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# Pay for Success: Financing Research-Informed Practice*

By Noelle S. Baldini, Community Engagement Associate

Undercapitalization of nonprofit organizations and years of seemingly stagnant results in addressing certain social problems have led many to hope that "pay for success (PFS) financing" will bring solutions in the form of new capital to support program delivery, improved accountability, and increased rigor in performance measurement. PFS financing, sometimes termed "social impact bonds (SIBs)," shifts the risk of a preventive social service's success from taxpayers to investors who finance programs and receive government repayments if, and only if, an agreed-upon performance metric is achieved. Through the use of a third-party evaluator tasked with measuring a program's success, this new financing strategy encourages research-informed practice that can deliver measurable results. This article explores the structure and potential benefits of PFS financing, as well as assesses challenges and opportunities.

**Why Pay for Success?**

Many government entities face significant fiscal stress, elevating the critical nature of wise budgetary decision-making. In such challenging fiscal environments, spending for community development activities is often reduced, leaving many organizations and service providers with insufficient capital to meet the needs of their communities.[1] Oftentimes, however, a significant amount of capital is spent remediating issues that might have been avoided had resources for preventive services been available. For example, in fiscal year 2013, 57.2 percent of Philadelphia Prison System (PPS) inmates returned to the PPS within three years of release.[2] Further, the PPS reported that roughly 63 percent of the daily cost per inmate (estimated at a daily cost of $20.29)[3] is a one-time cost at intake.[4] Experts cite supportive housing, mental health and substance abuse services, and workforce reentry as service gaps that are directly related to recidivism.[5] As the cost figures demonstrate, there is not only a moral case but also an economic case for delivering successful preventive social interventions.

In 2010, a group of stakeholders in the United Kingdom recognized that societal cost savings allow for the monetization of social impact and created a unique financial strategy that has since sparked international interest in rethinking how public funding is administered for social services. Social Finance, a global nonprofit organization with a base in London,[6] arranged for a group of investors to finance activities that they hoped would reduce recidivism in the Peterborough Prison. A contract was put into place with terms outlining that the United Kingdom Ministry of Justice would repay the investors with interest if the intervention resulted in a reduction in recidivism. Since this project, the first of its kind, was launched in the UK five years ago, interest in this PFS financing has grown and spread internationally.[7]

**What Is Pay for Success Financing?**

Outcomes-based funding, or performance contracting, is not an innovation in and of itself. In industries such as infrastructure development, service providers often receive government success payments upon the completion of a project. PFS contracting, however, is a recent innovation in public spending approaches in the social service sector. PFS financing, or SIBs, is a financial tool that uses private capital to cover upfront funding for PFS agreements, allowing service providers to implement programs without waiting for the backend payments

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* The views expressed here do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.
1 Keith Wardrip, *Fiscal Stress in the Small Postindustrial City: Causes, Consequences, and Implications for Community Development*, Special Report, Federal Reserve Bank of Philadelphia, May 2014, available at https://www.philadelphiafed.org/community-development/fiscalstress.
2 City of Philadelphia, "Five Year Financial and Strategic Plan for Fiscal Years 2015–2019," available at http://ow.ly/Qwiyd.
3 Claire Shubik-Richards, *Philadelphia's Crowded, Costly Jails: The Search for Safe Solutions*, The Pew Charitable Trusts Philadelphia Research Initiative, 2012, available at http://ow.ly/PXqS2.
4 Anna Fogel, Jeff Shumway, and Anant Udpa, *Roadmap for Pay for Success in Philadelphia*, Social Finance, 2015, available at http://ow.ly/PXrpy.
5 See Fogel et al., 2015.
6 See www.socialfinance.org.uk.
7 See http://ow.ly/QMr1o.

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to occur. The name "social impact bond" may cause some confusion, as "bond" is somewhat of a misnomer. Though some would like to see these instruments grow in availability and sophistication, the securitization of SIBs or the emergence of a secondary market to provide investors with liquidity has not yet occurred. At this point, SIBs function more as a loan to finance government receivables that are paid only if certain social performance metrics are achieved.

PFS financing brings together stakeholders from the public, private, and nonprofit sectors to combat a social issue and achieve agreed-upon goals. Through the SIB structure, a socially minded investor (or investors) finances services and a payer (often the government) is responsible for repayment of the investment contingent upon the demonstration of measurable results. An independent evaluator is responsible for ongoing program evaluation to determine if the repayment trigger is met.

Unlike the current state of most public social service funding, SIBs allow for evidence-based government investment, saving scarce resources by allocating capital based on outcomes, instead of outputs. SIBs appeal to socially oriented investors because they are one of the few products that require as much analytical rigor on the social impact measurement side as on the financial side. If the program yields successful outcomes for the target population relative to a comparison group, as determined by a randomized controlled trial or quasi-experimental study,[8] investors recoup their principal and can earn a specified rate of return, which may increase along a scale with improved program performance.

Relying on the advice of the old adage, "An ounce of prevention is worth a pound of cure," most PFS projects focus on preventive services that, if successful, will reduce future public spending on remediation. Although only eight SIBs[9] have been launched throughout the country to date, promising areas for interventions have emerged, including those aimed at reducing recidivism and homelessness. In these examples, the cost of counseling, supportive housing, or other interventions would reduce future social costs associated with bed days in prison, emergency room visits, and the operation of homeless shelters, among others. Additional intervention areas have been identified, including early childhood education, services for at-risk youth aging out of foster care or juvenile justice systems, and preventive programs and services to address the social determinants of health[10] in low-income areas.

### How Do Participants Benefit?

All parties involved in a PFS transaction receive specific benefits from their participation in the project:

## Current State of Pay for Success Financing in the United States

Two PFS projects have been financed in both Massachusetts and New York, and additional deals have been financed in Utah, Illinois, Ohio, and California. Though the projects in these locations have received financing, it is too early to determine if repayment triggers will be met.[a] One project — the New York City Rikers Island recidivism project — is an exception. The contract included a three-year performance checkpoint, which showed that the program failed to meet the 10 percent targeted decrease in recidivism. As a result, the city did not issue repayments.

In addition to those already mentioned, many additional states and cities are currently conducting feasibility studies and have issued requests for proposals for consultants to assist with PFS implementation.[b] The federal government is supporting PFS financing efforts through a variety of opportunities, including grants from the Social Innovation Fund (SIF) at the Corporation for National and Community Service. Additionally, the Workforce Investment Opportunity Act allows local workforce boards to reserve up to 10 percent of their funding for PFS activities,[c] and the U.S. Department of Justice's Second Chance Act includes PFS awards.[d] The U.S. Department of Health and Human Services, the U.S. Department of Housing and Urban Development, and the U.S. Department of Education announced that they will soon provide opportunities for PFS grant funding in the near future. Lastly, legislation has been introduced in both the U.S. House and Senate that would create a $300 million fund at the U.S. Department of the Treasury to support PFS programs at the state and local levels.[e] The Commonwealth of Pennsylvania was selected as a SIF subgrantee and is exploring state-level PFS opportunities with technical assistance from Harvard Kennedy School's Social Impact Bond Lab.[f] Additionally, the City of Philadelphia recently conducted a feasibility study of certain interventions that could be supported through PFS programs.[g] In New Jersey, a bill supporting the creation of a PFS pilot program and study commission was passed by both houses of the legislature and is awaiting the governor's signature.[h]

[a] For more information, visit http://ow.ly/PXwP9.
[b] For more details on the locations of projects being developed, visit http://ow.ly/PXwXG.
[c] See http://ow.ly/QxjVJ.
[d] See https://www.bja.gov/Funding/12PayforSuccessFAQ.pdf.
[e] See http://ow.ly/RcjNc.
[f] For more information, visit http://ow.ly/PXx7o.
[g] Anna Fogel, Jeff Shumway, and Anant Udpa, *Roadmap for Pay for Success in Philadelphia*, Social Finance, 2015, available at http://ow.ly/PXrpy.
[h] See http://ow.ly/Qxk5z.

[8] Evaluation methodologies differ with each unique SIB. Some stakeholders strongly believe that SIBs require a randomized controlled trial, whereas others believe that alternative methodologies may need to be used for ethical reasons or to allow for smaller sample sizes and reduced evaluation costs. For more information, see George Overholser and Caroline Whistler, "The Real Revolution of Pay for Success: Ending 40 Years of Stagnant Results for Communities," *Community Development Investment Review*, 9 (2013), pp. 5–11, available at http://ow.ly/Q0xR8.
[9] For more information about the new project in Santa Clara County in California, visit http://ow.ly/R9AZe. See http://ow.ly/QeEN8 for a list of the other seven current projects and some new projects planned for 2015.
[10] For more information on social determinants of health, see World Health Organization resources at www.who.int/social_determinants/en/.


Source: Center for Supportive Housing, *Social Impact Investing: A Tool to Finance Community-Based Supportive Housing and Fulfill the Integration Goals of Olmstead*, 2014

1. **Government** selects a desired intervention and contracts with all relevant parties.
2. **Investors** provide the upfront capital to finance the intervention.
3. **Intermediary** provides the service provider(s) with the working capital to implement the intervention.
4. **Service providers** deliver services to the **target population**.
5. Outcomes and costs are tracked and provided to the third-party **evaluator**.
6. The **evaluator** determines whether the agreed-upon metrics have been achieved.
7. **Government** makes success payments to either the intermediary for distribution or directly to the investors if outcomes are met.

- **Service providers:** Service providers receive a new form of multiyear funding that allows them to focus on program delivery versus fundraising. Although this will be very valuable to some organizations, others will require significant capacity building before they are ready to enter into a complex transaction that requires sophisticated reporting and data collection and sharing.
- **Investors:** SIBs provide a unique opportunity for "impact investors" or investors seeking to receive social as well as financial return.[11] By guaranteeing rigorous impact evaluation, SIBs provide investors with a clear understanding of the social impact of their investment.
- **Payers:** The back-end "payer" of a SIB is typically a government entity responsible for repaying the investor when the program successfully meets the impact metric serving as the repayment trigger. SIBs essentially shift the performance risk of a program from taxpayers to investors, and this risk reduction for the payer is a major benefit of the SIB structure.

