

**To:** Board Members and David Bean  
**From:** Wesley Galloway, Alec Schon, and Laura Beth Harville  
**cc:** GASB Staff and Meeting Observers  
**Date:** November 9, 2017  
**Re:** Research Memorandum: Social Impact Bonds  
**Att:** Appendix A: Existing Social Impact Bond Arrangements in the U.S.  
Appendix B: Interview Invitation  
Appendix C: Practitioner Advance Materials  
Appendix D: Preparer Advance Materials  
Appendix E: User Advance Materials  
Appendix F: Practitioner Interview Protocol  
Appendix G: Preparer Interview Protocol  
Appendix H: User Interview Protocol

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## **I. INTRODUCTION**

Social impact bonds or SIBs (also called “social benefit bonds,” “social innovation financing,” and “pay-for-success financing”) are a type of public-private partnership arrangement in which a third party provides resources to a government or another service provider to devote to an agreed-upon socially desirable program, such as alleviating homelessness or reducing recidivism among former jail inmates.

The first SIB was initiated in the United Kingdom in 2010. The focus of the highly publicized pilot program was to reduce recidivism rates in the Peterborough Prison. Since the launch date of the “Her Majesty’s Prison (HMP) Peterborough SIB,” 92 SIBs have been initiated worldwide, totaling over \$322 million of capital raised to fund the social intervention programs. In the United States, 16 SIBs have been initiated with an approximate total of \$178 million of capital raised. (Appendix A to this memorandum details in-process and completed SIB programs in the United States as of the completion of the staff’s research.)

In December 2016, the Board approved pre-agenda research to study SIBs. The research objectives were to obtain an understanding of the following:

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- What types of SIB arrangements have been conducted or are being considered
- How governments are reporting SIBs in their audited financial reports, if at all
- Whether that reporting conforms with existing standards and concepts
- What information users need, if any, regarding these transactions.

To achieve these objectives, the GASB staff conducted the following research activities:

- Reviewed relevant GASB literature, as well as literature from international accountancy and public finance professional groups
- Identified SIB transactions conducted by state and local governments in the United States and examined the details of each of the transactions
- Reviewed financial reports of governments that have conducted SIB transactions
- Reviewed professional and academic literature on SIBs
- Conducted telephone interviews with preparers, government officials, resource providers, intermediary organizations, and program evaluators
- Conducted telephone interviews with users regarding their specific information needs, if any, with respect to SIBs.

This memorandum begins with a background section that describes the nature and structure of SIBs. The memorandum then presents the research in Sections III through VI. Section III summarizes relevant GASB and research literature related to SIB arrangements. Section IV details the research questions the staff aimed to address during the pre-agenda research. Section V provides an overview of the research approach and methodologies employed, as well as the limitations of the research design. Section VI presents the results of the research and the GASB staff's analysis of those results.

## II. BACKGROUND

Although a bond instrument typically is not issued,<sup>1</sup> the term “social impact bond” is regularly used to describe these types of arrangements. In addition, although an SIB arrangement operates over a fixed period, SIBs do not offer fixed payments like traditional bonded debt. From the perspective of the government, SIBs resemble a network of service and finance contracts with the various parties involved in the transaction. To avoid misperceptions on the structure of cash flows between the parties, many organizations and governments use the term “pay-for-success contracts” in lieu of “social impact bonds.” (Liebman and Sellman, 2013)

SIB arrangements normally involve the following parties:

- Governments (outcome payor)—state or local government or governments that selects the target group or the issue the arrangement will address, and selects the third-party intermediary in most cases as well
- Third-party intermediary—typically an advisory and performance management firm that focuses on administering social financing arrangements
- Investors/resource providers—senior creditors, subordinate creditors, philanthropic organizations that provide resources to finance a social program
- Third-party service providers—typically a nonprofit organization responsible for providing social services
- Third-party program evaluators—typically an independent party responsible for evaluation of whether performance metrics have been met for the periods specified by the SIB contract
- Treatment persons/groups/factors—persons, groups, or factors targeted by social intervention through participation in the service provider program.

Governments are required to remit payments to investors only if the program achieves predetermined social outcomes. The predetermined social outcomes, or success metrics, serve as triggers for payments to the investors and are derived from the variables that affect the

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<sup>1</sup> The staff identified only one arrangement with marketable bond instruments issued. (Glazier, 2017)

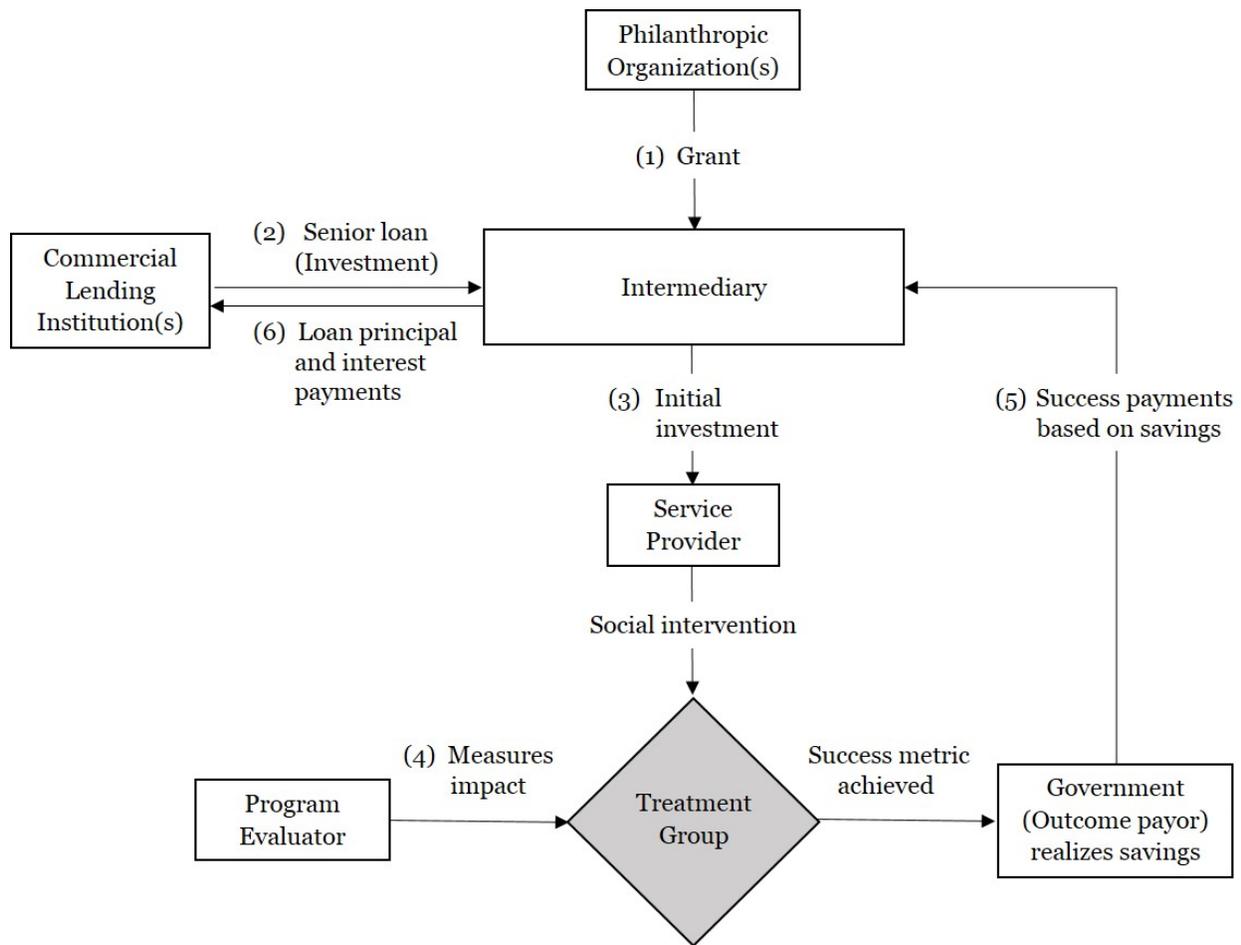
governments' cost of addressing or managing the social issue. (Barclay and Symons, 2013) Strategies for determining appropriate success metrics vary depending on the type of social initiative addressed by the SIB. For example, a success metric for an SIB aimed at reducing homelessness may be the number of months a person in the program is in a stable living arrangement.

Although the idea for the program may be proposed to the government by another entity that may ultimately be the intermediary or service provider, the government entity selects the target persons, groups, or factors to which the social intervention program will apply. Additionally, the government selects an intermediary, likely a not-for-profit organization that specializes in impact investing initiatives. The intermediary typically is responsible for selecting a nonprofit service provider, overseeing the completion of the project, soliciting funds from resource providers, and controlling the flow of resources between the parties of the SIB arrangement.

