

PRIVATIZATION BY STEALTH



THE TRUTH ABOUT **SOCIAL IMPACT BONDS**

SOCIAL IMPACT BONDS
PROVIDE PRIVATE INVESTORS WITH A
WHOLE NEW WAY TO MAKE OUT LIKE
BANDITS—AT OUR EXPENSE

UPDATED OCTOBER 2016





A wolf in sheep's clothing

BEWARE SOCIAL IMPACT BONDS

Social Impact Bonds are NOT what they might first seem to be.

They are NOT a new way to magically reduce the cost of government and still give us all what we want and need from government.

They are simply a new way to trick us into believing there is actually a way to do that. There isn't.

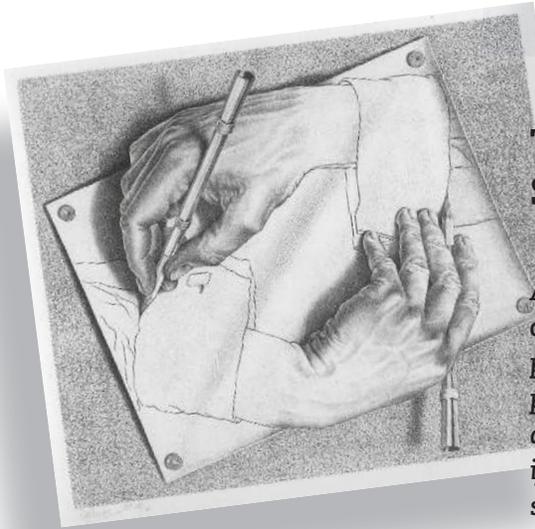
Social Impact Bonds are no more than a way to privatize public services without calling it that.

They don't reduce the cost of government. They don't improve the delivery of public services.

They are a wolf in sheep's clothing. And we are seeing more of them in Canada.

Beware.

An illusion of risk



The anatomy of a Social Impact Bond

A Social Impact Bond is nothing more than a contract: a deal between a government and private investors, who front the money for public services and control how the services are delivered. Technically investors only get paid if the service is a success. In practise it's one sweet deal for private investors. For the rest of us—not so much.

THE IDEA BEHIND Social Impact Bonds is that private investors and the government enter into a contract. Private investors fund services that have traditionally been funded by governments. Governments repay investors their capital, as well as an agreed-on profit—if agreed-on social outcomes are met. If the service does not meet the agreed-on social outcomes, investors get nothing back.

Usually an intermediary organization administers all aspects of Social Impact Bond projects including hiring the organization that is actually delivering the service.¹

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.²

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.

Just can't wait to do it

Governments are lining up to use Social Impact Bonds to privatize public services.

SOCIAL IMPACT BONDS have a lot of sex appeal for governments looking to dump their responsibility to fund public services. The fact SIBs increase administrative costs and reduce public accountability couldn't matter less. All that matters is that they give governments one more way to deflect criticism levelled at their obsessive drive to make deep cuts to existing services.

Social Impact Bond projects are operating in Canada and 13 other countries. More governments are planning to use them. While Social Impact Bond projects only started in 2010, the illusion of free money means they are spreading faster than a cold in a kindergarten.

Both the federal government and the Saskatchewan provincial government are already sponsoring Social Impact Bond projects. In Ontario, a two-year process to select a Social Impact Bond project has reached the short-list stage.

Manitoba premier Brian Pallister has expressed support for Social Impact Bonds. So has the BC government's Social Innovation Council and the ONE Nova Scotia Coalition.

There seems to be no limit to what Social Impact Bond projects are ready to take on. Social Impact Bond projects are either set up, or are in the process of being set up, in:

- Justice and corrections
 - Skills training
 - Public health
 - Child welfare
 - Services for seniors
 - Early childhood development
 - Education
 - Homelessness
 - Resources for families
- Other areas being discussed include:
- Developmental services
 - Supports for people with physical disabilities
 - Mental health

Like jelly to a wall

Proving Social Impact Bond projects make a difference will be almost impossible.