  The payer does not necessarily have to be a government entity. Some SIBs are currently being structured with hospitals, insurance companies, foundations, or other interested stakeholders that receive some sort of value or cost savings from a social intervention serving as the payer.
- **Target Population:** The target population for the program should receive benefits from the SIB in the form of effective service provision through high-quality program implementation. This shift in funding motivates those providing services to become more data-driven and allows for innovation that yields measurable results for people and communities.

**What Are the Potential Challenges?**

While there has been much discourse around the potential new sources of capital that SIBs may bring to community development efforts and the fiscal savings that will result from the structure, the social services and interventions

[11] This is a growing field. A 2015 report (available at http://ow.ly/SlYgm) by J.P. Morgan and the Global Impact Investing Network estimates current impact investing assets under management of $60 billion, an increase of more than 20 percent from 2014. Further, a 2013 report by the World Economic Forum (available at http://ow.ly/Q0yIq) projected the impact investing market to reach $500 billion by 2020.

that are likely candidates for PFS financing are limited by several factors. SIBs require the coordination of many parties, which means that transaction costs can be high and significant capacity commitments are needed throughout the planning and life of the SIB. Planning activities include a thorough cost-benefit analysis and feasibility study of the intended intervention, as well as the coordination of all players on agreed-upon contractual terms, including the length of the investment/intervention term and any necessary checkpoints to assess progress. Ongoing evaluation of the program and a sound process for sharing data are also key components to the success of the project. For these reasons, it has been recommended that interventions requiring an investment of less than $5 million seek other sources of funding that do not require such complexity in planning, coordination, and implementation.[12] Similarly, interventions that do not generate cost savings or significant outcomes of interest to the payer may not qualify for the additional transaction costs and interest payments necessary for PFS financing.

While PFS financing may effectively allow governments to finance more innovative strategies, it will also require innovation on the part of the government entity serving as the payer. This may require a culture shift and broader system changes. For example, participating in a SIB will require the government payer to be flexible and open to new legal, financial, and data analysis approaches. Additionally, sound policy to support PFS projects is critical. Since programs can last for several administrative terms, appropriations risk could become an issue without legislation or other safeguards in place to ensure that the SIB repayment remains a priority for elected officials. Coordination among different government entities also may be required for a successful PFS project. For example, if societal cost savings accrue across local, state, and federal government agencies, a SIB may require multiple payers and the ability of the intermediary to parse out the unique benefits to each payer during the initial SIB contracting.

Experts agree that the alignment of incentives between all stakeholders involved is critical to the success of a SIB. Since repayment risk is intrinsically linked to successful outcomes, "creaming" of the population (i.e., limiting service provision to those most likely to succeed) to achieve the intended social outcome has been cited as a common concern.[13] SIBs should be structured to overcome this concern through the use of intermediaries responsible for ensuring accountability for all aspects of the process. Although broader concerns often have been raised regarding potential conflicts that can arise when private capital is financing public projects,[14] SIBs seem to be uniquely suited to overcome these concerns. Unlike other public-private partnerships, SIBs inherently attract a specific type of investor willing to take some risk in order to achieve social impact. The resulting alignment of priorities with the government entity should help avoid the risk of private investors prioritizing financial motives over public good.

Although the inherent risk associated with SIB contracts could deter some investors, philanthropic partners have provided guarantees, loan loss reserves, or subordinated debt to reduce risk and attract senior investors in the SIBs that have been structured to date. This ongoing support from the philanthropic industry will remain crucial for PFS financing, at least until enough SIBs have been tested to attract a broader investor segment than the current early stage adopters.

**Conclusion**

PFS financing is a strategy that has attracted interest from public, private, and nonprofit stakeholders around the country eager to find ways to expand the pool of capital available to social service providers while saving limited public resources. Though there is much excitement about this innovation, it is important to note that PFS is not a panacea for the issues that exist in society today. Many problems are structural in nature and may not be solved without broader and deeper systemic changes. SIBs, like any financial instrument, are a morally neutral tool,[15] so deep analysis should be used to determine how and where they are used and the quality of the programs, partners, policies, and processes in place.[16] However, where applicable, PFS financing has the potential to support research-informed practice, generate societal cost savings, and create social impact by improving the lives of vulnerable individuals and communities throughout the country.

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[12] See Fogel et al., 2015.
[13] Mildred Warner, "Private Finance for Public Good: Social Impact Bonds," *Journal of Economic Policy Reform*, 16 (2013), pp. 303–319.
[14] See Warner, 2013.
[15] Clara Miller, "Can Social-Impact Bonds Really Have Big Impact?" *Chronicle of Philanthropy*, March 2015.
[16] Eileen Neely and Andy Rachlin, *From the 4 Cs of Credit to the 4 Ps of Pay for Success*. Washington, D.C.: Living Cities, March 2015, available at http://ow.ly/Q0yTa.

## Additional Resources

- Federal Reserve Bank of San Francisco, *Community Development Investment Review*, 9(1), (2013), available at http://ow.ly/Q0xR8.
- Nonprofit Finance Fund's Pay for Success Learning Hub, available at www.payforsuccess.org.
- Social Innovation Fund at Corporation for National & Community Service, *State of Pay for Success Field: Opportunities, Trends, and Recommendations*, April 2015, available at http://ow.ly/Q0zt9.

**Read the entire issue of *Cascade* at https://www.philadelphiafed.org/cascade.**

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# Investing to Create Good Jobs*

By Keith L. Rolland, Community Development Advisor, and Noelle S. Baldini, Community Engagement Associate

A growing number of foundation, nonprofit, and for-profit investors are making investments for measurable social and environmental impact as well as financial return.[1] The "impact investing" field includes a few investors that are investing in businesses specifically to create jobs for unemployed and underemployed residents. These investors also provide ongoing assistance to owners of the businesses to create "good quality jobs," which generally provide income above the minimum wage, health benefits, and training and opportunities for workers to move into positions with higher wages. Three investors that are at the forefront of making investments with the "intentionality" of creating good jobs are profiled in this article.

## HCAP Partners

HCAP Partners (formerly Huntington Capital) is a for-profit firm based in San Diego, CA, that invests mezzanine debt[2] and private equity in growing small and middle-market companies in the health care, technology, services, and manufacturing sectors in the Western U.S. The firm's first fund was formed in 2000 as a Small Business Investment Corporation licensed by the U.S. Small Business Administration, with limited partners including the State of California pension funds, as well as insurance companies, foundations, family investors, and financial institutions. HCAP Partners currently manages more than $200 million in total assets in three funds and is currently investing from its third fund.[3]

The firm believes that small and middle-market companies are underserved by traditional sources of growth capital, such as banks, venture capital firms, and private equity firms, and that these companies have the greatest potential to create jobs and spur growth. HCAP Partners typically invests $2 million to $9 million in businesses that have management with experience, annual sales of $10 million to $75 million, and earnings of $1 million or more before interest, taxes, depreciation, and amortization.

Hope Mago, senior associate at HCAP Partners, said that the firm measures success first by financial return to investors and second by the number and kinds of jobs that its portfolio companies provide to employees and by ancillary "spillover" benefits, such as increased economic activity, job creation, and tax base growth in the communities in which the companies are located.

A worker uses equipment at RPI, a print manufacturer and fulfillment partner that received an investment from HCAP Partners. RPI, which has facilities in Seattle, Atlanta, and the Netherlands, is in the consumer print-on-demand personalized publishing market. It is certified as a sustainable green printing company.

The company's mezzanine capital, positioned between equity and senior debt, is structured as long-term loans with warrants to purchase stock or the right to receive royalty payments based on performance. These investments give HCAP Partners leverage with management and a seat on the portfolio companies' boards of directors. HCAP Partners works with the leadership teams of its portfolio companies to enhance not only financial operations and performance but also job quality.

Mago said that HCAP Partners encourages companies to create jobs that pay living wages and provide paid sick days; health coverage, including preventive care; job training; advancement opportunities, including a "first look" at job openings for long-term employees; and opportunities for "broad-based participation," such as stock ownership. HCAP Partners believes that an ownership interest leads to increased productivity and reduced turnover and allows companies to add wealth in the long run.

Mago explained, "We work with companies to develop a roadmap around implementing impact metrics that drive good quality jobs. For example, in some of our transactions we work with management officials to create a broad-based employee stock option program and help them embrace changes such as implementing comprehensive training programs, providing opportunities for advancement to low- and moderate-income (LMI) employees, and setting up a paid sick day program that can be instituted over time. We want the companies to own these practices so that they are sustainable past our investment period."[4]

HCAP Partners measures impact on economic opportunity and health and wellness.[5] Late in 2014, HCAP Partners developed a "floor-and-ladder" approach to help companies implement improvements in job quality standards concerning living wages, health benefits, and paid sick days. "The floor-and-ladder approach is used for all portfolio companies in Fund III as a tool to drive good quality jobs and better outcomes at the portfolio companies we invest in," Mago said.

### FLOOR-AND-LADDER APPROACH

HCAP Partners developed tools to assist companies that received investments from its third fund to implement improvements in job quality standards concerning living wages, health benefits, paid sick days, opportunities for job advancement, and opportunities for broad-based worker ownership. The tools use a "floor-and-ladder" approach and were developed late in 2014 in collaboration with Transform Finance and Pi Investments. Download a PDF of the floor-and-ladder approach.

HCAP Partners produces annual reports on the impact of its investments. Mago explained that HCAP Partners originally monitored outputs ("what we do and who we reach") and now focuses on outcomes ("what difference we have managed to make") in economic opportunity, health care, and wealth creation.

Mago said the firm's emphasis on impact intentionality instead of impact measurement has led to HCAP Partners' recognition as a top impact fund manager.[6] In June 2015, HCAP Partners explained the firm's investing approach at an event of impact investors who plan to assist fund managers to adopt good job quality standards in their portfolios. The meeting, held at the Ford Foundation, involved Transform Finance,[7] the Surdna Foundation,[8] Pi Investments, and Ford.

HCAP Partners believes that a focus on quality job creation does not require the concession of financial return. Mago explained, "We believe that growth in a business's revenue, income, and shareholder value are intertwined with impact intentionality, and we think a healthy, well-aligned workforce helps to drive value creation for employees, customers, and shareholders."

