

# SOCIAL INNOVATION FINANCING

**CASE STUDY:**

# PREPARING FOR A PAY FOR SUCCESS OPPORTUNITY

Prepared with support from:  
**THE ROCKFELLER FOUNDATION**



**THIRD SECTOR CAPITAL PARTNERS**  
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## A Letter from our Co-Founder & CEO

### Third Sector Capital Partners

Dear Reader,

A mentor once told me that the most important time to recruit talent is when you least have time to do so. I suppose the same can be said for case-writing. The most critical time to share experiences is when many partners struggle together to implement a shared vision. Indeed, the dual innovations of Pay for Success (PFS) contracting and Social Impact Bond (SIB) financing have captured the imaginations of an awful lot of people in government, philanthropy, impact investing, management consulting, think tanks, the legal profession, the accounting profession, mainstream banking, social service provision and the media.

With so much happening all at once, it is no surprise that those interested in the field often feel confused and ill-informed. And so, even though this case study merely reflects the early days of Pay for Success pilot development in the Commonwealth of Massachusetts, and even though a great deal of what we share will evolve as negotiations move forward, we thought it worthwhile to lift our heads up from the day to day and relate some of the experiences we have had to date.

If there is any critical takeaway for those working in this nascent industry so far, it is this: as the Boy Scouts say... BE PREPARED!

We hope the case will help to make this clear. It takes a tremendous amount of work to put a PFS/SIB deal into place. So much needs to be just right: a rigorous way to evaluate impact, a strong cost-benefit analysis, a service provider that can scale with quality, government partners that are willing (and able) to engage deeply, investors and boards that have an appetite to understand and embrace new financial constructs, and last but not least, a willingness by all parties to communicate, communicate, communicate as the multi-party problem-solving process tumbles forward.

Truly, if Pay for Success and Social Impact Bond Financing weren't such incredibly promising ideas, no one in their right minds would be doing all of this hard work. But we believe the promise is undeniably there. For fifteen years, the social impact sector has been talking about measuring "social returns" -- now we have a potential mechanism to actually do so. For fifteen years, we have been talking about how social investors don't have a way to "exit" successful investments -- now we have an opportunity to create onramps to large-scale government funding streams. And for fifteen years we've been talking about harnessing "blended value" asset classes that tap into philanthropic and return-seeking investor dollars -- Social Impact Bonds are a promising way to make that dream come true, too.

At Third Sector Capital Partners, our mission is to accelerate America's transition to a performance-driven social sector. If you share that vision, we hope you will enjoy this case study and encourage others to pursue the levels of hard work and attention to detail that it describes.

Many thanks to the Rockefeller Foundation for generously supporting the write up of this case study, and for its long-term commitment to promoting the development of the social impact sector.

Kind regards,



**George Overholser**  
Co-Founder & CEO, Third Sector Capital Partners

# THE CHALLENGE

Massachusetts, like many other states and municipalities across the US, is grappling with a tremendous challenge: With increasingly strained budgets and growing social need, how can government funding be directed towards evidence-based programs that offer demonstrated cost-savings? Pay for Success and Social Impact Bonds (PFS/SIB) have emerged as potential mechanisms for making smart investments in effective social interventions by changing the way Government allocates and invests its resources – focusing on results and outcomes. In short, funding what works.

In May 2011, Massachusetts issued a Request for Information (RFI) with the goal of helping the Commonwealth determine “the areas of government activity where success-based-contracting strategies have the potential to improve outcomes and/or reduce costs.” The Justice System is one area of government activity with the potential to illustrate both improved outcomes and well-defined cost savings for the Commonwealth. In addition, Massachusetts has a variety of established service providers that offer preventative initiatives to populations involved with the Justice System, particularly young people. One of these successful and well-known providers, Roca, had worked with Third Sector Capital Partners (Third Sector) for a year and a half to prepare itself to be a successful candidate for this PFS/SIB opportunity.

After reviewing the RFI submissions and preparing for the next steps of the procurement process, Massachusetts issued two Requests for Responses (RFR), one regarding youth services/reducing incarceration rates and the other regarding

homelessness and reducing Medicaid and shelter expenses. Multiple organizations were preparing to respond to the solicitation, with varying degrees of programmatic detail. In considering a response to the youth services/justice RFR, much of Third Sector and Roca’s work were organized around eight key criteria:

- **Government leadership** to address and spearhead a public/private innovation.
- **Social needs** that are unmet, high-priority and large-scale.
- **Target populations** that are well-defined and can be measured with scientific rigor.
- **Proven outcomes from administrative data** that is credible and readily available in a cost effective means.
- **Interventions** that are highly likely to achieve targeted impact goals.
- **Proven service providers** that are prepared to scale with quality.
- **Safeguards** to protect the well-being of populations served.
- **Cost effective programs** that can demonstrate fiscal savings for Government.

This case study examines Roca and Third Sector's approach to examining these criteria as they prepared to respond to the RFR. Service providers like Roca must invest time and thought in the pre-feasibility stage in order to be adequately prepared to successfully pursue a PFS/SIB opportunity or government procurement. On August 1, 2012, the

Commonwealth of Massachusetts moved forward with its Pay for Success initiatives by announcing the selection of Third Sector to serve as lead intermediary, in partnership with Roca and New Profit Inc., for a youth recidivism project.<sup>1</sup> Massachusetts was the first state in the nation to pursue a competitive procurement process for Pay for Success.

*Pay for Success and Social Impact Bonds have emerged as potential mechanisms for making investments in effective social interventions by changing the way Government allocates and invests its resources – focusing on results and outcomes.*



It is the relentlessness of a youth who shows up day after day no matter what that awakens hope in a young person.

<sup>1</sup>Massachusetts First State in the Nation to Announce Initial Successful Bidders for 'Pay for Success' Contracts. August 1, 2012. Available at: <http://www.mass.gov/anf/press-releases/fy2013/massachusetts-first-state-in-the-nation-to-announce-ini.html>

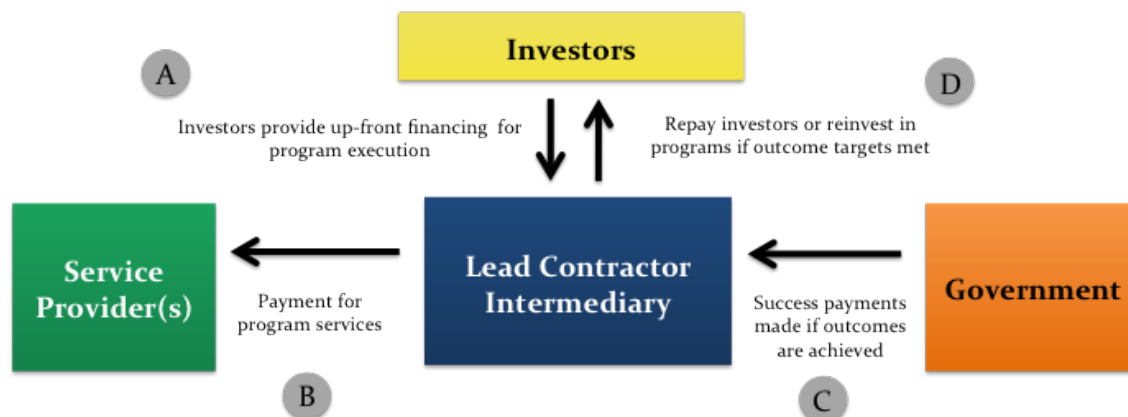
# PAY FOR SUCCESS AND SOCIAL IMPACT BONDS

Pay for Success is a general term for performance-based contracting between Government and providers of social services. Under this construct, Government pays when results are achieved as opposed to providing up-front and on-going payments for services. Social Impact Bonds are one potential financing option to support Pay for Success programs. They are not actually bonds. A Social Impact Bond brings together Government, service providers and investors to implement existing and proven programs designed to accomplish clearly defined outcomes. Investors provide the initial capital support and the Government agrees to make payments to the project, and therefore investors, only when outcomes are achieved.

Pay for Success/Social Impact Bond constructs are framed around several key principles:

1. Government, lead contractor and investors agree on targeted outcomes for a societal issue, for example, reducing recidivism or homelessness.
2. Government and lead contractor or intermediary enter a multi-year contract, in which the Government agrees to pay lead contractor or intermediary if targeted outcomes are achieved.
3. Private and/or philanthropic investors provide the necessary up-front capital to lead contractor to fund the program.
4. Lead contractor orchestrates the delivery of the social intervention via subcontracts with service provider(s).

*Exhibit 1: Pay for Success Cash Flows*



5. An independent evaluator monitors performance against agreed-upon benchmarks.
6. Lead contractor receives payments from Government only if targeted social outcomes are achieved, then repays investors or reinvests in programs.

### BENEFITS

In many cases, Pay for Success programs will not only achieve positive social outcomes, but also create fiscal savings for Government. This double-benefit makes Pay for Success politically attractive to multiple stakeholders. For example, \$250 million of investments towards preventative programs that reduce recidivism might eventually make it possible to close prisons that cost taxpayers \$1 billion per year to run. Other benefits of Pay for Success include:<sup>2</sup>

- Government funds impact and programs that work.
- Focus on social outcomes that change lives
- Reposition government spending to preventative programs.
- Attract new forms of capital to the nonprofit sector.
- Independent evaluation creates transparency for all parties.
- Shift and share risk of nonperformance from Government to private investors.

