Impact Bonds Working Group

LEVOCA IMPACT LABS SOCIAL FINANCE

WORKSHOP 1: BACKGROUND BRIEFING PAPER

Section 1: Impact Bonds Working Group

The objective of the Impact Bonds Working Group is to design and test strategies that will help members to use Impact Bonds and related Payment by Results (PbR) mechanisms effectively at scale, to help development agencies support governments to deliver on the SDGs.

The Impact Bonds Working Group has been established as a collaborative, donor-led, initiative with members working together to identify potential barriers to implementing Impact Bonds and related PbR mechanisms at scale, and the solutions and strategies to overcome them.

It will operate through periodic convenings at workshops aimed at designing a joint strategy or strategies, identifying what action needs to be taken and what resources are necessary for strategies to be implemented.

The first convening is a 2.5 day immersive workshop which takes place in Brussels on 15-17 May 2018. During this workshop Working Group members will develop their vision for implementation at scale and a common understanding of the barriers, together with a shortlist of potential solutions that could be further developed over the next few months.

This briefing paper aims to provide members with material to inform and ensure a common language for discussions. It includes:

- Background information on Impact Bonds and PbR mechanisms;
- A framework for thinking about current barriers to scale and possible solutions that builds on the member surveys and follow up interviews;
- Case studies of initiatives currently under development in the market; and
- Signposting to additional sources of information.

We look forward to working with you!

Section 2: Impact Bonds & Payment by Results mechanisms

Most members of the Working Group have some experience of working with PbR contracts or incentives in the past. There are many types of PbR mechanisms, and Impact Bonds are only one such example within this wider landscape (Figure 1).

Note:
Results-Based and Outcomes-Based are used by the field in different ways, and sometimes interchangeably. In this document, we use the following:

- *Outcomes-Based Commissioning (or Contracting):* Contracting on the basis of outcomes, which may or may not be pre-funded by investment. Investment may take different forms.
- *Results-Based Funding:* A broader group of instruments where delivery partners are paid if performance targets are met.
- *Fund:* Money that may be held in a separate entity or just a hypothecated budget line

Additional definitions of different mechanisms can be found in Appendix 1.

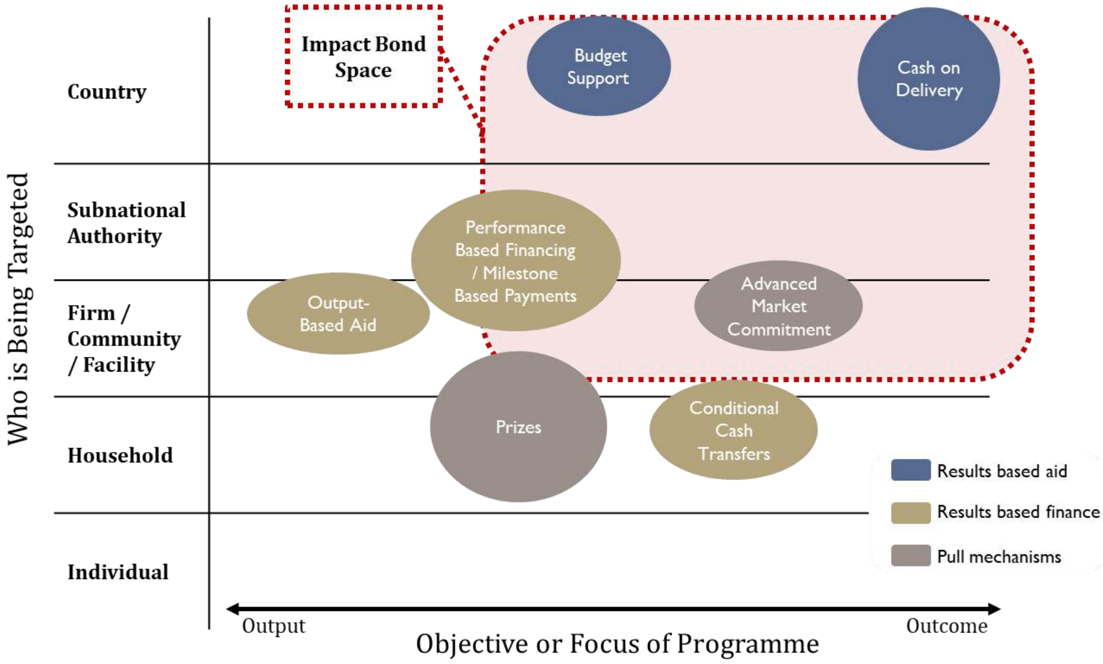

Figure 1 – Impact Bonds & Payment by Results Mechanisms[1]

In all instances, these approaches pay some or all programme funding only if pre-defined results are achieved. However, contracts vary significantly in terms of:

- **How much** programme funding is put at risk on an outcomes basis;
- **What type of results are paid for** - whether results are service user outcomes, rather than service provider activities or outputs; and
- **Who bears outcomes risk** - in most Results based Finance (RbF) contracts *providers* are paid ex-post for results and may bear significant financial risk if they cannot deliver those results; in Results based Aid (RbA), *governments* bear the risk.

As a commissioner, outcomes-based contracts (of which Impact Bonds are a part) have a number of benefits including:

- **Unlocking private sector innovation** - by linking payments to service user outcomes rather than service delivery, providers are incentivised to continually adapt and improve their interventions to maximise their impact, driving innovation and continuous improvement in the market.
- **Stimulating investment** - a clear link between funding and results creates a rational investment market enabling working capital loans, risk-sharing through equity and Impact Bonds.
- **Building the evidence base** - outcomes-based commissioning requires robust data reporting and analysis, strengthening provider accountability and increasing the data available to inform the global evidence base on what works well and where.

[1] Adapted from Savedoff, W. "Incentive Proliferation? Making Sense of a New Wave of Development Programs." Center for Global Development Essay (August 2011)

- **In-built market regulation:** aligns provider incentives with government and donor policy goals, and establishes a transparent framework for market regulation.

What outcomes-based investment brings - the Impact Bond delta

Outcomes-based contracts create a risk capital need for service providers – a need to identify funding to pre-finance service delivery before outcomes are delivered and payment is made. For government, this capital need is generally met off their own balance sheet; for service providers, recent research has shown that financing is usually provided by internal cash reserves or, less commonly, commercial loans and philanthropic funds.[2] This implies a current provider market restricted to "organisations with large unrestricted reserves" or "private companies with a financial track record".[3]

Impact Bonds provide a solution to this pre-financing need by involving private investors that take outcomes-based risk. Working Group members will be familiar with how the different parties come together in an Impact Bond, with a typical structure outlined in detail in Appendix 2.