As of June 30, 2015, HCAP Partners had invested in 57 small and medium-sized businesses, of which 49.4 percent are located in LMI communities, Mago said.[9]

Businesses that have received investments from HCAP Partners have increased the number of jobs they provide by 24.5 percent — or 1,510 jobs out of a combined workforce of 7,651 individuals, Mago said. The data are calculated from the time of HCAP Partners' investment to either December 31, 2014, or the "exit" of its investment.

### Inner City Advisors and Fund Good Jobs

Inner City Advisors (ICA), a nonprofit located in Oakland, CA, has provided entrepreneurial education, pro bono advising services, and hands-on assistance for the past 19 years to over 500 small businesses in the San Francisco–Oakland area. According to ICA, a good job is one that exceeds the minimum wage, offers full health and dental benefits, and provides opportunities for employees to move up in the company. Inner City Advisors (ICA), a nonprofit located in Oakland, CA, has provided entrepreneurial education, pro bono advising services, and hands-on assistance for the past 19 years to over 500 small businesses in the San Francisco–Oakland area. According to ICA, a good job is one that exceeds the minimum wage, offers full health and dental benefits, and provides opportunities for employees to move up in the company.

ICA helps companies define their staffing needs and recruit talent from hard-to-employ populations, such as ex-offenders, young people aging out of the foster care system, and people with limited education. ICA explained, "We partner with entrepreneurs who have both a solid business model and a commitment to creating a more equitable economy. We focus on the jobs they create and the individuals they hire. We assist companies in responsibly accessing capital and integrating good job creation in their growth plans from the start."

Of 73 businesses it assisted in 2013, 59 percent were female owned and 48 percent were minority owned, according to ICA. In 2013, 66 percent of these businesses hired workers with employment barriers, it said.[10]

In 2013, ICA launched a nonprofit loan fund, Fund Good Jobs (FGJ), which uses program-related investments and recoverable grants to invest in growing small businesses that have the potential to create good jobs. Sean Murphy, managing director of FGJ and interim chief executive officer (CEO) of ICA, explained that, to combat widening inequality in the San Francisco-Oakland, CA, area, ICA and FGJ work with companies in fast-growing industries that offer significant employment opportunities with low educational barriers, such as restaurants, food manufacturers, and professional and technical services.[11] Murphy added that there is a market gap in access to capital for growing companies that are seeking $150,000 to $2 million.

FGJ provides investments of $250,000 to $750,000 that are structured creatively to support companies of different sizes and capital needs. Companies can secure a lower interest rate on FGJ's investments by meeting certain targets, such as hiring individuals who face barriers to employment, providing health benefits, or offering professional development opportunities. As an investor, FGJ works closely with the leadership teams of its portfolio companies, attending weekly team meetings and board meetings to provide hands-on support in managing cash flow and forecasting revenue.

FGJ has made four investments in the following San Francisco–Oakland, CA, companies, which are located in LMI neighborhoods:

- Back to the Roots, a specialty food manufacturer with lines of sustainable, organic products
- Impact Hub Oakland, a coworking space, business incubator, and event venue that encourages socially conscious entrepreneurship and job creation in Oakland
- Prather Ranch Meat Company, which works with independent ranches and farms to provide high-quality, sustainably raised meats
- Firebrand Artisan Breads, a bakery that produces small-batch, hand-shaped artisanal bread products

FGJ is pursuing certification as a community development financial institution and hopes that this will allow it to access capital from community banks and impact investors. Murphy observed that the integration of capital and support to small business owners is essential for the creation of good jobs.

### Social Capital Partners

Bill Young founded Social Capital Partners (SCP), a national nonprofit based in Toronto, Canada, in 2001 following a successful career in the private sector. He funded SCP with some of the proceeds he received from the sale of two corporations, Hamilton Computers and Optel Communications Corporation, that he had managed as CEO. From its beginning, SCP has been focused on how meaningful job opportunities can be created for people who face employment barriers. The fact that SCP is self-funded has enabled it to make several "strategic pivots" in its work, Young said.

In its first phase from 2001 to 2007, SCP provided venture capital to six entities, comprising a combination of nonprofit and for-profit social enterprises, that employed disadvantaged, hard-to-employ residents. These enterprises included a property management firm in Vancouver that employed women who were victims of domestic violence, a housing renovation company in Winnipeg that employed Aboriginal Canadians, and a courier service in Quebec that hired young people from homeless shelters. Young said that the enterprises created several hundred jobs after five years, but "we [SCP] recognized that we needed to work with the private sector if we wanted to create significantly more jobs."

In a second phase of its work, from 2007 to the present, SCP has focused on providing subordinated debt to more than 50 small business franchise owners in over 80 locations, with the purpose of motivating these businesses to provide employment opportunities for disadvantaged residents. Some of the franchises have been in the auto services industry, which Young described as attractive because of its low educational attainment requirements along with opportunities for upward mobility. SCP offers reduced interest rates to franchise owners committed to hiring a certain number of disadvantaged residents who have been screened and assisted by community-based nonprofit organizations. SCP and the nonprofits take responsibility for any problems with the new hires and find replacements if necessary, Young explained.

In the organization's third and latest phase of work, SCP is looking for ways to make it simple and productive for employers to hire residents who have employment barriers. Young said that nonprofit and government efforts generally focus on the unemployed as the customer but that employers are just as important a customer. "Applying market-based solutions to systemic social issues is the key to sustainable impact," he said.

SCP commissioned Deloitte to develop two reports that were released in 2014: one proposed a "demand-led" Canadian employment and training system with a strong focus on employers[12]; and a second focused on the feasibility of an Ontario-wide program that would encourage small businesses to employ low-income individuals.[13] The second report, financially supported by the Ontario Ministry of Economic Development, Employment and Infrastructure (MEDEI), called for a pay-for-performance model that links payments with outcomes. The model would allow businesses to receive interest rate reductions for hiring low-income residents with employment barriers and retaining those employees for at least six months. In the model, loans would be provided by financial institutions that opt into the program, while funding for the interest rate reductions would come from the Ontario government, which could realize cost savings as low-income residents move from government assistance to stable employment.

Recently, the Ontario MEDEI announced a $4 million pilot known as the Ontario Community Loans Program. The program will give owners of small and medium-sized businesses discounted interest rates on financial products, such as loans, when they commit to hiring people who are faced with employment barriers, including people with disabilities. For loans, the interest rate will decrease for each person hired and retained for the required period. The ministry plans to work with Canadian banks, credit unions, and SCP to implement the pilot, which the ministry said was modeled on SCP's work. The pilot aims to support up to 500 small businesses in creating up to 1,100 new employment opportunities.

Young observed that the program is an example of how social finance strategies can unite public, private, and nonprofit stakeholders by allowing risk, return, and impact to be allocated so that each party's needs are met while delivering social outcomes that cannot be achieved by one party alone.

### Conclusion

Firms such as HCAP Partners, FGJ, and SCP are leading examples of investors who are making investment decisions with the intention of creating good jobs for LMI residents, coupled with ongoing encouragement and assistance to business owners. In the process, impact investors are also seeking to demonstrate that improving employment opportunities will benefit a company's productivity, retention, and morale and potentially result in increased financial return to investors.

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* The views expressed here do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

1 The Global Impact Investing Network (GIIN), a nonprofit that strives to increase the scale and effectiveness of impact investing, defines impact investments as investments made to companies, organizations, and funds with the intention of generating measurable social and environmental impact along with a financial return.

2 An explanation of mezzanine debt is available at http://www.hcapllc.com/investment-criteria/.

3 Limited partners in HCAP Partners' third fund include five banks and four foundations.

4 Huntington Capital changed its name to HCAP Partners in July 2015 to highlight the firm's partnerships with business owners and investors that seek to build profitable, socially responsible companies, noted Tim Bubnack, HCAP Partners managing partner.

5 HCAP Partners' impact reports are available at http://www.hcapllc.com/impact-investing/.

6 Huntington is included in the report *Impact Investing 2.0: The Way Forward — Insight from 12 Outstanding Funds*, available at http://ow.ly/QkH5M. See also ImpactAssets 50, a list of 50 top impact investing fund managers, available at http://impactassets.org/ia50_new/.

7 See http://www.transformfinance.org/.

8 See http://www.surdna.org/.

9 For an investment summary, see http://www.hcapllc.com/funds/. Examples of HCAP Partners' portfolio companies are available at http://www.hcapllc.com/portfolio/.

10 For further information, see Inner City Advisors' 2013 Impact Report at http://2014.innercityadvisors.org/.

11 Jose Corona, ICA's founder and former CEO, left ICA in July 2015 to become director of equity and strategic partnerships for the City of Oakland, CA.

12 The report is available at http://ow.ly/SCNKN.

13 The report is available at http://ow.ly/SCOdM.

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# Breakthroughs in CDFI Capital Access*

By Keith L. Rolland, Community Development Advisor

For a long time, community development financial institutions (CDFIs) have wanted to raise larger amounts of capital in order to make more loans and have greater social impact. A significant step in that quest was two California CDFIs being issued Standard and Poor's (S&P) ratings in April 2015. Two other important moves to raise capital are seven CDFI intermediaries raising $525 million through the CDFI Fund's CDFI Bond Guarantee Program (BGP) and 35 nondepository CDFIs becoming members of the Federal Home Loan Bank (FHLB) system. This article explores each of these developments.

### Two CDFIs Obtain Standard & Poor's Ratings

Housing Trust Silicon Valley provided a $125,000 predevelopment loan to Charities Housing, a nonprofit, for San Antonio Place, a development designed for residents who are steadily employed but who do not earn enough income to afford the high market rents in Silicon Valley. Of the 120 units, 70 percent are rented to very low-income residents, and the remaining units are rented to extremely low-income residents.

Clearinghouse CDFI, a 19-year-old for-profit CDFI[1] that has made $1.1 billion in loans, and Housing Trust Silicon Valley, a 15-year-old CDFI that has invested $94 million in affordable housing financing, received AA and AA– ratings, respectively, from the S&P Ratings Services' U.S. Public Finance Housing Enterprise Group.[2] Since these ratings were issued, S&P and the two CDFIs have received numerous inquiries from other CDFIs interested in receiving ratings.