Resource providers can be investors, philanthropic organizations, or in limited circumstances, the intermediary. (Arena et al., 2015) In a typical SIB arrangement, investors are commercial lenders and philanthropic organizations are not-for-profit charities or foundations. SIB arrangements are structured as private placement under Section 4(2) of the Securities Act of 1933 or in reliance on Regulation D; investors in SIBs are accredited investors under Rule 501(a) of Regulation D. (SEC No-Action Letter, 2014)

Figure 1 illustrates the flow of resources between the parties in one SIB arrangement.

**Figure 1**  
**Sample Flow of Funds in a Social Impact Financing Structure**



Source: Derived from Olson and Phillips (2013)

As illustrated, investors and philanthropic organizations provide resources to the intermediary. The intermediary distributes the resources to the service provider to implement the social intervention program. At various points throughout the term of the project, the independent program evaluator measures and reports on the metrics used to measure the success of social intervention. If the program evaluator determines that the target metrics have been met, the government remits success payments to an escrow account established by the intermediary. At agreed-upon dates, the funds are released from escrow by the intermediary and returned to the

investors as a return on their investment. Depending on the structure of the arrangement, success payments can be remitted at interim points and at the completion of the project.

### **III. LITERATURE REVIEW**

The staff reviewed existing GASB literature on the recognition and measurement of liabilities, including the definition of debt proposed in the Exposure Draft, *Certain Debt Disclosures Related to Debt, Including Direct Borrowings and Direct Placements*. Additionally, the staff examined relevant literature of other standards-setting bodies, including:

- International Public Sector Accounting Standards Board (IPSASB)
- Federal Accounting Standards Advisory Board (FASAB)
- Australian Accounting Standards Board (AASB).

The staff also examined literature from the Chartered Institute of Public Finance and Accountancy (CIPFA), a professional accountancy body for individuals working in public finance in the United Kingdom. This publication discusses the accounting implications for municipalities that engage in SIB arrangements.

#### **GASB Guidance on the Recognition and Measurement of Liabilities**

GASB literature on the recognition and measurement of liabilities is the most relevant source of guidance to examine the obligations a government may have under SIB arrangements.

#### **Definition of a Liability**

A government's obligation to make payments for social programs based on outcomes should be considered in the context of the definition of a liability under GASB Concepts Statement No. 4, *Elements of Financial Statements*. Paragraph 17 of Concepts Statement 4 defines liabilities as "present obligations to sacrifice resources that the government has little or no discretion to avoid." Further, paragraph 18 defines an obligation as "a social, legal, or moral requirement,

such as a duty, contract, or promise that compels one to follow or avoid a particular course of action.” In addition, paragraph 22 explains the following:

For an obligation to be a liability, it should be a present obligation. The event that created the liability has taken place. This distinguishes the item from a commitment that may become a liability in the future when the event giving rise to the liability occurs. The government may be able to withdraw from or avoid the commitment until a future event giving rise to the liability occurs.

### **Contingency Model**

A government’s obligation to make payments for social programs based on outcomes also might be considered in the context of the definition of a contingency under NCGA Statement 4, *Accounting and Financial Reporting Principles for Principles for Claims and Judgments and Compensated Absences*, and GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

Under this guidance, a government’s obligation to make payments under an SIB arrangement might be considered a claim based on contractual actions. Further, if the obligation meets the definition of a liability, it may meet the criteria for recognizing a liability if it is *probable* that a loss has been incurred and the amount of the loss is estimable. A contingency should be disclosed if it is *reasonable possible* that a loss has been incurred and the amount of the loss is estimable. Disclosure also may be required for certain *remote* contingencies that have the characteristics of guarantees.

### **Nonexchange Financial Guarantee Model**

Another approach for liability recognition is found in Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. Under that Statement, a liability is recognized when qualitative factors and historical data indicate that it is more likely than not that a government will be required to make a payment related to a nonexchange financial guarantee it has extended for liabilities of another entity or individual.

## **Definition of Debt**

A government's obligation to make payments for social programs based on outcomes also might be considered in the context of the definition of debt proposed in paragraph 4 of the Exposure Draft, *Certain Debt Disclosures, including Direct Borrowing*, issued in June 2017:

4. For purposes of disclosure in notes to financial statements, debt is defined as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of payment of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. For disclosure purposes, debt does not include leases or trade accounts payable. [footnote excluded]

An SIB would not meet this definition unless one or more payments were fixed at the date the contract is established. Some SIBs do establish minimum amounts required to be paid.

## **Guidance of Other Accounting Standards Setters**

The staff confirmed with members of the IPSASB, FASAB, and AASB that there are no current or proposed projects specifically relating to accounting and financial reporting for SIB agreements. In addition, staff of the CIPFA noted that the IASB revenue recognition guidance superseded the previous CIPFA guidance (discussed next) for SIB agreements and that there is no current or proposed project to further address SIBs.

## **CIPFA Report on Payments-by-Results Contracts**

The CIPFA issued a publication that outlines the recognition and measurement of liabilities from the perspective of the government outcome payor under payments-by-results contracts, including SIBs, as well as the recognition of income from the perspectives of the other parties involved in the arrangement. (Mason and Maddocks, 2012) The publication predates the issuance of IFRS 9, *Financial Instruments*, and IFRS 15, *Revenue from Contracts with Customers*, and has been superseded by that guidance. However, the publication's conclusions relating to the recognition and measurement of liabilities from the outcome payor's perspective still are relevant.

The authors believe that the economics of the transaction are best captured under IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*.<sup>2</sup> Under IAS 37, a provision (liability) should be recognized when the following conditions are met:

- An entity has a present obligation (legal or constructive) as a result of a past event
- It is probable (greater than 50 percent likelihood) that an outflow of resources embodying economic benefits will be required to settle the obligation
- A reliable estimate can be made of the obligation.<sup>3</sup>

Judgment would be required to determine if the obligations for payment under a payments-by-results arrangement meet the criteria to be recognized in the entity's financial statements. If it is not probable that payment is likely or a reliable estimate cannot be made, the entity may determine it is appropriate to disclose the nature of the obligation.

## **Academic and Other Research Publications**

The staff reviewed academic and other professional research to understand common development and implementation procedures for SIBs. The process by which SIBs are developed and implemented provides insight regarding (1) a government's motivations for entering into an SIB agreement and (2) the nature of the cash flows between parties. The staff noted several recurring themes, as discussed below.

### **SIBs as a Method to Generate Innovation in Social Services and Cost Savings**

Proponents of SIBs argue the arrangements help governments and nonprofits foster innovative social interventions, while shifting funding risk to investors. Some proponents also believe that nonprofit service organizations can more effectively utilize resources to sustain the program for future years, thus minimizing the cost of sustaining the social invention in the future (Barclay

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<sup>2</sup> The IPSASB adopted IAS 37 as IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*. The United Kingdom currently applies IASB standards.

<sup>3</sup> IAS 37 uses the term 'contingent liability' for liabilities that do not meet recognition criteria.

and Symons, 2013). SIB models focus on the outcomes of a social service program, not the inputs needed to develop and sustain such program. A successful program indicates that the program can be relied upon as a less-costly and proven social intervention that can be continued in future periods. The theorized advantage of utilizing the SIB model is that governments realize cost savings during both the initial execution of the program and in subsequent periods when the program is continued. In essence, a successful SIB arrangement is a self-financing program through a government's realized future cost savings—the cost savings are used as the foundation to pay back investors.

Skeptics of the SIB model have raised concerns that the costs to structure and negotiate the terms of these programs exceed the anticipated financial benefits. With respect to the first SIB (Peterborough, UK), critics hold that the program was too small to deliver substantial monetized benefits. (Disely et al., 2015) Regarding SIBs as a tool to facilitate innovation in social services, critics claim that these projects are narrowly scoped and difficult to replicate with a larger population. Furthermore, critics assert that there is no true budgetary relief because governments still allocate payments as if the maximum outcome payment will be due. Another criticism of the SIB model is that it shifts funding away from direct interventions that may be more effective in achieving a desired social outcome. For instance, governments can achieve reductions in recidivism rates by encouraging post-release employment opportunities. One way to achieve this would be to institute laws to shield nonviolent criminals from employment discrimination. (McKay, 2013; Cohen and Zelnick, 2015)

### **Development and Implementation of Success Metrics**

Determining what constitutes a fair and indicative success metric often is a costly task and is the most contested aspect during the SIB development process. Although government cost accounting systems may provide baseline cost information about certain programs, these systems may not provide enough detail or the level of accuracy needed to formulate reliable success metrics in a SIB project. (Hatry et al., 2017)

The first SIBs utilized a *direct cost savings approach*, which uses a government’s cost savings as a baseline to determine the amount investors will be repaid. As discussed next, there are two types of success metrics used under the direct cost savings approach, depending on whether a government has cost information available related to a similar program before entering into the SIB arrangement.

If a prior program was implemented by the government, cost savings are measured as the difference between the government’s “would be” budgeted amounts and the cost of the service provider developing and implementing the program, as a baseline to determine the amount investors will be repaid. Investors will earn the government’s cost savings if the service provider can deliver services below the government’s normally budgeted amounts. This methodology is utilized in one program identified in the research (Hatry et al., 2017).

