must repay private investors an amount including a return on their investment if interventions are deemed successful, investors lose the fronted funding if the intervention falls short (Figure 1). However, the intervention in almost all SIBs has had some previous track record of success, providing lower risk to investors than a first-time experiment.

Figure 1. How Social Impact Bonds Work



Source: Organization for Economic Cooperation and Development (OECD).⁴

On the surface, SIBs may appear to be great for everyone. The public sector gets to scale up improvements in public services without risking taxpayer money. Government, mostly at the local level, is viewed as more prudent in its use of tax revenues, since it takes less financial risk in developing more efficient approaches to recidivism reduction, homelessness, education, and other public services. Such investments are often proposed as positive innovations in public service delivery. Private investors get to make a return on their capital while investing in services that purportedly contribute to improving people’s lives, especially in those most in need. Financial institutions that have long been under public scrutiny, such as Goldman Sachs, get the favorable public relations associated with such projects. And, non-profit organizations receive more funding for their social projects than they could have ever hoped for in the current resource-stressed environment.

The SIB Landscape in 2019

Two models of SIBs have emerged in the past eight years: SIB funds and individual SIBs. The SIB funds model, popular in the UK, involves a branch of government establishing a

fund (for example, the Innovation Fund established by the UK's Department of Work and Pensions) and a "rate card" for each project listing payments for specific outcomes, based on the cost savings that each outcome might yield. Partnerships among service providers, investors, and intermediaries then bid on contracts with the government to deliver outcomes listed in the rate card. Contracts are awarded based in part on how much less than rate card prices partnerships are willing to accept for delivering the targeted outcomes. In an individual SIB or PFS program, the public agency (the payor) and the service provider contracted to deliver the services sign an agreement for the project. The intermediary is responsible for raising capital, structuring the contract, and providing an agreed-upon evaluator.⁵

The most comprehensive inventory of SIBs is the database of the UK's Social Finance organization,⁶ which was involved in the first SIB in 2012 and which promotes SIBs worldwide. Its database lists every SIB launched to date, classified by country, type of service ("issue area"), investor, payor (who pays investors for successful interventions), and service provider (who administers the intervention). The database also includes a description of each and every SIB already launched, including its cost. According to Social Finance, as of November 2019, 137 social impact bonds had been launched, raising \$440 million, and "touching" almost two million individuals through the financed interventions. According to the database, another 69+ SIBs are "in development." Seventy percent of the launched SIBs have been in four countries: UK (47), US (26), Australia (10), and Netherlands (11), but another 21 countries have at least one SIB, including Argentina, Cameroon, Canada, Finland, France, Germany, India, Japan, Kenya, and Peru. Most projects to date are in four issue areas: workforce development, homelessness/housing, health, and child and family welfare. Only 13 have been in education and another 12 in criminal justice.

SIBs were first introduced in England in 2010, with a social impact bond fund supporting a seven-year, £5 million project to reduce recidivism among people incarcerated for 12 months or less in Cambridgeshire's privately managed Peterborough prison. Investors included 17 foundations and trusts, and the intervention involved helping released individuals reintegrate into the community. If the project reduced the reconviction rates by 7.5%, the Ministry of Justice and the Big Lottery Fund would be payors for the project. In 2017, the Ministry of Justice announced that the reconviction rate had dropped by 9%, exceeding the 7.5% target. As a result, the investors were paid their original investment plus an amount representing a 3% annual return over the seven years. In the following two years, all but one of the SIBs in the UK were aimed at reducing youth unemployment by trying to alter young people's behavior, including increasing their participation in academic achievement skills training activities. The criteria for success were generally based on indirect measures of employability rather than employment itself, and in almost all cases, investors were paid back in full.

The first SIB in the US appeared in 2013, a project aimed at reducing recidivism among youth in a juvenile detention facility at Rikers Island, New York. We discuss this SIB in more detail below, but it is important to note here that it was the first of Goldman Sachs' forays into SIBs, that Bloomberg Philanthropies guaranteed most of the initial loan, and that the success criterion, a 10% reduction in recidivism, was higher than the rate required at Peterborough.