Doug Bystry, president and chief executive officer of Clearinghouse CDFI, said that the CDFI's primary motivation in seeking the rating was to attract investments from insurance companies in California. He said that senior executives in the insurance companies had told him that a rating from Moody's, S&P's, or a comparable source would be necessary for them to consider investing in a CDFI. He said that, to his knowledge, California insurance companies are encouraged by the state to make community development investments; however, they have made very few CDFI investments.[3]

Bystry said that the process of obtaining the S&P rating took eight months and was very detailed; the CDFI's policies, procedures, and practices and every loan in the organization's portfolio were carefully reviewed. While the S&P rating has the potential to be transformative in raising capital, not every CDFI may receive a high rating because of what Bystry described as S&P's objective and stringent evaluation.


Clearinghouse CDFI provided a $1 million loan and grant financing package to the Culinary Training Academy (CTA) in Las Vegas, NV, for working capital to support an expansion of services. CTA is a nonprofit that provides vocational training to help entry-level workers obtain good-quality jobs. CTA will hire 200 additional employees as a result of this business expansion.

Jim Mather, chief lending officer at Housing Trust Silicon Valley in San Jose, CA, said that the S&P ratings "expand the range of potential investors." He also said that the traditional capital-raising strategy in which banks provide loans to the CDFI and the CDFI, in turn, makes loans, supplemented by some capital from foundations and the CDFI Fund, has its limitations.

Mather said that Housing Trust is particularly interested in obtaining investments from insurance companies. He thought that the CDFI and insurance companies would get to know each other during the next year or so and that such investments were not likely to occur rapidly. In addition, the CDFI wants to attract investments from high-tech companies in Silicon Valley. Corporate treasurers look for an S&P or comparable rating, he noted.

Housing Trust is also developing plans for a single-family taxable mortgage revenue bond issue with a first tranche of $7 million that would fund 400 down payment second mortgage loans. The S&P rating will enable the CDFI to secure a "better interest rate and more potential investors," stated Mather. The rating also "makes it easier to start a conversation" with banks on Community Reinvestment Act–related investments and makes organizations "stand out." According to Mather, the rating took a little less than six months to complete and involved a very thorough multiyear audit. S&P and the two CDFIs declined to disclose the cost of the ratings.

S&P began analyzing the CDFI industry using its criteria for state housing finance agencies, according to S&P's Credit FAQ.[4] Mikiyon W. Alexander, senior director and analytical manager with S&P's U.S. Public Finance Ratings, explained that S&P had previously rated the Pennsylvania Housing Finance Agency, the New Jersey Housing and Mortgage Finance Agency, the Philadelphia Housing Authority, and the Newark Housing Authority.

In assessing a CDFI credit rating, S&P evaluates earnings quality, financial strength, and capital adequacy; asset quality; debt levels and types; and overall strategy and management, according to the FAQ. S&P said that "understanding a CDFI's overall impact enhances our perspective of a CDFI's strategy and management."

Alexander said that S&P takes into account the CDFIs' social mission when evaluating and rating CDFIs and noted that CDFIs are rated within S&P's Public Finance Department and not in its Corporate Finance Departments. He explained that "because of the social and mission-driven nature of CDFIs, the metrics and comparisons of financial performance are very similar to our other outstanding social lending– or social mission–based municipal or nonprofit organizations. We are not expecting financial ratios similar to what you would expect for financial institutions. … The portfolios are different in nature."

Alexander said that CDFIs may want to obtain an S&P rating to better position themselves with investors and potentially to enter the capital markets to help support their mission. The FAQ notes that "although we do not expect CDFIs to issue public-market debt to support their missions, the rating does allow such forms of financing to be a viable option."

### CDFIs Raise Money Through the CDFI Bond Guarantee Program

The Small Business Jobs Act of 2010 authorizes the U.S. Department of the Treasury to guarantee the full amount of bonds or notes issued to support CDFI loans and investments by providing CDFIs with long-term capital.[5]

Bonds totaling $525 million have been issued since 2013 by qualified issuers that assemble and submit BGP applications and issue bonds on behalf of CDFIs.

In BGP activity to date:

- the Opportunity Finance Network issued a $100 million bond in 2014 on behalf of Clearinghouse CDFI in California;
- the Community Reinvestment Fund, Inc., Minneapolis, MN, issued two bonds in 2014, one for $125 million on behalf of The Community Development Trust, LP, and one for $200 million for Capital Impact Partners, IFF, Low Income Investment Fund, and The Reinvestment Fund; and
- a Bank of America subsidiary, TriSail Funding Corporation, issued a $100 million bond in 2014 on behalf of Enterprise Community Loan Fund, Inc., and Local Initiatives Support Corporation.

### CDFIs Seek Federal Home Loan Bank Membership

Under the Housing and Economic Recovery Act of 2008, nondepository CDFIs became eligible for membership in the FHLB system, which consists of 12 regional FHLBs. Members receive loans, known as advances, from the FHLB in their region at favorable rates.

Thirty-seven nondepository CDFIs had become FHLB members as of June 30, 2015, according to the Federal Housing Finance Agency. Twelve nondepository CDFIs joined the FHLBs in 2014,[6] and five more joined in the first quarter of 2015. The Reinvestment Fund, based in Philadelphia, joined in 2014. Clearinghouse CDFI, as mentioned earlier, is a member of the Federal Home Loan Bank of San Francisco.

In 2015, the Community First Fund, a CDFI based in Lancaster, PA, became a member of the Federal Home Loan Bank of Pittsburgh (FHLBP). Joan M. Brodhead, executive vice president and chief operating officer of Community First, said that FHLBP membership is an alternative financing source that provides ready access to capital. Community First envisions that FHLBP's Banking on Business program will be a credit enhancement that will enable some small business borrowers to be approved for credit, she said. The CDFI, which also plans to explore the possible use of FHLBP's affordable housing programs, had discussed FHLBP membership for several years. After FHLBP revised some borrowing and collateral requirements, the CDFI applied for membership and was approved in several months.

A U.S. Government Accountability Office report[7] said that FHLB collateral requirements can discourage nondepository CDFIs from seeking FHLB membership and from obtaining advances. According to the report, "The FHLBanks generally impose collateral requirements on nondepository CDFIs that are comparable to those imposed on depository members categorized as higher risk and in some cases, comparable to those imposed on insurance companies." Some FHLBs have revised these requirements.

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* The views expressed here do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

1 Clearinghouse CDFI is one of a handful of for-profit CDFIs.

2 According to S&P, an obligor rated AA has very strong capacity to meet its financial commitments. The highest issuer credit rating assigned by S&P is AAA.

3 Insurance companies in California that write California premiums of $100 million or more annually have been required since 2011 to develop policy statements containing their goals for community development investments. For details, see http://ow.ly/RsAAt.

4 See http://ow.ly/RNOyl.

5 For program details, see http://ow.ly/Sz7dB.

6 See U.S. Government Accountability Office report on CDFI membership in Federal Home Loan Banks. The report, which states that the number of nondepository CDFIs that have become FHLB members has increased each year since the first one joined in 2010, is available at http://www.gao.gov/assets/670/669831.pdf.

7 See the U.S. Government Accountability Office report.

FEDERAL RESERVE BANK OF PHILADELPHIA

CASCADE: NO. 89, FALL 2015

# The Reinvestment Fund at 30: Insights and New Directions*

*Thirty years ago, a small group of community developers, activists, and business people formed a community loan fund in Philadelphia called the Delaware Valley Community Reinvestment Fund. In 1999, the organization was renamed The Reinvestment Fund (TRF). TRF is certified as a community development financial institution (CDFI) by the U.S. Department of the Treasury's CDFI Fund. Since 1985, TRF has made $1.5 billion in loans and investments and has financed housing, community facilities, supermarkets, commercial real estate, and energy-efficiency projects. The CDFI has been a leader in analyzing data and markets and in participating in regional and national policy discussions. To mark the organization's 30th anniversary,* Cascade *asked TRF to share insights from its experiences, explain the new directions in which the organization is headed, discuss best practices in impact measurement, and comment on the equity implications of its work.*

### 1. What insights and recommendations can TRF share from its lending, real estate development, research, and advocacy work?

The Reinvestment Fund (TRF) is now entering its fourth decade with a focus on integrating data, policy, and strategic investments to revitalize communities and improve people's lives throughout the country. TRF believes that this requires organizing people, capacity, data, and capital. Although it is not necessary for all these elements to be present in each project, TRF increasingly finds that much of its work brings all these elements together.

In Baltimore, TRF has worked with Baltimoreans United in Leadership Development (BUILD) since 2006 to reverse the tide of rapid decline in Oliver, a low-income neighborhood in East Baltimore adjacent to Johns Hopkins Medical Campus. TRF first engaged community residents in developing a neighborhood revitalization plan. Local residents surveyed the conditions of every neighborhood parcel, including more than 1,100 abandoned buildings and vacant lots, which had become magnets for drug trafficking and other criminal activity. Their findings became part of the data analysis in the final neighborhood plan, which uses a "build from strength" investment strategy. Through the strategy, investments are made in distressed areas that are near regional assets, such as universities, hospitals, employment cores, or transportation hubs, and the existing asset is leveraged.

TRF and BUILD partnered to create TRF Development Partners (TRF DP), TRF's real estate development affiliate, to implement the plan. In East Baltimore, there was no existing capacity to develop housing — no developers were investing in the market to build homes. Creating TRF DP was an effort to reverse that trend. Working with BUILD, TRF organized $10 million in capital from more than 20 institutional investors to fund the development effort. TRF DP has leveraged the initial capital pool to invest $55 million in housing development in East Baltimore. Vacancy dropped from 40 percent a decade ago to 8 percent today.[1] TRF has learned that increasing housing occupancy in a deteriorated area sends a clear positive market signal that stimulates greater reinvestment. Today, most new building permits for work above $25,000 in the area are from private investors. The development in East Baltimore was achieved without displacing any local families.