In their involvement of outcomes-focused investors, Impact Bonds differ from other forms of outcomes-based commissioning. We outline the potential benefits of investor involvement below:

- **Enabling greater focus on outcomes vs. outputs** - Solving the pre-financing needs of service providers through private investment enables governments and donors to focus a greater proportion of their payments on end user outcomes without worrying about putting service providers in financial jeopardy. This gives commissioners the flexibility to move away from input- or activity-based payments and monitoring. It also enables smaller or financially weaker service providers to participate.
- **Driving rigour in contract design** - Existing market experience suggests that the involvement of investors drives a rigour in contractual design that may not otherwise be present.
- **Creating a focus on continuous improvement** - The contractual scope for service adaptation to varied and changing local needs, through rapid feedback loops, is a key strength of the Impact Bond model and, in turn, should drive the best possible social outcomes. As Impact Bond investors typically take on asymmetrical risk – they have the potential to receive a modest return or face a complete loss of funds – they are highly motivated to ensure that data systems are developed and used to inform, adapt and improve service provision in real time to drive the best possible outcomes.

Considerations for Impact Bond use

Impact Bonds are only one tool within the broader spectrum of outcomes-based approaches and evidence is still emerging around when the approach adds the most value. The decision tree in Figure 2 outlines when outcomes-based contracts are useful and when an Impact Bond is most applicable vis-à-vis other instruments.

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[2] Supplier Access to Prefinance in Payment by Results Contracts – Research Report, Dalberg Intelligence, DfID (November 2017 - *unpublished*)

[3] Ibid.

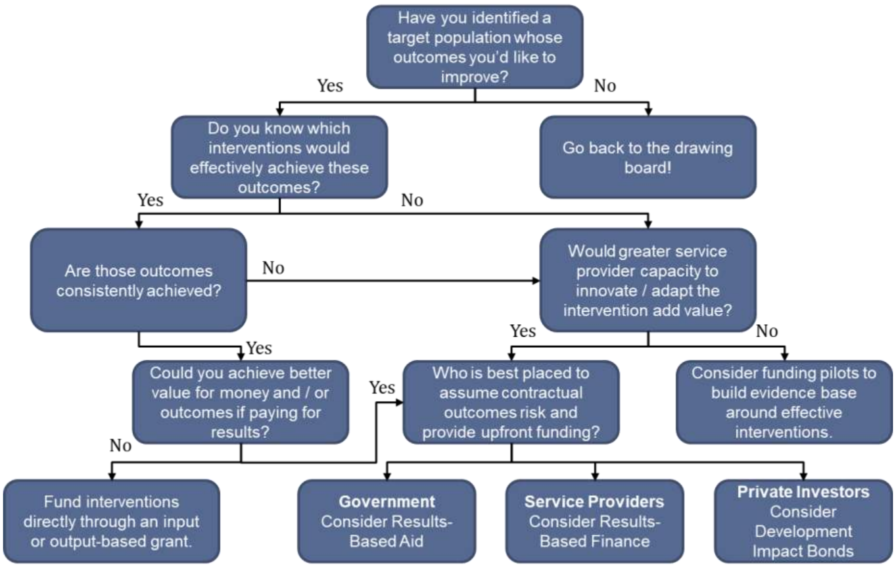

Figure 2 – PbR Decision Tree[4]

An Impact Bond potentially *adds value* when**:**

- **There is a demonstrated need for an outcomes focus** in the particular target sector/geography;
- **There are promising interventions** which can be expanded to support innovation, or scaling where there is an evidence base to support it; and
- **The chosen service providers cannot access adequate working capital** or are unable to bear the implementation risk.

It is potentially *feasible* when:

- **The data and evidence base are strong**, both target intervention group and outcome metrics can be clearly defined, with reliable data for benchmarking and performance;
- **Making progress with the target outcomes is a priority for both donor and the partner government**; and
- **The issue and geography is of interest to investors**, with a balanced transfer of risk.

Impact Bonds - like any other contract - are only as good as their terms. There are those that are carefully negotiated and well thought through, and those that are loosely put together and create perverse incentives that, for instance, encourage providers to work only with the easiest members of the target population while ignoring the rest (to 'cream and park'). Based on experience in the market so far, key features of a successful Impact Bond include[5]:

- **Leadership across and between organisations**, including a clear path for engaging government;
- **A focus on outcomes**, which are objectively measurable and definable and do not create perverse incentives. This may include payment for intermediate outcomes / outputs, if it takes significant time to observe and evaluate change; however, this should be balanced against the risk of additional complexity and deflection from the ultimate objective; and

[4] USAID Impact Bond Presentation, Social Finance (February 2016 - *Unpublished*)
[5] The LOUD SIB Model, Government Outcomes Lab (December 2017)

- **Data on both the eligible cohort and on the outcomes likely to be achieved** by the intervention, including the size of the cohort, the outcomes they are currently achieving and the current cost of supporting them.

Impact Bond activity to date

Social Impact Bonds

To date, 108 Impact Bonds have been launched worldwide across 10 sectors and in over 20 countries.[6] Most have been launched in high income countries as Social Impact Bonds (SIBs), where the commissioning authority, or outcomes funder, is a national or sub-national government body.

SIBs were pioneered in the UK where there are now 40 examples, including those where delivery has completed, and an emerging body of evidence is being studied to develop principles of good practice that can help commissioners. The largest scale SIB-funded projects to date are in the US, where more than US$200m of investor capital has been raised for SIB (Pay-for-Success) projects. Australia and the Netherlands were also early adopters of Impact Bonds, each now with 8 projects launched and a growing field of practitioners and public sector partners who are engaged in the field.