Since 2012-13, PFS projects have spread geographically and into issue areas beyond work-

force development and criminal justice reform. One of the most popular new areas in the UK and US has been homelessness, with housing provision as the main intervention used to reduce local jurisdictions' related health and incarceration costs. The first education SIB was in Salt Lake County in 2013, and the second in Chicago a year later. Both focused on early childhood education increasing children's kindergarten "readiness." We will discuss the Salt Lake County and Chicago projects in more detail below, since they are especially relevant to NEPC readers. The next nine education projects were spread across eight different countries.

Most PFS or SIB projects focus on cost savings for local public governments. In many cases, the criteria used to measure success are framed as directly related to such cost savings. For example, in Salt Lake County, the PFS project claims to have reduced the number of children requiring costly special education. Housing the homeless SIBs primarily promise cost savings by reducing expenses for emergency care and incarceration for the homeless. Some SIBs even tie payouts to investors to how much the intervention saved in public cost outlays over time. While all these arguments may make sense, it is striking to consider how few of the projects that have been evaluated fail to pay back investors. Of the first 18 SIBs listed in the Social Finance inventory from 2010-2013, almost all met criteria for success. The Rikers Island project stands out as the only failure in that early group, and, notably, Goldman Sachs lost only a small part of its investment because of Bloomberg's guarantee.

There are, however, some SIBs that do not specify cost savings. For example, a relatively small (\$270K) 2015 SIB (a Development Impact Bond) in Rajasthan, India, involves 9,000 girls not currently enrolled in primary schools and another 9,000 girls in grades three to five. The investor is a Swiss Bank Foundation, UBS Optimus, and the service provider is Educate Girls. The return to UBS if the project were successful is set at 7% to 13%. Outcomes are a combination of enrollment of out-of-school girls in government schools, and improved literacy and numeracy skills. These are measured against a control group in a randomized control trial. As in almost all SIBs, the project appears headed toward success, with UBS Optimus recouping 40% of its investment in the first year. However, the measured outcomes in this case are not necessarily related to a specific cost savings to the government agency payor, nor even directly to the outcome that forms the rationale for the project—that girls' education has high social benefits in the form of higher earnings, healthier and fewer children, and the greater likelihood of educated girls sending their own children to school. It may well be that a corollary payoff for the project resides in the data extracted as evidence of success. IDinsight, the third-party analytics firm that conducted the project evaluation,

Why allow global investors to profit from vulnerable communities?

lists funding partnerships that include the Bill and Melinda Gates Foundation, the Hewlett Foundation, the Omidyar Network, and other widely known foundations that are heavily steeped in policies that promote both the privatization and datafication of education in the US.

Further, not all investors involved in SIBs are such well-known financial entities as Goldman Sachs or UBS. Many are investors that specialize in social investments, such as Britain's Bridges Ventures Fund. Private foundations are also heavily involved in SIBS, often partnering with for-profit investors to share in a SIB or PFS project and distribute its financial risk. However, critics raise the larger question of precisely how risky these investments

actually are, since investors are party to setting the criteria for success, and it appears that the kinds of interventions financed by investors are rather reliable—especially in terms of the metrics specified to evaluate them. If risk is minimal, is the public sector in effect just borrowing money from private funders at rather high rates of interest to fund projects with interventions already shown to be effective? Ultimately, public revenues are used to pay for outcomes—so why not skip the intermediary? Or, as a more pointed critique, why allow global investors to profit from vulnerable communities?

Overview of US Legislation to Promote SIBs: SIPPRA and ESSA

One indication of how quickly we can expect SIBs to expand in the US is the passage of the 2018 Federal Social Impact Partnerships to Pay For Results Act (SIPPRA), within the Social Security Act, which set aside \$100 million in funding over 10 years to support outcome payments for PFS projects, feasibility studies, and project evaluations.⁷ According to the stipulations of the Act, its purposes are:

1. To improve the lives of families and individuals in need in the United States by funding social programs that achieve real results;
2. To redirect funds away from programs that, based on objective data, are ineffective, and into programs that achieve demonstrable, measurable results;
3. To ensure Federal funds are used effectively on social services to produce positive outcomes for both service recipients and taxpayers;
4. To establish the use of social impact partnerships to address some of our Nation's most pressing problems;
5. To facilitate the creation of public-private partnerships that bundle philanthropic or other private resources with existing public spending to scale up effective social interventions already being implemented by private organizations, nonprofits, charitable organizations, and State and local governments across the country;
6. To bring pay-for-performance to the social sector, allowing the United States to improve the impact and effectiveness of vital social services programs while redirecting inefficient or duplicative spending; and
7. To incorporate outcomes measurement and randomized controlled trials or other rigorous methodologies for assessing program impact.⁸

SIPPRA stipulates that the Treasury Department will accept applications for a score of different kinds of projects including: increasing the employment of the long-term unemployed; reducing recidivism rates; improving rates of high school graduation; reducing teen pregnancies; reducing child abuse; reducing homelessness; reducing the incidence of preventable diseases, such as asthma and diabetes; and, even increasing the proportion of children living in two-parent families—in sum, a list of most social and economic challenges in America.