**Wissahickon Charter School is a high-performing Philadelphia school that focuses on the environment as an integrating theme for K–8 instruction. In 2014, with TRF financing, the school opened the doors on its second campus, expanding to serve 478 students, increasing the school's total enrollment to 956 students. The new facility is adjacent to the 55-acre Awbury Arboretum, which functions as an outdoor classroom. TRF has worked with the school since 2002 and was its first lender.**
Photo Credit: Wissahickon Charter School

TRF also has learned that employment is necessary for neighborhood stability; therefore, TRF DP has tailored its construction process to accommodate smaller, local contractors. Seventy percent of TRF DP's construction projects in East Baltimore use local firms, and 50 percent of those firms are minority owned. Today, median household incomes for families moving into the area have risen 64 percent, and home sales prices for newly renovated units are 256 percent higher. TRF DP and BUILD have worked to retain long-term residents while also attracting new families to the area. This effort has increased the neighborhood's income integration. As TRF continues its efforts in East Baltimore, it plans to seek more investments from banks and other institutional investors.

**In Camden, NJ, TRF financing supported the opening of the city's first new supermarket in decades. The new store replaced a store that was closed for more than a year and created more than 80 jobs (some part time), many going to local residents. The project restored healthy food access to the surrounding underserved community by providing a full selection of fresh fruits and vegetables along with seafood, meats, dairy, and other grocery products.**
Photo Credit: The Reinvestment Fund

Access to healthy food is another area of TRF's work that brings together people, capacity, data, and capital. In Pennsylvania, TRF was part of a group of leaders and experts from state and local governments, the supermarket industry, and the civic sector who offered recommendations for improving the availability of affordable, nutritious food in underserved areas in the state. The group quickly identified financing as a barrier to helping grocers locate to neighborhoods with inadequate access to fresh, healthy food. To address this challenge, TRF partnered with the Commonwealth of Pennsylvania, the Food Trust, and the Urban Affairs Coalition to create the Pennsylvania Fresh Food Financing Initiative (FFFI) in 2004. TRF led the task of organizing capital for the initiative, using a seed grant of $30 million from the Commonwealth to leverage $145 million in additional investments for loans and grants for predevelopment, acquisition, and equipment and construction costs, as well as start-up costs, such as employee recruitment and training. Over a six-year period, the FFFI financed 88 projects, resulting in more than 5,000 jobs and improving healthy food access for 400,000 Pennsylvania residents. Building on the knowledge and experience gained from the FFFI, TRF established the New Jersey Food Access Initiative (NJFAI) with capital from the New Jersey Economic Development Authority, Living Cities, and the Robert Wood Johnson Foundation. Working with the NJFAI, TRF has provided more than $22 million in financing for

20 healthy food access projects in the past four years alone.

An important aspect of TRF's achievements in this sector is its commitment to data-advised decisions. TRF has produced 10 studies on food access subjects, including financing mechanisms, program design, and food systems. TRF's Limited Supermarket Access (LSA) analysis is devoted to understanding access to healthy, fresh food, particularly in low-income areas. The analytical tool quantifies disparate levels of food access and estimates the dollar amount that area residents spend outside their communities. TRF uses this tool to assist supermarket operators and potential investors to identify locations where local demand would support a new full-service store.

### 2. In what new directions will TRF be taking its work?

A key element of TRF's growth is taking its experience and expertise to other communities in need across the country. TRF believes that there is a real opportunity to help create transformational change in low-income communities beyond TRF's traditional service area in the Mid-Atlantic, which encompasses New Jersey, Pennsylvania, Delaware, Maryland, and Washington, D.C. The organization has already seen this through its healthy food work. For example, community development organizations, public officials, and community groups located outside TRF's Mid-Atlantic states have asked for the organization's help to increase access to healthy food in their own communities.

These requests for assistance were the impetus behind TRF's decision in January 2014 to create ReFresh, a national network of practitioners engaged in improving healthy food access across the U.S. With funding from the JPMorgan Chase Foundation, TRF supported an inaugural group of community development financial institutions (CDFIs) from California, Colorado, Florida, and Ohio with data and capacity-building assistance as they worked to launch or expand healthy food financing programs in their service areas. Since then, TRF has welcomed several new CDFI members to the ReFresh initiative, including most recently the First Nations Oweesta Corporation.[2] In addition, TRF plans to use the ReFresh platform to learn about and share innovations and trends from across the country. For example, several opportunities are emerging that connect supermarkets and grocery store development with strategies that increase population and community health and increase consumer demand for healthier food options. Supermarket operators are hiring dieticians to work in their stores or are partnering with community groups to offer nutrition education and cooking demonstration classes to their customers. In addition, federally qualified health centers are locating in supermarkets and collaborating on health and wellness programs. As TRF works with a network of healthy food providers across the country, it will be seeking additional capital investments to support this work.

**Kinder Academy is an early childhood education provider that prides itself on being a developmental partner with its students and their parents in order to comprehensively prepare children for kindergarten and beyond. TRF financing, in partnership with the CDFI Fund, is helping the high-quality provider expand to a fourth facility in Philadelphia. The new center will serve 130 children and create 25 jobs.**
Photo Credit: Kinder Academy

Another priority over the next five years is increasing TRF's impact on communities through a dual approach of data analysis and capital deployment. For example, TRF is working to improve access to high-quality early childhood education (ECE) in Philadelphia in partnership with the William Penn Foundation and the Public Health Management Corporation (PHMC). Philadelphia has only 169 high-quality ECE providers (defined as Keystone STAR 3 and 4 operators) out of almost 3,000 providers across the city, which means there are significant gaps in the availability of quality services to low-income children. Given the enormous benefits of high-quality ECE experiences, including improved outcomes and school readiness for young children, Philadelphia needed a transformative initiative to expand services. As part of its effort to understand the gaps, the William Penn Foundation made a grant to TRF to develop comprehensive information about the availability of high-quality ECE in Philadelphia. TRF's analysis is accessible through Childcare Map,[3] an interactive tool that helps identify the neighborhoods where high-quality care is most scarce and where investments are most needed. With $4.5 million from the William Penn Foundation and additional capital from TRF's network of more than 850 investors, Philadelphia now boasts a $7.6 million fund to support planning efforts and capital awards as part of the initiative. Child-care providers used the Childcare Map tool to identify gaps and expansion opportunities. In turn, the analysis helped TRF and the PHMC select award recipients and target resources and capital. In its first year, the fund selected 14 high-quality ECE providers to receive awards that are to be used for renovating existing facilities and opening new ones. The awards are expected to help serve an additional 850 children across the city.

Pay for success (PFS) programs are an emerging model that uses data and capital to effect change. Within PFS programs, success is based on the outcomes of specific human service interventions. Predetermined social impact data thus become the means by which investment returns are measured. In 2014, TRF participated in the nation's first county-level PFS program, which brought together Cuyahoga County in Ohio and FrontLine Service, a leading provider of comprehensive continuum of care services for homeless persons in Ohio. TRF's participation in this PFS program builds on its extensive experience financing affordable housing and community services. TRF also draws on its strong expertise in analyzing housing policy issues and, especially, inequities related to low-income and vulnerable populations. This summer, TRF closed on its second PFS project, which aims to reduce chronic homelessness in Santa Clara County through permanent supportive housing. It is California's first PFS project, and it brings together a diverse set of partners.

TRF is currently seeking a range of partners and conventional financial institutions to participate in a dialogue on PFS programs and to attract additional resources to this new social impact financing mechanism. Over the next five years, TRF will carefully assess the results of PFS programs, with the hope of replicating the model in other policy areas, including housing, education, social services, and health care.

Another priority for TRF is to continue to lead efforts to promote the social, economic, and physical health of low-income and vulnerable populations. TRF recognizes that strong, healthy communities are marked by far more than quality housing and accessible real estate markets. TRF's goal is to scale proven interventions nationwide (for example, TRF's work in financing healthy food access and community health centers) and seed innovation arising from locally identified collaborative efforts. The unsustainable costs of health care and the significant federal and state policy reforms that seek to address the problem equitably point to a conclusion: Urgent action must be taken to address the social determinants of health.[4] Reversing declines in health, especially in low-income communities, can be achieved only through the combined efforts of the community development and health-care sectors.

TRF is well positioned to play a leadership role in improving certain social determinants of health: TRF finances housing, grocery stores, schools and early childhood education centers, community health clinics, and sustainable energy projects — all of which are simultaneously markers and catalysts of community health. TRF is part of a five-year national initiative with the Kresge Foundation and the Public Health Institute (PHI) to align the resources of health and community development stakeholders. In selected communities across the nation, TRF is designing investment portfolios balanced across sectors to facilitate comprehensive health improvement strategies. The initiative, which is focusing resources in neighborhoods where both health and social inequities are concentrated, expects to build a field of practice that provides the tools, evidence, and models to support replication across the country.

### 3. What does TRF consider best practices on impact measurement? How can CDFIs and community development corporations (CDCs) that have funding and staffing constraints measure impact?

Almost 16 years ago, TRF formed a dedicated department, Policy Solutions, which monitors community outcomes, assesses impact, and researches policy-relevant issues central to TRF's mission. Policy Solutions does this work not only for TRF but also increasingly for a wide range of clients from the federal government and cities to foundations and civic organizations. Policy Solutions' work has helped mold TRF as an information intermediary as much as it is a capital intermediary.

PolicyMap is the online tool TRF uses to access and share data and analyses. TRF also uses the platform to understand the impact of TRF's work in context. TRF geocodes each of its investments and loads them into the PolicyMap platform. Using PolicyMap's 37,000 data indicators, TRF monitors community trends over time. For example, TRF monitors healthy food access investments against its own LSA analysis, along with the U.S. Department of Agriculture's Food Access Research Atlas. Through PolicyMap, TRF can plot areas (census block groups and tracts) with low access to healthy food, view the number of limited-service grocery stores, and estimate local grocery demand.

An important aspect of impact measurement is transparency. Making TRF's investment data accessible on PolicyMap is one way to achieve that. Another element of transparency is sharing the methodology TRF uses for its proprietary analytics, whether it is the LSA or TRF's Market Value Analysis (MVA) real estate investment tool. TRF makes its methodology available with every study that it completes.