A range of different initiatives have emerged to support outcomes-based commissioning and Impact Bonds in countries where multiple examples have been launched. For example:

- The **UK** has implemented a number of initiatives designed to facilitate transactional efficiency and efficacy, including establishing a SIB Centre of Excellence within government, developing template documents, and structured access to design funding. Most significant, has been the pioneering role that Outcome Funds have played in shaping and stimulating demand and innovation. A Government Outcomes Lab has now been established, bringing academic rigour to analysis of the emerging body of evidence from outcomes based commissioning (see Section 4).
- **Portugal** has also established an Outcome Fund, which aims to promote an outcomes-based culture in the public sector.
- The **US** has seen substantial support for design and feasibility funding from the Social Innovation Fund and philanthropic funders, among others. It was also an early pioneer in the provision of grant funded capacity support to public commissioners, through the Harvard SIB Lab (now, Government Performance Lab). Enabling legislation has been introduced or passed in over 20 states and at Federal level, and Federal agencies have offered support for local governments to explore the model.
- The State of New South Wales led the development of Impact Bonds (Social Benefit Bonds) in **Australia**. Soon after the first projects were launched, it established an Office of Social Impact Investment to develop commissioner capacity and standardise documentation, as well to provide a focal point from which to procure.

Development Impact Bonds

The Impact Bond market saw significant progress in 2017. Cumulative investment raised to support Impact Bonds globally has reached nearly US$400m and last year alone saw the launch of 33 Impact Bonds, with 9 more countries launching transactions for the first time. It was also significant for Impact Bonds in the development field with the launch of the CHF26m ICRC

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[6] Impact Bond Database, Social Finance (May 2018)

Humanitarian Impact Bond[7] and the $9m Utkrisht Impact Bond in Rajasthan[8] and Educate Girls reporting its second year results. In these examples, where the outcome funder(s) is not a national or local government, usually a development agency or philanthropic funder, they are termed Development Impact Bonds (DIBs) or as in the ICRC case, a Humanitarian Impact Bond (HIB).

Based on research carried out by Brookings Institution in 2017[9], a total of 28 Impact Bonds were then either contracted to be launched in low- and middle-income countries, or under development.

Early Learnings from the Field

2017 also saw the results published for the first ever Impact Bond in Peterborough, UK, which reported a reduction in reoffending of 9% over the life of the program, with the result that investors were repaid in full, with a 3% annualised return. However, most projects are at an early stage, with outcomes data not yet publicly available. Of those where information is available, market intelligence reports that, globally, at least ten projects have already achieved target outcomes that will see a return of investor capital, and eight others in progress have reported that they have been making interim payments to investors based on outcomes achieved.[10] It is to be expected that some projects will not fully return capital to investors, most notably to date the Rikers Island Impact Bond that reported in 2015 that it did not achieve its target impact, triggering a loss for investors and the philanthropic guarantee that supported their investment.

There is not yet a comprehensive body of learning on Impact Bonds, though reports to date highlight a number of themes:

- Impact Bonds can lead to more innovative and flexible service delivery[11] and incentives to improve performance can lead to programmatic innovation;[12]
- They can work as an incentivising mechanism for the achievement of outcomes while keeping beneficiaries' interests at the centre;[13]
- There are also examples that have been effective in coordinating multiple stakeholders and aligning interests; [14] [15] and
- Well-designed Impact Bonds can enable risk transfer from commissioners and providers, which may enable the adoption of new interventions, enhance performance management capabilities, and build the evidence base upon which to make future commissioning decisions.[16]

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[7] https://www.icrc.org/en/document/worlds-first-humanitarian-impact-bond-launched-transform-financing-aid-conflict-hit
[8] http://thepalladiumgroup.com/research-impact/The-Utkrisht-Impact-Bond-Design-Grant-case-study
[9] Impact Bonds in Developing Countries – the Early Years, Brookings (September 2017)
[10] Impact Bond Database
[11] Social Impact Bonds: The State of Play, Ecorys and ATQ, Nov. 2014. Available at https://www.biglotteryfund.org.uk/-/media/Files/Programme%20Documents/Commissioning%20Better%20Outcomes/SIBs_The%20State%20of%20Play_Summary%20Report.pdf
[12] Educate Girls DIB second year results press release 29.6.17
[13] Fair Chance Fund Interim Report Year 2. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/660583/Fair_Chance_Fund_interim_report_Year_Two.pdf
[14] See 2 above.
[15] Taking Impact Bonds to the Next Level, GO Lab, 2016. Available at https://golab.bsg.ox.ac.uk/blogs/taking-social-impact-bonds-next-level/
[16] https://golab.bsg.ox.ac.uk/basics/introduction-social-impact-bonds/overview-sibs-briefing-note-local-authorities/

However, it is also noted they been relatively slow, complex, and expensive to develop.[17] This is particularly the case for transactions which are a 'first' in an issue area or geography. Greater transparency of results is also needed, both for impact and investment performance.

Despite this emerging body of learning, it is still too early to evaluate the field as a whole and compare like with like. There are significant differences in the way deals are structured, their duration, governance, whether they implement an evidence-based or theory of change-based intervention (i.e. for scale or for innovation), or how they are measured. Most deals in the United States, for example, base their measurement on randomised control trials or other quasi experimental methodologies. The UK market, by contrast, has quickly evolved to use so-called 'rate cards' or tariff models, measuring results through more practical non-experimental methods. Each approach has strengths and weaknesses and needs to be selected for the right circumstances. These, and other factors need to be taken into account as learnings emerge.

Section 3: Overcoming Barriers to Scale

Summary feedback from Working Group Member survey

While momentum is growing, outcomes-based approaches are not yet mainstream within any donor organisation. At present, the time and effort required to commission Impact Bonds and other outcomes-based instruments is significant relative to both the scale of the deals and the scale of the problems they are trying to solve.

Working Group members have participated in a Survey and 1-1 discussions in advance of the first workshop. This has provided valuable feedback in preparation for the Workshop and will be shared in detail at the Workshop.

Benefits of Impact Bonds

Survey feedback indicated that the main perceived benefit of launching an Impact Bond is to make an organisation's funding more effective. Also ranking highly is the potential to engage private sector finance, bring services to underserved markets, and allow for more innovation in service delivery (Figure 3).

[17] See 2, 3, and 5 above.