THE FIRST SOCIAL Impact Bond project only started in 2010, and whether it even partially met the agreed on social outcomes was supposed to have been announced in the summer of 2016.³ This project 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. Privatization of most parole services in England and Wales led to the Social Impact Bond being wound down early, but under the original plan investors stood to make as much as £8 million from an investment of £5 million.⁴

Concerns have been raised that even if the project does meet its targets, it will not provide evidence that Social Impact Bonds work.⁵

An example is the way participants in the program were chosen. Participants in the program were those who volunteered – in other words those willing to make the greatest effort to stay out of prison. In the words of British statistician Sheila Bird, the intermediary organization running the Peterborough Social Impact Bond, “achieved an open goal for itself.”⁶

Similar problems have been identified with the first Social Impact Bond in the United States to receive a payout—a preschool program in Utah. When early-childhood education experts looked at the program they found the way success was measured made the program appear far more successful than it really was.⁷ The result was the multinational investment bank financing the project, Goldman Sachs, may have been paid far more than it would have received if it had been possible to accurately measure the program’s success.

There is also the larger question of whether it is even possible to figure out if Social Impact Bond projects – or other pay for success programs – make a difference.

As anyone working in community social services can tell you, there are a lot of things that affect how successful a service will be that have nothing to do with the quality of service being provided. It is a lot easier to help people with addictions or mental health issues if they have places to live. More people using employment counselling will find work when unemployment is low.

Researchers looking at which programs work put a lot of time and effort into making sure that any improvements they find are caused by the program they are studying. With a program to help former inmates that means finding ways to make sure a reduction of re-offending is due to the new service rather than things like a drop in unemployment or better access to housing. But the structure of Social Impact Bonds makes it impossible to look at all of the different things that can affect how successful social services are at addressing or preventing problems.

The control group used with the Peterborough Social Impact Bond project is an attempt to measure whether it is the project or other things that are having an impact. Unfortunately, the control group is far weaker than what would normally be acceptable for researchers. Even a report from the British Ministry of Justice, which is paying for the project,⁸ has suggested that the process will fail to answer the question of whether the Social Impact Bond project made a difference.

Stuck with the bill

Social Impact Bonds add a new layer of private sector bureaucracy and added cost.

A STUDY FOR the Maryland Department of Legislative Services looked at what the result would be if a project similar to the Peterborough Social Impact Bond was tried in Maryland. The study found roughly a quarter of the cost was due to the bureaucracy required by Social Impact Bonds and investor profits. In addition to investor profits, the costs were: intermediary organizations; program evaluation; and contract design.⁹

An example of how this works in practice is the first Social Impact Bond project funded by the Canadian government. This project is a basic skills training for up to 400 students, delivered by

community colleges in 4 provinces. While the Canadian government is providing up to \$2.75 million,¹⁰ no more than \$1.1 million will be going to the colleges delivering the program.¹¹ In other words, the extra costs that come with Social Impact Bonds will eat up 60% of the funding.

Intermediary group costs include expenses that would be unacceptable for governments or social service agencies. For example Social Finance, an intermediary group running several Social Impact Bond projects in Britain, spent \$52,500 hiring a lobbyist in Massachusetts.¹² At New Profit Inc., an intermediary for Social Impact Bonds in Massachusetts, the CEO makes over \$400,000 including benefits.¹³

In their defence intermediary groups would point out that their role is that of investment banks and that what they spend on costs like executive salaries and lobbying is less than most investment banks. The question that doesn't get asked is why funds for public services should be used to pay investment bank style expenses—modest or otherwise.

A whole world of trouble

Social Impact Bond contract negotiations are long and complex and so costly we should question the whole idea.

IT'S EXPENSIVE ENOUGH to find investors and to oversee how services are delivered; add to that the cost of negotiating the contracts under which Social Impact Bonds operate and it's hard to see why anyone would want to bother.

Contracts cover the social outcomes that the Social Impact Bond is supposed to meet, repayment and how to measure social outcomes. Contracts are also the only opportunity governments have to set standards for how services will be delivered.