In the more likely circumstance in which a government does not have cost information available relating to a similar project, cost savings are determined by a government’s realized decrease in costs that are affected by the aim of the SIB project. For instance, a SIB project aimed at reducing homelessness might be tied to Medicaid costs: A realized decrease in Medicaid costs triggers a payment from the government to the investors.

Most SIB projects to date have applied an *indirect cost savings approach*—also known as a *rate card approach* or *outcomes-specific approach*—to determine the appropriate success metric. Under this approach, the success metrics are developed to reflect the mission of the project. For instance, two programs identified in the research use special education avoidance as a success metric because decreased use of special education services will generate future cost savings for the respective governments. (Hatry et al., 2017)

The indirect cost savings approach could utilize relative or absolute success metrics. A relative success metric would utilize randomized controlled trial techniques to link outcome payments to the success of a treatment group (individuals receiving the benefits of the SIB program) against the success of a control group. An absolute success metric measures success on a person-by-

person basis—an individual achieving the desired outcome from the SIB program would trigger a success payment to resource providers.

SIBs may utilize various success metrics to determine the success of the project. For instance, one program identified in the research measures four different success metrics, each requiring different levels of payment if the measure has been achieved.

### **Outcome Payment Structure**

In addition to guidance for developing SIBs and determining appropriate success metrics, the literature suggests that state and local governments negotiate a maximum payment amount. Instituting a limit on the amount a government may need to remit reduces the risk of not appropriating enough funds to pay investors if the SIB program is fully successful. Except for one program identified in the research, the maximum payment amounts are explicit in the financing contracts between the governments and investors.

In most cases in the United States to date, governments have not remitted the maximum amount of outcome payments throughout the duration of the project. Generally, governments provide periodic outcome payments to an escrow account to fund future outcome payments. Those funds are released from the escrow account to the intermediary organization according to a predetermined payment schedule. Figure 2 illustrates the payment schedules for the a program identified in the research. Investors receive outcome payments at specified dates or when certain success metrics are achieved following the issuance of progress reports by the independent evaluator.

**Figure 2**  
**Example Success Metrics and Corresponding Outcome Payments**

| <b>Reduction in Re-Admission Rate</b> | <b>Projected Long Term Net Savings</b> | <b>City Payment to Intermediary</b> |
|---------------------------------------|----------------------------------------|-------------------------------------|
| ≥ 20%                                 | \$20.5 million                         | \$11.7 million                      |
| ≥ 16%                                 | 11.7 million                           | 10.9 million                        |
| ≥ 13%                                 | 7.2 million                            | 10.3 million                        |
| ≥ 12%                                 | 6.4 million                            | 10.2 million                        |
| ≥ 11%                                 | 5.6 million                            | 10 million                          |
| ≥ 10%                                 | 1.7 million                            | 9.6 million                         |
| ≥ 8%                                  | 1 million                              | 4.8 million                         |

Source: Derived from Olson and Phillips, 2013

### **Accounting for Outcome Payments**

RAND Europe, a nonprofit research organization that examines public policy initiatives, monitored the HMP Peterborough SIB throughout the five-year life of the project. The organization issued three reports, each at a different phase of the project’s implementation, describing the findings of the project. (Disley et al., 2011) During the second phase, the researchers inquired of the accountants at Ministry of Justice, the government payor, how outcome payments are accounted for and reported. The accountants stated that outcome payments may be disclosed in notes to financial statements as a contingent liability and that adjustments will be made accordingly following reports on the achievement of the predetermined success metrics. (Disley and Rubin, 2014)

The report does not clarify if adjustments are made to the disclosure or measurement and recognition of the contingent liability if the progress reports indicated the *likelihood* of achieving the success metric or if the success metric already had been reached.

The researchers also interviewed a representative from the HM Treasury, the British government department responsible for setting the direction of the United Kingdom’s economic policy. The representative stated that reporting outcome payments as contingent liabilities may not be applicable if implemented on a larger scale. (Disley and Rubin, 2014)

## **Examination of SIBs in Different Focus Areas**

Intermediary organizations have issued publications that address the issues unique to developing and implementing SIBs in different focus areas, such as criminal justice and homelessness. These publications provide a deeper analysis in determining the appropriate success metrics and length of project, among other project-specific attributes, based on the type of SIB. Governments also have utilized the websites of the Coalition of Evidence-Based Policy’s “Social Programs that Work” and the Washington State Institute for Public Policy to identify proven programs that could be repeated or enhanced by a SIB. (Liebman and Sellman, 2013)

## **Federal Legislation Related to SIBs**

There are several pieces of legislation pending at the federal level, each with the goal of focusing federal programming and resource allocation on evidence based policies. The staff includes this discussion because, in most cases, the proposed legislation affects state funding of social programming. Ongoing legislation at the federal level includes the following:

- S. 963 and H.R. 576, Social Impact Partnership to Pay for Results Act—comprehensive pay for success bill that would direct federal resources to states and local communities to support pay for success arrangements. This bill was introduced in the 113<sup>th</sup> and 114<sup>th</sup> Congresses (2013–2017).
- H.R 2824, Increasing Opportunity through the Evidence-Based Home-Visiting Act—legislation introduced in June 2017 that reauthorizes the Maternal, Infant, and Early Childhood Home Visiting Program using the pay-for-success model to allocate dollars. The House passed the bill in September 2017. A similar bill was introduced in the Senate, but a current timeline for moving forward is not available.
- S. 1730, Reach Every Mother and Child Act of 2017—legislation focused on ending preventable maternal, newborn, and child deaths globally by using the pay-for-success model. The bill was introduced in the Senate in 2017, but a current timeline for moving forward is not available.

## **IV. RESEARCH QUESTIONS**

The aim of this pre-agenda research was to collect information to help the Board determine if specific guidance is needed for SIBs and, if so, to establish standards. The research proposal identified the following questions to be considered:

- Do SIBs meet the definition of a liability that should be recognized in the financial statements?
- Are SIBs a contingent liability that should be disclosed in the notes to the financial statements? If so, what criteria should be applied to determine when recognition should occur?
- What information do financial statement users need regarding these transactions, their payment provisions, and the likelihood that a government will have to make a payment?

## **V. METHODOLOGY AND LIMITATIONS**

The objectives of interviews with practitioners and preparers were to understand the following:

- The types of SIB arrangements that have been entered into or are being considered by the individual's organization/government
- The features of existing SIB arrangements
- Recognition, if any, of SIB arrangements in the audited financial statements and how that reporting relates to existing reporting standards and concepts
- Individual's perception of the potential risks, if any, involved with these types of transactions.

The objectives of interviews with users were to understand the following:

- Individual's understanding of SIBs, and the level of interest in these arrangements with respect to their work
- Individual's views on the usefulness of information about SIBs to their work

- Individual's perception of the potential risks, if any, involved with these types of transactions.

## **Selection of Interviewees**

The project staff identified potential interviewees from the GASB stakeholder database and from articles, reports, and research papers. Twenty-six potential interviewees were invited to participate by email, with follow-up telephone calls if necessary. (The text of the invitation is presented in Appendix B to this memorandum.) Interviewees were provided materials in advance of the interview date that included a description of the objectives of the pre-agenda research and the questions that would be asked during the interview. (The advance materials can be found in Appendices C–E.) individuals were invited by email to be interviewed. One preparer and three practitioners declined to participate in a research interview, however, they answered selected questions from the interview protocol, emailed to them in advance of the interview. Those responses are reflected in the staff's analysis of the feedback received regarding SIB arrangements.

Two other individuals preferred responding to the interview questions in the interview protocol via email. Two of those responses were accepted because the project staff concluded the response was sufficient for achieving the interview objectives.

Interview protocols and other materials were developed in accordance with the provisions of the GASB's Research and Technical Activities (RTA) Manual. The interviewees were provided with advance materials by email prior to the interview. Those materials described the rationale for the research and presented the questions that would be posed.

The staff interviewed by telephone or received sufficient email responses from practitioners associated with SIBs and financial statement preparer and users during June–September 2017. (The interview protocols can be found in Appendices F–H.) Table 1 presents the number of individuals interviewed from each constituent group.

**Table 1**  
**Interviewees by Constituent Type**

| <b>Constituent Type</b>       | <b>Number of Interviews</b> | <b>Percentage of Interviews</b> |
|-------------------------------|-----------------------------|---------------------------------|
| Practitioner                  |                             |                                 |
| Intermediary                  | 6                           | 27%                             |
| Investor                      | 1                           | 5%                              |
| Third-party program evaluator | 1                           | 5%                              |
|                               | <b>8</b>                    | <b>36%</b>                      |
| Preparer                      | 5                           | 23%                             |
| User                          |                             |                                 |
| Oversight                     | 1                           | 5%                              |
| Bond industry                 | 3                           | 14%                             |
| Citizen and advocacy          | 5                           | 23%                             |
|                               | <b>9</b>                    | <b>41%</b>                      |
|                               | <b>22</b>                   | <b>100%</b>                     |

### **Limitations to the Methodology**

There are limitations to the methodology used in this research. Although a variety of stakeholders were interviewed, there are other types of stakeholders—and other stakeholders of the types included—who may be interested in this research subject. Those stakeholders, as well as the stakeholders who were invited to participate but declined, may have different views from those interviewed. Finally, the interviewees were not selected using a random process, nor were the findings statistically tested. Because the staff did not interview stakeholders associated with all of the SIBs identified, the results of the telephone interviews may not represent the complete population.