As CDFIs work to effect positive change in low-income communities, it is also good practice to look at changes over time. TRF has a strong focus on place and, in many neighborhoods, has been able to invest in multiple projects over several years.

For example, TRF is currently assessing the impact of its residential real estate activity on East Baltimore's Oliver neighborhood. Beginning in 2013, TRF has been using a variety of research methods to study the neighborhood. These methods include a quantitative analysis of indicators used in the MVA, the use of U.S. Census Bureau data to gauge trends in the demographic composition of residents and employees, and the gathering of qualitative data (e.g., through a resident survey). Additionally, TRF conducted a review of home sales and building permits within TRF DP's primary area of influence in the neighborhood between 2006 and 2014. Specifically, TRF is exploring home purchases by individuals and investors to determine how the sales market has changed within this area in the years since TRF DP started its work. Preliminary analysis suggests that through its work, TRF DP has contributed to the establishment of a rehab housing market with a share of the sales at prices far above levels seen before its involvement.

Similarly, with the recent update to the LSA analysis, TRF has applied the LSA methodology in years going back to 2005 as a way to understand changes in access over time. Philadelphia was one of the areas TRF examined in depth. According to TRF's analysis,[5] 133,019 people in Philadelphia lived in areas without easy access to healthy options in 2013, a decrease of 56 percent from 2005, when 301,397 people struggled to find healthy foods in their neighborhoods. TRF's study also revealed that TRF-financed retail grocers in Philadelphia are the nearest option for nearly 187,000 people. By locating in or near LSA areas, TRF-financed stores decreased potential LSA populations by 67,000, with substantial decreases seen in West and North Philadelphia.

Collecting and analyzing data enable the more strategic deployment of scarce resources in ways that can maximize impact. For example, in New Jersey, with support from the Robert Wood Johnson Foundation, TRF worked with potential borrowers to determine the likelihood that low-income residents will use new grocery stores in underserved areas. Using a Huff retail model,[6] TRF was able to estimate the potential customer base location. While the LSA finds areas of inequitable access, the Huff model measures the likelihood that LSA residents will shop at a proposed store, looking at factors such as store distance and the presence and size of competing stores.

While TRF has been fortunate to have the internal capacity to do its own data analysis and impact assessment, it realizes that many smaller CDFIs and CDCs may not have the resources to do this. But there may be different ways to approach impact assessment, given resource limitations. One barrier that has been lowered significantly over the past few years is the cost of technology and access to public data. Technological advancements have made it easier to access and use data in illustrative, robust ways. From online survey tools to platforms such as PolicyMap that provide free access to public data and the ability to spatially analyze data quickly, technology is becoming easier to use at a reasonable cost. For a small CDFI or CDC, these technological advancements can offer a path to understanding impact without incurring large resource burdens.

Another way in which impact can be assessed is through partnerships with educational institutions. Increasingly, smaller organizations are building relationships with academic institutions to assess impact in the communities they serve.

Finally, TRF thinks it would greatly benefit the CDFI industry as a whole if a centralized, standardized data collection platform was created and maintained. While CDFIs currently submit outcomes data to the CDFI Fund as part of the Community Investment Impact System (CIIS) reporting, the process is annual and the data requirements vary significantly. For example, North American Industry Classification System (NAICS)[7] codes are currently mandatory for business loans in CIIS, but not for all other loan types. TRF's real estate portfolio is not required to report industry codes, but TRF chooses to do so because it collects that information for internal analysis. Real estate transactions from other CDFIs typically do not include industry codes, so there is little indication as to how the loan provides services. This makes it difficult to analyze the data to understand impact. The development of a single, standardized nationwide database with spatial, financial, and social attributes of CDFI investments would create an effective platform for research and impact assessment.

Another benefit of such a system is that it would make expansion into new business lines easier. CDFIs are very diverse. Some are primarily focused on small business lending, while others have experiences in a variety of other sectors. For a CDFI that may be exploring a new business line, the ability to learn from the data captured by other CDFIs that have been working in that area could be beneficial, and the exchange of data would allow the CDFI to learn from the past experiences of other organizations.

### 4. How do CDFIs such as TRF build equity in low-income communities?

TRF complements its lending with a data and analytical approach designed to identify where inequities exist. For example, TRF's LSA analysis identifies areas with inequitable and inadequate access to healthy food as compared with well-served areas. This analysis is then harnessed for program delivery and strategic investment to address the inequities of access.

Similarly, TRF understands that the single greatest asset of many households — especially those with lower incomes — is a home. To this end, TRF has supported and promoted equitable housing practices for decades through TRF's lending, policy, and real estate development work. A recent example is TRF's work in Mount Holly, NJ. This is a community in which citizens alleged discriminatory housing practices after 300 homes were demolished in an effort to create new construction of market-rate housing. Those who were displaced were primarily low-income and minority residents. In 2013, the township contracted with TRF DP to help create a plan for a 44-home subdivision that includes 20 replacement units, which will ensure an integrated, mixed-income community. The first 26 units of affordable and market-rate housing will begin construction this year.

Through its policy analysis, TRF has worked to understand the dynamics that undermine the value of a home. For example, TRF's foreclosure research and analysis are designed to help understand its driving forces in an effort to curtail the impact on people of modest means and the communities in which they live. In Pennsylvania, TRF's analysis played a critical role in helping a group of housing advocates revive the state's widely successful Homeowners' Emergency Mortgage Assistance Program — better known as HEMAP. The popular program, launched in 1983 and managed by the Pennsylvania Housing Finance Agency, has saved thousands of homeowners from losing their homes to foreclosure. But despite its track record and impact, funding was eliminated in July 2011 and homeowners lost a significant resource to help them stay in their homes. Almost immediately after HEMAP was cut, housing advocates collaborated to make the case to reinstate it. They turned to TRF to develop a data-driven report that could demonstrate HEMAP's significant impact across the state. TRF's analysis was influential, showing the benefits and impact of HEMAP and the costs of foreclosure to homeowners, lenders, state revenues, and the wider economy. The case was so strong that it served as the catalyst to help persuade state officials to fund and restart HEMAP using Pennsylvania's proceeds from the national mortgage servicer settlement. After a year of dormancy, HEMAP was restarted in mid-2012.

Although TRF has made strides in increasing access to affordable housing, quality education, healthy food, and health care in several communities over the past 30 years, many low-income families across America continue to face economic and social hardship. There is great need for work like TRF's and an even greater urgency for more thoughtful and strategic ways to maximize impact for low-income communities.

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* The views expressed here do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

1 See The Reinvestment Fund, *30 Years: Celebrating 30 Years of Impact*, 2015, available at http://ow.ly/RhCac.

2 First Nations Oweesta Corporation supports economic growth in Native American communities through the creation, development, and capitalization of CDFIs. For information, see http://www.oweesta.org/.

3 See http://www.trfund.com/childcaremap/.

4 For more information on social determinants of health, see the World Health Organization's resources, which are available at www.who.int/social_determinants/en/.

5 See The Reinvestment Fund, *2014 Analysis of Limited Supermarket Access*, available at http://ow.ly/StPaj.

6 The Huff retail model is a way to calculate the probability that a resident in a given location (census block) will shop at a particular store based upon (1) distance traveled to a store on a road network and (2) store square footage. The basis of this methodology is the work of Dr. David L. Huff and is described in his article "A Probabilistic Analysis of Shoppinf Center Trade Areas," which is available at http://www.jstor.org/stable/3144521.

7 See www.census.gov/eos/www/naics/.

FEDERAL RESERVE BANK OF PHILADELPHIA

CASCADE: NO. 89, FALL 2015

# Spotlight on Research: Lessons Learned from Pay for Success Programs*

By Marvin M. Smith, Ph.D., Senior Community Development Economic Advisor

Various social problems, such as homelessness and prison recidivism, impose substantial costs on taxpayers. The mounting costs that result from these troubling social concerns at the local, state, and federal levels force officials to seek alternative ways to raise funds to deal with these issues. One such effort is to use a relatively new source of funding called "pay for success (PFS)," also known as "social impact bonds," or "SIBs." Currently, there are more than 40 PFS initiatives underway worldwide. A report by Emily Gustafsson-Wright, Sophie Gardiner, and Vidya Putcha discusses what PFS programs are and the lessons learned from using this type of financing to address pressing social issues.[1] The following is a summary of their report.

## Background

Marvin M. Smith, Ph.D.

Many nonprofit organizations both here and abroad often lack sufficient capital to maintain their operations. Moreover, efforts by governments to produce favorable social outcomes are similarly hindered by funding deficiencies. An alternative approach to generate funds to address social ills and promote positive outcomes was devised in the United Kingdom in 2010. For a detailed discussion of the origin and structure of PFS financing, see "Pay for Success: Financing Research-Informed Practice" by Noelle Baldini in this issue of *Cascade*. In short, the PFS approach relies on private investment capital to finance intervention programs to deal with social issues. Investors are repaid with interest only if predetermined goals are met. Thus, the risk of economic loss from an unsuccessful program is shifted from the government to the private sector.

The authors discuss the lessons learned from this new type of financing and assess its potential use to combat social problems.

## Methodology

The authors undertake a comprehensive study of the topic of PFS financing. Their analysis covers the experiences of programs using this type of financing worldwide. As part of their examination, they performed a thorough review of the literature on the topic using reports, working papers, and editorials among other types of documents. They also conducted numerous interviews with individuals who play a key role in the PFS arena. Additionally, the authors identified 38 PFS programs to study in depth and supplemented their study with surveys (in person, online, or over the telephone) with key stakeholders — investors, intermediaries, and service providers.