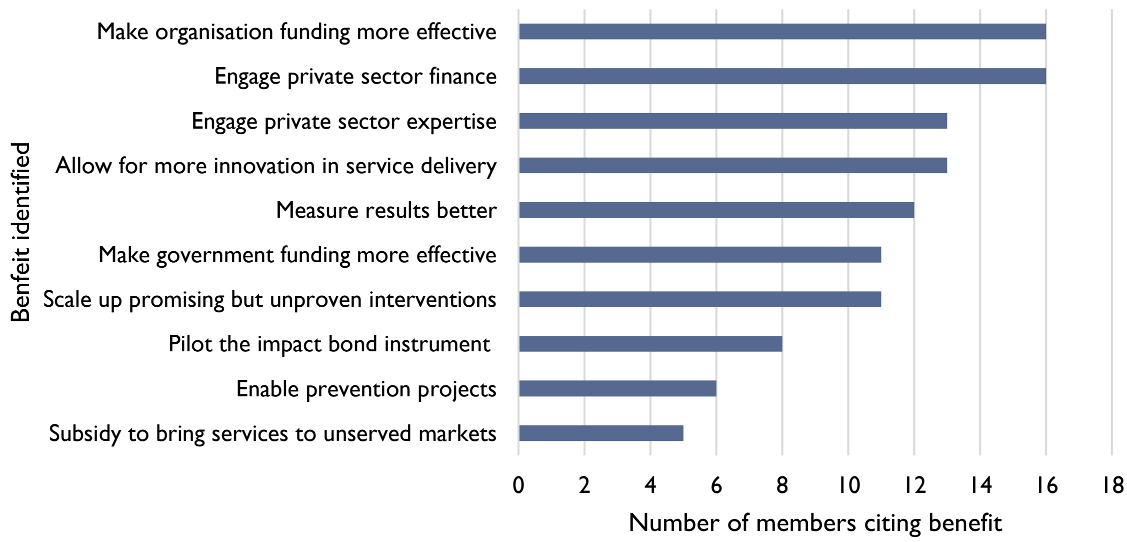


Figure 3 - Member perceptions around Impact Bond Benefits

Experience with and interest in Impact Bonds

Almost 50% of Working Group members have experience in launching an Impact Bond, and 75% are currently looking into launching an Impact Bond (Figure 4), with only one member who has not launched and is not looking into structuring one.

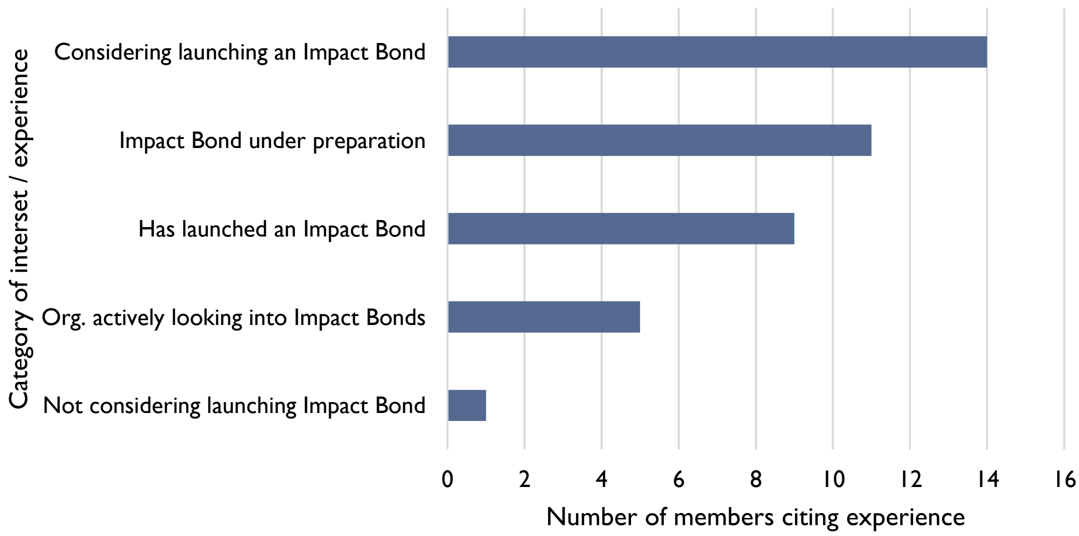


Figure 4 - Member Experience & Interest with Impact bonds

Challenges around designing and launching Impact Bonds

The main challenges perceived by members were around the nature of the deals i.e. deals were too time consuming or too expensive (Figure 5). Over half of members also highlighted a lack of conclusive evidence for the effectiveness of Impact Bonds, and a lack of understanding or awareness of the instrument.

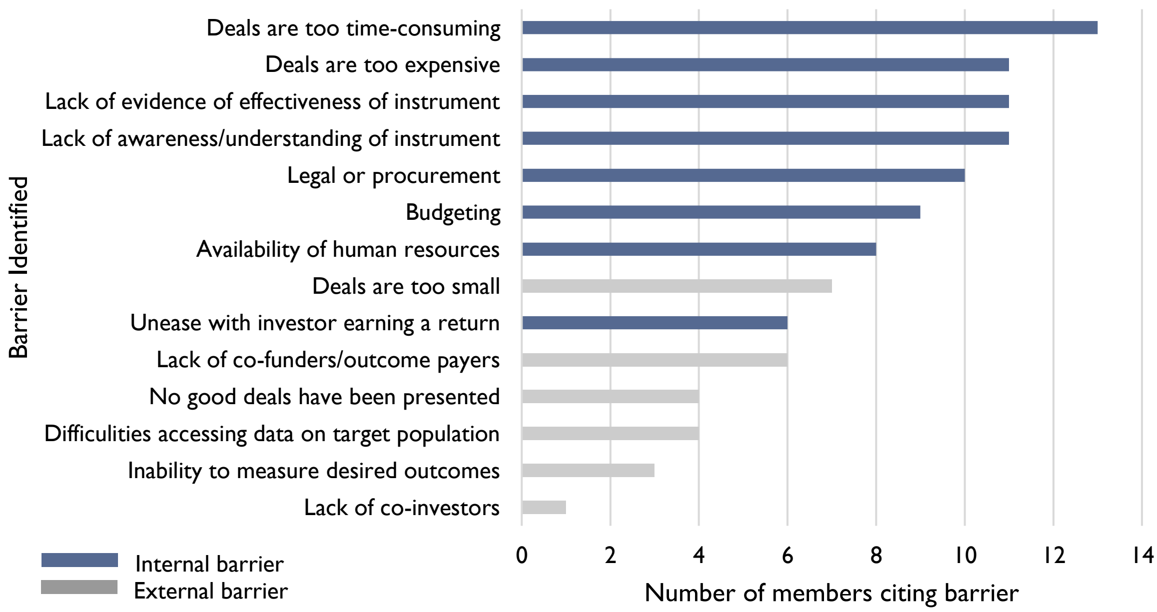


Figure 5 – Challenges around designing and launching Impact Bonds

A framework to evaluate potential options and solutions to overcome barriers to scale

For Impact Bonds and other forms of outcomes-based contracting to play a meaningful role in delivering the SDGs, new strategies are needed to address donor barriers and enable commissioning at scale.