### RISKS

Pay for Success initiatives do come with a variety of risks. All stakeholders must be aware of the possible risks inherent in these initiatives as well as risk mitigation and management strategies. As Pay for Success develops, it will become easier to reduce and appropriately allocate risk for all parties involved. Several of these risks include:

- Lead contractor or service provider non-performance.
- Lack of clarity and/or ability to measure social outcomes.
- Non-rigorous evaluation methodologies.
- Government data unavailable for cost effective evaluations.
- Insufficient rate of return for funders and providers.

Additional literature on Pay for Success and Social Impact Bond theory and practice is available through the Center for American Progress, Nonprofit Finance Fund and McKinsey and Co.<sup>3</sup> The remainder of this case will focus on one provider, Roca, Inc. and its experience with Third Sector Capital Partners conducting due diligence and exploring the Pay for Success concept. The goal of the work discussed in this case was to determine if it was feasible for Roca to participate in a Pay for Success procurement, and ultimately, contracting process with the Commonwealth of Massachusetts. At the time this case study went to print, Roca and Third Sector were still negotiating final contracting terms.

*“Pay for Success programs will not only achieve positive social outcomes, but also create fiscal savings for Government. This double-benefit makes Pay for Success politically attractive to multiple stakeholders.”*

<sup>2</sup> McKinsey & Company. From Potential to Action: Bringing Social Impact Bonds to the US. 2012.

<sup>3</sup> Please visit [www.americanprogress.org](http://www.americanprogress.org), [www.payforsuccess.org](http://www.payforsuccess.org), and <http://mckinseysociety.com/social-impact-bonds/> for more information.



# THE PROBLEM AND OPPORTUNITY

Every year, approximately 4,000 high-risk young people “age out” of the juvenile justice system or are on adult probation in the Commonwealth of Massachusetts. According to the Commonwealth 55% return to prison one or more times within three years of release. The Pew Center for the States estimates that it costs Massachusetts an average of \$47,000 to incarcerate a prisoner for a year.<sup>4</sup> Since each of these reoffenders spends an average of 28 months in a correctional facility over this time horizon<sup>5</sup>, this population generates over \$300 million in additional incarceration expenses for the Commonwealth.

Innovative social programs exist that can help these young people move away from criminal involvement. But all too often, these programs are underfunded and subscale. Tight budgets make state governments wary of putting taxpayer dollars at risk for new initiatives, while one-year budget cycles make it difficult to finance long-term, preventative measures. Meanwhile, without good metrics to shine a light on impact performance, other less effective programs continue to soak up a majority of government funding. Within this fiscal environment, Massachusetts offered few successful options for redirecting the lives of youth with high risk factors, such as previous arrests and school truancy, that make them more likely to re-enter the justice system. These young people are in the “deep end” and in desperate need of innovative, scalable and proven social interventions.



Given the intensive nature of Roca’s Intervention Model, it was important that Roca has been preparing itself to scale for the past several years and that the Massachusetts RFR directly aligns with Roca’s Strategic Business Plan.

*“According to the Commonwealth, 55% return to prison one or more times within three years of release, costing the Commonwealth on average \$47,000 per prisoner per year.”*

<sup>4</sup> In preparing the RFR response, Roca and Third Sector relied on information provided by the Commonwealth in both the official Request for Responses as well as answers provided by the Commonwealth to submitted RFR Questions. The Pew Center for the States. 1 in 31: The Long Reach of American Corrections in Massachusetts. (2011). The actual budgetary savings from reducing the number of prisoners could be much lower than \$47,000 because there are fixed costs that could not be eliminated without closing entire facilities.

<sup>5</sup> Department of Youth Services Internal Analysis. Commonwealth of Massachusetts. 2012.



# ROCA AND THIRD SECTOR CAPITAL PARTNERS

## **Roca**

The mission of Chelsea, MA based Roca is to help disengaged, disenfranchised young people move out of violence and poverty. Since its inception in 1988, Roca has helped more than 17,000 young people make positive, profound changes in their lives, creating a nationally acclaimed model of transformational relationships as a vehicle for youth development. Roca has spent nearly seven years looking at evidence-based practices and programs in an effort to more effectively serve their communities' highest risk young men who, without an intervention, face a reality of jail, violence, and poverty. Due to the lack of programs focused specifically on this target population, Roca felt the need to create an effective intervention model that consistently drives this group of young men toward positive outcomes.

With these goals in mind, Roca has developed and operates an Intervention Model designed to help the most high-risk young people break the destructive cycles of poverty, violence and perpetual incarceration. The Intervention Model pushes young people to identify, confront and overcome destructive behaviors and learn the skills needed to re-engage and succeed in society, education, and the economy. Roca's Intervention Model is based on the combined principles of cognitive re-structuring, skills development, motivational interviewing, and transitional employment.

Roca's Intervention Model enables young people to transform their lives and move toward the outcomes of economic independence (successfully keeping a job) and living out of harm's way (with a primary focus of staying out of prison). Building off of Roca's success to date and pulling from evidence-based

practices in behavioral health, criminal justice and workforce development, the Intervention Model includes two years of intensive programming with two additional years of follow up for retention and sustainability.

Roca's High Risk Youth Intervention Model is one possible intervention with success in redirecting "deep end" youth. Like many other nonprofits, Roca was in need of new financial tools that could enable it to increase funding and expand impact. But would Roca be able to scale its successful programs in a sustainable way while also delivering an attractive cost savings proposition for Massachusetts? And how would Roca prepare itself to be a strong and well-prepared candidate for future Pay for Success opportunities?



*“Third Sector is a nonprofit financial advisory firm and intermediary seeking to accelerate America’s transition to a performance driven social sector.”*

### THIRD SECTOR CAPITAL PARTNERS

Soon after the Massachusetts’s Pay for Success and Social Impact Bond (PFS/SIB) procurement was announced in May 2011, Molly Baldwin, the Founder and Executive Director of Roca, met with Third Sector Capital Partners regarding the opportunity. Founded in 2010, Third Sector is a nonprofit financial advisory firm and intermediary seeking to accelerate America’s transition to a performance driven social sector. Third Sector has risen to become a leading practitioner in implementing social innovation financing in the United States. Third Sector provides a variety of advisory and project structuring services for Government, service providers, investors and project intermediaries considering or pursuing PFS, SIB and growth capital initiatives.

Third Sector is actively involved in advancing PFS and other social finance innovations with partners in localities across the United States, including Cuyahoga County, OH, Santa Clara County, CA and the Commonwealth of Massachusetts. “Roca needed help in unpacking the ‘black box’ of the components of Pay for Success and Social Impact Bonds. Service providers will need to pursue opportunities to exchange ideas with outside, impartial organizations about the concept’s potential,” Molly Baldwin commented. “We appreciated Third Sector’s financial and evaluation experience as much as their willingness to learn from Roca’s history and programmatic expertise.” After submitting their RFI, Roca decided to engage with Third Sector more deeply to provide advice and technical assistance to help the organization prepare for an impending request for responses from the Commonwealth.



Roca engages young people where they are in the stages of change cognitively and behaviorally. By applying this evidence-based framework in the program delivery, young people move along a pathway of education, pre-vocational training, life skills, transitional employment and unsubsidized employment opportunities.

# FROM CONCEPT TO PROPOSAL

As experts in the PFS/SIB field, Third Sector would help Roca (a) evaluate the merits of PFS/SIB as it relates to Roca's mission and strategy, (b) analyze Roca's operations, economics, scalability, evidence of impact, financial outlook, and other factors through the lens of a possible PFS/SIB, (c) design an integrated PFS/SIB structure, (d) identify and recruit evaluation experts, funders and other partners into the proposed collaboration, and (e) prepare detailed responses to a Request For Responses (RFR) issued by the Commonwealth.

"This process was instrumental to our understanding of Pay for Success and how it would affect Roca's management and business model moving forward," Baldwin stated. "Their partnership with us produced

Theory of Change process took the nonprofit through an intensive examination that clarified its target population and intended outcomes, as well as identified and integrated the programmatic components and organizational infrastructure necessary to achieve those outcomes. Roca's efforts to implement its Theory of Change led the organization through significant modifications and two more theory of change processes to refine the model and organizational focus (with the last theory of change taking place in October 2011).

"Roca's journey to becoming a high-performing, effective nonprofit started many years ago when it began asking a critical question—Are we helping young people change their lives and how do we know?

*"Dedication to performance-based management had been a key tenet of Roca since its 2005 Theory of Change process, many years before Pay for Success."*

more than an RFR response, it changed the way that we do business and manage our organization to performance."

Roca's journey from concept to concrete PFS/SIB proposal was marked by several success factors. The first ingredient, dedication to performance-based management, had been a key tenant of the Roca organization since its 2005 Theory of Change process, many years before Pay for Success. Roca's

After realizing that, in spite of great dedication and hard work, Roca was not helping young people change behaviors to improve their lives to a significant degree, Roca engaged in a systemic cycle of research, design, action, tracking data, and use of data for continuous improvement to deliver an intervention worthy of the young people we serve."<sup>6</sup>

Since 2005, Roca has further clarified its model and target population, practiced performance-based

<sup>6</sup> Roca's Performance Benchmark and Outcomes Report. 2012. Available at: [www.rocainc.org](http://www.rocainc.org)

management and implemented stage based programming to increase outcomes for the young people it serves. The organization's commitment to young people extended beyond the first site in Chelsea to a new location, Springfield MA, in 2010. Roca's experience with replication in Springfield demonstrated not only a willingness to scale, but also a successful example of implementation through partnership and collaboration without sacrificing organizational commitment to measuring performance. This evidence of an ability to scale while maintaining programmatic fidelity was paramount to support participation in a Pay for Success pilot.

