

The background of the slide features a large, faint, circular seal of the U.S. Department of Education. The seal contains a central emblem with a tree and a globe, surrounded by the text "DEPARTMENT OF EDUCATION" at the top and "UNITED STATES OF AMERICA" at the bottom, with two stars on either side.

U.S. Department of Education

**The Potential Role of  
Social Innovation Financing  
in Career and Technical  
Education**

*This page intentionally left blank*

# The Potential Role of Social Innovation Financing in Career and Technical Education

Prepared for the

U.S. Department of Education  
Office of Career, Technical, and Adult Education

**NATIONAL CENTER FOR INNOVATION  
IN CAREER AND TECHNICAL EDUCATION**

Prepared by

George Overholser  
THIRD SECTOR CAPITAL PARTNERS

Steven Klein  
RTI INTERNATIONAL

**OCTOBER 2015**

This report was produced under U.S. Department of Education Contract No. ED-VAE-12-C0051 with RTI International, which administers the Department of Education's National Center for Innovation in Career and Technical Education. Carolyn Lee served as the contracting officer's representative. The views expressed herein do not necessarily represent the positions or policies of the Department of Education. No official endorsement by the U.S. Department of Education of any product, commodity, service or enterprise mentioned in this publication is intended or should be inferred.

U.S. Department of Education  
Arne Duncan  
*Secretary*

Office of Career, Technical, and Adult Education  
Johan E. Uvin  
*Deputy Assistant Secretary Delegated the Authority of the Assistant Secretary*

October 2015

This report is in the public domain. Authorization to reproduce it in whole or in part is granted. While permission to reprint this publication is not necessary, the citation should be: U.S. Department of Education, Office of Career, Technical, and Adult Education, *The Potential Role of Social Innovation Financing in Career and Technical Education*. Washington, D.C., 2015.

This report is available on the Department's website at: <http://cte.ed.gov> and on the National Center for Innovation in Career and Technical Education's website at: <http://ctecenter.ed.gov/index.php/page/our-research>.

Requests for documents in alternative formats such as Braille or large print should be submitted to the Alternate Format Center by calling 202-260-0852 or by contacting the 504 coordinator via email at: [om\\_ceos@ed.gov](mailto:om_ceos@ed.gov).

If you have difficulty understanding English, you may request language assistance services for Department information that is available to the public. These language assistance services are available free of charge. If you need more information about interpretation or translation services, please call 1-800-USA-LEARN (1-800-872-5327) (TTY: 1-800-437-0833), or email us at [Ed.Language.Assistance@ed.gov](mailto:Ed.Language.Assistance@ed.gov). Or write to U.S. Department of Education, Information Resource Center, 400 Maryland Ave., SW, Washington, DC 20202.

Content Contact: Carolyn Lee at [Carolyn.Lee@ed.gov](mailto:Carolyn.Lee@ed.gov).



# CONTENTS

	PAGE
List of Exhibits .....	iv
Abbreviations .....	v
Executive Summary.....	vi
<b>An Innovative Approach for Financing Social Programs.....</b>	<b>1</b>
Agents of Change.....	1
<b>Advantages of Social Innovation Financing .....</b>	<b>3</b>
Performance Advantages.....	3
Fiscal Advantages.....	4
Political Advantages.....	4
A Case Study: The Massachusetts Juvenile Justice Pay for Success Initiative .....	5
<b>Applying Social Innovation Funding to Career and Technical Education .....</b>	<b>8</b>
Career and Technical Education Financing Options.....	9
Financing Challenges.....	10
Assessing Program Outcomes.....	10
Establishing Workable Frameworks.....	11
Educating Transaction Coordinators .....	11
Ensuring Adequate Financial Returns.....	12
National Trends .....	13
Current Pay for Success Projects .....	13
Sampling of Other Pay for Success Projects Currently in Development.....	14
Enabling Actions at the Federal Level .....	16
U.S. Department of Labor Pay for Success Pilot Program .....	16
Social Innovation Fund .....	17
Workforce Innovation and Opportunity Act (WIOA).....	18
<b>Conclusion.....</b>	<b>19</b>
<b>References .....</b>	<b>20</b>

---

## EXHIBITS

	PAGE
Exhibit 1: Pay for Success/Social Impact Bond (SIB) Capital Flow.....	2
Exhibit 2: The Massachusetts Juvenile Justice Pay for Success Initiative Project Structure.....	7



## ABBREVIATIONS

<b>CEO</b>	Center for Employment Opportunities
<b>Commonwealth</b>	Commonwealth of Massachusetts
<b>CTE</b>	career and technical education
<b>DOL</b>	U.S. Department of Labor
<b>ED</b>	U.S. Department of Education
<b>MAJJ Initiative</b>	Massachusetts Juvenile Justice Pay for Success Initiative
<b><i>Perkins IV</i></b>	<i>Carl D. Perkins Career and Technical Education Act of 2006</i>
<b>PFS</b>	pay for success
<b>RFR</b>	Request for Response
<b>ROI</b>	return on investment
<b>SIBs</b>	social impact bonds
<b>SIF</b>	social innovation financing
<b>SNAP</b>	Supplemental Nutrition Assistance Program
<b>SSDI</b>	Social Security Disability Insurance
<b>TANF</b>	Temporary Assistance for Needy Families
<b>Third Sector</b>	Third Sector Capital Partners, Inc.
<b><i>WIOA</i></b>	<i>Workforce Innovation and Opportunity Act</i>
<b>YSI</b>	Youth Services, Inc.

---



## EXECUTIVE SUMMARY

A new class of financial tools is being developed to promote human capital investments that benefit society. **Social innovation financing (SIF)** entails raising private capital to support promising social interventions, with the expectation that those providing the funding will eventually be repaid. Funds are allocated based on service providers' achievement of measurable improvements in social conditions, under what is termed a **pay for success (PFS)** contracting model. **Social impact bonds (SIBs)** provide the upfront working capital for PFS contracts. This working capital is needed because a delay in payments is inherent in the PFS approach as it can take years to determine if it has achieved successful outcomes.