Any strategy for scale requires an assessment of the barriers to scale that currently exist – real and perceived – and an exploration of the tools and options that hold promise to break down those barriers and act as catalysts for change.

It is apparent that barriers take different forms, ranging from donor appetite to engage in a particular form of funding, through to the need to build capacity to design and execute transactions, including developing the legal and procurement tools that facilitate use of new instruments or, where disbursement is based on proven outcomes, matching deferred disbursement commitments with budget cycles.

In parallel, solutions need to recognise and address the very real challenges for an outcomes-based approach in the external environment, such as building capacity of providers or host country governments, or the quality of data and evidence.

A common understanding of barriers and the potential of different solutions is a key building block for moving forward. Table 1 below provides an initial framing for this discussion, and suggests the potential that different options/solutions could have based on experience to date and preliminary market feedback.

In this high-level framing, barriers to scale are grouped into *Barriers in the Internal Environment* (within donors) and *Barriers in the External Environment* (in the wider market).

A range of options and potential solutions are then mapped against these with a suggestion of how effective they might be to help address that particular barrier. Options and solutions are grouped around:

- **'Money Solutions'** – the stimulus that Paying for Outcomes at Scale or Outcomes-Based Investment could produce; and

- **'Knowledge solutions'** – which aim to reduce barriers to implementation by Building Market Capacity or Developing the Learning Ecosystem.

It seems clear that no single option will address all barriers, but, promisingly, by combining options into different strategies, progress can be made to build a market for outcomes characterised by:

- **Deal flow -** a strong pipeline of providers, delivering effective interventions at scale;
- **Reliable supply of Outcome Funding -** a programmatic approach to paying for outcomes, building market confidence; and
- **A functioning market for risk capital.**

The framework is not comprehensive, but rather, has been prepared for the Working Group with the aim of stimulating ideas and discussion. Working Group members are invited to reflect on how this framework matches to their own experience, and to consider:

- What barriers are missing?
- What are viable solutions?
- What other options should be explored?

Table 1: Illustrative Framework of Impact Bond Barriers & Solutions for Scale

			Barriers to scale									
			Barriers in the Internal Environment				Barriers in the External Environment					
			Mandate	Budget Constraints	Skills & Capacity	Transaction Costs	Data and Evidence	Investors	Provider Capacity	Evaluator capacity	Country Government	Transaction Advisory
019- Options and Solutions	Money Solutions	***Pay for Outcomes at Scale***										
		Single Payer Outcome Fund										
		Multi Payer Outcome Fund										
		Commissioning Platforms										
		Co-Funding Facility										
		Outcomes funder for single at scale IB(s)										
		Stimulate Outcomes Based Investment										
		Impact Bond Fund investment(s)										
		Single Impact Bond investment(s)										
		Guarantees/first loss insurance										
		Blended / Concessional Finance										
	Knowledge Solutions	***Build Impact Bond Market Capacity***										
		Donor capacity										
		Government capacity										
		Provider capacity										
		Intermediary capacity										
		Evaluator capacity										
		Subsidised transaction costs										
		Ensure Ecosystem Learning										
		Standardised contracts and processes										
		Codified knowledge										
		Impact Bond centre of excellence										

Ambition:

Deal Flow

Strong marketplace of providers who are able to operate with consistency at scale to deliver outcomes

Supply of Outcome Funding

Programmatic funding available at scale, building market confidence

Market for Risk Capital

A functioning market for risk capital, with a sufficient volume of investors from across the spectrum

Key

	Good potential to address this barrier
	Some potential to address this barrier
	Helpful to some extent for this barrier – and/or potential will increase in significance over time
	No/nominal use in addressing this barrier

A: Barriers to Scale

Barriers in the Internal Environment - those identified by Working Group members that relate to a donor's internal operations and mandate:

- **Mandate / Regulatory** – limitations relating to mandate, including, for example, paying investor returns, restrictions on ability to fund certain interventions, etc.
- **Budget Constraints** – inability to commit to outcome payments beyond donor's current funding cycle; and/or to ring-fence for contingent outcome payments.
- **Skills & capacity** - in-house expertise and experience to commission, procure, manage and evaluate an outcomes-based contract. Includes knowledge of how and when instrument can be used or not.

Barriers applicable to both the Internal and External Environment:

- **Transaction Costs** – real (time and money) and/or perceived costs of completing a transaction, including both 'true' transaction costs (i.e. costs that do not generate any value beyond the transaction itself, such as legal fees for contracting) and 'project costs' that can be seen as investments with value that persists beyond the Impact Bond itself (e.g. spending on performance management systems to improve data collection & analysis).

Barriers in the External Environment - barriers relating the wider market:

- **Data & Evidence** – confidence in the ability to measure and price outcomes appropriately, including reliable performance and cost data on providers, and robust information on the target population to inform baseline.
- **Investors** - availability and access to risk capital on reasonable terms.
- **Provider Capability**– availability of delivery organisations with capacity and expertise to deliver against an outcomes-based contract, including rigorous data management systems which enable adaptive interventions.
- **Evaluator Capacity** – availability of evaluation organisations with capacity and expertise to measure and evaluate contractual outcomes.
- **Country Environment** – capacity and experience of country government and key ministries to work with outcomes-based contracts on reliable terms, including an enabling regulatory environment (e.g. around private sector engagement in service delivery, creation of blended capital structures, using local investment vehicles, safeguard measures, etc.), political stability and rule of law.
- **Transaction Advisory** – availability of feasibility and design consultants with experience and technical skills to support donor/provider/country government/investors as needed.