Given its longstanding commitment to performance and successful replication, Roca was well-prepared to take advantage of the Pay for Success opportunity in Massachusetts. However, the Roca team did not understand the nuances of the concept, or fully grasp what participation could mean for the organization. Over the nine months between the Massachusetts Request for Information and Request for Responses, Roca worked with Third Sector to understand the ways that Pay for Success could impact the organization's budget and business model, impact measurement and growth strategies for the future.

Even though Roca staff already had a deep understanding of their economics, the Third Sector team helped them quantify their programmatic cost per success and the trade-offs between expected cash flows from entering into an outcomes-based performance contract versus existing cost-reimbursement government contracts. Third Sector also assisted Roca in exploring how, if successful, the organization could use performance-based

### ROCA'S CRITICAL SUCCESS FACTORS

- Existing dedication to performance-based management and use of data to drive towards outcomes.
- Demonstrated experience with replication to new geographies.
- Commitment to understanding the organization's economics and Pay For Success with Third Sector over nine months between RFI and RFP.
- Use of Pay for Success methodology to strategically change the organization's revenue model.
- An unwavering commitment to improving results for the population served.

payments as a way to make government funding a more significant component of Roca's revenue model. "We might have put in a response without Third Sector," Molly said. "But there is no way we would have understood how to operationalize this financial mechanism without assistance from an outside organization."

*"Since 2005, Roca has further clarified its model and target population, practiced performance-based management and implemented stage based programming to increase outcomes for the young people it serves."*

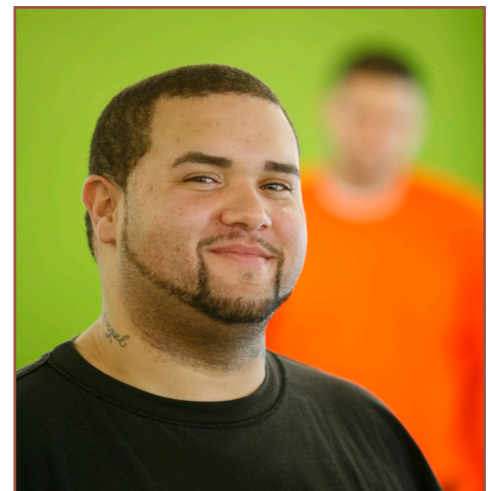
# MASSACHUSETTS REQUEST FOR RESPONSE OVERVIEW

The RFR issued by the State sought service providers that could achieve proven reductions in the rate of incarceration among young people leaving the juvenile corrections system. For four years (flanked by a one year ramp up and one year wrap up) a selected lead contractor would be asked to coordinate and/or deliver services to a target population. The contract would provide no up-front compensation, but for each foregone incarceration achieved, the State estimated that a payment of approximately \$30,000 could be made. To finance the time lag and performance risk inherent to PFS contracting, a potential lead contractor could choose to arrange SIB financing.

building upon evidence-based practices unless the organizations have collaborated in a proven model before. The second is to build upon the programs of one or two particularly strong, evidence-based providers to achieve a contract's outcome metrics. We believe that both approaches can be successful as long as evidence of outcomes and evaluation are equally rigorous." Roca, with its proven model and ability to serve a large target population, is an example of a strong sole provider model of intervention design for social innovation financing.

*"For each foregone incarceration achieved, the State estimated that a payment of approximately \$30,000 could be made."*

Roca's response to the RFR was created in partnership with Third Sector and guided by the eight key criteria outlined in the introduction. These criteria provided valuable organizational and conceptual learning for both Roca and Third Sector, revealing the challenges and complexity of preparing a service provider to participate in this social finance innovation. "There are two fundamental ways to approach feasibility design of these Pay for Success opportunities" George Overholser, Co-Founder and CEO of Third Sector, commented. "The first is a multi-organization, collective action approach, combining several interventions together to try and move the needle against a social goal. In this case, you can harness the power of collective action, but may not be





# ASSESSING ROCA AGAINST EIGHT PFS CRITERIA

## GOVERNMENT LEADERSHIP

Before investing time and effort in the PFS/SIB opportunity, Roca staff, Board and supporters visited with government officials and assessed the political landscape to ensure that the Commonwealth was committed to follow through with what appeared to be a new and complex process. Several observations led them to conclude that the opportunity was indeed a real one: the Governor had expressed his clear support, the Secretary of Administration and Finance had announced his intention to be a major driver, the Boston Globe had covered the story positively on its front page, many of the officials throughout Roca's government network were both aware of and supportive of the initiative, and government officials had demonstrated interest in Roca's key competency area. On this basis, and with Board-level commitment, Roca decided to move forward with exploring and responding to the RFR.

## SOCIAL NEEDS THAT ARE UNMET, HIGH-PRIORITY AND LARGE-SCALE

Roca's next step was to examine the specific social needs the organization addressed, and to affirm that those needs were indeed significant in the larger Commonwealth context. The United States is one of the countries with the highest rate of incarceration per capita in the world - with 2.3 million, or 1 in 100, of its adults behind bars at any given time. States spend over \$51 billion each year on corrections with prisons accounting for the majority of that cost. Over

the past 20 years prison populations have doubled and the average length of incarceration has increased by nine months, or 35%, creating an additional \$10 billion in costs for states.<sup>7</sup> Compared to other states, Massachusetts has a relatively low share of adults in prison or jail, but the 26,000 individuals Massachusetts incarcerates each year results in more than \$500 million in costs.<sup>8</sup>

In 2008, studies by the Pew Center for the States found that it cost \$130.16 per day, on average, to incarcerate an individual in Massachusetts.<sup>9</sup> Based on this figure, a full year of incarceration would cost approximately \$47,500. Assuming an average young person aging out of Massachusetts's Department of Youth Services (DYS) or Probation who is incarcerated as an adult would be sentenced to 12 to 18 months in prison, the twelve to eighteen month incarceration cost for this young person to the Commonwealth would range from \$47,508 to \$71,263. These costs are only those attributed to a first incarceration. The Pew Center for the States further explains that between 2004 and 2007, 42.2% of adults released from incarceration recidivated within three years, meaning that the costs of individuals re-entering the justice system could reach over \$100 million.<sup>10 11</sup>

In the RFR, the Commonwealth projected that 11,000 young people would age out of DYS and Probation in Massachusetts over a four-year period. The RFR also indicated that, in the absence of new interventions, 55% of these young people will be reincarcerated

<sup>7</sup> The Pew Center for the States. Time Served. The High Cost, Low Returns of Longer Prison Terms. (2012).

<sup>8</sup> The Pew Center for the States. 1 in 31: The Long Reach of American Corrections in Massachusetts. (2011).

<sup>9</sup> The Pew Center for the States. 1 in 31: The Long Reach of American Corrections in Massachusetts. (2011).

<sup>10</sup> Pew Center for the States. "State of Recidivism: The Revolving Door of America's Prisons." (April 2011), p. 10.

<sup>11</sup> Of those released from incarceration, 33% were reincarcerated for a new crime and 9% were reincarcerated for a technical violation. It should also be noted that between 1999 and 2007 when the Pew Center for the States conducted this study, recidivism rates in Massachusetts increased by 10.7%. (Source Pew/ASCA Recidivism Survey). The actual budgetary savings from reducing the number of prisoners could be much lower than \$47,500 because there are fixed costs that could not be eliminated without closing entire facilities.



within three years.<sup>12</sup> Since these individuals are aging out of supportive services, there are currently few to no government resources directed at this population, and programs and services are ad hoc and uncoordinated to serve those at highest risk of incarceration.

Roca and Third Sector's counterfactual analysis (see section on Administrative Data) revealed that there would be 1,538 young people that fit Roca's service model and geographic reach with a high-likelihood of recidivating. Should these "deep end" individuals, many with a greater than 55% re-offending rate, recidivate they would create an estimated \$100 million in incarceration costs to Massachusetts.

Roca focuses intensively on these low-income young people who are in the deep end: gang and court involved, school dropouts, and teen parents who are disconnected from social institutions that might

### TARGET POPULATIONS THAT ARE WELL-DEFINED AND CAN BE MEASURED WITH SCIENTIFIC RIGOR

The Massachusetts RFR identified young people "aging-out" of government systems such as Youth Services and Probation as the target population. While this population was reasonably well defined and measureable, Roca and Third Sector concluded that a sharper definition would be required to better identify young people with the greatest need of support services. PFS contracts have the potential for greater success when programmatic efforts and evaluations of impact can be mapped clearly to a specific population.