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.”¹⁴ In Massachusetts, names of the organizations that were meant to provide 2 Social Impact Bond projects were announced on August 1, 2012,¹⁵ but it took 17 months to get one contracted signed¹⁶ and over 2 years to launch the other.¹⁷

Those involved in negotiating Social Impact Bond contracts aren't releasing the costs and it isn't hard to guess why. With people making or losing millions of dollars, depending on how the contract is worded, some expensive lawyers and accountants are going to be involved in the negotiation process. When the negotiation process is taking over a year those bills are going to add up—for both intermediary organizations and governments.

The envy of loan sharks

Governments are ready to use public money to pay private investors returns as high as 200%.

SKY HIGH RETURNS on our money are not something any of us expect. A Royal Bank GIC will pay 2.02%—if you leave the money with them for five years. The best you can do with a savings account at TD Canada Trust is 1.05%—even if you invest \$5M! But, put your money into a Social Impact Bond project and the sky's the limit.

The first Social Impact Bond in Australia will hand investors a return of up to 15% per year.¹⁸ Investors in the Peterborough prison project in England, the world's first Social Impact Bond project, were told they could make as much as £3 million on an investment of £5 million—a return of over 60%. For a project on Merseyside in England, the British government could end up paying £4.5 million to investors who only provided £1.5 million.¹⁹ That's a 200% return. Something unheard of outside of the casinos in Las Vegas.

Proponents of Social Impact Bonds defend large profits by pointing to the savings that Social Impact Bonds might generate if they were used to fund programs to prevent social problems. This defence ignores the key question. If borrowing money to fund programs to prevent social problems costs governments less than profits for Social Impact Bond investors, why use Social Impact Bonds?

Two other questions that are also emerging are whether Social Impact Bonds really save money and whether tax credits or other incentives for Social Impact Bond investors will further increase costs.

As seen on TV

Social Impact Bond investors want money-back guarantees.

RISK IS NOT something investors in Social Impact Bonds want to worry about. They want every Social Impact Bond project to come with a money-back guarantee. Just like some “miracle” product offered in TV infomercials

There was one attempt to get individual investors to put money into a Social Impact Bond without the investment being guaranteed. It failed.²⁰

Charities in the United States agreed to guarantee most of Goldman Sachs’s investments in Social Impact Bonds in New York City and Utah.²¹ Even though Goldman Sachs made US\$6.1 billion last year, when the Social Impact Bond it funded in New York failed, most of its losses were covered by a charitable foundation.²²

Most of the investment for the Peterborough Social Impact Bond came from charitable foundations. The only other significant funders are government or quasi-government sources. These include: Big Society Capital, which was created by the British government to encourage social investment; the Big Lottery Fund; and the Cabinet Office Social Outcomes Fund.

Social Impact Bond cheerleaders continue to press for measures to increase profits and reduce risk for those investing in Social Impact Bonds. A July 2013 report from the Social Market Foundation in Britain suggested, “significant subsidy will still be needed from philanthropists or government if mainstream investors are to enter the market.”²³

Tax credits for Social Impact Bond investments in Britain mean taxpayers cover 30% of investments in Social Impact Bonds. This is on top of any profits investors receive.

Nothing that generous has been proposed in Canada—yet. However tax credits to encourage investments in Social Impact Bonds and social enterprises are being discussed. As early as 2012, there was a suggestion that the Ontario government guarantee at least some of first-time investments in Social Impact Bonds.²⁵

Wild goose savings

The promises of Social Impact Bond savings never stop. The delivery of savings never starts.

HUNTING FOR THE savings promised by Social Impact Bonds is always a wild goose chase.

There is no dispute: funding programs to prevent social problems has the potential to save money. There is strong dispute as to whether Social Impact Bonds can be an effective way to do that. The evidence so far is either unconvincing or, even worse, absent.

A Maryland Department of Legislative Services study found Social Impact Bond costs were \$4.1 million and savings were less than \$250,000.²⁶ It was clear the savings the project would generate would not be enough to cover the cost. The stark reality was most of the funds to pay for the Social Impact Bond project would come from increasing taxes or cutting other services.

A report by a British think tank, Social Market Foundation, came to a similar conclusion. Their report, *Risky Business*, stated “Social Impact Bonds are an expensive method of expanding social interventions.”²⁷

In Canada, the experience with the first federal government Social Impact Bond, where only 40% of funds are going to the colleges delivering the service, raises questions about whether it would be possible to achieve savings.