The Act also requires that applicants cite existing evidence showing that the proposed intervention is likely to be successful; they must also detail the structure of the financial partnership, the evaluation design, and all other elements related to attracting investors. Points 5 and 6 above are especially important. While Point 5 suggests that these are “scale up” projects based on already proven interventions, few of the SIBs to date anywhere are large scale, and most are very small. Point 6 makes clear that the broader purpose of the program is to make public spending more cost-effective—a laudable goal, but in fact one that is simply a continuation of cost-benefit and cost-effectiveness analyses in place since the 1930s, when benefit-cost assessments were made compulsory and first used to evaluate large scale, publicly financed water resource projects.⁹ The only new element is the participation of private investors, giving them an opportunity to profit from relatively low-risk social interventions in the public sector—while profiling vulnerable populations in the process. Many of the projects are framed as supporting social services, yet the SIPBRA program is administered largely through the Department of the Treasury. Centering responsibility at the federal rather than the local levels may create structural gaps in both oversight and administration of projects.

In addition to SIPBRA funding, PFS initiatives are also embedded directly into federal education legislation through the 2015 Every Student Succeeds Act (ESSA):

40. PAY FOR SUCCESS INITIATIVE.—The term ‘pay for success initiative’ means a performance-based grant, contract, or cooperative agreement awarded by a public entity in which a commitment is made to pay for improved outcomes that result in social benefit and direct cost savings or cost avoidance to the public sector. Such an initiative shall include—
- (A) a feasibility study on the initiative describing how the proposed intervention is based on evidence of effectiveness;
 - (B) a rigorous, third-party evaluation that uses experimental or quasi-experimental design or other research methodologies that allow for the strongest possible causal inferences to determine whether the initiative has met its proposed outcomes;
 - (C) an annual, publicly available report on the progress of the initiative; and
 - (D) a requirement that payments are made to the recipient of a grant, contract, or cooperative agreement only when agreed upon outcomes are achieved, except that the entity may make payments to the third party conducting the evaluation described in subparagraph (B).¹⁰

The origins of ESSA’s PFS provisions can be traced to America Forward, a policy initiative of the New Profit national venture philanthropy fund. America Forward describes having “worked closely with Congress to shape key elements of the [ESSA] bill, including the development of language and advocacy around the addition of Pay for Success language and authority.”¹¹ Members of the America Forward coalition include, among others, Teach For America, KIPP, New Leaders, New Teacher Center, Nonprofit Finance Fund, and Third Sector Capital.

Three Case Studies of Social Impact Bonds

Rikers Island Youth Recidivism

The first PFS project in the US was at Rikers Island prison in New York City in 2013. More than half of the young men 16-18 years old sent to Rikers Island returned within one year of their release. The three-year project's objective was to reduce this recidivism rate and to benefit the city through reduced incarceration and increased youth employment. The initial target population included some 3,000 16- to 18-year-old males spending four days or more at Rikers Island; it was later expanded to include 19- to 21-year-olds. The lead investor Goldman Sachs supported the intervention with \$9.6 million, but Bloomberg Philanthropies guaranteed \$7.2 million to reduce Goldman's risk. Bloomberg also funded intermediary and evaluation costs. Social Finance's website describes the intervention and related metrics as follows:

The Young Men's Initiative, a citywide initiative in New York, developed the Adolescent Behavioral Learning Experience (ABLE) intervention. ABLE provides Moral Recognition Therapy (MRT), an evidence-based intervention that focuses on improving social skills, personal responsibility, and decision-making. It consists of cognitive behavioral therapy (CBT) and counselling, training, and educational services delivered to adolescents before release from Rikers Island. The Osborne Academy and the Friends of Island Academy lead the intervention. There was a single outcomes metric for this Pay for Success initiative, a reduction in 'recidivism bed days' (RBDs) for the intervention group compared to a matched historical group. This measure captures the number of days participants are held in jail during the 12 months following their release from Rikers Island. For investors to receive an outcomes payment, each yearly cohort had to reduce RBDs by 10% compared to the matched historical group, with returns increasing incrementally with performance up to a cap of \$11.7M at a reduction in RBD rate of 20%.¹²

The Osborne Academy ABLE intervention did not meet the agreed-on metrics for success in its first year of operation, and the project was terminated in August 2015. This triggered Bloomberg Philanthropies' guarantee to Goldman. Thus, Goldman lost \$1.2 million and Bloomberg lost its \$6 million guarantee, but SIB advocates still could claim victory because New York City lost not a penny, and further, ". . . the rigorous process of constructing the social impact bond required a new type of program management and pushed New York City government toward more outcomes-based decision making."¹³

Many methodological complexities were evident from the project's start, so it is difficult to tell whether the MRT intervention was ineffective for this particular subgroup of youth or whether the problem lay in the way the project was conducted and evaluated. According to Osborne Associates' CEO Elizabeth Gaynes, Osborne had extensive experience working with New York City's prison populations, but it was asked to implement the intervention without having any input into the previously determined evaluation protocol. Gaynes also told us that the results may have been affected by the requirement that the initial evaluation

be conducted after the first six months of intervention, a period marked by normal start-up challenges. Finally, the original evaluation design of randomly selected treatment and control groups in that cohort was abandoned because, given Rikers' housing conditions, it was impossible to keep youth in the control group from participating in MRT classes. The evaluator, Vera Associates, substituted a "quasi-experimental" design comparing the recidivism rate of the treatment group of 16- to 18-year-olds in 2013 with "a matched historical group who passed through the jail before the program was established (from 2006-2010)." To control for external factors, the evaluators tracked recidivism "for 19-year-olds over the same periods and then adjusted the results of the analysis accordingly."¹⁴ The evaluation summary indicates that 19-year-olds were selected for comparison purposes because they were not eligible for receipt of ABLÉ services and trend data had indicated similarity in recidivism rates for 16- to 18-year-old and 19-year-old cohorts. However, there may have been age-related differences in how youth experienced the interventions, so a methodologically sound comparison by age matching would not have been revealed by these analyses.

Utah High-Quality Preschool Program

The first social impact bond project in the US with an education focus started in 2013 in Salt Lake County, Utah. Private capital from Goldman Sachs and the J.B. and M.K. Pritzker Family Foundation financed the expansion of the *Utah High Quality Preschool Program* to provide early education services to over 3,500 children within five cohorts. Summaries of the project indicate that Goldman Sachs loaned approximately \$4.6 million to the United Way of Salt Lake and that the Pritzker Family Foundation provided that organization with a second \$2.4 million loan, reducing the financial risk to the senior lender if the evaluators found the program did not meet success criteria. United Way of Salt Lake, the initial recipient of the funding, also managed project implementation and repayments to the investors. Voices for Utah Children provided research and analytic supports, while the Granite School District and the Park City School District provided the preschool program to 3- and 4-year-old participants.¹⁵ PFS terms allowed for investors to be paid a return if "participating at-risk children avoided being assigned to special education," with the rationale being the assumption that reducing the number of special education students would save the districts significant funds. Children were deemed at-risk for special education based on their scores on the Peabody Picture Vocabulary Test.

The project has been critiqued for the metrics used to determine success. Because there was no definitive proof that the children not placed in special education would have been placed into it without the preschool experience, the findings are deeply problematic. There was no comparison group to test any of the project's assumptions or claims. Moreover, the test used to determine academic ability has been criticized as overestimating the number of vulnerable children—especially non-English-speaking children—initially deemed at-risk for special education. Many non-English speakers naturally learned English through subsequent years of the study and were not placed in special education.

Nevertheless: The investors still earned all of their money back, along with an additional 5% interest. Critics argue that the structure of the project favored investors, and that future

studies would need to involve a greater range of measures.¹⁶ More data, however, will not necessarily mean a better study without attention to appropriate research design, methods, and ethical standards of practice.