Leveraging private-sector resources to finance government investments can dramatically expand the funding available for service delivery. Moreover, because the upfront costs and risks of implementing social programs are borne by outside agents, taxpayers are not required to make payments for the programs unless they produce an agreed-upon set of outcomes. SIF has the added advantage of providing funders with some assurance that their money will be invested responsibly. This is because well-designed SIF projects that incorporate PFS-SIB approaches target programs that (1) are research-backed, (2) are implemented by trained professionals vetted by investment officers, (3) produce measurable outcomes for participants, (4) include an evaluation component to measure impact, and (5) offer the potential of some return on investment.

PFS-SIB investments to date primarily have been directed at addressing the needs of high-risk populations (e.g., prison inmates, juvenile delinquents) for which social investments may reap substantial returns. The potential applications of SIF in educational and workforce training programs for other populations are as yet unknown.

This paper introduces the PFS and SIB concepts, describes their applications nationwide, and explores their potential for generating resources that can be used to finance the delivery of high-quality career and technical education (CTE) programming. State and local policymakers can use the principles presented in this paper to develop new applications for this innovative, yet still emerging method of social service procurement.

---



# AN INNOVATIVE APPROACH FOR FINANCING SOCIAL PROGRAMS

**Pay for success (PFS)** and **social impact bonds (SIBs)** have emerged as two promising approaches for expanding societal investment in effective programs and interventions. They operate by changing the way that government agencies at the federal, state, and local levels allocate and invest resources—shifting the focus from process to results. This new approach to financing human capital investment, termed **social innovation financing (SIF)**, entails raising private capital to support promising social interventions, with the expectation that those providing the funding will eventually be repaid.

PFS describes an approach in which government pays for services based on the achievement of measurable improvements in social conditions. Service providers develop evidence-based interventions that are designed to address a pressing societal issue, then enter into a multiyear contract in which an oversight body, typically a state or local government, agrees to make payments for success to the extent that measurable outcomes are achieved.<sup>1</sup> Compared to other forms of performance-based contracting, PFS focuses strongly on performance metrics that take counterfactuals into account. For example, in the workforce development area, payments for success might be based not just on how many participants gain employment but also on how many participants *would not have otherwise gotten jobs*.

SIBs are a means of providing private upfront working capital for PFS contracts. This working capital is needed because a delay in payments is inherent in the PFS approach as it can take years to determine if it has achieved successful outcomes. Typically SIBs weave philanthropic grants or loans, or for-profit loans into an integrated working capital structure that is offered in exchange for a share of the government payments if performance targets are met.

## AGENTS OF CHANGE

Developing a SIF approach is a complicated undertaking that brings together a wide range of individuals from different sectors. And because a PFS-SIB transaction is a

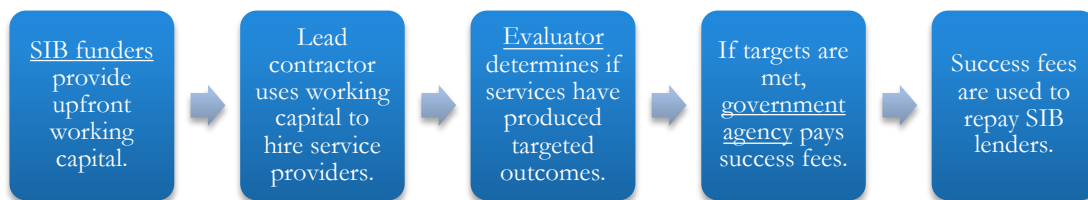
---

<sup>1</sup> <http://www.thirdsectorcap.org/pay-for-success/what-is-pay-for-success/>

contractual arrangement that entails raising money in capital markets, a level of financial scrutiny and legal protocols must be observed.

Most PFS-SIB transactions are created with the technical assistance of a **transaction coordinator**. The coordinator works with public and private stakeholders to facilitate the range of economic and operational analysis, negotiation, financial structuring, due-diligence investigation, contract formation, and logistical tasks that must be managed to design and launch a robust PFS-SIB project. Transaction coordinators may also function as financial arrangers, in which case they are responsible for designing integrated SIB financing structures, attracting the SIB funders, and orchestrating all stakeholders toward a closed transaction (see exhibit 1).

**Exhibit 1: Pay for Success/Social Impact Bond (SIB) Capital Flow**



SOURCE: Third Sector Capital Partners, Inc.

As illustrated in exhibit 1, PFS-SIB transactions begin when one or several **SIB funders** either grant or lend upfront working capital to a **lead contractor**. The lead contractor (sometimes referred to as “project intermediary”) then uses the working capital to hire and manage **service providers**, either nonprofit or for-profit, who deliver program services that are designed to improve pre-specified social outcomes. Service providers are typically paid on a fee-for-service or cost reimbursement basis, although some elect to have a portion of their payments tied to performance outcomes. After a period of time, an independent third-party **evaluator** determines whether the services have brought about changes in the targeted social outcomes. If so, a **government agency** then pays fees for success to the lead contractor, who then uses the funding to repay the SIB lenders.

# ADVANTAGES OF SOCIAL INNOVATION FINANCING

Performance funding offers a number of unique benefits that make it particularly well suited for financing public services or interventions that offer a positive **return on investment (ROI)** but might not otherwise be launched due to a lack of resources. Potential benefits fall into three broad categories.