## Insights from the Analysis

The authors draw several observations from their inquiry of a PFS financing approach, some of which are as follows:

- The balance of PFS efforts thus far have centered on sectors and problems with certain characteristics. Some deal with areas in which the government has already engaged nongovernmental agencies to deliver services (e.g., programs concerning job and life skills training). Some involve issues in which "service inputs are fairly complex but the outcomes are simple to measure, such as homelessness, foster care, and prison recidivism." Some also deal with matters outside core government services, such as job training for prisoners rather than law enforcement activities.
- The authors weigh in on the issue of whether PFS programs or SIBs can attract a pool of private funding. They find there are several facets to the issue. The prospect of receiving a financial return on an investment that yields social benefits might be appealing to traditional private funders, such as foundations. The participation of these private funders in PFS initiatives might be in addition to their existing grant programs. SIBs might attract funding from new types of private funders seeking investment opportunities beyond traditional capital markets. These new funders might include high-net-worth individuals, credit unions, commercial investors and banks, and pension funds.
- PFS programs potentially contribute to social service delivery but must contend with certain programmatic concerns. The development of deals that are an integral part of the financing approach can be challenging because of the difficulty in getting the many different types of players involved to collaborate. Further complications might be introduced with the complexity of multiyear contracts. Moreover, deal-making also can be made difficult when determining the appropriate outcome metrics as well as calculating the costs and benefits of the intervention being undertaken.
- The authors find that there exists a great deal of variation in the PFS projects to date in terms of structure, mechanics, and stakeholder roles. This, according to the authors, bodes well for the future use of this type of funding, since there is tremendous flexibility in structuring a deal. This allows for deals to be tailored to the specifications necessary to address the social problem being targeted. The authors point out that the PFS model was devised as one of two models: either as an individual transaction dealing with a particular intervention, or as a fund intending to achieve a set of outcomes involving (potentially) multiple service providers.
- In the authors' assessment of the 38 PFS initiatives studied in detail, they recognize four factors that were key in structuring a deal: measurable outcomes, evidence of intervention impact, government support, and dedication and collaboration of the stakeholders. Most of the deals examined relied on administrative data or specific data collected in conjunction with the intervention impact. The outcomes or outputs of all the deals were identified, and there was evidence in many deals that the participating service providers were capable of delivering the services and achieving the outcomes. However, considerable variation existed in the robustness of the evidence. The authors attribute this to some degree on the level of risk the investors were willing to accept. The authors determine that none of the deals studied would have been possible without government support. They also report that the "stakeholders overwhelmingly highlighted the importance of all of the actors' willingness to put in the necessary time and effort" to structure the deals.
- According to the authors, it is too soon to tell whether PFS programs sustain impact. These initiatives might be a "passing fad and things will go back

to business as usual after deals are complete." However, the authors think the deals that provide multiyear contracting do achieve longer-term impact by providing consistent care over time and are a step in the right direction. Multiyear contracting also has an added feature in that it "helps to protect the provision of social services from politically influenced ebbs and flows of funding."

- The authors believe that over time the process of deal-making will become more manageable and that evidence of this is already occurring. Among the 38 deals studied, deal development ranged from six months to three years. In the UK, where the market for this type of funding is the most mature, the development of deals almost always takes six to nine months. The authors anticipate the development of standardized systems as lessons are learned and the resulting operating models are refined over time.
- The authors indicate that only eight of the 38 deals studied made use of rigorous experimental or quasi-experimental evaluations of the deals for measuring impact as a condition for determining repayment. The majority (28) of the deals investigated used administrative data. The authors note further that the type of evaluation was determined to some extent by the nature of the intervention and, in part, by the desire of investors and outcome funders[2] to verify the causality of the outcomes.
- The authors find that a majority of the existing PFS initiatives do not achieve substantial scale. Twenty-five of the 38 deals serve populations with 1,000 or fewer individuals. The authors hasten to add that this does not mean that PFS programs are incapable of serving larger numbers of people. They point out that the Innovation Fund in the UK, which brings together multiple investors to jointly support a set of outcomes to be provided through many service providers in 10 deals, serves more than 16,000 individuals. According to the authors, the use of SIB funds supported by multiple large donor agencies might be one approach to tackle large-scale social issues. In many deals, the number of individuals who benefit from the intervention is dictated by the specific target population mandated in the specific PFS program.
- While the authors feel the development of PFS programs has a bright future worldwide, the challenges in implementing them are likely to be considerable in developing countries. In these cases, the efforts and cooperation of the many parties involved in the deal-making process (concerning the choice of the target population, the government's role, and the outcome and evidence identification) will be even more imperative. In order to assist in these contexts, the authors stress the crucial role that philanthropy might play. Philanthropists can help by funding the collection of data and evidence necessary to start the conversations about outcome-based financing with outcome funders.
- The authors offer some guiding principles for the future of PFS programs. They think that meeting the challenges of complex deal-making in the future will be tempered by creative thinking and collective effort. Also, future use of this nascent form of financing might be enhanced by increased transparency and knowledge sharing. They suggest that the implementation of PFS initiatives can be nurtured by collaborating with those who have practiced this type of funding in addition to attending workshops and conferences on the topic as well as accessing readily available information online.

### Closing Remarks

The preceding merely scratches the surface of the contribution made by the authors. They provide a wealth of knowledge gleaned from a comprehensive inventory of all active PFS initiatives contracted as of March 1, 2015. For more details on their work, see their full report.

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* The views expressed here do not necessarily represent the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

1 Emily Gustafsson-Wright, Sophie Gardiner, and Vidya Putcha, "The Potential and Limitations of Impact Bonds: Lessons from the First Five Years of Experience Worldwide," The Brookings Institution, July 2015, available at http://ow.ly/RpMTb.

2 An outcome funder is the entity responsible for handling the pay for outcomes. It is usually a government agency, foundation, or development agency.

# MAPPING OUR COMMUNITY

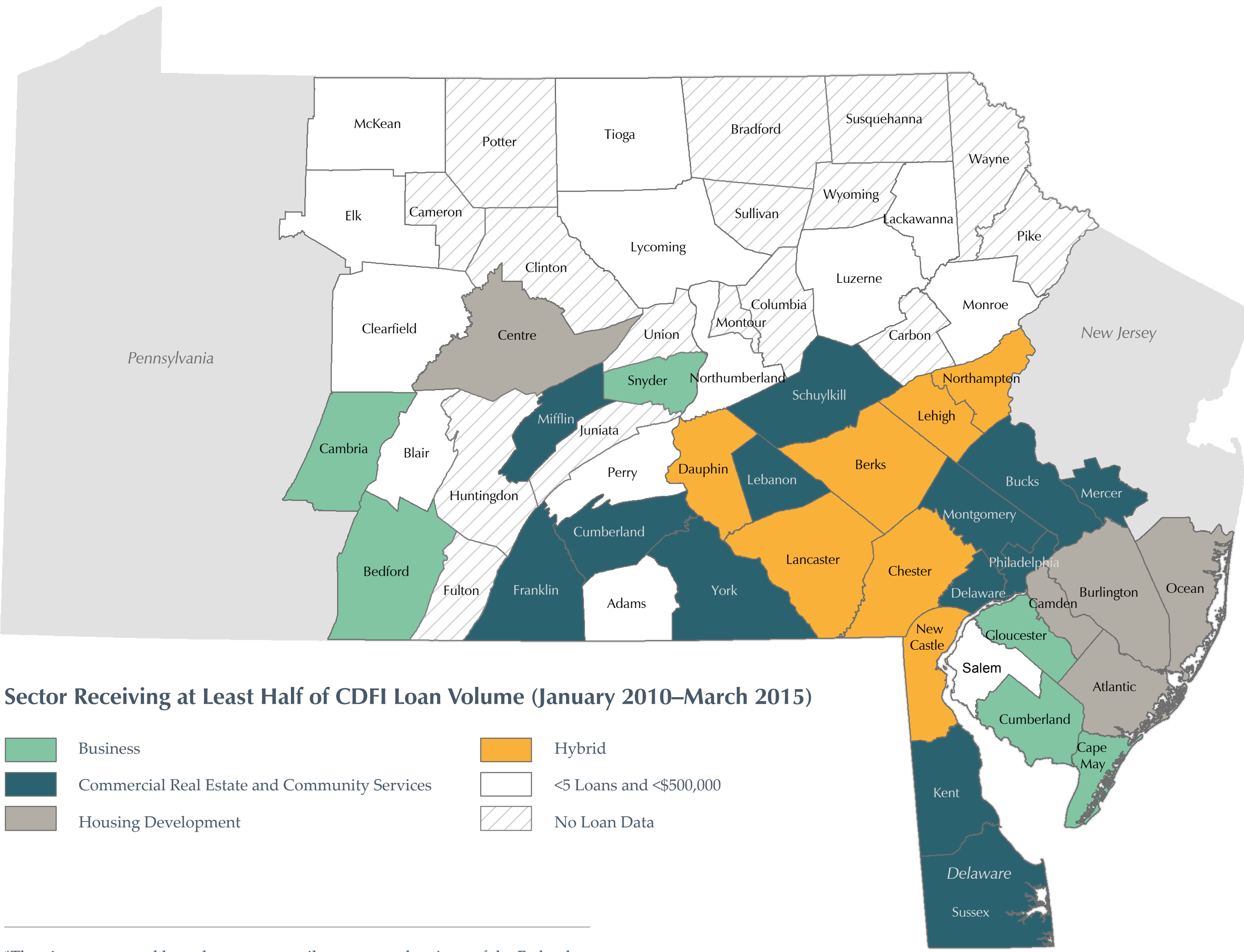
## Third Federal Reserve District

KEITH WARDRIP, COMMUNITY DEVELOPMENT RESEARCH MANAGER

### A Sample of Community Development Financial Institution Lending*

Community development financial institutions (CDFIs) provide financing to promote community and economic development in a variety of ways. The Opportunity Finance Network collects data contributed voluntarily from both member and nonmember CDFIs. This feature summarizes the loans made by 24 participating CDFIs between January 2010 and March 2015.[1] The map indicates which sector (business, commercial real estate and community services, or housing development) received at least half of the reported CDFI financing during this period based on loan volume; counties in which no sector received a majority of financing are labeled "hybrid."

The roughly 1,600 loans made by participating CDFIs in the Third Federal Reserve District since 2010 totaled more than $610 million, with Philadelphia County accounting for three-quarters of this volume. In Philadelphia, as in 12 other counties, the majority of lending was directed to commercial real estate and community services, while loans to businesses and for housing development were more common in New Jersey and some central Pennsylvania counties. CDFI lending was more evenly distributed across sectors in seven "hybrid" counties.