Since Massachusetts Office of Public Safety (EOPSS) data indicate that young men comprise 95% of the incarcerated population and have higher recidivism rates,<sup>12</sup> Roca suggested further defining the target

*"Should these 'deep end' individuals, many with a greater than 55% re-offending rate, recidivate they would create an estimated \$100 million in incarceration costs to Massachusetts."*

otherwise provide support, protection and pathways to employment. Clearly, if the Commonwealth's goal is to reduce rates of incarceration, and the accompanying costs, this deep-end population is a critical and viable group to target. Based on the estimated \$100 million per year cost of the problem, and on Roca's keen insights into the lives of young people in the deep-end, Roca and Third Sector concluded that the Massachusetts RFR did focus on a significant and challenging social need that could be addressed with Roca's Intervention Model.

population as: young men being discharged from DYS or juvenile probation who demonstrate a strong propensity for violence, crime and/or adult incarceration. Roca proposed to work with DYS and juvenile probation to determine individuals with the highest likelihood of being incarcerated as adults. Specifically Roca proposed a focus on young men with high-end misdemeanor and/or felony charges in their arrest records who fall into a Grid Level 4 or higher as defined by DYS<sup>13</sup>. Roca would also focus on young people convicted at age 16 or older in the adult system, while younger individuals would continue to be served under DYS and juvenile probation.

<sup>12</sup> "Frequently Asked Questions about the DOC". Executive Office of Public Safety and Security. August 2012. Available: <http://www.mass.gov/eopss/agencies/doc/faqs-about-the-doc.html>

<sup>13</sup> MA Department of Youth Services Grid 3 includes charges such as felony B&E and felony larceny. Grid 4 includes charges such as assault and battery with a dangerous weapon, armed robbery, and distributing cocaine. Grid 5 includes charges such as armed assault and robbery and attempted murder. Grid 6 includes home invasion and murder. Depending on the number of young people projected to be in each level, Roca may include those with Grid Level 3 offenses as well.

## Social Innovation Financing Case Study: Preparing for Pay for Success Opportunities

Note: this focus has been designed to serve those most at risk of re-incarceration. Those at less risk of incarceration would not receive the intervention as part of the proposed project.

Roca proposed to coordinate services for the highest risk young men who are aging out based on DYS or Juvenile Probation regulations. Roca would also work with young men who are charged as youthful offenders, and age out at 21; however, in working with this group Roca would seek to begin developing relationships pre-discharge.

Another recommendation was the need to exclude certain young people from what would be defined as the target population. For example, among aged-out youth, Roca is not able to serve sex offenders, arsonists, and individuals with mental health issues that make them unable to respond to cognitive-behavioral interventions. A workable PFS contract would need to be able to exclude these individuals from analyses of impact.

This highly defined target population falls directly in line with Roca's overall service population. Roca's Intervention Model focused on 17-24 year old men in crisis and on the streets, particularly those involved



Roca focuses intensively on these low-income young people who are in the deep end: gang and court involved, school dropouts, and teen parents who are disconnected from social institutions that might otherwise provide support, protection and pathways to employment.

*“PFS contracts have the potential for greater success when programmatic efforts and evaluations of impact can be mapped clearly to a specific population.”*

with Massachusetts’s criminal justice system. Roca chooses to focus on this group because it is the group that has most often been underserved or neglected by public and private institutions, with the exception of the criminal justice system, and is the group responsible for the majority of violence in Massachusetts’ cities.

To maximize focus, Roca used its RFR response to recommend that the Commonwealth employ the “risk principle”. According to the Crime and Justice Institute, “the risk principle identifies who to target for the most intensive of services and programming. Specifically, limited resources should be directed to those at highest risk for involvement in the criminal justice system. Further, higher risk clients should receive the greatest dosage of treatment and intervention. This principle is of critical importance given the serious constraints of limited budgets and working with growing community supervision and prison and jail populations.”<sup>14</sup> Interventions that focus on a population that has a high likelihood of re-offending, being convicted of more serious offenses and returning to prison multiple times have the potential to generate more significant cost savings if total incarceration days for this group can be reduced. For lower risk groups, convictions are less serious, result in less incarceration time, and therefore less savings to Government if those types of incarcerations are reduced. As outlined earlier, the

### WHAT IS A COUNTERFACTUAL?

Governments should pay for programs that actually improve lives, and not for results that would have happened anyway.

To measure true impact, an evaluation design is developed which is able to discern the effect of the program when compared to what would have happened in the absence of the intervention. This is often called a “counterfactual” because it considers whether or not, in the case of a juvenile justice program, those treated would actually commit a crime if they had not participated in the program.

Counterfactuals are also key to help identify “deep end” youth most in need of services versus those who would succeed without outside assistance.

<sup>14</sup> Bechtel, Kristin and Barbara A. Pierce, MPPM. “An Overview of What Works in Correctional Interventions.” Crime and Justice Institute (January 2011).

cost savings in reducing the amount of more serious sentences could be between \$47,508 to \$71,263 per incarcerated individual over a twelve to eighteen month period.

Multiple studies and meta-analyses<sup>15</sup> have repeatedly shown that programming that focuses on lower risk individuals or mixes high and low risk groups actually increases rates of recidivism for the lower risk client.<sup>16</sup> Programs that adhered to the risk principle were able to reduce recidivism by 19 percent, whereas programming that served mixed risk groups had a



Roca and Third Sector proposed serving three targeted geographic areas which would result in Roca reaching 42% of the total population of young people aging out of DYS and/or juvenile probation.

<sup>15</sup> A meta-analysis is a summary of existing studies. The finding from a meta-analysis is commonly referred to as the treatment effect and is often presented as a correlation. Larger and positive correlations suggest that a better outcome was produced by the program or intervention being evaluated.

<sup>16</sup> Andrews, D.A. Zinger, I. Hoge, R.D., Bonta, J., Gendreau, P., & Cullen, F.T. (1990). Does correctional treatment work? A clinically relevant and psychologically informed meta-analysis. *Criminology*, 8, 369-404; Andrews, D.A. & Dowden, C. (1999). A meta-analytic investigation into effective correctional intervention for female offenders. *Forum on Corrections Research*, 11, 18-21.; Dowden, C. & Andrews, D.A. (1999a). What works for female offenders: A meta-analytic review. *Crime and Delinquency*, 45, 438-45; Dowden, C. & Andrews, D.A. (1999b). What works in young offender treatment: A meta-analysis. *Forum on Corrections Research*, 11, 21-24; Dowden, C. & Andrews, D.A. (1999a). What works for female offenders: A meta-analytic review. *Crime and Delinquency*, 45, 438-452; Dowden, C. & Andrews, D.A. (1999b). What works in young offender treatment: A meta-analysis. *Forum on Corrections Research*, 11, 21-24; Lipsey, M.W. & Wilson, D.B. (1998). Effective intervention for serious juvenile offenders: A synthesis of research. In R. Loeber & D. Farrington (Eds.), *Serious and Violent Juvenile Offenders: Risk Factors and Successful Interventions*. Thousand Oaks, CA: Sage; Lowenkamp, C.T., Latessa, E.J., & Holsinger, A. (2006). The risk principle in action: What have we learned from 13,676 offenders and 97 correctional programs? *Crime and Delinquency*, 52, 77-93; Lowenkamp, C.T. & Latessa, E.J. (2005). Increasing the effectiveness of correctional programming through the risk principle: Identifying offenders for residential placement. *Criminology & Public Policy*, 4, 263-290; Lowenkamp, C., Smith, P., & Bechtel, K. (2007) "Reducing the harm: Identifying appropriate programming for the low risk offender." *Corrections Today*, December, 50-52; and, Latessa, E., Lowenkamp, C., Bechtel, K. (2008) "Community Corrections Centers, Parolees, and Recidivism: An Investigation into the Characteristics of Effective Reentry Programs in Pennsylvania."

<sup>17</sup> Lowenkamp, C.T. & Latessa, E.J. (2005). Increasing the effectiveness of correctional programming through the risk principle: Identifying offenders for residential placement. *Criminology & Public Policy*, 4, 263-290.



four percent increase in recidivism. Findings from a large halfway house study conducted in Ohio suggest that intensive programming for higher risk offenders decreased recidivism by 10 to 30 percent. Yet, these same programs consistently increased recidivism for the lower risk offenders while also being much more costly to provide.<sup>17</sup>

To help confirm that the targeting could work from a practical standpoint, Roca conducted meetings with various long-standing partners<sup>18</sup> and was able to compile a zip-code level count of young people aging out of the Department of Youth Services and Probation. These counts were overlaid onto Roca's geographical service area to confirm there was a strong degree of overlap in service delivery capacity. In other words, Roca was looking to ensure that the geographic areas it proposed to serve would address at least 40% of the young people aging out across the Commonwealth. At the same time, it became

clear that adding an additional site in Boston may strengthen Roca's ability to serve more young people and deliver against the RFR goals, in this or another Massachusetts geography.

Using information from DYS included in the RFR, Roca and Third Sector proposed serving three targeted geographic areas which would result in Roca reaching 42% of the total population of young people aging out of DYS and/or juvenile probation. The targeted municipalities (Chelsea, Boston and Springfield, MA) were selected because they reflected some of the most heavily impacted communities across the Commonwealth, and, at the same time, would allow for Roca's place-based model to be implemented with fidelity (i.e., all young people could effectively engage in programming in one of Roca's three proposed facilities). With the target population and locations defined, the next step became understanding how a population would be referred to the program and how outcomes would be tracked using existing government administrative data.

### THE 'CREAMING' PROBLEM

Issues of "creaming," the act of serving individuals who are less likely to commit crimes and are therefore easier to serve, can be dealt with effectively by using an "intent to treat" experimental frame. For example, Roca and Third Sector proposed that Roca's impact be evaluated based on the incarceration outcomes for all high-propensity youth in Roca's service area, including youth that were not enrolled into Roca's program. Exhibit 2 on p.19 traces hypothetical outcomes for the entire population of aged out young people, over a four-year period, and illustrates the underpinnings of a possible "intent to treat" evaluation design.