The Chicago Child-Parent Center Pay for Success Initiative

In 2014, nearly \$17 million of private capital poured into a project to expand access to pre-K learning for high-needs children in Chicago. The project was aimed at providing early education child development centers for 2,600 children over the project's four years (2014-2018). Chicago Public Schools (CPS) and the City of Chicago were the leading partners. Goldman Sachs Social Impact Fund, the Northern Trust Company, and the Pritzker Family Foundation provided nearly \$17 million capital for the program. The Finnegan Family Foundation underwrote a portion of evaluation costs and IFF, a local nonprofit, served as the Project Coordinator, managing the funding flow between investors and Chicago Public Schools. IFF distributed loan dollars for Child Parent Center operations and repaid lenders with success payments from Chicago Public Schools and the City of Chicago. IFF also contracted Metropolitan Family Services and the Independent Evaluator, SRI International (formerly Stanford Research Institute). Metropolitan Family Services served as the program intermediary, helping the school district identify best practices that could be used to improve the success of the project.¹⁷

Payments to the funding partners came from “savings achieved through avoidance of special education and other programs” on the following terms:

- Payments for decreases in special education were \$9,100 annually, compounding at an annual rate of 1.0% for each student that avoided special education after attending the CPC program.
- Payments for increases in “kindergarten readiness” were \$2,900 for each student that was “prepared for kindergarten” after attending the CPC Program.
- Payments for increases in “third grade literacy” were \$750 for each student that scored above the national average on the nationally administered third grade reading test.¹⁸

According to an SRI International report, 59% of the children who participated in CPC pre-school during 2014-15 had kindergarten readiness ratings that met or exceeded national averages. Because this exceeded the agreed-upon metrics, it triggered returns to the investors. In effect, the children's performance on the various behavioral and academic test scores served as investment instruments for the bankers. Metrics for the study, however, are under scrutiny (Sanchez, 2016). As revealed in a documentary exposé on impact investing, there were discrepancies between the success metrics used by the SIB project to trigger payments to the investors and the measures used by the school district.¹⁹

Technical, Technological, Data, and Ethics Issues

For SIBs to work properly, they require clearly established goals. In practice, the public

agency ready to pay back investors usually sets the goals in terms of money saved. For example, in the case of keeping homeless people housed for certain periods of time or reducing recidivism among prison inmates by a certain percentage, the underlying rationale is that achieving these goals saves a certain amount of money for the public sector. When UK public agencies publish SIB funds rate cards for PFS performance contracts, they are essentially telling bidders that their services must achieve performance norms at lower cost than rate card prices, which estimate public sector savings the performance norms would yield. On the Rikers Island SIB, the link between the reduction in youth recidivism and savings was more implicit, but everyone understood that the goal of reducing recidivism by a certain percentage was intended to save the city enough money to make repayment to Goldman Sachs worth the money invested.

There are several important drawbacks to trying to solve social problems through SIBs.

Appealing and straightforward as the basic rationale may seem, there are several important drawbacks to trying to solve social problems through SIBs. First, apart from the premium the public sector pays to the investors should criteria be met, SIBs are expensive to set up and administer. “The complex nature of stakeholders’ contracting arrangements generates considerable transaction costs. In addition, SIBs are technically difficult to commission and require considerable expert input, often (not coincidentally) by the same experts pushing the model.”²⁰ One example is that “Goldman Sachs reported that the contracts for the Massachusetts Juvenile Justice SIB, one of the largest in the world involving multiple investors and delivery partners, took 1,100 hours of consultant time.”²¹ Furthermore, in addition to the legal and administrative fees associated with writing a complex set of contracts, designing and implementing a randomized control trial can also be costly.

A second issue is the validity of experimental designs and metrics used to estimate the effects of the service provider’s interventions. According to the OECD, the evaluations used in SIBs met criteria of causal inference.²² However, there are two caveats associated with these evaluations. One is that in individual SIBs, where the relationship between cost savings and the outcome goal is implicit (not based on a rate card), investors have an incentive to negotiate down the minimum requirement for success. Another is whether providers may be incentivized to game the metrics to demonstrate success—even though they are paid regardless of outcome. Saltman writes about a situation with a Massachusetts PFS project in which a caseworker “received constant phone calls from an investment bank encouraging the caseworker to have the metrics turn out in favor of the bank so that the bank would earn the maximum amount possible through the bond.” He cites Jon Pratt, head of the Minnesota Council of Nonprofits, who stated, “You’re definitely creating incentives that would be considered corruption pressures.” Pratt’s point, as Saltman describes, is that “by having allegedly independent measurement tied to the possibility of profit or loss, a not-so-independent incentive is created to game the outcomes or cheat.”²³

