



EXECUTIVE OFFICE ON EARLY LEARNING
HONOLULU

TERRY LOCK
DIRECTOR

Testimony Relating to
H.B. 1402, Relating to Social Impact Bonds
By Terry Lock, Director

House Committee on Human Services
February 7, 2013
9:30 a.m., Room 329

Chair Carroll, Vice-Chair Kobayashi, and Members of the Committee:

Aloha, I am Terry Lock, Director of the Executive Office on Early Learning (EOEL).

H.B. 1402 would require EOEL to conduct a study on the feasibility of using social impact bonds to fund early learning programs and services in the state.

We note that these types of bonds are new and we do not have much information on the pros and cons of their use. However, we support looking at various resources to support early learning. EOEL would be willing to conduct such a study if funding is provided.

Thank you for the opportunity to testify.

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LEGISLATIVE REFERENCE BUREAU
State of Hawaii
State Capitol, Room 446
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Written Comments

HB1402 **RELATING TO SOCIAL IMPACT BONDS**

Comments by the Legislative Reference Bureau
Charlotte A. Carter-Yamauchi, Acting Director

Presented to the House Committee on Human Services

Thursday, February 7, 2013, 9:30 a.m.
Conference Room 329

Chair Carroll and Members of the Committee:

Good morning Chair Carroll and members of the Committee, my name is Charlotte Carter-Yamauchi and I am the Acting Director of the Legislative Reference Bureau. Thank you for providing the opportunity to submit written comments on H.B. No. 1402, Relating to Social Impact Bonds.

The purpose of this bill is to:

- (1) Require the Executive Office on Early Learning to conduct a study on the feasibility of using social impact bonds to fund early learning programs and services in the State; and
- (2) Require the Legislative Reference Bureau to assist the Executive Office on Early Learning with preparing the feasibility study, recommendations, and any proposed legislation.

While the Legislative Reference Bureau takes no position on this measure, we submit the following comments for your consideration.

The measure requires the Bureau to "assist the Executive Office on Early Learning with preparing the feasibility study, recommendations, and any proposed legislation."

As you know, the Executive Office on Early Learning is an Executive Branch agency that is currently administratively attached to the Office of the Governor. While the Bureau is statutorily charged with the responsibility to provide comprehensive and impartial research services to the Legislature, it does not have specific statutory authority to assist the Executive Branch in its research activities. The phrase "assist the Executive Office on Early Learning with preparing the feasibility study, recommendations, and any proposed legislation" is problematic due to its vague nature and could be interpreted to require the Bureau to provide more research and drafting services to an Executive Branch agency than has been customarily provided in the recent past.

We believe that the limited resources of the Bureau would be utilized more effectively on the Legislature's behalf if the measure is amended in the following manner:

- (1) Clarify that the Executive Office of Early Learning will be responsible for the initial preparation and draft of the study and any initial draft of proposed legislation; and
- (2) Direct the Bureau to produce the final version of the report requested in the measure and finalize any draft of proposed legislation; provided that the Executive Office on Early Learning submits its draft report and proposed legislation to the Bureau no later than November 1, 2013.

These amendments will allow us to manage our workload effectively and minimize interference with our ability to provide research services and draft bills and other requests for legislators during the busy period prior to the start of session. The proposed submission deadline to the Bureau would also provide sufficient time for the Executive Office on Early Learning to review the Bureau's draft of the final report and make any necessary edits prior to the actual submission deadline to the Legislature.

Thank you again for this opportunity to provide written comments.

To: Representative Mele Carroll, Chair
Representative Bertrand Kobayashi, Vice Chair
Members of the HOUSE COMMITTEE ON HUMAN SERVICES

From: Kathy Murphy, Executive Director
Hawaii Association for the Education of Young Children (HAEYC)

Subject: HB 1402 – Relating to Social Impact Bonds

This bill would require the Executive Office on Early Learning to investigate, with the assistance of the Legislative Reference Bureau, the feasibility of using social impact bonds to fund early learning programs and services in the state.

Social impact bonds (SIB) is a recent funding mechanism to fund public services that are intended for the common good. Since the method of funding is new, there have not been long-term studies to assess the effectiveness of the SIB and, in particular, whether it is more effective for certain kinds of public services than others.

HAEYC supports HB 1402 for the Executive Office on Early Learning to study the feasibility of introducing the social impact bond as a way of funding early learning programs and services. To aide in the Committee's consideration of this bill, attached is one of the best short papers available on the social impact bond for your review.

We acknowledge the vision and courage it takes for legislators to enact laws that will come to fruition after they leave office. Investing in early childhood development and education will be your lasting legacy.

HAEYC is a professional membership organization of early childhood development and educational professionals, with nearly a 1,000 members across the state of Hawaii. We would like to continue to be a positive contributor to ongoing policy conversations about Hawaii's children. Our volunteers and staff would be happy to provide you with more information to facilitate your decision-making. Please contact us at (808) 942-4708 or haeyc@hawaiiaeyc.org.