## VI. RESULTS AND ANALYSIS

Based on the interviews and a literature review conducted as part of the pre-agenda research, the research staff noted the following factors pertinent to consideration of a potential project on SIB arrangements:

- The preparers interviewed generally view their obligations under SIB arrangements as being immaterial at present.
- Although the preparers interviewed view their obligations under SIB arrangements as contingent liabilities, only one preparer's government disclosed a SIB-related contingent liability.
- The number and size of SIB projects do not appear to be gaining significant momentum at this time.
- Perhaps as a consequence of these factors, the research staff was not able to locate general purpose financial statement users who currently use information about SIB arrangements in their work. Rather, external users of SIB information currently appear to be limited primarily to resource providers. The resource providers are interested in whether success metrics that trigger payments have been met. That information is provided in third-party evaluators' progress reports.

The following discussion is organized by the source of the information—archival research and telephone interviews.

### Archival Research

The staff examined the most recently issued financial reports reflecting financial reporting disclosures by governments engaged in SIB transactions.<sup>4</sup> Existing disclosures, to date, are shown below.

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<sup>4</sup> The staff notes that only one SIB project has been completed by the date of this report. The staff reviewed the most recent (2016) Comprehensive Annual Financial Report (CAFR) of the city for

## County Government

*13.3 Pay for Success Commitments*—In December 2016, the County entered into a pay-for-success contract for criminal justice and homelessness initiatives. Pay-for-success contracting allows the County to commit to measurably improving outcomes for at-risk populations in the County by 1) implementing performance-based contracting that shifts performance risk for social programs to the private sector, 2) building capacity for local non-profit service providers, 3) holding service providers more accountable using data-driven performance evaluation, and 4) creating mechanisms which allow the County to discontinue inefficient service programs.

Initial funding for the initiatives is from private investments, grants, and donations. The County can become obligated for successful outcomes at a maximum of \$6.0 million for the criminal justice program and \$5.6 million for the homelessness program. Outcomes are measured by comparing program participants against a control group. Measurement of success will begin after pilot periods which run thorough 2017. Thereafter, measurements will be made every six months. As target outcomes are achieved, the County will transfer agreed-upon amounts to an escrow account. The majority of transfers to the escrow account are to be made after the fourth and sixth years of the programs. Disbursements from the escrow account will be paid to investors at the end of each program.

The County will record expenditures in the governmental funds as payments to the escrow account as they become due. For the government-wide financial statements, liabilities and related expenses will be recorded based on success measurements and the likelihood payments to the escrow account will eventually be required.

## State Government

### *F. SOCIAL IMPACT BONDS*

In January 2014, the Commonwealth entered into a “pay for success contract” (“Social Impact Bonds”) with a nonprofit intermediary organization and a nonprofit social service agency to reduce the recidivism rate of young men in the juvenile justice system or on probation. The Commonwealth is obligated to make success payments totaling \$28 million through calendar year 2019 and the Commonwealth’s obligation to make such payments is a general obligation for which the Commonwealth’s full faith and credit are pledged. Payments are only made based upon successful achievement of specified outcomes based on defined performance targets contained in the contract. The Commonwealth entered into a second such contract in December 2014 to address chronic individual homelessness. The contract obligates the Commonwealth to make up to \$6 million in success payments, in the aggregate, through fiscal 2021. In June, 2016 the Commonwealth entered into a third contract to assist individuals in Adult Basic Education (ABE) or English for Speakers of Other Languages (ESOL) programs to transition to employment, higher wage jobs, and higher education. The contract obligates the Commonwealth to make up to \$15 million in success payments, in the aggregate, through fiscal 2023. The total amount of payments backed by the full faith and credit of the Commonwealth under such contracts may not exceed, in the aggregate, \$50 million. As the amount required to be paid as of June 30, 2016 cannot be determined until performance targets have been achieved as determined by independent evaluators, no liability has been accrued in these financial statements for these contracts.

information about this SIB. No information was included, likely due to the transactions small size relative to other financial statement elements.

## Water and Sewer Authority

### **(b) Subordinate Debt**

Payments of the Authority's subordinate debt are made after payments of senior debt and after certain reserves have been funded (see "Bond Covenants" below).

In September 2016 the Authority issued \$25,000 of tax-exempt public utility subordinate lien revenue bonds, 2016 Series B (Environmental Impact Bonds) (the "2016 Series B Bonds"). The 2016 Series B Bonds are multimodal variable rate bonds, initially issued bearing a 3.43% fixed rate through the mandatory tender date, April 1, 2021. The net proceeds (after payment of \$472 of issuance expenses) of \$24,528 of the 2016 Series B Bonds will be used for construction of green infrastructure (GI) in Rock Creek Project A (RC-A). The GI practices are designed to mimic natural processes to absorb and slow surges of stormwater during periods of heavy rainfall, reducing the incidence and volume of combined sewer overflows (CSOs) that pollute the District's waterways. The 2016 Series B Bonds are designated

### **(11) Long-Term Debt (Continued)**

as Environmental Impact Bonds and, as such, include provisions for the possibility of an Outcome Payment by the Authority to the Original Purchasers of the 2016 Series B Bonds of \$3,300 in the event of a runoff reduction greater than 41.3%, and for the possibility of a Risk Share Payment by the Original Purchasers to the Authority of \$3,300 in the event of a runoff reduction less than 18.6%. Runoff reduction means the percentage reduction of storm water runoff in RC-A per impervious acre treated to manage the volume of runoff produced by 1.2 inches of rain as compared to the existing conditions runoff in RC-A as defined in the Private Placement Agreement between the Authority and Original Purchasers. The potential obligation of the Authority to pay the Outcome Payment is an unsecured obligation. No provision has been included in these financial statements for the potential obligation related to the Outcome Payment due to the uncertainties surrounding the effectiveness of GI in RC-A, which will be independently assessed prior to the mandatory tender date.

The county disclosure presented above was included in the Construction and Other Significant Commitments note. Similarly, the State disclosure presented above was included under Commitments and Contingencies. The Water and Sewer Authority disclosure presented above was included in the Long-Term Debt note.

## Telephone Interviews

The pre-agenda research identified 16 SIB projects that are or were actual or potential liabilities of states, counties, large cities, and a special-purpose government engaged in water-quality activities. SIB projects have not involved small governments (Phase 3 governments) thus far. Some of these arrangements have terminated and others are ongoing.

## **Practitioner Interviews**

The first group of individuals the staff interviewed were non-government parties to SIB projects (practitioners). The following sections present general themes identified from those interviews.

### *Structure of SIBs*

The following questions related to the structure of SIB arrangements were asked during practitioner interviews:

- What SIB arrangements have you entered into or plan to enter into?
  - How was the arrangement structured (or, how will it be structured)?
  - Who initiated the arrangement?
  - What payment(s) could the government be required to make?
  - What are the conditions for requiring payment(s)?
    - What legal or financial documents describe the details of structures and obligations?
  - Is there a formal offering statement?
- Are there grant agreements (for example, with a foundation)?
- If the arrangement involved issuing debt, do the debt instruments trade?

According to the interviewed practitioners, the government normally initiates a SIB project by issuing a request for proposal (RFP) to intermediary organizations. The intermediary typically issues its own RFP to local not-for-profit organizations that are involved with the social issue the government is attempting to address. Similarly, the intermediaries typically contract with another organization to serve as the third-party program evaluator. The research found one instance of a government both initiating an SIB project and providing intervention services to the treatment group. That SIB, nevertheless, used an intermediary to administer the contract and select a third-party evaluator.

Many of the responses to the question about what payments the government could be required to make focused on the formulation of the success metrics. The interviewees confirmed that the

success metrics have evolved from the direct cost savings approach to an outcomes-specific approach (indirect cost savings approach). Some interviewed intermediaries stated that accumulating the necessary data to objectively state that the government realized cost savings was unattainable using the direct cost savings approach. The outcomes-specific approach more clearly establishes if a program is successful because the metrics tied to outcome payments are directly observable. However, the challenge with the outcomes-specific approach is that it is difficult to estimate the government's realized cost savings for a successful outcome. For instance, parties to an SIB project aimed at reducing homelessness may need to negotiate what the success payment will be when a target person achieves sustainable housing for the specified length of time.

The contract between the intermediary and the government details the structure of the government's obligations under SIB arrangements. A related contract between the intermediary and the resource provider(s) establishes the investment and grant amounts to be provided. Additionally, the intermediary has a contractual agreement with the service provider and program evaluator that describe each of the party's roles and responsibilities for the SIB project.

As previously stated, typical SIBs are not in the form of traditional bonded debt and are not traded in the market. The one exception is structured as a traditional bond with variable interest payments tied to decreases in water runoff.