A third issue is whether private investors, who do stand to lose if performance criteria are not met, will only participate in projects that target the most likely to succeed potential clients, leaving behind those more costly to serve—the most vulnerable groups among the homeless, unemployed youth, and students with special needs for whom public funds may be relatively scarce. The fact that the Rikers Island project is the only one to date that has

failed to pay out investors suggests that SIB advocates' claims that SIBs or pay-for-performance contracts promote innovation supporting high-needs groups are largely untrue. As noted earlier, until now, SIB contracts are almost all focused on tried-and-true approaches that have already worked on similar groups elsewhere.

There is almost no evidence that SIBs encourage innovation. In fact, almost all SIB-funded projects are based on well-established models. This should not be surprising: Financiers motivated by a return on investment (as opposed to meeting social objectives) have little incentive to fund risky innovative policy experiments.²⁴

A fourth point to consider about SIBs is that they are necessarily short-term because private investors and even social enterprises that provide the up-front money for these projects will not invest if the payout is long-term. Whereas short-term results may be indicative of interventions' longer-term impacts and cost savings, the short-term may overestimate longer-term effects. As of 2016, no SIB had produced a longer-term evaluation, so we have no solid indication of whether the successful SIB projects' performance metrics held up in the long run.²⁵

A final area for concern is that third-party evaluators in SIB and PFS projects often use untested, innovative technologies to gather data on project participants, often including data that are not used for the project's evaluation. The third-party assessors are not necessarily bound by ethical standards of research practice, nor are they required to ensure protections for the participants' privacy.

Analyses of PFS program evaluations in the US indicate widespread collection of data on outcomes that are tracked—but not necessarily tied to investor payments.²⁶ While it is unclear why additional metrics would be gathered, one could hypothesize two potential reasons: to undertake more in-depth research on the participants, and/or to potentially gather and either use or sell data to provide yet another return on investment. Without a public process to vet the privacy policies of companies collecting data, vulnerable populations may be subject to new data harms. Madden and colleagues document the matrix of vulnerabilities that allow for potential exploitation of data from members of disenfranchised communities, many of whom are poised to be the most likely participants in impact investment projects.²⁷ According to Fordham's Center on Law and Information Policy, vast amounts of student data are already regularly being bought and sold in underground markets where their source cannot be identified.²⁸

In addition to tracking recidivism rates, for example, the NYC ABLE Project for Incarcerated Youth also tracked the “intensity/dosage of service and progress through the program stages, as well as the number of safety incidents and conflicts reported.”²⁹ For the Chicago Child-Parent Center PFS Initiative, outcomes tied to success payments included measures of kindergarten readiness, avoidance of the use of special education services, and third grade literacy scores. However, additional items tracked but not tied to success payments included “student mobility and retention, improvements in social-emotional learning, parent engagement, and school attendance.”³⁰ For the Utah High Quality Preschool Program, longitudinal data are being gathered over 12 years of the participants' education paths; while special education and remedial services are the sole metrics that trigger payments to investors,

additional outcomes tracked include “numeracy and literacy, secondary and post-secondary school completion, college readiness, and connection to health insurance and healthcare provider.”³¹

One of the ways that data might be used to document the impact of SIB and PFS projects is through the use of smart contracts and blockchain digital identity data systems.³² Despite reassuring promotional literature, such new contracts and associated blockchain technologies are controversial and fraught with serious security problems.³³ According to Frankenfield:

A smart contract is a self-executing contract with the terms of the agreement between buyer and seller being directly written into lines of code. The code and the agreements contained therein exist across a distributed, decentralized blockchain network. The code controls the execution, and transactions are trackable and irreversible.³⁴

Primarily because data held in blockchain digital identity systems are irreversible and because data being gathered on youth are longitudinal—especially in early learning and/or juvenile recidivism impact projects—the California NAACP (in April 2019) and the national NAACP (in July 2019) passed resolutions opposing the use of blockchain identity systems. During its state conference in 2018, the California NAACP also passed a resolution opposing SIBs, PFS programs, and related outcomes-based financing schemes. The many impact investing projects that use integrating systems producing immutable and ineradicable data appear structurally poised to do more harm than good to the communities they purport to help.³⁵