HAEYC's mission is to promote, support, and expand quality and professionalism in early childhood programs and services for Hawai'i's children (0-8) and their families.

Mahalo for the opportunity to testify on this measure.

Katherine E. Murphy
Executive Director
HAEYC

Attach: *Social Impact Bonds Primer and Landscape January 2013*

Social Impact Bonds: A Primer and Landscape
Prepared by Anna Torsney-Weir, Ounce of Prevention Fund
January 2013

A Primer on Social Impact Bonds

The term “**impact investing**” refers to traditional investments where the investors are seeking both a financial return and a positive social impact from their investment. Impact investing falls somewhere between philanthropy, in which investors do not expect any financial return on their investment, and socially responsible investing, in which the main priority is a financial return but investors want to “do no harm” to society.

Social Impact Bonds (SIB) are one of the most innovative mechanisms of impact investing because they facilitate government spending on social service or education strategies and encourage high quality. In the case of early childhood education, SIBs provide a unique opportunity to “put our money where our mouth is:” we say that educating children early in life is less costly and more effective than intervening later in life. SIBs require proof that this is true and allow additional investment if it is.

SIBs are bonds in the sense that they constitute a contract between a lender (investor) and a borrower (a government agency), but they are NOT like traditional government bonds (municipal, Treasury, etc.) in the sense that the contract does not require the borrower to repay the lender if the outcomes defined by the government as “success” do not come to fruition. In other words, **SIBs are a pay-for-performance mechanism:** if the service strategy is successful, lenders are repaid their initial investment plus an agreed-upon interest rate, and the service provider(s) receive a bonus. If, however, the service strategy is unsuccessful, the lenders do not get repaid and lose their investment. Thus, all of the risk in the bond is transferred to the lender, and the government is actually able to delay spending money until the bond reaches maturation. Obviously, if the program is successful, it is more expensive for the government borrower down the road because they must repay the investors plus a bonus, and pay a bonus to the provider(s).

There are several implications of the structure of SIBs that are important to consider :

- Due to the risk of not being repaid, SIBs are not attractive to typical investors. The most likely pool of initial investors are those who are currently philanthropists because they are interested in creating beneficial social impact but do not expect a financial return on their investment – therefore, a potential return on their investment plus a bonus might be very attractive to them. Venture capitalists might also be interested since SIBs are similar to venture capital projects.
- To attract investors, the proof of concept for the service provider is very high: they must be able to show strong, quantifiable evidence that they provide a high-quality service that can feasibly achieve success. It’s easiest to pick something that already has been tested and has a strong evidence base.
- Because they can delay spending money temporarily, SIBs are attractive to state and local governments who have financial difficulties and especially those who are having trouble meeting their financial obligations to service providers. Governments also might like that they have the power to define “success,” the maturation date, and the terms of repayment.
- SIBs are very new and therefore are not well-tested.
- Besides the borrower, service provider, and lender, SIBs require two other players: a social impact bond-issuing organization or other loan guarantor (e.g., UK-based Social Finance), and an independent evaluator to assess whether the service provider achieved its stated outcomes.

The SIB Landscape

Note: because Social Impact Bonds (SIBs) are very new and relatively untested, the landscape is full of people who are interested in and excited by the concept but is sparsely populated by people with real experience in executing the concept.

- To date, the only case in which SIBs have been fully implemented (but not yet fully tested) is to reduce prison recidivism in the UK. New York City recently announced that it will be the first U.S. city to test

the strategy, also on prison recidivism, with investment from Goldman Sachs' Urban Investment Group. The players in these models are:



- **SIBs have not yet been used for early childhood.** So far, programs under consideration involve reducing prison recidivism, reducing chronic homelessness, supportive elderly housing to delay nursing home admission, and community-based alternatives to juvenile detention and adult incarceration. Massachusetts recently announced that it is completing negotiations with two nonprofit groups to finance juvenile justice and homelessness programsⁱ. The federal government, Connecticut, Rhode Island, New York State, and Cuyahoga County, Ohio, among others, are at various stages of considering using the bonds to harness new funds for human-services programs.
- **There are misleading claims that SIBs are being used in Pennsylvania and Utah.** The initiatives in Pennsylvania and Utah are not bonds – they can more accurately be described as “savings reinvestment strategies”, where rigorous cost-savings studies are conducted on an early childhood program showing that, for example, high-quality PreK Special Education reduces the costs of K-12 special education, which are then used to justify additional investments in early childhood programs. This is a separate process from SIBs, but also worth looking into as a strategy.
- The Manhattan borough president recently announced his intention to explore the use of SIBs to expand access to Early Head Startⁱⁱ, but there have been no media releases on this since mid-October. Note: One of the biggest concerns about the applicability of the social impact bond model to Early Head Start is whether the program pays for itself through cashable savings at the city or state level.

ⁱ http://www.nytimes.com/2012/08/02/nyregion/goldman-to-invest-in-new-york-city-jail-program.html?_r=1

ⁱⁱ <http://www.nytimes.com/2012/10/16/nyregion/manhattan-borough-president-seeks-bonds-to-expand-head-start.html>