



## Social impact bonds are advancing

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Proposals under consideration by Massachusetts officials offer the first detailed public glimpse into how the state's first-in-the-nation effort to raise private capital to fund social services is likely to work.

Group are competing for state permission to sell what are called "social impact bonds." Winning organizations plan to use the proceeds of bond sales to contract with hands-on social service providers.

One contender, a consortium consisting of the Massachusetts Housing and Shelter Alliance, the United Way of Massachusetts Bay and Merrimack Valley and Third Sector New England, proposes raising \$10 million to fund organizations working on homeless issues. The proposal divides the \$10 million into three tranches: \$7 million issued in social impact bonds, also called low interest loans, with a presumed 2 percent return; \$2 million in grants for which investors would be paid back without interest; and \$1 million in philanthropic grants. Traditional philanthropists would comprise the bulk of the investors and grant-makers, along with corporate funders the United Way would bring and Community Reinvestment Act spending by banks.

"It's a brave new world and no one knows for sure what it will look like," said Joe Finn, president of the Massachusetts Housing and Shelter Alliance.

"In age of scarcity, the fact that (the state) is looking at financing something like this is exciting."

Under another proposal, a firm called Social Finance seeks to raise about \$25 million for Massachusetts work, targeting high net worth individuals, foundations and Community Reinvestment Act funds. Only qualified investors as defined in federal **Securities and Exchange Commission** guidelines would be eligible to buy the bonds; the bonds would not be a retail instruments, said [Tracy Palandjian](#), CEO of Social Finance, whose U.K. affiliate did an \$8 million social impact bond deal in England recently.

Palandjian said the Social Finance model projects as much as \$34.8 million in savings for the state compared to typical state spending on chronic individual homelessness and related costs.

Both proposals center on an approach to tackling chronic individual homeless developed by Finn's organization.

Finn found fault in the traditional model of serving the homeless, which called for addressing people's addictions and mental health issues before putting them in permanent housing, Finn says data from a state-funded pilot program that Massachusetts Housing and Shelter Alliance ran demonstrates outcomes improve and costs go down — particularly related medical costs — when homeless individuals are permanently housed, whether or not they have kicked addictions or addressed mental health issues. The approach has drawn support from, among other places, the city's commercial real estate industry.

"There's a recognition on the part of the public and on the part of the state of the cost-benefit, of outcomes, that what they're funding actually works," said [Tom Collins](#) of Cushman & Wakefield.

The sale of social impact bonds in Massachusetts will involve a multi-step process.

First, the state must set aside money to pay off bonds, pending successful completion of work. Massachusetts has earmarked \$50 million for the anti-homelessness effort.

Next, middlemen must win permission from the state to sell bonds. Secretary of Administration and Finance [Jay Gonzalez](#) said a decision on the current proposals is likely by summer's end.

Only after that happens will the middlemen be allowed to sell the bonds to investors seeking a mix of both financial returns and social outcomes. Then the middlemen will use the money to contract with direct care providers.

The up-side for the state is that it only will spend taxpayers' money after projects have worked.

"We would not pay unless we got those positive results," Gonzalez said in an interview.

Returns will vary by project. One proposal before the state now would offer a 2 percent annual return on an investment of several years.

Even internationally, there are few models to follow.

While many nonprofit leaders and social entrepreneurs applaud Massachusetts' efforts, social financing raises concern among its skeptics.

"It is good to have a financial incentive, but our industry works on another bottom line," said [Michael Weekes](#), CEO of the Providers' Council, which represents social service organizations. "Our efforts are geared toward making people better and safe. Those don't always appear on the bottom line of a balance sheet."

Questions abound among those familiar with the process as to exactly how the state plans to structure the financing and, more importantly, how it will measure success – critical answers that will shape what Massachusetts' social innovation financing will look like.