The draft 2014 United States budget provides an indication of how expensive subsidizing Social Impact Bonds could become. It's proposed that half a billion dollars be spent on subsidies for "payment by results" schemes, including Social Impact Bonds.²⁸ When the U.S. has fewer than 20 Social Impact Bond projects in the planning stages or in operation, that's a huge amount of money.

The obvious, common sense conclusion is impossible to miss: If governments have money to pay these and other costs that come with Social Impact Bonds, they have the money to fund services directly.

It is a conclusion governments continue to ignore.

Cooking the books

Governments use Social Impact Bonds to keep debt off the books.

IT'S NOT POSSIBLE and governments know it. They know they cannot cut programs in order to reduce spending and still deliver the level of public services people need and want. Their way out is to cook the books to hide the truth of how they actually get the money they need.

The truth is they are still borrowing money. But they do it in a new and indirect way. They do it by way of Social Impact Bonds. So, it does not get entered in the books as debt. It becomes part of the fiction that there is a way to borrow money for free; that there is a way to borrow money without adding to your debt.

It's the same fiction that once made P3s so attractive. Now, as auditors are catching up with P3s, Social Impact Bonds offer a chance to repeat that same shell game.

Don't get in our way

The less transparency and accountability, the better they like it.

PROMOTERS SAY SOCIAL Impact Bonds require, “Government to place few, if any, controls on the way that the intermediary organization accomplishes the outcome.”²⁹ 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 will be kept secret on the grounds of “commercial interest.” When NUPGE obtained a copy of the funding agreement for the first Canadian government Social Impact Bond through an Access to Information Act request, the section dealing with the targets the project was expected to meet and returns on investment was blacked out.³⁰ This means the public will have no idea whether a Social Impact Bond service is meeting the standards in the contract because they won't know what those standards are.

Easy money

The drive to make an easy profit will exclude those who need help the most.

HELPING PEOPLE IS hard work. Sometimes it pays off right away—sometimes it doesn't. But we use our public services to keep helping people as long as they need it. Social Impact Bonds don't work that way.

Investors in Social Impact Bonds will only make money if very specific goals are met. If they aren't, the investors lose their money. That means investors will cherry pick. They will only do what is fast and easy. They will not be interested in providing funding for projects to help those who need a lot of care for a long time. They will not invest in projects where the severity of the problems means success is uncertain and expensive.

Those most in need of help will be deliberately excluded through the contract provisions that set up the Social Impact Bond project. The method of selecting participants in the Peterborough project shows how it would be done.³¹

There is little chance that governments would insist that projects include people who are expensive to help—even though they could. It is not likely such projects would ever get off the ground. It would simply be impossible to find investors ready to back a project with so little promise of easy profit.

If governments rely on Social Impact Bonds to fund new services the outcome will always be the same: those most in need of assistance will be pushed aside or forgotten in the relentless drive to turn a profit.

He who pays the piper

Community-based agencies will lose control to Social Impact Bond investors.

IT'S THEIR MONEY so they get to call the shots. That's what investors in Social Impact Bonds expect. That's what they get. It's the last thing community agencies need or want.

Community agencies want to rebuild and help people recover from years of government cuts. They need money to do that. Social Impact Bonds offer that. But there's a catch. The only way to get the money is for the agencies to let somebody else decide what they can and can't do.

Social Impact Bond funding is structured so that community agencies no longer deal directly with government. They have to deal with “intermediary groups” instead. These intermediary groups will have control over how the project is run. Their first priority will always be profit for their investors.

Good intentions won’t matter. What the community agency knows is best for the people they serve won’t matter. The number one requirement, ahead of everything else, will always be profit.

In their report, the Social Market Foundation admitted that Social Impact Bonds, “could acquire characteristics of the prime contractor model with investors setting delivery requirements”.³² That’s bad enough, but there is also a danger of smaller agencies being squeezed out completely.

To achieve significant savings Social Impact Bond projects have to be on a large scale. It’s been assumed that intermediary groups would operate larger projects by hiring a large number of community agencies.