### PROVEN OUTCOMES FROM ADMINISTRATIVE DATA THAT IS CREDIBLE AND READILY AVAILABLE IN A COST EFFECTIVE MEANS

In the RFR, the Commonwealth required that responders:

"Propose appropriate metrics for assessing the success of the program model and describe how the necessary data could be acquired... The State will work with the intermediary and service providers to select appropriate performance metrics. Data on arraignments, convictions, and incarceration spells are all potentially available."

In its response, Roca recommended that incarceration, arrest, pre-conviction and sentencing

<sup>18</sup> Roca is committed to shifting the trajectories of not only our young people, but of all the institutions in a young person's life—schools, local government, agencies and organizations—which are just as influential to the needs and growth of a young person as Roca. Recognizing this, Roca has created partnerships with these institutions, opened the lines of communication, and each benefits from the other's expertise. This can be seen through evolving and developing partnerships which include the cities of Chelsea, Revere, Boston, and Springfield; Hamden County Sheriff's Department in Springfield, MA; Chelsea, Revere, and Springfield Police Departments; Chelsea Public Schools; The Federal District Court, Chelsea District Court and the Department of Probation; Massachusetts General Hospital / Roca health clinic; and more than 70 area employers.

outcomes for success payments be tracked using government administrative data from the DYS and Probation systems. These data systems were selected because they were credible, readily accessible, relatively standardized and cost effective. In addition, these systems allowed for historical look backs that could help define outcomes that would occur without the program. The use of administrative data rather than customized field surveys could greatly reduce the expense of conducting impact evaluations<sup>19</sup>, and it would make it possible to measure impact for all young people in the target population (not just those enrolled in Roca), on an ongoing basis.

Roca and Third Sector also proposed creating a secondary PFS metric tied to workforce participation. It was not clear from the RFR, however, whether the Commonwealth would be willing to offer PFS

With the help of Third Sector, Roca contracted with Chapin Hall to provide expertise in evaluation designs that leverage administrative data as part of an independent program evaluation. Chapin Hall, at the University of Chicago, is a leader in developing performance-based contracts for youth services nationwide.<sup>20</sup> Roca's work with Chapin Hall has focused on a growth and learning agenda with a specific emphasis on helping Roca demonstrate its Intervention Model as an evidence-based intervention. Together, Third Sector, Roca and Chapin Hall analyzed Roca's historical program data to develop an understanding of Roca's impact and then used that as a guide for navigating what happens to individuals not involved in the program.

The RFR required responders to suggest "a rigorous approach to establishing a credible counterfactual."

*"Roca's Intervention Model is based on the implementation of a combination of evidence-based practices and has been touted as a national best practice by many Governments, advocates and service providers."*

rewards for improvements in employment among the juvenile justice population. Roca believes that the surest way to keep a young adult out of prison is sustainable employment that puts them on a path to self-sufficiency. Roca partners with corporations and other employers to ensure full-time placement upon graduation from transitional employment. If agreed to as a success benchmark in the PFS benchmark, of the 66% who are projected to complete the two year intensive component of the model, Roca would commit to placing 75% in sustained employment. This additional metric was proposed by Roca because of their belief that it would strengthen outcomes for all parties.

Rigorous evaluations are indeed essential to a successful PFS contract structure. Governments need to pay for programs that actually improve lives, and not for results that would have happened anyway. To truly measure impact, the evaluation design must be able to discern the effect of the program when compared to counterfactuals, or what would have happened in the absence of the intervention.

Roca and Third Sector proposed that the evaluation methodology should employ models that rely on available administrative data to identify the specific young people who are most likely to be incarcerated. If Roca's program could be targeted towards young people with a high counterfactual propensity for incarceration (a high likelihood of going to jail), its

<sup>19</sup> "Rigorous Program Evaluations on a Budget: How Low-Cost Randomized Controlled Trials Are Possible in Many Areas of Social Policy." Coalition for Evidence-Based Policy. March 2012. Available at: <http://coalition4evidence.org/wordpress/wp-content/uploads/Rigorous-Program-Evaluations-on-a-Budget-March-2012.pdf>

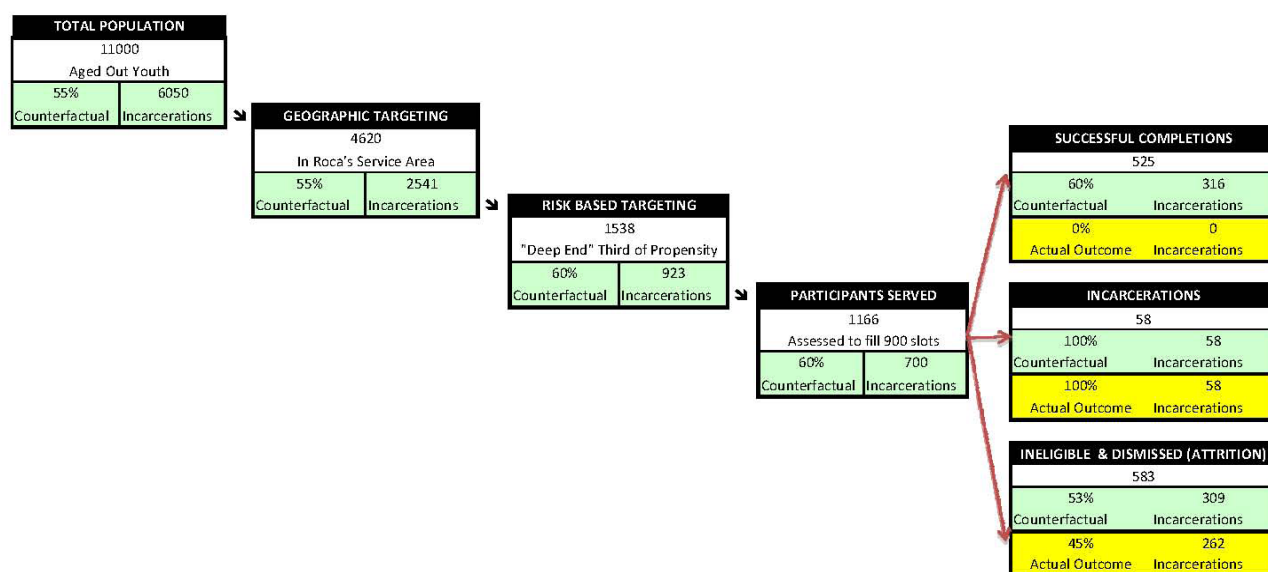
<sup>20</sup> For more information on Chapin Hall, please visit [www.chapinhall.org](http://www.chapinhall.org).



programmatic efforts will be more likely to bring about a measureable reduction in incarcerations. Variables such as gender and severity of prior justice involvement could be used to identify a sub-population that is significantly more likely to become incarcerated than the overall aging out population. Confident that a robust means of incorporating counterfactuals into the PFS measures of impact

the risks can be developed. Detecting change involves establishing baseline utilization using historical data for comparison with data from the program. At scale, a comparison can be used to detect whether the amount of jail used by residents within a community has changed relative to past patterns. The statistical properties of these baseline/target/actual

*Exhibit 2: Constructing a Counterfactual to Estimate Potential Population for Roca*



could be devised, Roca and Third Sector proposed three approaches to establishing a counterfactual in the RFR response. Each approach would be similarly cost-effective given the use of administrative data for the analysis. Additionally, these approaches are not mutually exclusive; one could design a program that integrates one, two, or all three approaches.

1. The first counterfactual approach involves a self-to-self comparison. Self-to-self counterfactual can be referred to as the historical comparison. It is an unfortunate fact that jail use tends to cluster in certain areas. Changing utilization in these hot spots can have significant public health level benefits which go beyond incarceration to reduced policing costs and increased community safety if programs large enough to counteract

models are robust enough to detect meaningful change in what is often called a 'difference-in-difference' framework.

2. The second approach to constructing a counterfactual involves a similar strategy except that the counterfactual is constructed from comparison sites that resemble the target site, with both sets of sites operating at the same time. This is a cross-site counterfactual. The fact that the sites are operating simultaneously means that any unique effects of when the program is operating (e.g., economic downturns) generally affects both sites. Sites can be randomized using cluster-randomized designs to achieve an even more robust design. Cross-site and historical counterfactuals can be combined

to answer whether the rates of change in the utilization of jails proceeded in a comparable manner. Again, there are a variety of ways to test the significance of the effects including a difference-in-difference approach.

3. Finally, the counterfactual can be constructed using random assignment. Random assignment is a practice in experimental design where participants have equal likelihood of being assigned to the group receiving the intervention or the non-intervention group. Random assignment can occur at the individual level, the neighborhood/cluster level, or both. Randomization of individuals already identified as deep-end can also be used in conjunction with the other approaches. Roca did voice concern that random assignment would mean denying care to individuals in need. With this concern in mind, Roca and Third Sector recognized that

any approach to constructing a counterfactual would likely be a blend of the three different approaches.

Exhibit 2, included in the RFR response, illustrates that there are 11,000 young people that the State projects will age out of DYS and Probation in Massachusetts over a four-year period. Roca and Third Sector assumed that, based on the information included in the RFR, in the absence of a new intervention, 55% of those young people would be incarcerated within 2 years. Thus, at the Massachusetts population level, the counterfactual is 6,050 incarcerations.