## PERFORMANCE ADVANTAGES

- *Incentive to innovate.* Because PFS arrangements are structured around outcomes rather than pre-specified inputs, the government can be more flexible in paying for a wide array of innovative programs that would not otherwise be eligible for reimbursement. As they compete for PFS payments, service providers have an incentive to develop new ways to address social problems, which they might not attempt if they were being held responsible for a prescribed set of grant activities.
  - *Impetus to improve administrative data systems.* PFS contracting works hand-in-glove with databases that are already generated as a byproduct of administering government functions. By creating formal contractual linkages between financial payments and rigorous measures of outcomes, PFS creates an economically compelling reason to develop more reliable and inexpensive sources of ongoing administrative data. Placing emphasis on data collection and use also can drive providers to make greater use of data, as well as improve the quality of the information they report.
  - *Access to private talent.* SIB transaction coordinators and funders become deeply involved in PFS public and private partnerships, and bring expertise in due diligence, project structuring, project management, impact evaluation, computer science, communications, and financial reporting. These functions may be lacking in federal, state, and local government agencies, which are hampered by reduced staffing levels due, in part, to diminishing levels of government funding. Importantly, these private stakeholders have financial stakes that are aligned with the goal of generating superior social outcomes for families and communities in need.
-



## FISCAL ADVANTAGES

- *Improved allocation of social spending resources.* By paying only for programs that work, the PFS model uses taxpayer dollars more efficiently, typically in three ways. First, it uses the money to create new spending streams that are rigorously justified by its cost-benefit relationship. Second, the mix of expenditures is shifted within existing spending streams away from programs that are not effective and toward those that bring about the greatest levels of impact per dollar spent. Third, the PFS model discontinues spending on programs with no discernable level of impact (in which case PFS payments are not made). The sum total of these efficiencies must be weighed carefully against expenses associated with building PFS project structures, including the social science costs of measuring ongoing impact and the financing costs of paying interest for SIB loans.
- *Transfer of financial risk.* By transferring the financial risk of program underperformance to private SIB funders, PFS-SIB helps to increase government willingness to test social innovations. Similarly, because SIB loans are “forgiven” if social outcomes are not met, PFS-SIB arrangements insulate vital service providers from financial risk.
- *Access to private capital.* Many government agencies, be they at the federal, state, or local level, simply do not have near-term funding available to provide the working capital needed to launch innovative initiatives. The PFS-SIB approach taps into private sources, making it possible for government officials to launch initiatives that offer promising economic and societal returns that would otherwise not be realized.

## POLITICAL ADVANTAGES

- *Projects are both fiscally conservative and socially progressive.* PFS has natural, broad appeal in that it both increases the degree of accountability associated with government spending and focuses investment toward the improvement of social outcomes.
- *Projects outlast typical political time frames.* The multiyear time frames associated with most PFS initiatives often outlast the terms of elected government officials, making it possible to tackle social problems and implementation challenges that require long periods of focus to overcome. The presence of private SIB funders is often critical to the continuity and completion of these multiyear projects.



- PFS is a means of accomplishing money transfers between agencies, and between one level of government and another.* Frequently, one agency or level of government pays for a program that produces benefits in a separate agency or level of government. For example, a local diabetes program can produce Medicaid savings at the federal level, or a family rehousing program can bring about reduced costs in the foster care system. With PFS-SIB, private funders can work to deliver a social program with one government partner, and then seek payments for success from another.

## A CASE STUDY: THE MASSACHUSETTS JUVENILE JUSTICE PAY FOR SUCCESS INITIATIVE

The Massachusetts Juvenile Justice Pay for Success Initiative (MAJJ Initiative) (see exhibit 2), launched in January 2014, is an example of a SIF project employing a PFS-SIB approach that aims to reduce recidivism and improve employment outcomes for young men at high risk of reoffending. Massachusetts estimates that historically 55 percent of juvenile males have been reincarcerated within a three-year period, at a cost of \$47,500 per prisoner, amounting to almost \$300 million in incarceration expenses per year for the Commonwealth of Massachusetts (Commonwealth of Massachusetts 2012; Pew Center for the States 2011).

Seeking innovative ways to address the needs of this high-risk population, Massachusetts's Executive Office of Administration and Finance initiated a **Request for Response (RFR)** in January 2012, which sought lead contractors and service providers that were prepared to enter into a rigorous PFS contract. Grant awardees were expected to negotiate a PFS contract with the Commonwealth and recruit external, private SIB funders to provide working capital for the project (Third Sector Capital Partners 2013).

The RFR resulted in the selection of Third Sector Capital Partners, Inc., a nonprofit advisory firm headquartered in Boston that collaborates with government sectors, funders, and providers to address social needs through PFS-SIB, as the transaction coordinator (<http://www.thirdsectorcap.org/>). Roca, a nonprofit organization with a 25-year history serving this high-risk population, was selected as the service provider (<http://rocainc.org/>). Roca's programming consists of street outreach and targeted life skills, education, and employment programming, delivered over an intensive two-year period followed by two years of follow-up engagement.



The initiative was targeted to deliver Roca’s high-impact intervention to 929 at-risk young men aged 17 to 23 and to bring about reductions in the number of incarcerated youths from the 540 expected to 180 actual recidivists. Officially launched in January 2014, the PFS contract obligates the Commonwealth of Massachusetts to pay up to \$27 million in payments for success over a seven-year period. PFS payments will depend primarily upon the extent to which Roca participants exhibit fewer days in prison than a randomly selected group of similar nonparticipants. Additional payments will be tied to rates of program completion and employment that Roca participants achieve, as compared to randomly selected nonparticipants.