B: Options and Solutions

Money Solutions

Pay for outcomes at scale – options that focus on paying for outcomes (results):

- **Single Payer Outcome Fund for Multiple Outcome-based Contracts** – a dedicated fund capitalised by a single actor that can commission multiple transactions or providers, concurrently or in successive rounds. Single payer outcome funds could focus on a geographic or thematic area – for example, Malaria reduction; Education in West Africa or India or could work alongside an investment fund to support pre-finance of delivery, where needed. Market examples - *UK Department of Work & Pensions Innovation Fund, Portugal Inovação Social*
- **Multi-Donor Outcome Fund for Multiple Outcome-based Contracts** – a pool of funds from multiple donors to fund multiple outcomes-based transactions from multiple providers. Multi-donor funds could focus a single issue or geography or on multiple issues and geographies, and could be bid into by both governments and non-state actors. Multi-donor or single payer outcome funds, could also provide pre- Impact Bond proof of concept capital.
- **Commissioning Platforms** – Coordinated response to a common social need in by bringing together a combination of: risk capital, delivery expertise and tested structures for working in partnership with commissioners and providers in multiple areas. Market examples: *UK Mental Health and Employment Partnerships*
- **Co-funding facility** - outcome funding facility to co-finance outcome payments alongside governments (national and sub-national) for specific projects with the ambition of catalysing multiple markets. Market examples: *UK Life Chances Fund; IDB/SECO Co-financing Facility with the Colombian Government.*
- **Outcomes Funder for Single at Scale Impact Bond** - commitment to purchasing outcomes for a single large-scale project.

Stimulate outcomes-based investment – options that focus on ensuring sufficient and suitable investment capital is available:

- **Impact Bond Investment Fund** - dedicated investment fund that seeks outcomes risk. Donors could play a role in supporting/cornerstoning alongside e.g. an Outcomes Fund.
- **Investment in Single Impact Bond** - risk capital to pre-finance an outcomes based contract against an outcomes commitment from another party.
- **Guarantees/First Loss Insurance** - protection against uncertain/higher risk transaction elements.
- **Blended and concessional finance facilities** - blend concessional resources with conventional sources of development finance (e.g. IFC) to mobilise private sector investment.

Knowledge Solutions

Build Impact Bond market capacity – options that focus on direct capacity building and/or capacity building resource for key market participants:

- **Donor** - build internal knowledge and capacity e.g. dedicated innovative finance team and/or supplemented by market resource. Market example: *UK Centre for SIBs*.
- **Government** - building capacity in government to understand and participate e.g. advisory support or directly funding government. Market example: *IDB SIB Program*
- **Provider** - support development of provider capacity to manage to an outcomes-based contract e.g. project based support through a technical assistance grant; grant funded

mobilisation period to support capacity building, supplementary funding to providers / community of providers to update data systems for outcomes delivery, innovation pilots that test investment readiness of promising providers and interventions to build up a portfolio of investment ready solutions. Market examples: *Development Grants, Investment Readiness Funding (UK, US)*

- **Transaction Advisors -** strengthen organisations who can support contracting partners to design, execute and manage contracts, particularly at local level.
- **Evaluator -** subsidize cost-effective capability of local and international M&E experts.
- **Transaction Cost Subsidy** – for example design, legal, evaluation, baseline data collection.

Develop Knowledge Base – options that focus on building a community of practice:

- **Standardise Contracts and Processes -** develop contract templates to streamline deal negotiation and reduce transaction costs. Market example: *UK Centre for SIBs*
- **Codify and Share Knowledge -** codify and share knowledge through a virtual platform (or similar) or community of practitioners. Market example: *Pay-for-Success Hub managed by the Non-Profit Finance Fund (US)*
- **Impact Bond Centre of Excellence** – pooling best practice and learning, forum for training and thought leadership, convening, develop toolkits.

Section 4: Solutions for Scale - Exemplar Case Studies

Case Study 1: 'Money Solution' - Paying for Outcomes at Scale

Country Examples

United Kingdom

Following the launch of the first Impact Bond in 2010, the UK Government adopted a number of policy initiatives and strategies to support the commissioning of multiple Impact Bonds.

A central strategy has been the use of 'Outcome Funds', a government-led approach which has driven the growth of the Impact Bond, and related outcomes-based commissioning, market in the UK.

Outcome Funds have supported programmatic funding in two ways:

- As an allocation of budget by a central government department to commission and pay for specific, pre-designed outcomes in a particular issue area (**'thematic'** approach); or
- As an allocation of budget set aside by central government to stimulate and incentivise outcomes-based commissioning by local and regional commissioners across multiple policy areas, where decision making is wholly or partly delegated to a team of officials or the external agency that holds the funds as fiduciary (**'co-funding'** approach).

Outcome Funds launched to date in the UK are shown in Figure 6. The Government Outcomes Lab (GO Lab) has now been established to document, consolidate and analyse the learning that is emerging and to inform policy (see Case Study 2).

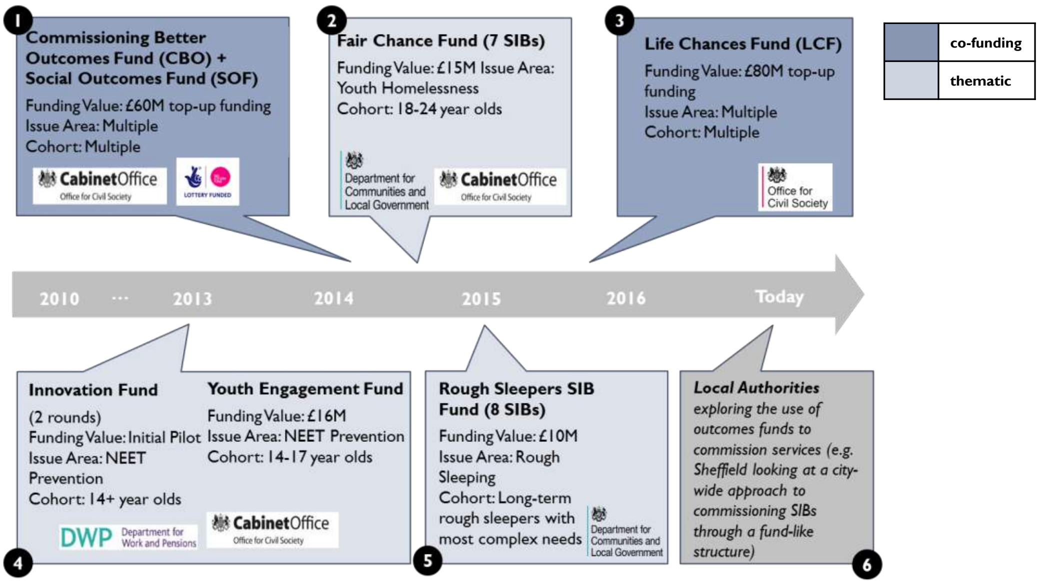


Figure 6: Outcome Funds launched to-date in the UK

Outcomes Funds have:

- Been used to fully fund outcomes (4) and to leverage co-funding for outcomes (1,3)(Single Payer; Co-funding);
- Been used for centrally commissioned (2,4,5) and locally-designed outcomes-based interventions (1,3) with contract design support funding available;

- Aligned the budgets of different outcome funders in a joint/aligned strategy (1) (Multiple Payer);
- Incentivised outcomes-based commissioning at a local level when used as top-up funding (1,3);
- Supported the development of new models and commissioning platforms, and the scaling of pilots to a regional level (1,3); and
- Stimulated potentially significant developments such as co-funding municipal authorities to set up a local outcomes fund (6).

Portugal

Portugal provides an interesting point of comparison with the UK experience. **Portugal Inovação Social** (PIS) was launched in 2015, with source funding from Portugal's allocation of regional development budget for the current EU budget cycle.[18] The fund has four disbursement pillars, including lending via funds of funds, capacity building and outcomes funding. The structure has provided some valuable early learnings:

- Pays for 100% of outcomes: As a result, there is no incentive for local government to co-fund or develop capacity to commission for outcomes
- Rules on disbursement of EU funding: It is difficult to align activity-based funding for outcome-based disbursement
- Challenge of working with applicable (EU) accounting and audit rules: This creates a risk of disallowed or delayed funding which then needs to be actively managed.

Lessons Learned

The Outcomes Fund approach resonates with key themes emerging in the international development sector, where effective and efficient distribution of development assistance is a priority for donors, pointing to a move away from a short-term 'project-by-project' approach towards a longer-term programmatic approach, where interventions are part of an ongoing commitment by donors to a series of investments. Strategic programming allows a move away from start-stop approaches which limit scale-up and deters co-investment.

The examples show that there are many ways in which such an approach can deploy funding at scale. These include:

- A **Single Payer Outcome Fund,** which deploys outcome funding to support **Multiple Outcome-based Contracts**, providing the whole of the outcome funding requirement for those contracts;
- A **Multiple Payer Outcome Fund**, in which funders come together to provide the whole of the outcome funding requirement on a pooled or aligned/co-funding basis to support **Multiple Outcome-based Contracts**;
- A Single Payer or Multiple Payer **Co-funding/Top-up Facility** which provides a proportion of the outcomes funding requirement with a view to crowding-in other outcome funders, such as philanthropic funders, country government, or other donors who have not participated in the co-funding facility. Co-funding/top-up may be particularly relevant where a transition away from a donor relationship is envisaged –

[18] https://inovacaosocial.portugal2020.pt/

such structures can facilitate step down and build commissioning capacity, avoiding cliff edges and smoothing the transition to country government ownership.[19]

In addition:

- Funds can focus on a priority **sector** or sectors. Sector focus supports learning and market development, providing a formal, institutional structure to capture, scale and disseminate knowledge – for instance, around how to define and price outcomes effectively in that sector.
- Alternatively, they can be used to stimulate an outcomes-commissioning **market** in a particular **geography** across a range of sectors. Concentrating funding on a market builds the structures to capture and share knowledge and learning for that market, and build momentum and capacity among local market actors and institutions, including country government.
- Outcome Funds are not limited to supporting Impact Bonds and could include support for other subsidy or enterprise based outcome instruments,

A comparison of the structure, scope and selection process for the UK's Life Chances Outcomes Fund and Portugal Inovação Social is set out in Table 2, which also highlights potential considerations for donors that may be interested to explore such an option.

[19] See also briefing note on Outcome Funds:
https://www.socialfinance.org.uk/sites/default/files/publications/sf_outcomes_fund_note_feb_2018.pdf

Table 2: Design Considerations for Outcomes Funds

Parameter	Life Chances Fund (LCF)	Portugal Innovação Social (PIS)	Considerations for Donors
Amount	£80m	EUR15m (part of total PIS EUR150m funding)	N/A
Fund lifetime	9 years (2016-2025)	5 years (2016-2020)	Long-term – long enough to build durable capacity and support wider market development.
Structure/ management	- Grant held by Big Lottery Fund (non-departmental public body) - Oversight by departmental policy lead	- Funds held by Portugal's managing authority for EU funds (MA). - Administered by PIS, separate entity with autonomous management board.	Will depend on number/identity of donors. Could include e.g. IFI, host government, private sector fiduciary entity
Sectoral focus	Includes addiction; children's services; early years; older people; healthy lives	- Promote outcomes culture in public sector; support projects with proven intervention. - Regional focus	Consider: - Single issue thematic focus *vs.* multiple issues (or, multiple with thematic calls) - Country/regional/global - Fully fund or leverage co-funding
Sourcing and selection process	Expressions of Interest (EOI) →Selected projects make Full Submission →Expert Panel recommendation →Ministerial approval of final decision	EOI or Full Applications (can go direct to Full Application) → Operational and impact assessment by PIS →MA checks eligibility with EU rules →Approval of final decision by PIS management board	Well-structured processes can contribute significantly to capacity building and market development
Support to applicants	Development funding available for bids selected for Full Submission. Capacity building support by nominated provider for promising proposals from inexperienced bidders.	Capacity building grants to purchase external support available. Additional market-based support for bid development (e.g. workshops).	Important but needs to be targeted and structured to support bids and build capacity.
Applications and awards	41 EOI's received for first application round (23 received development funding) ~100 EOIs for latest (last) round	100 EOIs received for first call 9 Full Applications submitted 3 outcome funding awards made New proposals currently under review	N/A

Source: Social Finance internal research (unpublished)

Case Study 2: 'Knowledge Solution' – supporting Impact Bond policy and learning

United Kingdom – *Centre for Social Impact Bonds & Government Outcomes Lab*

The Centre for Social Impact Bonds is a multi-disciplinary team set-up within the UK Cabinet Office in late 2012 to address some of the barriers to developing SIBs, and to promote the development of more and better Impact Bonds.