Using DYS data to analyze the cities within Roca's implementation area, the geographic targeting box illustrates the number of young people estimated to be aging out in Roca's service area. This covers 42% -- 4,620 -- of the youth that will age out. With no additional data to suggest otherwise, Roca and Third

*Exhibit 3: Participants Served in Basic Transitional Employment*

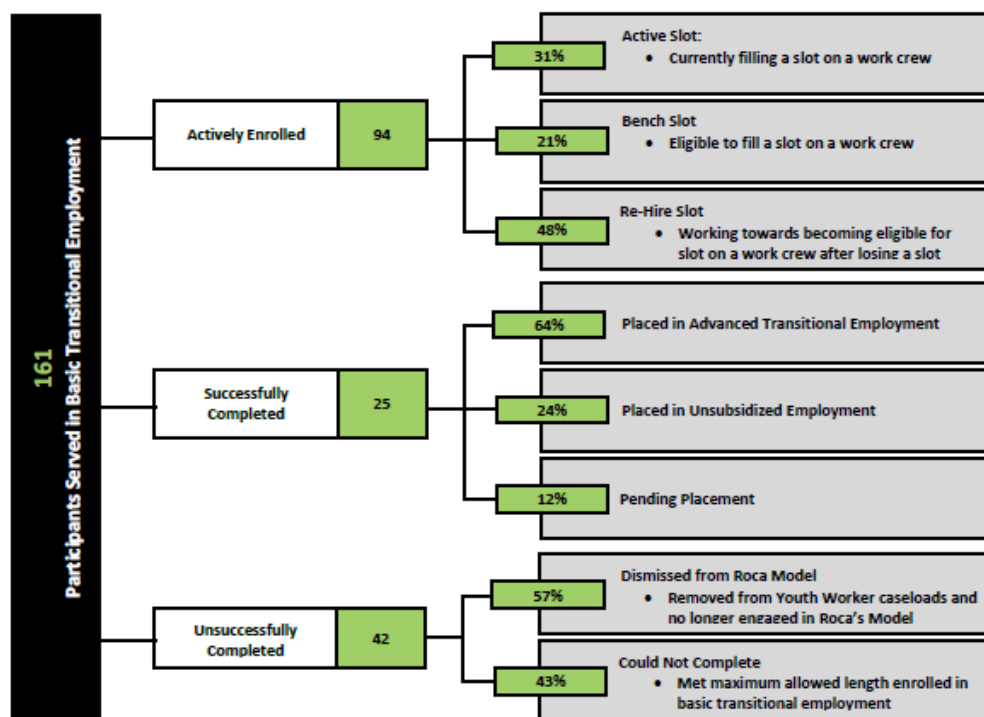
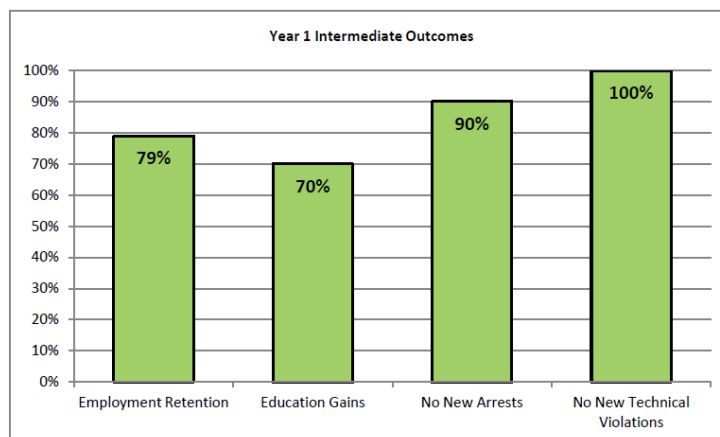


Exhibit 4: Roca Intermediate Outcomes



Sector assumed that these youth have the same likelihood of being incarcerated as those that are not in Roca's service area.

Roca and Third Sector then focused further on the highest risk young people by asserting that a model might be constructed, based on historical administrative data, which predicts a likelihood of being incarcerated for each youth on the list of 4,620 in Roca's service area. It was assumed that the model would be powerful enough to identify the one-third of this population (1,538 youth) that has a 60% average (counterfactual) likelihood of being incarcerated within two years.

The chart illustrates those young people who are successfully recruited into the program and assessed to fill a proposed 900 programming slots across four years of enrollments. In the absence of data to suggest otherwise, Roca and Third Sector assumed similar 60% counterfactual propensities for this group as well. (Roca management believed that their intake system would actually result in a served population that has a higher than 60% counterfactual propensity).<sup>21</sup>

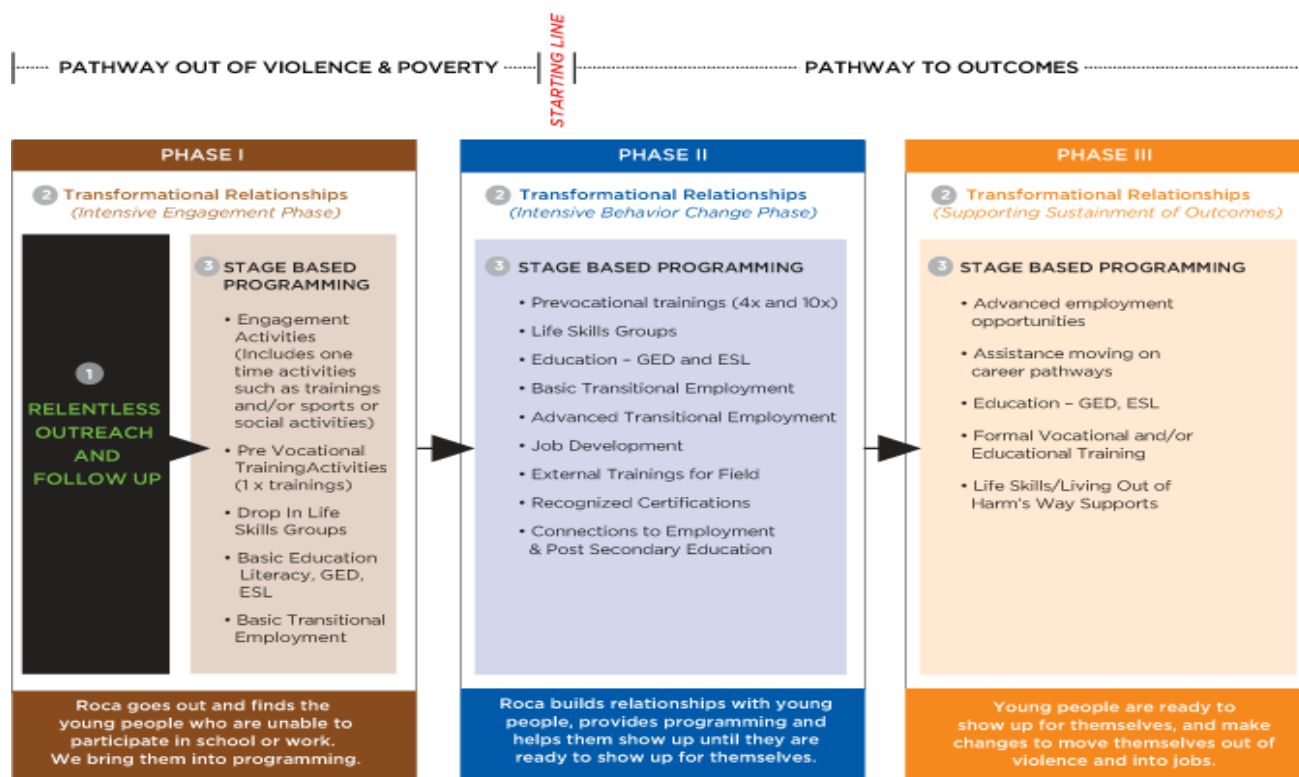
Lastly, the three boxes to the right of the chart illustrate (in yellow) what actually happens due to Roca's intervention: Among those who stay in the program,

none go to jail, although 316 would have gone. This is because in order remain in as a participant in the program the individual cannot be incarcerated. Among those who attrite, an estimated 262 go to jail, although 309 would have gone in absence of the intervention. This is the projected "Roca effect" of having a participant partially complete the program. In other words, based on a 60% counterfactual, this graphic illustrates a possible impact of 360 foregone incarcerations among individuals ( $309 - 262 = 47 + 316 = 363$ ) successfully recruited into the program.

By creating a statistical model that could use data such as gender and prior arrest records to predict each young person's likelihood of becoming incarcerated in the future, Roca proposed a critical tool needed to take a step towards a more targetable and measurable population. With this risk assessment model in place, it would be possible to identify and assign specific deep end young people to Roca's program in a scientific way that would lend itself well to impact evaluation. Essentially, this was a way to ensure that Roca's efforts to reduce incarcerations would not be diluted by serving young people who were not likely to become incarcerated. Roca's efforts would also be more cost-effective, as serving the deep end group means the intervention needed to serve just two individuals to ensure a success payment, versus 3, 4 or more if the counterfactual was lower.

<sup>21</sup> Wulczyn, F. (2007). Monitoring Child Welfare Programs: Performance Improvement in a CQI Context. Chapin Hall at the University of Chicago: Chicago, IL.