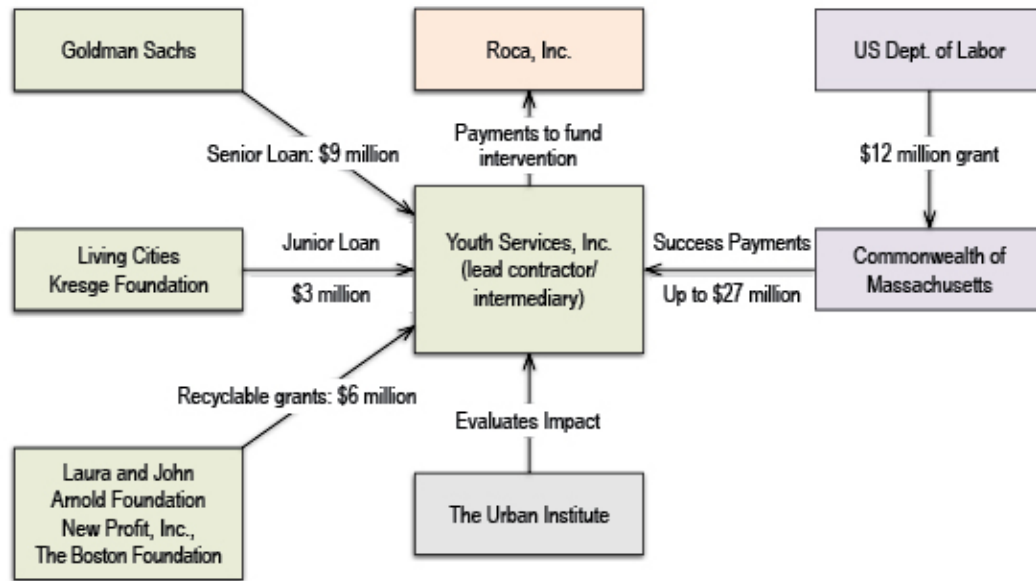
The Urban Institute, a think tank based in Washington, D.C. that carries out economic and social policy research, and provides technical assistance and evaluation expertise, will serve as the project’s independent evaluator (<http://www.urban.org/>). The Urban Institute is conducting a randomized control trial to determine the levels of Roca’s impact on outcomes. As an additional source of rigor, the Public Consulting Group, a public-sector management consulting and technology firm, will play the role of validator, ensuring that the evaluator adheres faithfully to the detailed evaluation plan that was contractually agreed to by all parties (<http://www.publicconsultinggroup.com/>).

To cover working capital needs, Third Sector helped the project raise \$18 million of private SIB commitments, which are being furnished by the following organizations through a combination of \$9 million of for-profit loans, \$3 million of philanthropic loans, and \$6 million of philanthropic grants:

- Goldman Sachs (<http://www.goldmansachs.com/what-we-do/investing-and-lending/urban-investments/>)
- Living Cities (<https://www.livingcities.org/>)
- Kresge Foundation (<http://kresge.org/>)
- Laura and John Arnold Foundation (<http://www.arnoldfoundation.org/>)
- New Profit (<http://www.newprofit.com/cgi-bin/iowa/home/index.html>)
- Boston Foundation (<http://www.tbf.org/>)

If Roca performs as targeted and the Commonwealth therefore makes full PFS payments, 100 percent of the \$18 million will be replenished, and a modest rate of interest for the loans will be earned. It is possible, however, that poor outcomes could result in a 100 percent loss of the \$18 million SIB capital stake.

Exhibit 2: The Massachusetts Juvenile Justice Pay for Success Initiative Project Structure



SOURCE: Third Sector Capital Partners, Inc.,

A new entity called Youth Services, Inc. (YSI) was formed to play the formal lead contractor role. As is common with PFS initiatives, YSI is a nonprofit entity whose sole purpose is to provide a limited-liability legal structure through which PFS and SIB monies will flow (<http://www.thirdsectorcap.org/wp-content/uploads/2014/01/MA-JJ-PFS-Fact-Sheet-Revised-Final.pdf>). YSI is housed within Third Sector’s nonprofit corporate structure, but, as a practical matter, YSI is controlled collaboratively by all of the stakeholders in the PFS public and private partnership.

# APPLYING SOCIAL INNOVATION FUNDING TO CAREER AND TECHNICAL EDUCATION

There are several reasons why career and technical education (CTE) may be particularly well-suited for PFS-SIB financing. First, CTE efforts are often associated with educational and workforce outcomes that generate cash savings for governments. CTE programs tend to have concrete outcomes that, at least in principle, are readily measurable and quantifiable. These include direct benefits, such as increases in participants' rate of employment, hours worked, and wages earned, as well as indirect results, such as increases in taxes paid. Measurable savings in terms of federal, state, and local government benefits and subsidies that are avoided (e.g., unemployment benefits, Temporary Assistance for Needy Families [TANF] payments, Social Security Disability Insurance [SSDI] payments, health care subsidies, Supplemental Nutrition Assistance Program [SNAP] benefits) also may accrue.

Importantly, CTE outcomes often are able to generate financial returns within a reasonable time frame. Many SIF projects seek to pay back investors over a three- to seven-year time frame based on the accomplishment of agreed-upon outcomes. Effective CTE programs generally would be able to demonstrate ROI within that time frame, in part because services are intended to assist individuals in transitioning into advanced education or training, and/or into gainful employment. These outcomes typically are realized within the year following students' exit completion of the program.

Second, because there are hundreds of testable innovations and providers serving millions of students, CTE is well-suited for an outcomes-driven reward system. Because SIB funders insist upon a rigorous and statistically stable measurement of outcomes, PFS thrives where the law of large numbers<sup>2</sup> can be used to apply actuarial techniques for measuring impact. CTE, with its many types of programs and educational institutions, and its substantial base of students for whom outcomes can be tracked, is particularly well-suited to a measurement-based system that encourages the identification of superior innovations and providers, and allows them to be differentially rewarded.

Third, CTE is well-positioned to take advantage of available data for key outcomes. Several large-scale databases, including the National Student Clearinghouse, state

---

<sup>2</sup> The law of large numbers is a principle of probability and statistics that states that as a sample size grows, its mean will get closer and closer to the average of the whole population (<http://www.math.uah.edu/stat/sample/LLN.html>).



unemployment insurance databases, statewide longitudinal data systems, the Wage Record Interchange System,<sup>3</sup> and the Federal Employment Data Exchange System,<sup>4</sup> can be used to match postsecondary and employment outcomes with secondary school student-level records to assess outcomes in an inexpensive and ongoing way. Metrics such as high school or college graduation rates, postsecondary enrollment rates, entry to college without need for remediation, employment rates, and earnings are all critical CTE outcomes that may be verified by these databases.