### *Risks to Governments and Resource Providers*

Practitioners were asked the following question related to the perceived risks to governments: What risks, if any, do you believe the government is exposed to from these transactions?

Interviewed practitioners identified recognition risk and pricing risk as risks to governments. These risks relate to the obligations for payments in an SIB arrangement. Recognition risk is the risk of a statistical type 1 error: the program evaluator assesses that a success metric has been achieved when, in fact, it was not achieved. Pricing risk relates to the value assigned to an achieved success metric and its relationship with a government's cost savings. Governments risk

overpaying for a successful outcome because the value assigned to an achieved success metric is an estimate (not actual amount) of a government's cost savings.

Some interviewees stated that an additional risk governments face is reputational/political risk. One interviewee stated that some constituents commented that SIB programs could serve as a mechanism to privatize certain governmental functions.

Several practitioners commented on the resource providers' appropriations risk. For most SIB arrangements, payments are not protected by legislation that requires the government to appropriate and remit payments to an escrow account to fund outcome payments. Only one government examined in the research pledged the full faith and credit of the entity to fund SIB obligations.

#### *Motivations for Resource Providers and Governments to Enter SIB Arrangements*

The following questions relate to the motivations of the various parties for entering into SIB arrangements: What questions, if any, are you receiving about these transactions? Who is asking these questions?

Intermediaries interviewed stated that a common question they receive regarding SIBs relates to the Community Reinvestment Act (CRA). Commercial lending institutions have inquired as to whether the upfront capital to fund a SIB program would satisfy the institution's obligations under the CRA. According to an interviewed investor, these loans do satisfy the requirements of the CRA.

#### *Future Use of SIBs*

The following question relates to the expectations regarding future SIB use and implementation: What is the potential trend on SIB arrangements?

The staff received mixed responses on expectations for the use of SIBs in the future. One representative of an intermediary organization asserted that they are communicating with governments daily to perform feasibility tests on potential SIB projects. Other interviewees,

however, expressed that they do not expect these programs to increase at the rate originally expected. These interviewees stated that the time to develop and high transaction costs of these program have inhibited widespread use of SIBs.

Some interviewees expressed that governments became wary of these programs during the feasibility testing phase when conducting the cash flow analysis for the government. Some governments initially believed that SIBs would relieve cash flow and budgetary pressures; however, intermediaries and resource providers often require the government to remit periodic payments to an escrow account to fund outcome payments, resulting in little or no cash flow relief.

### **Preparer Interviews**

The staff interviewed individuals from five governments engaged in SIBs. The following sections present general themes identified from those interviews.

#### *Risks Associated with SIBs*

The following questions related to how risks associated with SIBs are reported, if at all, were asked during preparer interviews:

- What risks, if any, do you believe the government is exposed to from these transactions?
  - How are those risks reflected in the financial statements—on the face of financial statements, in notes to financial statements, or in MD&A?

In preparer interviews, a common response to questions about the accounting and financial reporting for SIB arrangements was that the transaction was immaterial to the government's financial statements. Due to the limited size and scope of SIBs within each government, most of the governments did not consider financial disclosure in the form of a contingency or other type of liability. Instead, most arrangements were accounted for as service contracts, with payments to investors recorded as expenditures in the year incurred. When asked if current guidance was sufficient for accounting for SIB arrangements, most preparers responded that they did not

consider contingency or other types of liability guidance because they believed the transactions were appropriately treated as expenditures as incurred. The following representative comments illustrate the principal responses:

This is a small pilot project to determine if this program is effective and if it should be replicated across the state. Recognition in the CAFR would occur only if the program expanded to the point that it would have the potential to be a material expense to the State.

\* \* \*

Performance metrics and reporting requirements have been identified and agreed upon between the State and the nonprofit vendor. The metrics report will indicate if and when payment milestones have been achieved.

\* \* \*

While these results may not represent the entire population of governments involved in SIB transactions in the United States, the project staff has no reason to believe the SIB arrangements entered into by the governments interviewed were substantially different from the SIBs not represented in the interviews. (See Appendix A for information regarding maximum outcome payment amounts for all SIBs in the United States.)

### *Recognition Point*

The following questions related to the recognition point in the financial statements were asked during preparer interviews:

- How has your government reported the agreements (for example, in the financial statements as debt, provisions, or grants; in notes to financial statements; or, not at all)?
  - What issues have arisen in determining whether and how to recognize and measure the transaction?
  - What challenges did you face in determining whether the metrics of success that may trigger payment have been met?
  - [If disclosed in the notes:] What was disclosed and why?

[If the arrangement was not recognized in any manner on the face of the financial statements (whether not reported at all or only disclosed in notes to financial statements):]

- What additional event would cause these transactions to rise to the level of recognition?

[If the arrangement was not reported in the audited financial report:]

- Why not?

Preparer responses to questions about recognition of repayment obligations indicate that, if a government were to report a contingent liability for payments in an SIB arrangement, the amount of the liability would be disclosed in the notes to financial statements rather than recognized as a liability in the financial statements. In one case, the preparer determined that the recognition of an estimable liability was not appropriate because, at the date of the financial statements, parties in the arrangement had not yet determined if the required performance metrics had been met. Principal responses from preparer interviews are represented by the following:

The Social Impact Bonds are currently only disclosed in the Contingencies/ Commitments footnote in the FY16 CAFR as the potential liability cannot be accrued as it was not determined if the required performance targets were achieved.

\* \* \*

They [third party intermediary] have an economic forecast...for how they anticipate [performance metrics] to be met, and in what quarter, and how the expenses line up. Our plan now is to use their forecast with, depending on how it's coming out, to decide how we recognize our expenditures for [the payment as a whole] and reasonably allocate those in the government-wide statements over the three years as they're earned.

We were looking at it like a contingent liability...right now you don't have a liability until they've met the metrics. We're trying to figure out how realistic that is...We're probably going to involve some of our attorneys in looking at it in the same way they help us evaluate our other contingent liabilities. The most recent conversation we had with our external auditors was related to the balloon payment and how to allocate that to the period where the services provided and where the progress was made. I think we all [project committee, external

auditors] agree that we'll probably have a little bit of an indication before the final measurement period which way it's going to go.

\* \* \*

### *Use of GASB Guidance*

The following questions related to the use of GASB guidance were asked during preparer interviews: What financial reporting guidance did you consider related to SIBs? Is that guidance sufficient?

Overall, preparer feedback did not find issues with the applicability of current liability guidance to payments made to service providers in SIB arrangements. Depending on the materiality of the transaction to the government, payments made in SIB arrangements are recorded as expenditures related to a service contract or disclosed as a contingency, but not accrued as a liability in the financial statements.

Although most preparers interviewed expressed that they did not experience challenges in determining the appropriate accounting treatment for payments made in an SIB arrangement, there was at least one exception. One interview was conducted before the government had decided on an accounting treatment. Through this interview in particular, the project staff was able to gain an understanding of the deliberation process involved between the government's SIB project committee, financial reporting team, external audit team, and legal support in accounting for the payments under the SIB arrangement. In this case, the interviewee (from the financial reporting team) articulated that the team was considering contingency guidance as well as a "more likely than not" threshold when determining the recognition point for performance based payments.

### **User Interviews**

Overall, user interviews were structured to obtain feedback from users of governmental financial statements on the usefulness to their work of information related to SIB arrangements and what kind of information about SIBs users would seek in the future.

The staff interviewed nine users from an oversight body, bond industry firms, and citizen and advocacy groups.

The staff was not able to locate general purpose financial statement users who currently use information about SIBs in their work. Rather, external users of SIB information currently appear to be limited primarily to resource providers. The resource providers are interested in whether success metrics that trigger payments have been met. That information is provided in third-party evaluators' progress reports.

#### *Relevance to Work*

The following questions related to the relevance of SIB arrangements were asked during user interviews:

- 1) What information have you seen about pay for success programs or social impact bonds?
- 2) How useful is that information to your work?
  - a) How have you used that information in your work?

Users generally responded that these arrangements are currently immaterial or irrelevant. Legislative and citizen/advocacy group users expressed interest in learning more about SIB arrangements; however, these users stated that they are not concerned about related disclosures in the financial statements due to the relatively small size and scope of these arrangements. A bond industry user stated that, in the rare case that these arrangements do contain an actual bond instrument, they would want information on the impact of the expected interest payments on financial ratios. The user appears to believe that, even if the arrangement itself is not material to the financial statements, the expected interest payments on the bond may have a material impact on the government's financial ratios.

#### *Future use of SIBs*

The following questions related to the future use of SIB arrangements were asked during user interviews:

- What types of risks do you think these transactions may pose to the governments involved, if any?
- If pay for success programs or social impact bonds become more common, would information about these transactions become more valuable to your work?
  - What kinds of information about pay for success programs or social impact bonds would become more valuable to your work?
  - How would you use that information in your work?

Some users interviewed, including one from an oversight body, articulated their belief that SIB arrangements were unlikely to be profitable or effective transactions for governments to engage in, even in the future. This speculation is primarily based on the high transactional costs of initiating SIB arrangements and the misalignment of investor and government interests with respect to risk sharing and cost savings. In contrast, other users interviewed expressed hope that, as SIB arrangements become more widely used, transactional costs may decrease as the number of successfully implemented programs achieve scalability.