Exhibit 5: Roca's Intervention Model



Several meetings with government officials and data experts were required to assess the current state of the Commonwealth's administrative data. With the help of these experts, Roca and Third Sector concluded that the data indeed exists. In its RFR response, Roca and Third Sector stressed the importance of the development of risk assessment models as a necessary pre-condition to successful PFS contracting.

### AN INTERVENTION THAT WAS LIKELY TO WORK

Roca has interwoven two decades of experiential knowledge, internal evaluations, and evidence-based

practices from cognitive-behavioral therapy to solidify a program into what is referred to as the High-Risk Youth Intervention Model. This model provides two years of intensive programming and two years of follow-up. The intervention relies on intensive relationships between adults and high-risk youth, as well as targeted programming (i.e., life skills, education, and employment). Young people develop the necessary skills to reduce violence and create positive behavioral changes, which contribute to reductions in incarcerations and increased job placement and retention. The model has four key attributes:

*“The core of Roca’s High-Risk Youth Intervention Model is the Transformational Relationship (TR). This relationship is not a friendship—it is more profound—effectively intentional, and mutually respectful.”*

**1. Relentless Outreach And Follow Up:** Youth workers build relationships by finding young people where they are, learning where they hang out, knocking on their doors, and continuously circling the neighborhood in the infamous Roca vans. It is the relentlessness of a youth worker who shows up day after day, no matter what, that awakens hope in a young person. A youth worker must relentlessly reconnect with a young person who periodically rejects them and refuses to engage in programming. This pattern is crucial to the process and must happen continuously throughout the relationship. While a young person may show up at Roca three times in one week, they may just as likely refuse to come back the following week. It is the youth worker's responsibility to track down that young person and reengage him.

**2. Transformational Relationships (Intensive Case Management):** Roca knows that when a young person is re-engaged through positive and intensive relationships, he can go on to gain competencies in life skills, education and employment. Therefore, at the core of the High-Risk Youth Intervention Model is the Transformational Relationship (TR). Their relationship is not a friendship—it is more profound—effectively intentional, and mutually respectful. Youth workers are trained in motivational interviewing and cognitive behavioral strategies preparing them to use their self effectively to guide and support young people.

**3. Stage-Based Programming:** Roca engages young people where they are in the stages of change cognitively and behaviorally.<sup>22</sup> By applying this evidence-based framework in the program delivery, young people move along a pathway of education, pre-vocational training, life skills, transitional employment

and unsubsidized employment opportunities. By matching programming to a young person's stage of change, instead of placing all young people into a one-size-fits-all curriculum, Roca is driving this population, who will not move in a straight trajectory, toward positive outcomes.

**4. Work With Engaged Institutional Partners:** The institutions that are in a young person's life—schools, local government, agencies, and organizations—are just as influential to the needs and growth of a young person as Roca. Roca's integrated delivery model establishes open lines of communication and benefits from the expertise of partner organizations.

Roca's Intervention Model is based on the implementation of a combination of evidence-based practices and has been touted as a national best practice by many Governments, advocates and service providers. Given the intensive nature of Roca's Intervention Model, it was important that Roca has been preparing itself to scale for the past several years and the Massachusetts RFR directly aligns with Roca's Strategic Business Plan. Through this business plan, Roca proposes to focus the continued delivery of its Intervention Model to address the needs of 17-24 year old young men who demonstrate a strong propensity for violence, crime and/or adult incarceration, who are either: 1) aging out of the juvenile justice or juvenile probation systems; 2) connected with the adult justice system; or, 3) are high risk youth from the community being served. Roca is in an early-stage growth for impact that meets the criteria of "organizations that have demonstrated a significant level of effectiveness and are increasing their capacity for scale."<sup>23</sup> A Pay for Success program was viewed as an opportunity for Roca to scale sustainably its intervention to new geographies.

<sup>22</sup> Roca has taken Prochaska's stages of change and adapted them for a very high-risk youth development model. Backed by evidence from multiple disciplines (e.g. substance abuse, medicine, harm reduction, etc.), promoting young people through the stages of change allows them to develop the intrinsic skills, desires, and capacities to successfully move towards safety and self-sufficiency.

<sup>23</sup> As defined by the Social Impact Exchange and found at [http://www.socialimpactexchange.org/bpc\\_overview.cfm](http://www.socialimpactexchange.org/bpc_overview.cfm), organizations prepared for early stage growth: 1) offer a clear understanding of key program elements and processes required for scaling; 2) have piloted in at least one site for a minimum of one year; 3) have collected data [inputs, activities, outputs] and documented early results indicating effectiveness and the potential for impact at scale, using data from the actual implementation, not general research data that states a certain method works; and 4) have a well defined strategy for further expansion.

### PROVEN SERVICE PROVIDERS THAT ARE PREPARED TO SCALE WITH QUALITY

Although Roca's program design was clearly well suited to the goals of the Massachusetts RFR, it was nevertheless important to demonstrate that Roca was fully capable of scaling and executing the proposed program design in a way that achieved impact. As mentioned in the previous section, Roca was well

prepared to scale. The organization had a clear understanding of how key program elements would need to scale, had piloted in a site for at least a year, had collected data to document program efficacy and had a well defined strategy, as part of Roca's Strategic Business Plan, outlining expansion. Roca shared the following data from FY12 Performance Indicators and Outcomes for the primary target of 17-24 year old high risk young men involved in the criminal justice system as evidence of program impact specific to the target population proposed in the RFR.<sup>24</sup>

#### ROCA HIGHLIGHTS

##### Of the 409 young men served in Roca's Intervention Model:

- 298 remain actively engaged.
- 111 were dismissed.
- 80% of all participants were engaged in stage based programming.
- 172 unduplicated participants were served in Transitional Employment.
- 161 were served in Basic Transitional Employment.
  - Of those who successfully completed Basic Transitional Employment, 86% have retained employment.
- 31 were served in Advance Transitional Employment.
  - Of those who successfully completed Advanced Transitional Employment, 75% have retained employment.
- 67% of young people placed in unsubsidized employment in FY12 were still working at the end of the fiscal year.
- 73% had no new arrests.
- 67% had no new technical violations.

##### Of the 409 young men served:

- 178 had been enrolled prior to FY12.
- 231 were new enrollments in FY12.

##### Of the 409 young men served in Roca's Intervention Model:

- 298 remain actively engaged.
- 111 were dismissed.

The ultimate impact of Roca's Intervention Model is also assessed by examining how well program participants do once they are no longer engaged through the intensive parts of the model (Phase 1 & Phase 2). While in Phase 3, young people are supported in their ongoing development and to participate in formal certifications, educational programming as needed, job retention support and replacement as needed, and support for long-term goal planning and career development.

##### In FY12, 39 primary population participants graduated to a Phase 3:<sup>25</sup>

- 79% were retaining unsubsidized employment placements.
- 70% had continued educational gains.
- 90% had no new arrests.
- 100% had no new technical violations.

<sup>24</sup> 2012 Roca Outcomes Report.

<sup>25</sup> 2012 Roca Outcomes Report.



### Most importantly for the PFS contract:

- Only 14% of those who had originally enrolled into the four-year program had become incarcerated within four years.
- This compared favorably with the State's estimated 55% counterfactual probability of incarceration, had these young people not enrolled into Roca.

There was also a need to demonstrate that Roca and its intermediary partners were proven in their ability to raise the SIB capital that would be needed to finance the PFS contract. In their RFR responses, all three organizations (Roca and intermediary partners Third Sector and New Profit Inc.) were able to document prior results of having raised capital that was well in excess of the approximately \$10 million that would be required. New Profit, a venture philanthropy and portfolio organization based in Cambridge, MA, had raised over \$120 million to invest in high-performing nonprofits. And two members of the Third Sector team had helped raise over \$320 million in growth capital for nonprofits while working at Nonprofit Finance Fund Capital Partners.

### SAFEGUARDS TO PROTECT THE WELL-BEING OF POPULATIONS SERVED

A critical benefit of PFS contracting is its focus on outcomes and thus its movement away from contract terms that specify the programmatic design that service providers must follow. On the other hand, Government must nevertheless continue to ensure safeguards for the target population, and that services are not withheld.

For twenty-five years, Roca has partnered closely with government officials in the Justice and Health and Human Services departments to implement strict monitoring and accountabilities designed to ensure the safety of the young people they serve. Roca has clearly identified processes and protocols for intervening in and managing crises and critical incidents internally and externally (flow charts,

protocols, processes) covering fights, weapons, injuries, etc. As part of this protocol, Roca has young people sign safety contracts that clearly define what is not allowable in the building in order to maintain a safe space for everyone and the consequences that could occur if the contract is not followed. All of these elements made Roca well positioned to provide sufficient and institutionalized programmatic safeguards.

In addition, Roca and Third Sector proposed that the data collection plan and evaluation design go before an Institutional Review Board (IRB). Because the RFR contemplated changing a public benefit program, the IRB would provide oversight so that everyone understands the ethical obligations in clinical settings. In addition, the real-time monitoring proposal would provide enough feedback to know whether, as a result of the program, risk to the served population is increasing rather than decreasing as intended. Should that happen, program developers face an informed choice regarding whether to continue moving forward.