David McDonald, a senior economist with the Canadian Centre for Policy Alternatives, refers to SIBs as “profit-driven, government-funded business deals—the Wall Streetification of public services.”³⁶ It’s not surprising then, to note that many investors bet on early learning projects featuring tech-related initiatives. Once embedded into social impact markets and armed with data from earlier projects, investors can game future markets by selecting participants more likely to succeed, and either increase their investments or “short” on deals inclined to fail in attempts to maximize profit. In a summary of proposed early learning investments, Schiller³⁷ highlights Pritzker funding of the Utah SIB preschool project and, among others, notes that four projects proposed by the Bridgespan Group involve technology applications and software programs such as *Text4Baby*, *Ready4K*, *LENA*, and *UPSTART*. Each of these programs involves some form of digital behavioral data tracking to assess narrow metrics of project effectiveness. While it remains to be seen which projects impact investors will support, key players and intermediaries with plans for early learning investments include The Bridgespan Group, the Silicon Valley Community Foundation, Omidyar Network, Chan Zuckerberg Initiative, and the Bezos Day One Fund.^{38 39}

Conclusions and Recommendations for Education Leaders on SIBs, Pay for Success, and Results-Based Financing Structures for Education and Social Services

SIBs and PFS financing of social interventions are trending largely because they satisfy the needs of many social service delivery entities. In theory, they provide up-front private sector funding allowing governments to finance ostensibly risky, innovative approaches to resolving such high-cost social problems as homelessness, recidivism, youth unemployment, special needs, and early education. They help social service delivery non-governmental organizations (NGOs) attract new funds to implement interventions among vulnerable populations. They create new markets for private companies that conduct social impact evaluations. And, of course, they provide private investors with new investment possibilities that improve their social image even as they provide higher-than-market returns.

The troubling aspect of SIBs and PFS financing structures, however, is that they shift public monies to private investor profits for what are actually low-risk, tried-and-true, cost-saving interventions that the public sector could just as well have financed and directly managed itself. Our review of existing SIB and PFS projects has uncovered considerable evidence that many of the rationales for such private financing are questionable. Following the critiques outlined by Saltman,⁴⁰ we summarize these dubious rationales into several distinct categories:

- 1. Market accountability.** SIB proponents argue that public sector projects do not use adequate accountability measures to monitor the effectiveness of their service providers in meeting outcome goals. However, there is much evidence that this is simply not true. Large federal dam projects in the 1930s and 1940s were the inspiration for cost-benefit analysis, and human capital analysis in the 1950s and 1960s demonstrated the relatively high rates of return to public investments in education and other social services. The same service providers contracted by SIB projects can bid directly on public contracts for social services based on the perceived cost-benefit analyses carried out by public agencies, and public contracts can specify that providers meet specific contractual objectives—or go unpaid.
- 2. Transfer of risk from public to private.** Although the shift of risk from public to private sectors is a purported benefit, the Social Finance database indicates that, to date, almost no SIB or PFS projects have failed to meet performance metrics, largely because their interventions have worked before on similar populations. It is arguable that the failed Rikers Island intervention was tried on a different, younger, inmate population than in previous, successful incarnations, and it would also have succeeded if the service provider had more time to organize its intervention. The point here is that generally private investors in SIBs do not experiment because the risks are too high. Therefore, given that projects rarely fail, it seems to make more sense for the public agency to directly take on the intervention funding, saving the payoff to investors.
- 3. Cost savings.** Almost all SIBs are related to interventions that would reduce public sector spending for social services. However, organizing SIBs, as we argued earlier, is

not cheap. There are high costs associated with preparing project contracts and with designing and running a randomized trial. In addition, the public sector has to pay a premium to investors if the intervention meets success metrics, which it almost always does. Private sector investors have to pay higher interest rates for their investments than the public sector, and so they need higher returns.