### *Accountability Concerns*

The following questions related to additional information about SIB arrangements were asked during user interviews:

- What other information, if any, do you need about pay for success programs or social impact bonds?
  - How would you use that information in your work?

Some users interviewed expressed an interest in the disclosure of success metrics of the arrangement and the related maximum payment obligations if a project is determined to be successful. Some users from legislative and citizen/advocacy groups expressed interest in understanding results of success metrics for tracking the effectiveness of social intervention by the government. Others expressed interest in information about a government's obligations under a SIB arrangement for the purpose of maintaining financial transparency to the public.

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## APPENDIX A

### Existing Social Impact Bond Arrangements in the U.S.

Information for this table was derived from:  
<http://www.socialfinance.org.uk/database/> (Last updated July 2017)

| <b>Project Overview</b>                                                                                                                                                  | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | <b>Performance Outcomes</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Launched in Jan 2013, this 3 year project seeks to reduce juvenile recidivism. The project has raised 9.6M from investors with maximum outcome payments of 11.7M.</p> | <p>The Young Men’s Initiative, a citywide initiative, developed the Adolescent Behavioral Learning Experience (ABLE) intervention. ABLE provides Moral Recognition Therapy, an evidence-based intervention that focuses on improving social skills, personal responsibility, and decision making. It consists of cognitive behavioral therapy and counselling, training, and educational services delivered to adolescents before release from jail. There was a single outcomes metric for this Pay for Success initiative, a reduction in ‘recidivism bed days’ (RBDs) for the intervention group compared to a matched historical group. This measure captures the number of days participants are held in jail during the 12 months following their release. For investors to receive an outcome payment, each yearly cohort had to reduce RBDs by 10% compared to the matched historical group, with returns increasing incrementally with performance up to a cap of \$11.7M at a reduction in RBD rate of 20%.</p> | <p>In the first year of this Pay for Success initiative, the majority (87%) of adolescents that entered jail attended at least one session ABLE session. However, the fall in recidivism for eligible 16-18-year olds was not statistically significant when compared with the comparison group and so did not meet the pre-defined threshold of a 10% reduction in recidivism days. The Pay for Success initiative was therefore discontinued as of August 31, 2015, meaning no payments were made to investors, thus triggering Philanthropies’ \$6m guarantee paid by a philanthropy entity.</p> |

| <b>Project Overview</b>                                                                                                                                                                          | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | <b>Performance Outcomes</b>                                                                                                                                                                                                                                                                                                                                                                                                        |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Launched in September 2013, this 7 –-year project supports education and early year development in children. This project has raised 7M from investors, outcome payments are undisclosed.</p> | <p>The intervention is the 'High Quality Preschool Program' lasting 1 or 2 years. This is a locally-designed, structured preschool model, and is delivered in public schools and by a number of private providers to improve school readiness and academic performance. There is one outcome metric - decrease in the use of special education in K-6. At the beginning of the pre-school program, participants are given the Peabody Picture Vocabulary Test, a strong predictor of future need of special or remedial education. Those children scoring 70 or less enter the 'payment' cohort; the payment cohort is at-risk of needing special or remedial education at some point in their education in the absence of the intervention. These students are then tracked through 6th grade to determine if they use special education services, with investors receiving a payment for every year that special education is avoided.</p> | <p>Of the first cohort of 595 four-year old's, 110 tested as likely to need special education services. At the end of these students' kindergarten year, only one out of the 110 required special education. This resulted in a total savings for Cohort 1 of \$281,550, based on a state resource special education add-on of \$2,607 per child. Investors received an outcomes payment equal to 95 percent of these savings.</p> |
| <p>Launched in December 2013, this 5.5-year project targets recidivism and employment. The project has raised 13.5M from investors with maximum outcome payments of 21.5M.</p>                   | <p>The Center for Employment Opportunities provides comprehensive employment services through training, transitional jobs, and job placement. Investors receive outcomes payments if the program participants achieve at least approximately an 8-percentage point reduction in recidivism and a 5-percentage point increase in employment when compared to a control group after three years for each cohort.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | <p>Interim outcomes are not yet available for this project. Performance data will become available after the evaluation period is complete.</p>                                                                                                                                                                                                                                                                                    |

| <b>Project Overview</b>                                                                                                                                        | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       | <b>Performance Outcomes</b>                                                                                                            |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------|
| <p>Launched in 2014, this 7-year project targets juvenile recidivism. The project has raised 18M from investors, offering maximum outcome payments of 27M.</p> | <p>The service provider supports young men to develop the skills necessary to reduce violence and create positive behavioral changes. The four-year model, consisting of two years of intensive engagement and two years of follow-up, includes four basic elements: relentless outreach to young men by the service provider’s staff; intensive case management; life skills, educational, prevocational, and employment programming; and work opportunities with community partners. There are three outcomes for this Pay for Success: i) reduction of days of incarceration; ii) increases in job readiness, and iii) increases in time employed; all three are measured against a comparison group as part of a randomized controlled trial. The majority of payments are available for reduction in incarceration, with returns increasing incrementally with performance, and the project’s target impact is a 40% decrease in days of incarceration. The service provider will not refuse services to young men in the comparison group if they seek support on their own or through an outside referral. It will serve a larger number of young men than necessary for evaluation purposes to avoid potential “treatment contamination.”</p> | <p>Payments will be made between the second and seventh year of this initiative. Interim performance results are expected in 2019.</p> |

| <b>Project Overview</b>                                                                                                                                                     | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | <b>Performance Outcomes</b>                                                                                                                                                                                                                                                                                                  |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Launched in October 2013, this 4-year project targets pre-school education. The project has raised 16.9M from investors, offering 34.5M in maximum outcome payments.</p> | <p>In this program, the school district will expand a high-quality preschool education model, the Child-Parent Center (CPC), to six schools serving low-income communities, with plans to roll out the program to additional schools in the later years of the project. Under the CPC model, young children receive pre-school teaching, and dedicated staff also engage with parents and families to help foster better learning at home and address any broader challenges families face. Success will be measured on three outcomes: i) increase in kindergarten readiness; ii) increase in third grade literacy (that is, scoring above average on a nationally administered third grade reading test); and iii) decrease in special education services.</p>                                                                                                                                                                                                                                                   | <p>An April 2016 performance report indicated that 59% of the children who participated in CPC preschool during 2014-15 had kindergarten readiness ratings that met or exceeded national averages. Investors received an outcomes payment of \$500,000 based on the kindergarten readiness results for the first cohort.</p> |
| <p>Launched in December 2014, this 6-year project targets homelessness. The project has raised 3.5M from investors, offering 6M in maximum outcome payments.</p>            | <p>The project provides 500 units of supportive housing over six years, using the Home and Healthy for Good model. The model uses a network of community providers to provide placement and supportive housing based on Housing First principles. Local agencies identify participants (the average length of homelessness is 5 years) and provide “low-threshold” access to housing. Supportive housing is paired with medical and mental health services, substance abuse treatment, and vocational training, coordinated by a case manager. The outcome for this initiative is the increase in housing stability, measured as the number of people stably housed for one full year. Payment is based on the number of “Qualified Participant Days” in which a participant is stably housed for one year and longer, with a per diem rate for each Qualified Participant Day of \$8.22. Payments will be made each quarter after the first year once the independent evaluator validates the quarterly data.</p> | <p>Not available yet.</p>                                                                                                                                                                                                                                                                                                    |

| <b>Project Overview</b>                                                                                                                                                                | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  | <b>Performance Outcomes</b>                                                                   |
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| <p>Launched in January 2015, this 6-year project targets child welfare and family homelessness. The project has raised 4M from investors, offering 5M in maximum outcome payments.</p> | <p>To help stabilize families, the service provider will provide access to affordable housing and an intensive case management system known as ‘Critical Time Intervention’ (CTI). CTI helps vulnerable families that are experiencing homelessness to slowly reconnect to community support networks and settle successfully in newly attained housing. CTI provides intensive services upfront, tapering over time as the caregiver regains the skills and support to achieve their goals, including family reunification. CTI will be paired with age-appropriate, evidence-based trauma services that will strengthen healthy and secure caregiver-child relationships. By providing caregivers critical access to housing before they are reunited with their children, this program will allow caregivers to more successfully receive mental health services, complete substance abuse counseling, set up job interviews and allows for an increased amount of child visitations with their caregivers in a safe home environment. These factors will accelerate the caregiver’s progress on the reunification checklist overseen by the County’s Division of Children and Family Services (DCFS), thereby empowering DCFS to grant reunification decisions to these families sooner and allow children to exit foster care earlier. Success payments are based on the reduction of the combined number of out-of-home placement days for children in the treatment group, as measured against a control group as part of a Randomized Control Trial.</p> | <p>One outcomes payment will be made in the first quarter of 2021, year 6 of the project.</p> |