Evidence of changing workplace skill demands, and in particular the expansion of middle-skills jobs,<sup>5</sup> may provide a compelling narrative for PFS-SIB investment in CTE.<sup>6</sup> Low rates of student persistence and completion of postsecondary education, coupled with projections of worker shortages in skilled jobs, may offer an opportunity for using CTE to expand the pool of trained workers.

## CAREER AND TECHNICAL EDUCATION FINANCING OPTIONS

At the high school level, SIF could create greater incentives for CTE programs to focus on aligning secondary school and postsecondary course work within broadly defined career pathways that expose youths to a range of professions. It could be used to confirm the value of rigorous standards-based academic instruction that is anchored within industry-recognized technical content, or to reward CTE programs that allow students to earn college credit while still enrolled in high school, thereby accelerating the path to employment. Such programs of study<sup>7</sup> may offer the broadest approach for applying private-sector financing to public education programs.

---

<sup>3</sup> See <http://www.doleta.gov/performance/wris2.cfm>

<sup>4</sup> See <http://www.doleta.gov/performance/fedes.cfm>

<sup>5</sup> Middle-skill jobs are those for which individuals require more than a high school diploma, but less than a four-year college degree. See Carnevale, Jayasundera, and Hanson (2012) for a description of middle-skills jobs and their relationship to CTE fields.

<sup>6</sup> See Carnevale, Smith, and Strohl (2013) for a discussion of the educational attainment required for future workers. For state demand, see the National Skills Coalition's Middle-Skill Job Fact Sheets, which provide state-by-state data on middle-skill job demand (<http://www.nationalskillscoalition.org/state-policy/fact-sheets>).

<sup>7</sup> The content areas to be included in a program of study are described in Sec. 122(c)(1)(A) of the *Carl D. Perkins Career and Technical Education Act of 2006 (Perkins IV)*. It includes the expectation that CTE programs “(1) incorporate secondary and postsecondary education elements; (2) include coherent and rigorous academic and technical content aligned with challenging academic standards in a coordinated, nonduplicative progression of courses that align secondary education with postsecondary education to adequately prepare students to succeed in postsecondary; (3) may include the opportunity for secondary education students to participate in dual or concurrent enrollment programs or other ways to acquire postsecondary education credits; and lead to an industry-recognized credential or certificate at the postsecondary level, or an associate or baccalaureate degree.”



If the inclusion of CTE instruction in programs of study can be shown through rigorous evaluation to bring about a measurable educational benefit to students, then there may be value in using PFS-SIB offerings to expand student access to CTE programs. This could entail, for example, investing in a state or regional program, preferably in an industry area in which large, in-demand, high-wage openings are projected. Student performances would be tracked over time, with payments tied to successful student transitions from high school into college, or net differences in unemployment rates relative to a control group of students.

In lieu of investing in CTE as a stand-alone program, investments could be made in programs that seek to harness CTE as an instructional design strategy for the delivery of academic content. This could include investing in career academies, which operate as schools-within-schools offering college-prep studies organized around an industry specialty, such as health or computer technologies. Other interventions, such as the Linked Learning initiative, which connects rigorous academics with real-world experiences in a range of fields, also could be incentivized and tested using PFS-SIB.

Options also exist for financing occupationally focused training. For example, a PFS-SIB could be developed to expand community college students' access to quality CTE programming by expanding work-based job placements or providing for competency-based learning that engages students in real-world applications. New approaches for recruiting students, such as offering credit for prior learning, also could be used to expand the pool of students. Providing student supports, such as dedicated career counselors, or social supports, such as day care for children or transportation allowances, also may prove effective.

## FINANCING CHALLENGES

So long as outcomes are measurable and offer a quantifiable ROI, in the form of financial benefits or savings, then a CTE program may be a viable candidate for a PFS-SIB approach. There are a number of challenges that must be addressed, however, before it is possible to introduce social innovation financing to CTE.

### *Assessing Program Outcomes*

The pace of PFS-SIB adoption may be affected by social service providers' capacity to rigorously evaluate program impacts. While data resources have improved tremendously in recent years, much work remains to be done in collecting CTE data that can be used to accurately assess program outcomes.



Not all of the performance indicators identified in *Perkins IV* can be used to obtain valid or reliable data on student and program outcomes. For example, some provide limited information about the extent to which CTE contributes to student learning; others ask local providers to collect and report data that are not obtainable — for example, measures of employment placement that require the use of a student’s social security number to match records. Given that PFS-SIB financing is contingent upon soliciting financing from private or public investors and/or third-party organizations, evaluators must be able to provide assurances that they have access to accurate, valid, and reliable data to assess the economic and social ROIs of funded programs.

### ***Establishing Workable Frameworks***

While there is interest in moving toward evaluation, many nonprofit providers do not have the resources or capacity to conduct rigorous research to assess program outcomes. Such research requires employing complex experimental methods, for example, randomized control trials or quasi-experimental studies that rely on experimental and control populations. One key to mitigating this problem is to leverage national and statewide administrative databases more effectively, so that outcomes can be monitored and evaluated inexpensively and with less disruption at the service provider level. Options also must exist to compare and contrast performance across multiple providers. Again, this may present challenges for some states that have not yet deployed state longitudinal data systems or whose statutes or administrative policies may limit administrators’ ability to access outside databases.

Government agencies will also require funding to build PFS-SIB capacity and to access specialized technical assistance. PFS project construction is time-intensive and complex. It requires sophistication on the part of government (whether at the federal, state, or local level) in designing and negotiating PFS constructs, working across agencies, and devoting the necessary resources to contract implementation. Developing an offering in CTE, and in particular for programs that cross education levels, would entail securing agreement across secondary school and postsecondary providers, who each would need to invest resources and time to improve service coordination and track student outcomes. In the absence of some financial remuneration, building this support could be problematic.

