

# HOUSE BILL REPORT

## HB 1501

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**As Reported by House Committee On:**  
Early Learning & Human Services

**Title:** An act relating to public-private financing for prevention-focused social services.

**Brief Description:** Concerning public-private financing of prevention-based social service programs.

**Sponsors:** Representatives Zeiger, Kagi, Magendanz, Muri, Walkinshaw, Walsh, Ryu, Robinson, Hayes, Stokesbary, Gregerson, Condotta, Sawyer, Jinkins, Farrell, Senn, Appleton, Goodman and McBride.

**Brief History:**

**Committee Activity:**

Early Learning & Human Services: 2/6/15, 2/20/15 [DPS].

**Brief Summary of Substitute Bill**

- Authorizes the Office of Financial Management (OFM) to enter into a Pay for Success (PFS) contract with an investor and a social service provider if sufficient nonstate moneys are secured to procure, manage, or make payments related to the PFS contracts.

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### HOUSE COMMITTEE ON EARLY LEARNING & HUMAN SERVICES

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 8 members: Representatives Kagi, Chair; Walkinshaw, Vice Chair; Walsh, Ranking Minority Member; Dent, Hawkins, Kilduff, Ortiz-Self and Senn.

**Minority Report:** Do not pass. Signed by 3 members: Representatives Scott, Assistant Ranking Minority Member; McCaslin and Sawyer.

**Staff:** Luke Wickham (786-7146).

**Background:**

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

A Pay for Success (PFS) contract or Social Impact Bond (SIB) is a contract between a private party and the public sector, where the private party pays for a social program with the potential to result in government savings. Investors are repaid if certain social outcomes are achieved, presumably with savings associated with the achievement of those outcomes.

A variety of governments around the world are piloting SIB initiatives in subject areas ranging from public safety to housing.

The first PFS contract in the United States is a New York City project that began in 2012. For this project, Goldman Sachs provided a \$9.6 million loan to a social services provider to pay for a 4-year program intended to reduce the recidivism rate for adolescent males released from Rikers Island Correctional Facility in New York City. If the program reduces the recidivism rate by 10 percent, Goldman Sachs would be repaid the full amount they invested. If the recidivism rate reduces beyond 10 percent, Goldman Sachs would make a profit. If the performance targets are not met, New York City would not make any payment.

Since the inception of the New York City project, governmental entities throughout the United States have executed PFS contracts, including the Commonwealth of Massachusetts, and the City of Chicago, among others.

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#### **Summary of Substitute Bill:**

The Office of Financial Management (OFM) is authorized to procure and enter into a multi-year PFS contract with an investor or investors and a provider if sufficient nonstate moneys are secured. No state moneys may be used to procure, manage, or make payments related to PFS contracts described in the bill. This PFS contract would require that the investor(s) pay for a social service intervention that could involve maternal or child health, early childhood education, juvenile justice, homelessness, or child welfare. The OFM must designate performance measures and outcomes if a PFS contract is executed. The investor(s) would then receive a payment of nonstate moneys from the OFM at the end of the contract term if the intervention met the performance measures and outcomes identified in the contract as determined by a third-party evaluator.

The PFS contract must include:

- a requirement that a substantial portion of the payment be conditioned on meeting specific performance outcomes;
- a requirement that no more than \$5 million be spent by the investor on the social service intervention;
- a requirement that any payment to the investor may not exceed \$10 million; and
- an objective process for the independent evaluator to determine whether the performance targets are met.

The OFM must consult with the Washington State Institute for Public Policy (WSIPP) and the Department of Social and Health Services (DSHS) in reviewing and selecting the contract.

The OFM must also consult with the WSIPP and the DSHS in developing clearly defined and measurable performance targets. At a minimum, these targets must demonstrate decreased recidivism among participants. The third-party evaluator must monitor the participants after completing the intervention for a period of time ending before the contract term ends to identify whether the performance targets were met.

The OFM, in consultation with the WSIPP and the DSHS, shall develop a methodology for calculating savings to the State General Fund from the intervention meeting the performance targets, and estimate those savings. These projected savings must be used to determine the payment provided to the investor upon meeting the targets.

**Substitute Bill Compared to Original Bill:**

The substitute bill specifies that no state moneys may be used to procure, manage, or make payments related to the PFS contracts authorized by the bill. Authorization for the OFM to procure, manage, or make payments related to PFS contracts is contingent upon securing sufficient nonstate moneys to execute and carry out the PFS contracts.

The types of interventions that may be used with a PFS contract described in the bill are expanded to include a social service intervention that could involve maternal or child health, early childhood education, juvenile justice, homelessness, or child welfare areas.

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**Appropriation:** None.

**Fiscal Note:** Available. New fiscal note requested on February 23, 2015.

**Effective Date of Substitute Bill:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.

**Staff Summary of Public Testimony:**

(In support) Pay for Success contracts have been used in other states and they should be used here in Washington. Too often government functions to manage problems. This program would solve these problems. This bill would incentivize the private sector to solve these problems. There was a bill last year that would have set up a task force to look at PFS contracts in Washington that passed out of committee. The Housing Finance Committee (HFC) was identified in the bill because of their work with bonds. However, SIBs are not genuine bonds. These are contracts. The HFC is interested in trying to find a way to enter into these contracts and identify investors. The HFC does not have enough information to negotiate the contracts. The general return amount for bonds is approximately 2 to 5 percent. Partners for Our Children has been very interested in SIBs and PFS contracts. This really does not reflect a new approach. The government has been contracting for private services for some time, but the different approach in the bill is the use of private investment to pay for these services. There is a concern that if you lower the cap on payment back to an investor, you may not attract enough investors. In almost all instances of these PFS contracts, there is some private investment and philanthropy. In general, the objections to

SIBs fall into two categories: (1) technical operational concerns; and (2) a philosophical objection that if there are successful programs that could be offered, why doesn't the government fund those services. This is about the most restrictive investing model that exists. No one is going to make much money on this. This is not a sustainable investment system, but similar to a startup. However, this approach could lead to systems change. Many individuals are interested in the Salt Lake City example of this. Utah does not have a taxpayer-supported early learning program. The experiment that is being tested there is whether special education services can be avoided once a child enters the K-12 system by investing in early learning.

(Opposed) Over the last year, there have been many stakeholder meetings around SIBs leading to this bill. Innovative financing methods need to be developed. However, incentivizing investment is not the solution. Social impact bonds are more costly than if the government simply paid for these programs. Investors may choose social service interventions that are low-hanging fruit, and receive a large return. The fiscal note only relates to developing the PFS contract. The 50-percent cap on the contract amount is undefined because there is no idea how large the savings could be.

**Persons Testifying:** (In support) Representative Zeiger, prime sponsor; Kim Herman, Housing Finance Commission; Ben De Haan, Partners For Our Children; and Steve Leahy, Ready Nation.

(Opposed) Jeanine Livingston, Washington Federation of State Employees.

**Persons Signed In To Testify But Not Testifying:** None.