- 4. Private sector social responsibility.** Proponents of SIB arrangements implicitly argue that the private sector has a basic commitment to social responsibility. This argument has been used to justify privatizing public service delivery, and to justify turning over education, health care, prisons, pension funds, military operations and other public goods to private for-profit investors. However, the same concerns voiced by critics about privatizing other areas hold true for SIBs:

The introduction of a profit incentive fundamentally alters the relationship between the service provider and user. The principal client and dominant stakeholder of any given SIB is its financier, not those who receive the services it finances and whose voice rarely figures into any discussion. The motivation propelling private investment in SIBs is profitable return on investment, rather than assisting or changing the circumstances of citizens in need. SIBs reduce this latter feature—which we might regard as a central purpose of social public policy—to a byproduct of investment. This does not seem to trouble SIBs many proponents, who blandly assume that the interests of private financiers can be aligned with the needs of service users, and are content to see the changing fortunes of citizens instrumentalized as payment triggers. SIBs thereby transform citizens into commodities. The inevitably complex contracting arrangements that SIBs entail also transform the nature of policy accountability with governance and reporting systems geared toward the needs of private funders rather than elected officials. SIBs exemplify the financialization and privatization of social and public policy; they reduce the rights of citizens both as service users and as a polity.⁴¹

In addition, private investors, as we pointed out earlier, are interested in short-term returns, so the kinds of projects that attract SIB and PFS funding will necessarily avoid and undermine attention to more complex, deeper structural inequities that fuel continuing disparities at the root of social problems. “Most social problems are complex and require comprehensive programs and policies that stay the course. A bias toward programs that produce quick, measurable results narrows the public dialogue and waters down findings.”⁴²

In the current policy landscape, SIBs are poised to substantially alter the ways public resources are used to address social issues. The newest forms involve success metrics tethered to digital smart contracts, which will be narrowly designed in ways to produce investor profits. One layer of such future privatization will involve contracting with private entities for the actual delivery of public services, eliminating current public oversight. Another will involve allowing data from youth/participants in studies to be siphoned into private tech firms’ databases, allowing those firms to sell the data in increasingly valuable longitudinal data markets. By design, such models provide social service programs accountable to

investors, not the communities ostensibly being served. The new structures are also likely to involve the outsourcing of research to third-party evaluators, who may not have the best interests of the public in mind.

Recommendations

Recent legislation means that education leaders need a good understanding of SIBs: Pay for Success (PFS) financing structures are embedded in the Every Student Succeeds Act (ESSA), and through the Social Impact Partnerships to Pay for Results Act (SIPPR), millions of dollars are likely to soon be distributed to support SIB arrangements. Therefore, we urge education leaders to recognize that such projects have been designed to: (a) turn public services into centers for the extraction of private profit; (b) view individuals from a deficit lens, as in need of being “fixed” with narrow/short-term metrics of success; (c) amass vast amounts of data that can be used for predictive profiling of targeted communities; and (d) remove community voice and control from governance of public services. In cases where public agencies already have PFS projects under way or are in nascent stages of enacting such projects, we recommend the following:

1. Before contracting out a social impact project, the public agency involved should be able to show that previous experience with the intervention indicates its risk of failure is high enough to warrant spending public money not only on the considerable administrative costs required to develop the SIB contracts, but also to pay off the investor. Otherwise, the public agency should directly execute the intervention.
2. Projects vying for SIPPR and/or ESSA funding should be required to demonstrate alignment with the Belmont Principles and Guidelines for the Protection of Human Subjects of Research. These include full, informed consent/assent from participants, assurances of data privacy, confidentiality and anonymity, and opportunities to discontinue participation at any time without penalty or harm. Private researchers should adhere to basic research ethics, especially when working with vulnerable populations and extracting public funds for projects that yield both data and profits.
3. If private firms are to collect sensitive social/emotional, behavioral, attitudinal, health, and/or learning data from youth, and if longitudinal research on the projects are to include predictive analytics of any sort, the firms should make clear to families how data will be used and what type of predictions about participants will be produced. In addition, a clearly communicated opt-out option should be available to families who want to receive services but not participate in data collection.

More generally, policymakers and others should be skeptical of the hype that SIBs are a win-win for all concerned and without downsides. Such claims are often made by private investors, and even by NGOs legitimately seeking more funding to engage in social interventions. We should be sincerely skeptical about bringing the private sector further into the areas of social services and education. No matter how well-intentioned private investors may appear to be, they are ultimately governed by private interests. No matter how easily and often those private interests can be rationalized as aligning with public interests, that is unlikely to be the case.

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