### ***Educating Transaction Coordinators***

Transaction coordinators, who facilitate many aspects of the PFS contract (including aligning and negotiating with all parties to agree upon outcome metrics and payment schedules, seek funding, and serve as project manager), are expected to provide technical

---



advice to help structure grant programs. Finding transaction coordinators with content knowledge of CTE may present initial challenges. Overcoming this barrier will require building understanding in the financial and larger grant-making community of the academic and workforce development benefits that 21st-century CTE may offer.

### ***Ensuring Adequate Financial Returns***

PFS is taking off on a national scale, with significant interest from state and local governments in increasing social impact and funding what works. Current projects (documented below) target a wide range of social interventions that include financing for programs that address juvenile justice, homelessness, education, health, and other issue areas. This focus on assisting at-risk populations is predicated in part on equity and in part on fiscal concerns. Many minority and low-income populations face substantial barriers to economic success, and social service programs are designed to provide additional supports to help individuals in these groups move ahead.

A small percentage of individuals also accounts for a large percentage of societal costs, making investments targeted toward at-risk populations particularly attractive. For example, while only a fraction of youths drop out of high school and enter the prison system, the costs associated with incarcerating these individuals (financial as well as societal) introduce a significant drag on the economy and Americans' quality of life. For this reason, small investments in social programs serving at-risk populations can reap substantial benefits. If CTE is to prove a workable candidate for PFS investing, there must similarly be a sizeable return to justify investments. If the returns are not sufficient, then CTE may prove a weak choice for impact investing. Other programs may offer higher net present value, making them better investments. And generating paybacks sufficient to service investment vehicles may require CTE populations of a scale that precludes a workable implementation.

The pace of PFS-SIB adoption in CTE will also be driven by the level of comfort that private funders have that federal, state, or local government will honor its obligation to make payments for success. While special sinking funds<sup>8</sup> and enabling legislation can be used to satisfy these private funder requirements, CTE operates within a larger systemic context that may stand in the way of such approaches. The need for buy-in among teachers unions, the need for students to achieve state academic graduation requirements, school scheduling and transportation, and a host of other issues—legal,

---

<sup>8</sup> A sinking fund is used as a means of repaying investor resources that were generated through the issuance of a bond. In lieu of repaying the full principal of a bond issue on its maturity date, a company buys back a portion of the issue on an annual basis at the lesser of a fixed par value or the current market value of the bonds. This provides a level of safety to investors, since the issuer is less likely to default on repayment of the remaining bond principal because the final amount due at maturity is smaller.



political, and logistical—all contribute to creating an environment of uncertainty. Securing funding will require convincing potential investors that these systemic factors will not undermine PFS approaches.

Although there is no shortage of challenges confronting PFS-SIB adoption in the CTE field, similar challenges have already shown evidence of being navigable, as demonstrated by the dozens of PFS-SIB projects currently either launched or in development across many issue areas nationally.

## NATIONAL TRENDS

Now is an opportune time to consider introducing PFS-SIB investing in CTE. A changing global economy is reframing domestic labor market needs and the skill requirements of workers. While the returns on a baccalaureate education are still strongly positive, the increasing costs of attending a four-year college or university may be an obstacle to enrolling in one for many individuals, and may represent a bad investment for those uncertain of their career plans. The lingering effects of the recent recession also continue to direct policymakers' attention to workforce development, and in particular, the employability skills of younger generations. Well-designed CTE programs can help impart basic workplace skills — academic, technical, and employability — to help fill projected job openings in middle-skill occupations.

### ***Current Pay for Success Projects***

- *Social Impact Bond Project at Rikers Island.* A \$9.6-million PFS project is providing a cognitive behavioral therapy program for 16- to 18-year-olds detained at New York City's Rikers Island, with the goal of reducing the high recidivism rate for this population by at least 10 percent by focusing on personal responsibility education, training, and counseling. An independent evaluation of the project, produced by the Vera Institute of Justice and released on July 2, 2015, found that the intervention did not lead to reductions in participant recidivism and consequently did not meet its performance targets.<sup>9</sup> As a result, the New York City is not required to pay the investors who provided seed funding. However, although the program did not achieve its intended outcomes, the SIB financing mechanism operated as designed, with the result that over 4,000 individuals received treatment over the lifetime of the project.

---

<sup>9</sup> See <http://www.vera.org/sites/default/files/resources/downloads/adolescent-behavioral-learning-experience-evaluation-rikers-island-summary.pdf> for a summary of project findings. A full technical report was not available at the time of this publication.

- *New York State Center for Employment Opportunities Social Impact Bond.* This PFS project will provide \$13.5 million over a 5.5-year investment life to expand the work of Center for Employment Opportunities (CEO), a world-class provider of evidence-based training and employment programs to recently incarcerated individuals in New York state. CEO’s preventative program will assist 2,000 individuals over a four-year service period to break the downward cycle of recidivism while obtaining gainful employment.
- *Utah High Quality Preschool Program.* Up to \$7 million of SIB funding will deliver a high-impact and targeted curriculum to increase school readiness and academic performance of 3- and 4-year-olds. As a result of entering kindergarten better prepared, fewer children are expected to use special education and remedial services in kindergarten through grade 12, which results in cost savings for school districts, the state of Utah, and other government entities.
- *City of Chicago Early Childhood Education Social Impact Bond.* A \$16.9-million PFS program will provide early childhood educational services (pre-K) to up to 2,620 children over a four-year period. The intervention goals include increasing kindergarten readiness, improving grade-three literacy, and reducing the need for special education.
- *Cuyahoga County Family Homelessness and Foster Care PFS Project.* A \$5-million PFS contract with Cuyahoga County, Ohio, will provide subsidized housing, critical supportive services, family reunification services, and evidence-based trauma services to 135 homeless families over a five-year period, with the goal of decreasing days in foster care by 25 percent.