**Sector Receiving at Least Half of CDFI Loan Volume (January 2010–March 2015)**

- Business
- Commercial Real Estate and Community Services
- Housing Development
- Hybrid
- <5 Loans and <$500,000
- No Loan Data

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[1] Of the 24 participating CDFIs, eight are located in counties in the Third Federal Reserve District. Because many of the roughly 30 CDFIs within the Third District do not contribute data to the Opportunity Finance Network, this is not a complete picture of all CDFI lending in Third District counties. See https://www.cdfifund.gov/programs-training/certification/cdfi/Pages/default.aspx for a nationwide list of certified CDFIs.

**Sources:** Author's calculations using CDFI lending data provided by the Opportunity Finance Network, which can be explored interactively on the organization's CDFI Coverage Map at http://ofn.org/cdfi-coverage-map; Esri, derived from Tele Atlas; U.S. Census Bureau

## County-Level Summary of CDFI Lending (January 2010–March 2015)

| State | County | Loans | Volume (000) | Average Loan Amount |
|---|---|---|---|---|
| Delaware | Kent | 6 | $7,532 | $1,255,333 |
| | New Castle | 32 | $7,573 | $236,651 |
| | Sussex | 7 | $5,085 | $726,429 |
| New Jersey | Atlantic | 16 | $1,817 | $113,588 |
| | Burlington | 12 | $2,317 | $193,078 |
| | Camden | 47 | $7,954 | $169,225 |
| | Cape May | 9 | $248 | $27,556 |
| | Cumberland | 11 | $289 | $26,317 |
| | Gloucester | 10 | $330 | $32,978 |
| | Mercer | 24 | $3,408 | $142,004 |
| | Ocean | 15 | $5,463 | $364,217 |
| | Salem | 2 | $35 | $17,500 |
| Pennsylvania | Adams | 2 | $200 | $100,000 |
| | Bedford | 11 | $1,071 | $97,364 |
| | Berks | 231 | $14,954 | $64,735 |
| | Blair | 2 | $355 | $177,500 |
| | Bucks | 18 | $1,730 | $96,127 |
| | Cambria | 1 | $500 | $500,000 |
| | Centre | 2 | $900 | $450,000 |
| | Chester | 23 | $1,076 | $46,796 |
| | Clearfield | 1 | $385 | $385,000 |
| | Cumberland | 20 | $4,710 | $235,475 |
| | Dauphin | 52 | $4,750 | $91,355 |
| | Delaware | 31 | $16,503 | $532,341 |
| | Elk | 2 | $425 | $212,500 |
| | Franklin | 4 | $525 | $131,250 |
| | Lackawanna | 1 | $4 | $3,940 |
| | Lancaster | 290 | $34,790 | $119,964 |
| | Lebanon | 14 | $903 | $64,464 |
| | Lehigh | 97 | $2,277 | $23,475 |
| | Luzerne | 2 | $392 | $195,858 |
| | Lycoming | 1 | $29 | $28,800 |
| | McKean | 2 | $170 | $85,000 |
| | Mifflin | 2 | $904 | $452,000 |
| | Monroe | 3 | $12 | $3,940 |
| | Montgomery | 47 | $8,839 | $188,063 |
| | Northampton | 81 | $3,226 | $39,824 |
| | Northumberland | 2 | $20 | $10,000 |
| | Perry | 2 | $242 | $121,000 |
| | Philadelphia | 432 | $461,280 | $1,067,778 |
| | Schuylkill | 6 | $785 | $130,893 |
| | Snyder | 1 | $1,300 | $1,300,000 |
| | Tioga | 1 | $130 | $130,160 |
| | York | 74 | $4,833 | $65,313 |

FEDERAL RESERVE BANK OF PHILADELPHIA

CASCADE: NO. 89, FALL 2015

# Recommended Reading

By Baylee Childress, Community Development Intern

## Pay for Success Financing

Humphries, Kevin W. "Not Your Older Brother's Bonds: The Use and Regulation of Social-Impact Bonds in the United States." *Law and Contemporary Problems*, Duke University (2014), pp. 433–452.
*This report offers a detailed overview of social impact bonds and how they influence the marketplace.*

Nonprofit Finance Fund: Pay for Success Learning Hub
*This website, organized by the Nonprofit Finance Fund, provides extensive resources on pay for success financing.*

Pauly, Mark, and Swanson, Ashley. "Social Impact Bonds in Nonprofit Health Care: New Product or New Package?" National Bureau of Economic Research Working Paper 18991, (April 2013).
*This paper examines the relationship and similarities between social impact bonds and existing financing methods in the nonprofit sector.*

Rinzler, Dan, Philip Tegeler, Mary Cunningham, and Craig Pollack. "Leveraging the Power of Place: Using Pay for Success to Support Housing Mobility," Working Paper 2015-04, Federal Reserve Bank of San Francisco (July 2015).
*This report explores the opportunities for and potential impact of pay for success financing for housing mobility among low-income persons.*

## Impact Investing

B Corporations
*Benefit corporations, often called B corporations, create a material positive impact on society and the environment and are required to consider the impact of their decisions not only on shareholders but also on workers, the community, and the environment. Legislation enacted in 26 states and the District of Columbia authorizes the establishment of B corporations. B Lab, a nonprofit organization, certifies B corporations and provides a platform to measure impact.*

Clark, Cathy, Jed Emerson, and Ben Thornley, et. al.*Impact Investing 2.0: The Way Forward — Insight from 12 Outstanding Funds,* Insight at Pacific Community Ventures, Duke University's Center for the Advancement of Social Entrepreneurship and ImpactAssets, (November 2013).
*This report provides research findings on a cross-section of high-performing impact investment funds and is designed to be a resource for those interested in impact investing.*

Global Impact Investing Network (GIIN)
*GIIN is a nonprofit organization that works to increase the scale and effectiveness of impact investing. Impact investors seek to generate meaningful social and environmental impact as well as a financial return. An example of a GIIN initiative is the Impact Reporting and Investment Standards (IRIS).*

Miller, Clara, and Toni Johnson. "Mission-Aligned Investing: More Complex Than It Seems," *Stanford Social Innovation Review* (June 2015).
*This article discusses the driving forces behind seemingly misaligned investments and the difficulties associated with divesting in these companies.*

Rein, Adam. "Impact Investing and a 200-Year-Old Debate," *Stanford Social Innovation Review* (May 2015).
*This article examines commonly used models of impact investing and their role in the current marketplace.*

Saltuk, Yasemin, Ali El Idrissi, Amit Bouri, Abhilash Mudaliar, and Hannah Schiff. *Eyes on the Horizon: The Impact Investor Survey,* Global Impact Investing Network and J.P. Morgan (May 2015).
*This report presents the findings of the fifth annual impact investor survey conducted by the Global Impact Investing Network and J.P. Morgan.*

U.S. National Advisory Board on Impact Investing. *Private Capital, Public Good: How Smart Federal Policy Can Galvanize Impact Investing — and Why It's Urgent,* (June 2014).
*This report discusses strategies for how governmental agencies can partner with impact investors.*

## Community Development Financial Institutions (CDFIs)

Fairchild, Gregory B., and Ruo Jia. "Risk and Efficiency Among CDFIs: A Statistical Evaluation Using Multiple Methods," Darden School of Business, University of Virginia, and Stanford Graduate School of Business, (August 2014).
*This research report, prepared for the CDFI Fund, finds that CDFIs show no greater risks of institutional failure than similar mainstream peer institutions and notes CDFIs' overall efficiency and institutional stability.*

*Strategies for Community Banks to Develop Partnerships with Community Development Financial Institutions,* Federal Deposit Insurance Corporation, (March 2014).
*This report provides guidance for community banks to help them identify and evaluate partnering opportunities with CDFIs.*

Swack, Michael, Eric Hangen, and Jack Northrup. "CDFIs Stepping into the Breach: An Impact Evaluation — Summary Report," Carsey School of Public Policy, University of New Hampshire (August 2014).

*This research report, which was prepared for the CDFI Fund, discusses the state of CDFI impact measurement and analyzes CDFI lending activity.*

CASCADE: NO. 89, FALL 2015

# Message from the Community Affairs Officer

By Theresa Y. Singleton, Ph.D., Vice President and Community Affairs Officer

Impact investing is generating a fair amount of excitement and interest across the community development field. As defined by the Global Impact Investing Network, impact investments are investments made into companies, organizations, and funds with the intention to generate social and environmental impact as well as a financial return. Financing tools for pay for success programs, sometimes termed social impact bonds, are seen as ways to provide critically needed funding for social programs while promoting new levels of innovation and accountability. Several articles in this issue of *Cascade* provide an overview of these financing tools and examples of how they are being used in communities across the nation.

**Theresa Y. Singleton, Ph.D., Vice President and Community Affairs Officer**

The Federal Reserve's community development function is using its research and convening powers to better understand and support the deployment of impact investing dollars in underserved domestic communities. In late 2014, staff from each of the Reserve Banks convened an Impact Investing Working Group. The goals of this group are to foster communication and collaboration among Reserve Bank staff working in the impact investing field and potentially identify System-wide initiatives related to impact investing. Participants are working to identify strategies to increase the amount of impact dollars available for community development activities as well as helping to strengthen local capacity to use impact funds more effectively.

We are working on a number of efforts to help increase our knowledge of this topic, including hosting a pay for success meeting here in Philadelphia on November 4. This event will provide participants with a solid understanding of pay for success financing and create opportunities to understand and discuss different perspectives about the purpose, appropriate uses, and potential challenges of this new tool. Additionally, we hope to create a community of interest in the development of pay for success financing and opportunities for government officials, potential investors, and service providers to explore working together to leverage this financing structure to implement and/or scale social innovation.

There are efforts underway to use impact investing to fund projects ranging from early child care to homelessness. There is still a lot to learn from earlier projects, however, as to how impact investing can be implemented most effectively to the benefit of those who need these resources the most. Evaluations of earlier projects will be critical to helping the field identify the strengths and weaknesses of this approach. It is clear that these efforts herald a new era of innovation and creativity in the financing of community development solutions.

Theresa Y. Singleton