Social Impact Finance for Early Childhood Development

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Janis Dubno, M.B.A.
Voices for Utah Children

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- "Financing Human Capital Development for Economically Disadvantaged Children: Applying "Pay for Success" Social Impact Finance to Early Childhood Development"

  Ready Nation Working Paper: authors: Janis A. Dubno, Robert H. Dugger, and Michele R. Smith

- Link to the full paper
  http://www.readynation.org/uploads/db_files/RN%20PFS%20Finance%20Dubno%20Dugger%20Smith%20Paper%20130610.pdf

Voices for Utah Children 25 Years of speaking up for kids

Applying “Pay for Success” Social Impact Finance to Early Childhood Development

- “Pay for Success” (PFS) Social Impact Finance refers to performance based financing and contracting between government, investors and services providers.

- Early childhood research shows a significant reduction in special education assignment for low income children who attend high quality prekindergarten. Reduction in special education costs may be sufficient to pay for a prekindergarten PFS project.

- In addition to reductions in special education, sources of short and long term cost avoidance for government include grade retention, crime, welfare, and increased earnings.

Early Childhood Development PFS Economics

- There are three important relationships in a PFS project for high quality prekindergarten:

- (1) the ratio of the cost of the intervention (prekindergarten) to the cost of the remediation (special education).

- (2) the ratio of intervention impact to non-intervention impact.

- (3) the combination of private investor funding, state funding, and federal funding for PFS scholarships for economically disadvantaged children to attend high quality prekindergarten.

Two Financing Structures

- Two loan structures are examined:

- (1) the guaranteed fixed interest and principal structure whereby interest and principal guaranteed by accrued savings and a philanthropic backstop; and

- (2) The unguaranteed payment pass-through structure.

Base Case Structure and Assumptions

- The model uses information from the Bethlehem School District prekindergarten program: a reduction of the special education assignment rate of 18% to 3% for low income children; $7,850 per year cost of the prekindergarten program per child, and a cost per child per year of $12,141 (only 80% or $9,713 captured in the model) of special education

- The base case scenario examines a combination of 75% investor funding, and 25% state funding for the PFS project and 500 children are funded.

Three Funding Combinations for PFS Scholarships

- The paper analyzes variations of combinations of investor, state and federal funding of PFS scholarships for both financial structures. The combinations examined were:

- (1) 75% investor funding, 10% state funding, and 15% federal funding;

- (2) 50% investor funding and 50% state funding ; and

- (3) 50% Investor funding, 25% state funding, and 25% federal funding .

Federal Funding in a PFS Financing Structure

- The introduction federal funding increases the returns to the state.
- The inclusion of federal funding is appropriate as the federal government also funds a portion of special education costs to districts, and benefits from improved educational outcomes, as well as improved social outcomes and reduction in long term costs for other social programs.

Results of the Sensitivity Analysis

- The three PFS funding combinations were analyzed, varying the percent reduction in special education assignment rates.

- The 50% Investor funding, 25% state funding, and 25% federal funding combination provides positive returns to the state in the Fixed Debt structure even if the special education assignment rate is reduced only to 7% (instead of 3% used in the case model).

- Positive returns to the state are evident in the pass through structure if the assignment rate is reduced to 6% (instead of the base case reduction to 3%).

Policy Considerations for State Legislation

- What are the funding sources for loan repayment? Ongoing appropriations or capitalize a restricted repayment fund?
- Full Faith and Credit?
- Who negotiates for the state?

More Policy Considerations

- What are the performance metrics?
- Which programs are eligible to receive funding from a PFS contract?
- How much detail should there be in the enabling legislation?

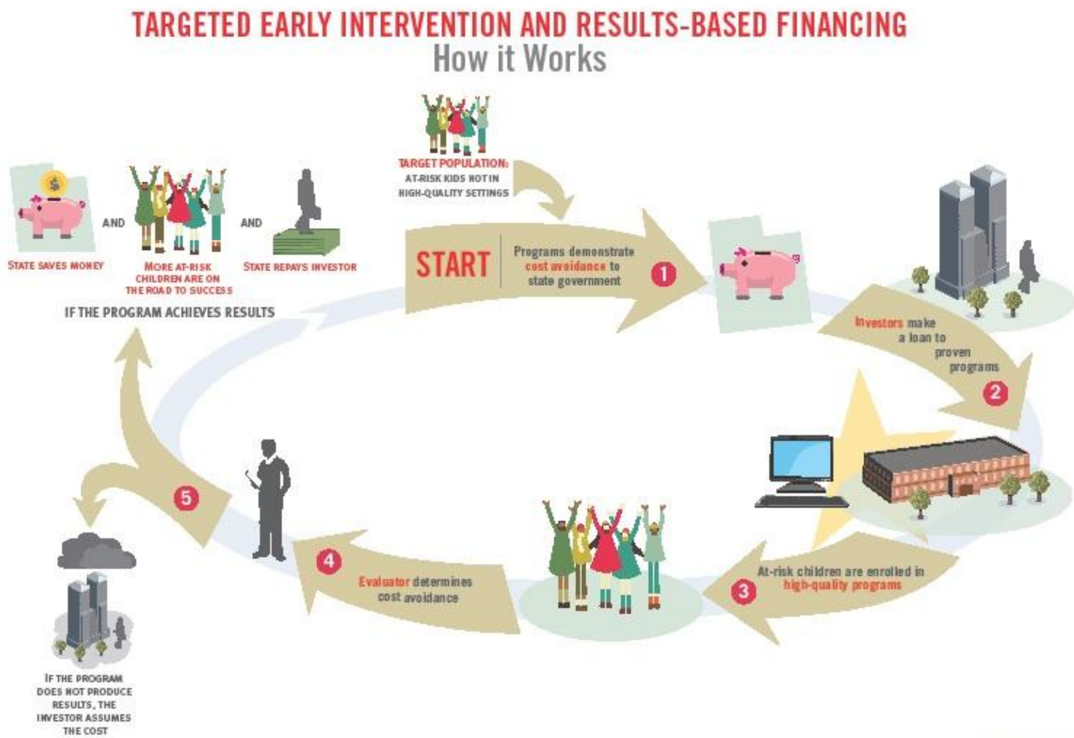
The First Social Impact Loan for High Quality Preschool in Utah

- Lenders: Goldman Sachs Urban Investment Group is the senior lender; J.B. Pritzker is the subordinated lender.
- Providers: Granite School District, Park City School District, the Guadalupe School (charter), YMCA (non profit), Childrens' Express (daycare center). Lit'l Scholars (daycare center).
- The United Way of Salt Lake and Salt Lake County capitalized a repayment fund to repay the investors based on special education cost avoidance.
- The United Way of Salt Lake is the intermediary.

The First Social Impact Loan for High Quality Preschool in Utah

- 600 additional economically disadvantaged 3 and 4 year olds are currently enrolled in preschool who would not have had access otherwise!!
- Only the first cohort of five cohorts is funded. State legislation is needed to go forward.

Utah Social Impact Loan Transaction Chart



Conclusions

- PFS financing structures can work for high quality early childhood programs for economically disadvantaged children with proven success.

- Different combinations of state, federal and investor funding can leverage returns to the state and investor.

- More research regarding cost avoidance is needed.

Contact Information

Janis Dubno, M.B.A.

Voices for Utah Children

Early Childhood Senior Policy Analyst

(801) 364-1182

janis@utahchildren.org