### ***Sampling of Other Pay for Success Projects Currently in Development***

Reflecting the accelerating rate of adoption of this funding model, more than 20 additional PFS and SIB projects are currently in development across the country. These include the following targeted projects and their locations:<sup>10</sup>

#### *Adult basic education*

- Massachusetts

#### *Homelessness*

- Massachusetts
- Denver, Colorado

---

<sup>10</sup> Because these projects are still early in their development, online citations are not yet available.

- Santa Clara County, California

*Home nurse visitation*

- South Carolina
- New York
- Los Angeles, California
- Michigan

*Mental health*

- Connecticut
- Santa Clara County, California

*Teen pregnancy*

- Washington, D.C.

*Youth recidivism*

- Illinois
- New York

*Substance abuse*

- Connecticut

Of particular interest with regard to CTE is the Massachusetts PFS-SIB transaction that will focus on improving employment outcomes driven by *adult basic education* interventions. This PFS-SIB will take advantage of waiting lists for these programs to allow researchers to conduct a randomized control trial in evaluating the approach, and will use the state unemployment insurance database to capture employment outcomes inexpensively. Separately, in Boston, the public school system is in the early stages of exploring how a PFS-SIB may utilize aspects of CTE to improve outcomes among disconnected youths.

Although *workforce development* PFS-SIB projects have not yet materialized, several feasibility studies will soon be launched, particularly in the areas of (1) using technology to accelerate technical learning that leads to employment and (2) combining vocational training with business-backed apprenticeships in the context of community colleges.

Additional PFS-SIB feasibility studies, which have not yet identified specific target populations or issue areas of focus, are under way in the following locations:

- San Francisco, California



- Los Angeles, California
- Salt Lake County, Utah
- Pima County, Arizona
- Philadelphia, Pennsylvania
- Virginia

## ENABLING ACTIONS AT THE FEDERAL LEVEL

Several federal programs have been enacted, with more potentially on the way, that are designed to enable PFS-SIB arrangements and that will provide an incentive for states and local government agencies to incorporate PFS-SIB projects into their CTE agendas.

### ***U.S. Department of Labor Pay for Success Pilot Program***

The U.S. Department of Labor (DOL) played an important, catalytic role in bringing about the MAJJ Initiative. In July 2012, the DOL issued a solicitation announcing the availability of up to \$20 million in grants to support “Pay for Success Pilot Projects” that would “demonstrate the feasibility and viability of the PFS funding model for providing positive workforce outcomes” (U.S. Department of Labor 2011). In December 2012, Massachusetts, Roca, and Third Sector jointly applied to the DOL solicitation and were eventually awarded \$12 million of federal funding, which will be used primarily as a source of funds for the MAJJ Initiative’s \$27 million of contingent PFS payment obligations.

The DOL solicitation required that applicants have a fully formed partnership in place at the time of their submission, as demonstrated by a signed partnership agreement. This agreement included the entities acting in the roles of the state labor departments or local labor programs, the intermediary, the investor(s), and an independent outcomes validator. The partnership agreement also was required to include the following:

- a well-defined problem and associated target population;
- a preventative service delivery strategy that is managed, coordinated, and guided by the intermediary, and has either an evidence-based history of success or a justifiable level of confidence for success;
- a commitment of funds from independent investors to cover all operating costs of the intervention, including administrative and overhead costs of the intermediary;





- one or more well-defined, achievable outcome target(s) that are an improvement on the current condition of the target population and have been agreed to by all required project partners;
- a financial model showing public-sector savings significant enough that an ROI may be provided to investors, and additional cost savings or efficiency gains are also realized by the public sector;
- a payment arrangement between the applicant and the intermediary, to be triggered by the verified achievement of the proposed outcome(s) within the grant period; and
- a validation methodology and a payment plan that is derived from quantifiable data, measures outcome targets for the target population relative to a well-defined comparison population or control group, and credibly demonstrates that achievement of the outcome targets is due to the intervention and not to random chance, general economic conditions, or participant selection.

The DOL solicitation affected the MAJJ Initiative in several important ways:

- It *raised awareness of the PFS concept and catalyzed action* among Massachusetts agencies that focus on workforce issues.
- It provided the MAJJ Initiative with an *incentive to include workforce-related outcomes* as drivers of its PFS payments for success, which had previously focused solely on reductions in incarceration.
- It offered a new source of federal funds that helped to *galvanize consensus among state leaders*.
- It *fostered collaboration among multiple state-level agencies* by enabling the braiding of DOL funds with state-level funds, and by making the use of those funds flexible enough to support multiyear contingent PFS contracting.
- It *accelerated progress* by imposing a strict deadline on the grant application due date and by insisting that the projects be fully negotiated as a precondition.

*It is possible that the U.S. Department of Education could use a similar approach to catalyze PFS-SIB pilots in ED's CTE work.*

### **Social Innovation Fund**

Twenty percent of the Social Innovation Fund, included within the American Recovery and Reinvestment Act signed into law by President Obama in April 2009, has been

designated for funding the exploration and structuring of PFS initiatives at state and local levels.<sup>11</sup> In October 2014, \$11.9 million in federal grants were awarded to eight organizations to provide technical assistance to governments and service providers that intend to implement a PFS initiative. Social Innovation Fund grants require that private contributions match the funding dollar-for-dollar. Dozens of state and local government agencies and service providers are expected to compete for the services that these grants will fund. The Social Innovation Fund is expected to administer an additional round of similar grants in future years.