| <b>Project Overview</b>                                                                                                                                                          | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   | <b>Performance Outcomes</b>                                                                                              |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------|
| <p>Launched in September 2015, this 6-year project targets homelessness. The project has raised 6.9M from investors, offering 8M in maximum outcome payments.</p>                | <p>Two evidence-based interventions, Assertive Community Treatment and Housing First, will be delivered by the service provider under the 'Welcome Home' project. Participants will have access to housing integrated with supportive services that will support their mental and behavioral health. Project Welcome Home's target outcome is a reduction in chronic homelessness on a per-participant basis. Success payments by the county will be determined by the number of months project participants spend in continuous, stable housing. The project partners are aiming for more than 80% of participants to achieve stable tenancy for 12 months. Success payments will be made every three months for the first year in housing (12-month total: \$12,420) and \$1,035 for each month of continuous housing after the first year.</p> | <p>The project will accrue outcome payments for each participant that reaches 3, 6, 9, 12+ months of stable housing.</p> |
| <p>Launched in February 2016, this 4-year project targets early childhood development. The project has raised 30M from investors, offering 7.5M in maximum outcome payments.</p> | <p>The service provider's intervention pairs vulnerable mothers with specially trained nurses, who, through home visits from early pregnancy through the child's second birthday, support mothers to have healthy pregnancies, and become knowledgeable and responsible parents. By strengthening families and improving early childhood development, this intervention also aims to improve the wider health and wellbeing of communities. The success of this Pay for Success initiative is measured in four ways: i) reduction in pre-term births; ii) reduction in child hospitalization and emergency department usage due to injury; iii) increased in healthy spacing between births; and iv) increased number of first-time mothers served in pre-determined ZIP codes with high concentrations of poverty.</p>                           | <p>Not available yet.</p>                                                                                                |

| <b>Project Overview</b>                                                                                                                                             | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     | <b>Performance Outcomes</b> |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|
| <p>Launched in February 2016, this 5-year project targets homelessness. The project has raised 8.7M from investors, offering 11.4M in maximum outcome payments.</p> | <p>The intervention approach combines two models - Housing First, and a modified Assertive Community Treatment (ACT) model of intensive case management. The Housing First model simplifies and streamlines the process of accessing housing, and ensures that supportive housing tenants are not subject to conditions of tenancy exceeding that of a normal tenant (for example, participation in treatment). 210 new housing units also will be constructed for this project, including two new buildings exclusively for participants. ACT will fit the clients' needs throughout the housing process, and is designed to help: i) address barriers to housing stability; ii) manage mental illness; iii) reduce interaction with the criminal justice system; and iv) improve health outcomes. Services include intensive case management, crisis intervention, substance use counseling, mental health treatment, peer support, skills building, connection to primary care, and various other services identified as appropriate to the client's goals. There are two categories of outcomes, Housing Stability and Jail Reduction. For Housing Stability, a successful outcome is achieved if a participant sustains a tenancy for one year. The City pays \$15.12 for each day that a participant spends in housing minus the number of days spent in jail. For Jail Reduction, outcomes payment will be made if jail bed days of participants are at least 20% less than in a control group, with maximum outcomes payments triggered at a 65% reduction in bed days.</p> | <p>Not available yet.</p>   |

| <b>Project Overview</b>                                                                                                                                                      | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             | <b>Performance Outcomes</b> |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|
| <p>Launched in September 2016, this 3-year project supports green infrastructure. The project has raised 25M from investors, offering 28.3M in maximum outcome payments.</p> | <p>The proceeds of the bond will be used to construct green infrastructure designed to mimic natural processes to absorb and slow surges of storm water during periods of heavy rainfall, reducing the incidence and volume of combined sewer overflows that pollute the District's waterways. The program will be evaluated on the percentage reduction of storm water runoff.</p>                                                                                                                                                                                                                                         | <p>Not available yet.</p>   |
| <p>Launched in September 2016, this 4-year project supports family stability. The project has raised 11.2M from investors, offering 14.8M in maximum outcome payments.</p>   | <p>Family-Based Recovery has a track record of success in reducing involvement with Department of Children and Families (DCF) and in keeping families together through intensive support. Families will receive in-home treatment that focuses on parent-child attachment and substance use recovery. The State will repay funders if the service provider achieves outcomes and creates benefits for the State. Specifically, the project will measure the impact on four outcomes: 1) prevented out-of-home placements; 2) prevented re-referrals to DCF; 3) reduction in substance use; and 4) successful enrolment.</p> | <p>Not available yet.</p>   |
| <p>Launched in December 2016, this 6-year project targets homelessness. The project has raised 4.4M from investors, offering 5.5M in maximum outcome payments.</p>           | <p>The Homes Not Jail program provides individuals with services including move-in support, time-limited rental assistance, roommate matching for peer support and cost efficiency, and intensive case management for self-sufficiency and employment needs. The initiative measures four outcomes: 1) improvement on months without jail or shelter; 2) successful graduation to permanent locations; 3) improvement in substance abuse treatment enrollment; and 4) improvement in mental health treatment enrollment.</p>                                                                                                | <p>Not available yet.</p>   |

| <b>Project Overview</b>                                                                                                                                                              | <b>Intervention and Metrics</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | <b>Performance Outcomes</b>                                            |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------|
| <p>Launched in December 2016, this 6-year project targets recidivism. The project has raised 4.6M from investors, offering 5.95M in maximum outcome payments.</p>                    | <p>The REACH program will provide participants with tailored, evidence-based therapies, short-term housing support, and case management. These services will address criminogenic risks tied to recidivism, substance abuse, and mental health services. The project's impact will be measured on four outcomes: 1) reduction in days incarcerated; 2) reduction in state-wide arrests; 3) improvement in quarters of employment; 4) successful program engagement.</p>                                                                                                                                   | <p>Not available yet.</p>                                              |
| <p>Launched in March 2017, this 6-year project supports immigrant and refugee employment. The project has raised 12.4M from investors, offering 15M in maximum outcome payments.</p> | <p>The program will provide adult English-language learners with targeted vocational English-language classes, occupational-skills training, and college-transition programming through four distinct program tracks. The project will measure success based on three outcomes: 1) earnings, 2) successful transitions to higher education, and 3) program engagement. Measurement for all four program tracks will be conducted by an independent evaluator.</p>                                                                                                                                         | <p>Social and financial performance information not yet available.</p> |
| <p>Launched in April 2017, this 5-year project targets female incarceration. The project has raised 2M from investors, offering 2M in maximum outcome payments.</p>                  | <p>The service provider will work closely with the criminal justice system and various community partners to ensure program participants receive supervision, substance abuse and mental health treatment, education, workforce readiness training, and family reunification services. The initiative defines success as a participant not being incarcerated in the State Department of Corrections at four key milestones: upon successful graduation from the program, 24 months after the program start date, 36 months after the program start date, and 54 months after the program start date.</p> | <p>Social and financial performance information not yet available.</p> |

## **APPENDIX B**

### **Interview Invitations**

#### *A. Practitioners and Preparers*

EMAIL SUBJECT LINE: GASB Social Impact Bond Research: Invitation to Participate in an Interview

The Governmental Accounting Standards Board (GASB) is conducting research on social impact bonds or SIBs (also called “social benefit bonds,” “social innovation financing,” and “pay-for-success financing”). These are transactions in which financing is provided to a government or another service provider to pay for an agreed-upon socially desirable program, such as alleviating homelessness or reducing recidivism among former jail inmates. The financing may be provided by a foundation or a financial firm, or may derive from the issuance of debt. The government agrees to repay the foundation or firm (or the issued debt) if desired outcomes are achieved.

*We would like to invite you to participate in this interview in the next two weeks.* The purpose of this interview is to help us understand **[practitioners, only:** what types of SIB arrangements have been entered into or are being considered, as well as the features of those arrangements] **[preparers, only:** how governments are reporting SIB arrangements in their audited financial statements and how that reporting relates to existing reporting standards and concepts] **[both practitioners and preparers:** what information users of governmental financial information may need, if any, regarding SIB arrangements]. The interview should last about 30 minutes.

Please respond to this email to let us know whether you are willing to participate. Please also indicate when you will be available during the weeks of June 5 and 12. We will contact you to schedule a specific date and time and will send you the actual questions before the interview.

We understand you are knowledgeable in this area, and believe your input will be valuable to this research. If you have any questions, please do not hesitate to contact us. Thank you in advance for your assistance.

Best regards,

**Wesley A. Galloway**  
*Senior Project Manager*

GOVERNMENTAL ACCOUNTING STANDARDS BOARD  
OF THE FINANCIAL ACCOUNTING FOUNDATION  
401 Merritt 7, P.O. Box 5116, Norwalk, CT 06856  
T: 203.956.5272 // F: 203.849.9470  
[www.gasb.org](http://www.gasb.org)

## B. Users

EMAIL SUBJECT LINE: GASB Social Impact Bond Research: Invitation to Participate in an Interview

The Governmental Accounting Standards Board (GASB) is conducting research on social impact bonds or SIBs (also called “social benefit bonds,” “social innovation financing,” and “pay-for-success financing”). These are transactions in which financing is provided to a government to pay for an agreed-upon socially desirable program, such as alleviating homelessness or reducing recidivism among former jail inmates. The financing may be provided by a foundation or a financial firm, or may derive from the issuance of debt. The government agrees to repay the foundation or firm (or the holders of the debt) if desired outcomes are achieved.