### COST EFFECTIVE PROGRAMS THAT CAN DEMONSTRATE FISCAL SAVINGS FOR GOVERNMENT

In the Massachusetts RFR, the State made it clear that it would not pursue PFS contracting unless fiscal savings in the costs of incarceration would equal or outweigh the fiscal expense of paying out PFS rewards. Then, as guidance to responders, it expressed willingness by Government to pay \$30,000 for each two-year period of foregone incarcerations that could be achieved among the target population. This presented a challenge to Roca and its intermediary partners, as the partnership estimated the cost to serve each Roca enrollee amounts to almost \$20,400, cumulatively, across a four-year intervention. Thus, the only way Roca would be able to recoup its expenses from a \$30,000 PFS payment per avoided incarceration would be if almost every young person they served resulted in a forgone incarceration. More specifically, this would require that:

- a) Almost every young person in the target population was destined to become incarcerated in the absence of a Roca intervention (a higher than 55% counterfactual)
- b) The program would have an almost 100% success rate in helping young people avoid incarceration

Roca and Third Sector concluded quickly that an alternative approach would need to be proposed. Their insight was that Roca's program was designed to produce four-year (not two-year) periods of non-incarceration. On that basis, they suggested that the Commonwealth should be able to afford a PFS success payment of \$50,000 rather than \$30,000 as

they would be measuring success over twice the time frame.

They then conducted detailed research and analysis to become satisfied that a \$50,000 success payment, combined with their anticipated rate of programmatic success, and adding the full costs of the intermediary partnership and SIB financing expense, would be enough to cover the full cost of the intervention for all individuals served, whether ultimately successful or not.



While in Phase 3, young people are supported in their ongoing development and to participate in formal certifications, educational programming as needed, job retention support and replacement as needed, and support for long-term goal planning and career development.

# PROGRAM DESIGN AND KEY ASSUMPTIONS

## PROGRAM DESIGN & KEY ASSUMPTIONS

Much of Roca and Third Sector's work together focused on identifying and solidifying the program design and key assumptions that would inform the project's financial structure and feasibility. The assumptions would become the central starting points for negotiations with the State and investors and therefore required significant attention. The RFR response outlined the following design assumptions:

- **Target Population:** "High-risk" youth, ages 17 to 24. Select individuals with the highest propensity to become incarcerated as demonstrated by established assessment tools.
- **Counterfactual:** Among the targeted population, a 60% counterfactual likelihood of becoming incarcerated within four years was assumed.
- **Cohort Size:** 900 individuals.
- **Program Period:** Six years (four years of service delivery and two years follow-on evaluation).
- **Targeted Outcome:** Program participants avoid recidivism for 48 continuous months after being released from the juvenile justice system. A recommendation was made to consider using "bed days of incarceration" as an alternative metric.

- **Government Success Payments:** \$50,000 paid per foregone incarceration, defined as two years out of prison post-aging out. Payments would begin two years after initiation of program delivery, which was estimated to be the time that impact could be detected between incarcerations expected and those actually observed in the Roca population. This payment level would have the potential to generate \$18 million in Pay for Success payments.

## SOCIAL INNOVATION FINANCING & REPAYMENT

Roca and Third Sector evaluated a variety of financing options to see which had the best potential to support a successful program while also being realistic and feasible for project partners. It is important to remember that there are a myriad of ways to finance PFS using different combinations of investors, both philanthropic and return-seeking.

In fact, one of the major draws of social innovation financing is its potential to attract dollars from mainstream capital markets, as evidenced by the recent New York City social impact bond project financed with a \$9.6M loan by Goldman Sachs, in partnership with the Bloomberg Foundation.<sup>26</sup> If the programs succeed in reducing recidivism by 10% or more, Goldman stands to earn profits of as much as \$2.1M after eight years. The Bloomberg Foundation provided \$7.2M in loan guarantee (also referred to as credit enhancement) for Goldman Sachs to limit the bank's investment risk on its \$9.6M loan.<sup>27</sup>

<sup>26</sup> For more information about the New York City Social Impact Bond, please visit the Nonprofit Finance Fund's Learning Hub at: <http://payforsuccess.org/>. New York Times announcement available at: <http://www.nytimes.com/2012/08/02/nyregion/goldman-to-invest-in-new-york-city-jail-program.html>

For the purposes of the RFR response to the Commonwealth, Roca and Third Sector projected that the total financing required for this project would be between \$15-\$20 million. Roca and Third Sector expected that the structure would be revised and changed during negotiations with the State and investors.

Since there is not a “one-size-fits-all” approach to financing PFS, Roca and Third Sector proposed a structure that would allow for flexibility during contract negotiations as well as include a diverse set of investors with differing levels of capacity, risk tolerance, and return on capital requirements.

### OUTCOME SUMMARY

- Out of those served via the PFS, the initiative anticipates reducing the number of young people that become incarcerated from 540 expected incarcerations to 180 actual incarcerations.
- Under a \$50,000 payment per foregone incarceration plan, total government PFS payments are \$18 million. Payments are made in years three to six of the six year project period.
- Potential net savings for Massachusetts (after reimbursing under the PFS payments) range between \$9.4 million- \$23.4 million costs and performance outcomes.<sup>28</sup>

- **First Tranche:** SIB investors provide initial working capital to cover feasibility stage work and cash requirements for the first several years of operations. This tranche of investors would experience a 100% return of capital, plus a 2-4% risk premium, through net PFS payments (after service delivery costs are paid) and would be the first tranche to be reimbursed.

- **Second Tranche:** Additional investment from philanthropic grant capital is used to provide funding for the early years of program operations. This tranche is composed of recoverable grants that would experience a 100% return of capital, but no risk premium, through net PFS payments (after service delivery costs are paid). In addition, this tranche would be “second loss”, only to be re-paid after return seeking SIB investors received PFS payments.
- **Third Tranche:** Additional investment in the form of non-recoverable philanthropic grant capital that would serve as “first loss” capital, or capital to re-pay return-seeking investors in the event that the project did not achieve anticipated outcomes.
- **Government PFS Payments:** PFS payments would commence in year three – only if outcomes are achieved. These payments would be used to fund service delivery costs as well as reimburse investors as necessary.

### POTENTIAL OUTCOME SUMMARY

#### BASED ON RFR PROPOSAL

- Out of those served via the PFS, the initiative anticipates reducing the number of young people that become incarcerated from 540 expected incarcerations to 180 actual incarcerations.
- Under a \$50,000 payment per foregone incarceration plan, total government PFS payments would be \$18.0 million. Payments are made in years three to six of the six year project period.
- Potential net savings for Massachusetts (after reimbursing under the PFS payments) range between \$9.4 - \$23.4 million over the six-year project based on historical costs and performance outcomes.

<sup>27</sup> “I’ll put \$2.4 Million on Recidivism to Fall”. The Economist August 6, 2012. Available at: <http://www.economist.com/blogs/democracyinamerica/2012/08/social-impact-bonds>

<sup>28</sup> Based on avoided per diem costs for twelve month and eighteen month incarceration periods. Cost per day derived from The Pew Center for the States. 1 in 31: The Long Reach of American Corrections in Massachusetts. (2011).

# SERVICE PROVIDER ENGAGEMENT WITH PAY FOR SUCCESS

On August 1, 2012, Roca was selected as lead service provider for the Massachusetts juvenile justice project, and Third Sector, in partnership with New Profit Inc., was selected as lead intermediary. Since the announcement, Roca and Third Sector have begun negotiations with the State to revise and finalize terms and conditions of the contract, including the target population, outcome metrics and success payments, and financing requirements.

As Pay for Success continues to gain momentum across the country, service providers will need to understand that accessing the PFS opportunity is only possible by thorough, thoughtful and dedicated feasibility work. Third Sector Capital Partners' technical assistance work with Roca reveals the complexities and time required to enable a service

provider to be a successful PFS candidate. As Molly Baldwin observed, "When Roca met Third Sector, we already knew what outcomes-based management meant. Over the nine months we have been working with them, Third Sector has taught us how to combine our commitment to impact with outcomes-based financing to support our organization and a sustainable business model."

At Third Sector, we believe that the approach Roca took to evaluate the social innovation financing opportunity can be replicated and developed with other service organizations across the country. We look forward to sharing additional knowledge of our own experiences in this space and supporting other service providers interested in participating in PFS projects.

*"Over the nine months we have been working with them, Third Sector has taught us how to combine our commitment to impact with outcomes-based financing to support our organization and a sustainable business model." - Molly Baldwin, Roca*

# ABOUT Us

**At Third Sector Capital Partners**, our mission is to accelerate America's transition to a performance-driven social sector. We believe in the importance of bringing performance-driven social innovations to scale, in a way that is financially sustainable.

Founded in 2010, Third Sector Capital Partners is a nonprofit that collaborates with government, funders and providers to create **Pay for Success (PFS)** and **Social Innovation Finance (SIF)** solutions.

We bring proven experience in finance, project management, rigorous evaluation methodologies, and cross-sector collaboration to ensure our clients are **educated, engaged and equipped** to participate in PFS and SIF initiatives. Our services include:

- **Transaction Advisory Services:** Program feasibility, program risk evaluation and partnership formation.
- **Deal Construction:** Financial structuring, capital raising, contract negotiations, vetting of partnership stakeholders.
- **Post-Closing Intermediary Services:** Project management, investor relations, evaluation advisory services.
- **Education and Advocacy:** Services and activities to advance the development of a performance-driven social sector.



**Third Sector Capital Partners**  
[www.thirdsectorcap.org](http://www.thirdsectorcap.org)



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