*The \$11.9 million of Social Innovation Fund resources are eligible to be deployed toward CTE-related projects.*

### **Workforce Innovation and Opportunity Act (WIOA)**

Under the recently reauthorized *WIOA*, up to 10 percent (approximately \$223 million nationwide) of local workforce board funds may now be directed toward pay-for-performance uses, including PFS. The *WIOA* uses the following criteria to define what constitutes a pay-for-performance contract:

- a fixed amount that will be paid to an eligible service provider based on achievement of a specified level of performance for target populations as identified by the local board;
- a predetermined time table for achieving outcomes and related success payments, which may include bonus payments for the service provider to expand its capacity;
- independent validation of the achievement of the performance described in the contract; and
- a description of how the state or local area will reallocate funds not paid to a provider because the predetermined outcomes are not achieved.

The PFS concept in *WIOA* differs from traditional performance-based contracting in that it is not focused on inputs (e.g., number of people served through a training program). Rather, it is focused on outcomes (e.g., job placement and retention for six months or more).

*The approximately \$223 million of WIOA funds that PFS provides can be used for CTE-related projects.*

---

<sup>11</sup> The Corporation for National and Community Service oversees the Social Innovation Fund. For more information on the Corporation and its work see <http://www.nationalservice.gov/>.

## CONCLUSION

SIF is gaining considerable traction across the nation and across a broad array of issue areas. Although there are currently no PFS-SIB initiatives in CTE programs, it appears that CTE is well-suited to the model.

With millions of lives affected by government-backed social initiatives, PFS-SIB initiatives offer a potential breakthrough for America’s most vulnerable communities and for taxpayers at large. This approach can target government resources toward the innovations that work best. And it represents an opportunity to tap into large quantities of private risk capital, as well as private-sector expertise that would otherwise not be brought to bear on important social issues.

CTE may be particularly well-suited for PFS-SIB financing. First, CTE efforts are often associated with educational and workforce outcomes that generate the “cashable” savings for governments that make for economically attractive PFS arrangements. Second, because there are hundreds of testable innovations and providers serving millions of students, CTE is well-suited for an outcomes-driven reward system. Third, with several large-scale databases already well-established, CTE is positioned to take advantage of available data to gauge key outcomes.

As CTE programs weigh the benefits of PFS-SIB funding, the programs must consider several potential challenges, including the relative absence of

- *high-quality, valid, and reliable data* to allow for a comprehensive assessment of project outcomes;
- *methodologically rigorous evaluation protocols* to ensure that outcomes can be accurately quantified;
- *knowledge of CTE program benefits among transaction coordinators*, who need to understand how CTE programs function if they are to provide technical advising to help structure grant programs; and
- *compelling cost-benefit analyses* that can be used to show the economic return on an investment in CTE programs.

Despite these challenges, PFS projects present great potential for CTE programs and may help pave the way for successful and sustainable educational impacts and funding streams.

## REFERENCES

- Carnevale, Anthony P., Jayasundera, Tamara, and Andrew R. Hanson 2012. *Career and Technical Education: Five Ways that Pay Along the Way to the B.A.* Washington, DC: Georgetown University Public Policy Institute, Center on Education and the Workforce. Retrieved on July 9, 2015 from <https://cew.georgetown.edu/wp-content/uploads/2014/11/CTE.FiveWays.FullReport.pdf>
- Carnevale, Anthony P., Nicole Smith, and Jeff Strohl. 2013. *Recovery: Job Growth and Education Requirements Through 2020.* Washington, DC: Georgetown University Public Policy Institute, Center on Education and the Workforce. Retrieved on April 16, 2015 from [https://cew.georgetown.edu/wp-content/uploads/2014/11/Recovery2020.FR\\_Web\\_.pdf](https://cew.georgetown.edu/wp-content/uploads/2014/11/Recovery2020.FR_Web_.pdf)
- Commonwealth of Massachusetts. 2012. Department of Youth Services Internal Analysis.
- National Skills Coalition. 2014. *Forgotten Middle-Skill Jobs: State by State Snapshots.* Washington, DC: National Skills Coalition. Retrieved on April 16, 2015 from <http://www.nationalskillscoalition.org/state-policy/fact-sheets>.
- Pew Center for the States. 2011. *1 in 31: The Long Reach of American Corrections, Massachusetts.* Washington, DC: The Pew Charitable Trusts. Retrieved on April 16, 2015 from [http://www.pewtrusts.org/~media/legacy/uploadedfiles/pes\\_assets/2009/PSPP1in31factsheetMApdf.pdf](http://www.pewtrusts.org/~media/legacy/uploadedfiles/pes_assets/2009/PSPP1in31factsheetMApdf.pdf).
- Third Sector Capital Partners. 2013. *Social Innovation Financing Case Study: Preparing for a Pay for Success Opportunity.* Cambridge, MA: Third Sector Capital Partners. Retrieved on April 16, 2015 from [http://www.thirdsectorcap.org/wp-content/uploads/2013/04/Third-Sector\\_Roca\\_Preparing-for-Pay-for-Success-in-MA.pdf](http://www.thirdsectorcap.org/wp-content/uploads/2013/04/Third-Sector_Roca_Preparing-for-Pay-for-Success-in-MA.pdf).
- U.S. Department of Labor. 2011. *ETA Solicitation for Grant Applications: SGA/DFA PY 11-13.* Retrieved on April 16, 2015 from [www.doleta.gov/grants/pdf/pfs\\_sga\\_dfa\\_py\\_11\\_13.pdf](http://www.doleta.gov/grants/pdf/pfs_sga_dfa_py_11_13.pdf).
-



Vera Institute of Justice. 2015. *Impact Evaluation of the Adolescent Behavioral Learning Experience (ABLE) Program at Rikers Island: Summary of Findings*. Retrieved on July 9, 2015 from <http://www.vera.org/sites/default/files/resources/downloads/adolescent-behavioral-learning-experience-evaluation-rikers-island-summary.pdf>.



The Department of Education's mission is to promote student achievement and preparation for global competitiveness by fostering educational excellence and ensuring equal access.

[www.ed.gov](http://www.ed.gov)