However, the need to make Social Impact Bonds more attractive to investors could well lead to an intermediary group favouring large for-profit companies over community-level, non-profit agencies.

It’s a sucker bet

**Even if Social Impact Bond projects don’t work,
governments are likely to still be on the hook.**

SUCKER BETS NEVER deliver the big payoff they promise. Just like Social Impact Bonds cannot.

The big payoff offered by Social Impact Bonds is that they will reduce the cost of government by using private money. It is not likely to work out that way. First of all, the people making the bet get to say what outcomes they are willing to bet on. Second, the same people will be looking for ways to get paid, regardless of any outcome. The fix is in. Costs to government are bound to rise.

The fix starts with the contract negotiation where investors will try to make it as easy as possible to meet the desired social outcomes. For example, the decision to allow participants in the first

Social Impact Bond project to self-select has made it almost impossible for the project to fail.

Moreover, there is an inherent difficulty in measuring success in areas that are less than an exact science. This will always allow investors to claim some success no matter what.

Even for a project as simple as reducing re-offending, there are a number of things that can affect the outcome that have nothing to do with the effectiveness of the service being provided. 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?

Plus, private contractors are notorious for using the courts to try and get their pound of flesh out of government regardless. Such court cases will cost the government a lot—win or lose.

Finally, charitable foundations and pension funds are the most likely sources of investment in a Social Impact Bond. Governments are not likely to risk the political fallout from deciding a Social Impact Bond Project has failed and so bankrupting a charity or pension plan.

Weapon of mass distraction

Social Impact Bonds are just another way to take attention away from cuts to public services.

IT'S A MAGICIAN'S trick. They call it misdirection. They get us to look away while they work their "magic." Governments use Social Impact Bonds for the same reason: they want to get us to look away while they make deep cuts to public services.

Social Impact Bonds are promoted as a way to fund new services. The hard truth is that it is government cuts that create the need for these new services. Worse still, the funds provided by Social Impact Bonds are never close to enough to replace the services cut. But project announcements make a big splash and provide a way of diverting attention away from the cuts.

The first federal government Social Impact Bond project in Canada was for job skills and literacy. This project was announced a few months after the federal government cut funding for provincial job skills programs. But \$2.75 million for a Social Impact Bond comes nowhere close to replacing the \$300 million that was cut.

Just as Social Impact Bonds originated in Britain, so did using them as a smokescreen for cuts. In 2011, the British government announced Social Impact Bonds to fund early intervention services after cutting funding for programs to support young families.³³

A year later, cuts to services for youth got the smokescreen treatment. After career services for young people were drastically cut,³⁴ the British government put a lot of resources into publicizing Social Impact Bond projects that fill similar functions, but will only help a small number of young people.

Governments in Canada that are looking at Social Impact Bonds are all ones that have been cutting funding for public services that people value. Even if they don't see Social Impact Bonds as a tool for large scale privatization, they definitely see them as a way to deflect attention away from the cuts.

Killing a good idea

**Social Impact Bonds help undermine
the original intent of social finance.**

IT'S A GREAT idea: do good and make some money at the same time. That was the original goal of what we now call "social finance."

The heart of the idea was that investors would willingly accept a lower rate of return, if their investment helped make the world a better place.

There are plenty of positive examples of what can be achieved by social finance and the social enterprises it funds. Economic development by first nations or construction of affordable housing are just two areas where social finance has made a difference. Social finance can also be a way of increasing local control over the economy.

But Social Impact Bonds turn the original ideals of social finance on their head. Instead of making a profit to help the most vulnerable, the goal becomes making a profit from the most vulnerable. And something that could be a valuable tool in strengthening communities and our economy is undermined.

The big picture

FOR MORE INFORMATION on the value of public services, potential threats to them, and how we can respond, please visit:

- www.nupge.ca
- www.publicservicesfoundation.ca
- alltogethernow.nupge.ca

Endnotes

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- ³⁴ Peter Walker, "Careers advice reforms led to worrying deterioration in standards, say MPs," The Guardian, January 23, 2013, <http://www.theguardian.com/education/2013/jan/23/careers-advice-reforms-mps>.