*We would like to invite you to participate in this interview in the next two weeks. The objectives of the interview would be to seek the following:*

- Your understanding of SIBs (pay for success programs, and so on), and your interest in them with respect to your work
- Your views on the usefulness of information about social impact bonds to your work
- Your perception of the potential risks, if any, involved with these types of transactions.

The interview should last no more than 30 minutes.

Please respond to this email to let us know whether you are willing to participate. Please also indicate when you will be available during the weeks of August 14–18 and 21–25. We will contact you to schedule a specific date and time and will send you the questions we intend to ask before the interview.

We understand you are knowledgeable in this area, and believe your input will be valuable to our research. If you have any questions, please do not hesitate to contact me at [wagalloway@gasb.org](mailto:wagalloway@gasb.org) or 203-956-5272. Thank you in advance for your assistance.



Best regards,

**Wesley A. Galloway**  
*Senior Project Manager*



GOVERNMENTAL ACCOUNTING STANDARDS BOARD  
OF THE FINANCIAL ACCOUNTING FOUNDATION  
401 Merritt 7, P.O. Box 5116, Norwalk, CT 06856  
T: 203.956.5272 // F: 203.849.9470  
[www.gasb.org](http://www.gasb.org)

## **APPENDIX C**

### **Practitioner Interview Advance Materials**

The following questions will help the GASB understand what types of social impact bond, or SIB, arrangements have been entered into or are being considered and what their features are.

- 1) What SIB arrangements have you entered into or plan to enter into?
- 2) How was the arrangement structured (or, how will it be structured)?
  - a) Who initiated the arrangement?
  - b) What payment(s) could the government be required to make?
    - i) What are the conditions for requiring payment(s)?
  - c) What legal or financial documents describe the details of structures and obligations?
    - i) Is there a formal offering statement?
    - ii) Are there grant agreements (for example, with a foundation)?
- 3) If the arrangement involved issuing debt, do the debt instruments trade?
- 4) What risks, if any, do you believe the government is exposed to from these transactions?
- 5) What questions, if any, are you receiving about these transactions? Who is asking these questions?
- 6) What is the potential trend on SIB arrangements? Increasing? Decreasing?
- 7) Is there anything else you would like to tell us about SIB arrangements?

## **APPENDIX D**

### **Preparer Interview Advance Materials**

The following questions will help the GASB understand how governments are reporting SIB arrangements in their audited financial reports and how that reporting relates to existing reporting standards and concepts/what information users of governmental financial information may need, if any, regarding SIB arrangements.

- 1) How has your government reported the agreements (for example, in the financial statements as debt, provisions, or grants; in notes to financial statements; or, not at all)?
  - a) What issues have arisen in determining whether and how to recognize and measure the transaction?
  - b) What challenges did you face in determining whether the metrics of success that may trigger payment have been met?
  - c) What was disclosed and why?
  - d) What additional event would cause these transactions to rise to the level of recognition?
  - e) Why not?
  
- 2) What financial reporting guidance did you consider related to SIBs?
  - a) Is that guidance sufficient?
  
- 3) What risks, if any, do you believe the government is exposed to from these transactions?
  - a) How are those risks reflected in the financial statements—on the face of financial statements, in notes to financial statements, or in MD&A)?
  
- 4) What questions, if any, are you receiving about these transactions? Who is asking these questions?
  
- 5) Is there anything else you would like to tell us about SIB arrangements?

## **APPENDIX E**

### **User Interview Advance Materials**

The objectives of the interview would be assist the GASB in understanding of SIBs, including: your interest in them with respect to your work, your views on the usefulness of information about social impact bonds to your work, and your perception of the potential risks, if any, involved with these types of transactions.

- 1) What information have you seen about pay for success programs or social impact bonds?
- 2) How useful is that information to your work?
  - a) How have you used that information in your work?
- 3) What other information, if any, do you need about pay for success programs or social impact bonds?
  - a) How would you use that information in your work?
- 4) What types of risks do you think these transactions may pose to the governments involved, if any?
- 5) If pay for success programs or social impact bonds become more common, would information about these transactions become more valuable to your work?
  - a) What kinds of information about pay for success programs or social impact bonds would become more valuable to your work?
  - b) How would you use that information in your work?
- 6) Do you have any other comments about pay for success programs or social impact bonds?

## **APPENDIX F**

### **Practitioner Interview Protocol**

Introduce:

Wesley Galloway  
Alec Schon  
Laura Beth Harville

Before we start, do you have any questions for us?

As we mentioned in the materials we sent you prior to this interview, our standard practice is to record interviews for internal analytical purposes. No one outside of the GASB and the Financial Accounting Foundation will have access to the recording and neither you nor your [firm/organization] will ever be publicly identified or associated with the feedback you provide during this interview. Is it okay with you if we record this interview?

OK, let's just walk through the questions. If you have no opinion or you think you have already answered the question, just say so and we will move on.

- 1) What SIB arrangements have you entered into or plan to enter into?
- 2) How was the arrangement structured (or, how will it be structured)?
  - a) Who initiated the arrangement?
  - b) What payment(s) could the government be required to make?
    - i) What are the conditions for requiring payment(s)?
  - c) What legal or financial documents describe the details of structures and obligations?
    - i) Is there a formal offering statement?
    - ii) Are there grant agreements (for example, with a foundation)?
- 3) If the arrangement involved issuing debt, do the debt instruments trade?
- 4) What risks, if any, do you believe the government is exposed to from these transactions?

- 5) What questions, if any, are you receiving about these transactions? Who is asking these questions?
- 6) What is the potential trend on SIB arrangements? Increasing? Decreasing?
- 7) Is there anything else you would like to tell us about SIB arrangements?

## **APPENDIX G**

### **Preparer Interview Protocol**

Introduce:

Wesley Galloway  
Alec Schon  
Laura Beth Harville

Before we start, do you have any questions for us?

As we mentioned in the materials we sent you prior to this interview, our standard practice is to record interviews for internal analytical purposes. No one outside of the GASB and the Financial Accounting Foundation will have access to the recording and neither you nor your [firm/organization/government] will ever be publicly identified or associated with the feedback you provide during this interview. Is it okay with you if we record this interview?

OK, let's just walk through the questions. If you have no opinion or you think you have already answered the question, just say so and we will move on.

- 1) How has your government reported the agreements (for example, in the financial statements as debt, provisions, or grants; in notes to financial statements; or, not at all)?

[If recognized in the statements:]

- a) What issues have arisen in determining whether and how to recognize and measure the transaction?
- b) What challenges did you face in determining whether the metrics of success that may trigger payment have been met?

[If disclosed in the notes:]

- c) What was disclosed and why?

[If the arrangement was not recognized in any manner on the face of the financial statements (whether not reported at all or only disclosed in notes to financial statements):]

- d) What additional event would cause these transactions to rise to the level of recognition?

[If the arrangement was not reported in the audited financial report:]

- e) Why not?
- 2) What financial reporting guidance did you consider related to SIBs?  
[If they identify specific guidance:]
    - a) Is that guidance sufficient?
  - 3) What risks, if any, do you believe the government is exposed to from these transactions?  
[If they identify any:]
    - a) How are those risks reflected in the financial statements—on the face of financial statements, in notes to financial statements, or in MD&A)?
  - 4) What questions, if any, are you receiving about these transactions? Who is asking these questions?
  - 5) Is there anything else you would like to tell us about SIB arrangements?

## **APPENDIX H**

### **User Interview Protocol**

Introduce:

Wesley Galloway  
Alec Schon  
Laura Beth Harville

Before we start, do you have any questions for us?

As we mentioned in the materials we sent you prior to this interview, our standard practice is to record interviews for internal analytical purposes. No one outside of the GASB and the Financial Accounting Foundation will have access to the recording and neither you nor your [firm/organization/government] will ever be publicly identified or associated with the feedback you provide during this interview. Is it okay with you if we record this interview?

OK, let's just walk through the questions. If you have no opinion or you think you have already answered the question, just say so and we will move on.

- 1) What information have you seen about pay for success programs or social impact bonds?
- 2) How useful is that information to your work?

[If the information has been useful at all, go to question 2a. If not, go to question 5.]

- a) How have you used that information in your work?
- 3) What other information, if any, do you need about pay for success programs or social impact bonds?

[If they identify any information, go to question 3a. If not, go to question 4.]

- a) How would you use that information in your work?
- 4) What types of risks do you think these transactions may pose to the governments involved, if any?

[If question 4 is posed, do not ask question 5. Skip to question 6.]

- 5) If pay for success programs or social impact bonds become more common, would information about these transactions become more valuable to your work?
  - a) What kinds of information about pay for success programs or social impact bonds would become more valuable to your work?
  - b) How would you use that information in your work?
- 6) Do you have any other comments about pay for success programs or social impact bonds?