The Centre for SIBs works to increase understanding of SIBs across government and to provide support to SIB developers. It does this in four ways:

- Increasing awareness and understanding of SIBs through online resources and at workshops and conferences;
- Reducing transaction and set-up costs by developing standard tools such as template contracts;
- Helping SIB developers to estimate cross-cutting benefits by making more data publicly available about the costs to government of providing specific public services;
- Supporting SIB developers by providing strategic advice and analytical support.

In 2016 the Cabinet Office partnered with the Blavatnik School of Government at the University of Oxford to jointly fund and launch an independent centre of academic excellence for innovative commissioning of public services. Through rigorous academic research, the resulting Government Outcomes Lab seeks to deepen the understanding of outcomes-based commissioning and to provide independent support, data and evidence on what works and what does not. Underpinned by its research, the GO Lab also provides practical on the ground support to local commissioners, through a mix of in-person and executive education.

The GO Lab is led by a small team of academics and practitioners, supported by a wider network of Fellows of Practice.

Appendix 1: Definitions

Term	Definition
Advance Market Commitments (AMC)	AMCs use upfront donor commitment to purchase a certain quantity of a product at a specified price. AMCs are often associated with incentivizing vaccine production through the GAVI Alliance.
Budget Support	Direct transfer of funds from a donor to a partner country's budget where they can be managed using national systems.
Cash-on-delivery aid (COD)	COD aid offers a fixed payment to recipient governments for each additional unit of progress toward a commonly agreed-upon goal.
Conditional Cash Transfers	Payments are made to target individuals / households based on meeting pre-agreed conditions (e.g. child vaccination, school enrolment, etc.).
Impact Bonds	Impact bonds encompass social impact bonds (SIBs), development impact bonds (DIBs), and humanitarian impact bonds (HIBs). In all forms of impact bonds, a donor agency or government (referred to as the "outcome funder") commits to pay for improvements in specific and quantifiable outcomes through a pay-for-results contract. Based on this contract, investment is raised from third-party investors as working capital to pay for interventions to deliver results (outcomes). If target outcomes are achieved, the outcomes funder pays the full amount and the investor is repaid its investment with a return. If not, the investor is repaid only part or none of its investment.
Milestone-based payments	Milestone-based payments are a cost reimbursement model that link the disbursements of funds directly to the achievement of specific program indicators.
Output-based aid (OBA)	OBA models link the payment of subsidies to a private operator after the delivery of specific outputs and outcomes—for example, connection of poor households to electricity grids or delivery of basic healthcare services.
Prizes	Prizes provide a cash incentive to motivate external actors to develop innovative solutions to a specific challenge, and allow the funding organization to direct their resources to the best solution that achieves the desired outcomes.

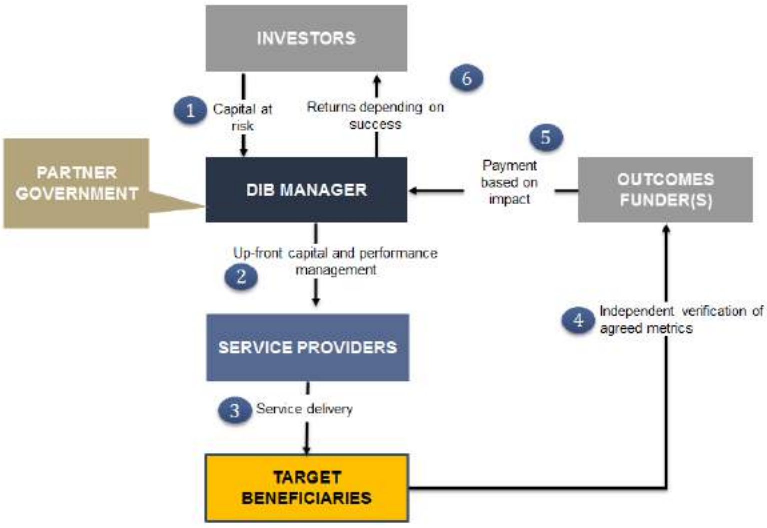
Appendix 2: Typical Impact Bond Structure

Impact Bonds bring together investors and outcomes funders to finance a program that aims to achieve outcomes. The key actors are:

Outcomes funders repay investors if – and only if – the program succeeds in delivering agreed outputs and outcomes. The outcomes funder and partner government (if different) set the fiduciary guidelines that the program must adhere to but do not dictate program delivery. The Outcomes Funder unconditionally committed to paying for verified, agreed results.

Investors provide pre-financing to cover Impact Bond costs. Since outcomes funders only make payments if agreed results are achieved, investors bear the risk of underperformance. Alignment of investor returns to results means provides a strong incentive for investors to support effective oversight and performance management.

Country Governments may play a range of roles. In most cases, governments would work with outcomes funders and others to define the programme, including target population and success metrics. Depending on resources, governments may co-fund outcomes with donors. Governments may also have a role in overseeing contracts with private providers. Impact Bonds could be a way to help improve government capacity to implement outcomes-based contracts, develop robust data systems and scale up successful programmes.



*The **Impact Bond Manager*** oversees the delivery of agreed outputs and outcomes, and liaises with investors. The manager analyses service delivery and output/outcome data continuously, and guides the work of the service providers, shifting resources as needed. The manager is typically remunerated by investors via an annual fixed fee for service alongside a performance-related fee.

Service Providers deliver the intervention, sometimes with a principal service provider playing a coordinating role. It is possible to have only one service provider, although complex delivery problem are more often best tackled by multiple service providers working together. A clear advantage to service providers of the Impact Bond model compares to other results-based models is that the necessary project financing is provided from investors, at risk.

Further Reading

- Balancing Evidence and Risk, *CIFF and Social Finance*
    - https://www.socialfinance.org.uk/sites/default/files/publications/ciff_report_final.pdf
- Impact Bonds in Developing Countries: Early Learnings from the Field, Brookings Institution and Convergence
    - https://www.brookings.edu/research/impact-bonds-in-developing-countries-early-learnings-from-the-field/
- Impact Bond Database, *Social Finance*
    - https://sibdatabase.socialfinance.org.uk/
- LOUD SIB Model, *Government Outcomes Lab*
    - https://golab.bsg.ox.ac.uk/documents/138/loud_sib_model.pdf
- Outcomes Funds, *Social Finance*
    - https://www.socialfinance.org.uk/sites/default/files/publications/sf_outcomes_fund_note_feb_2018.pdf