The Massachusetts Juvenile Justice PFS Initiative

LESSONS LEARNED

Third Sector capital partners

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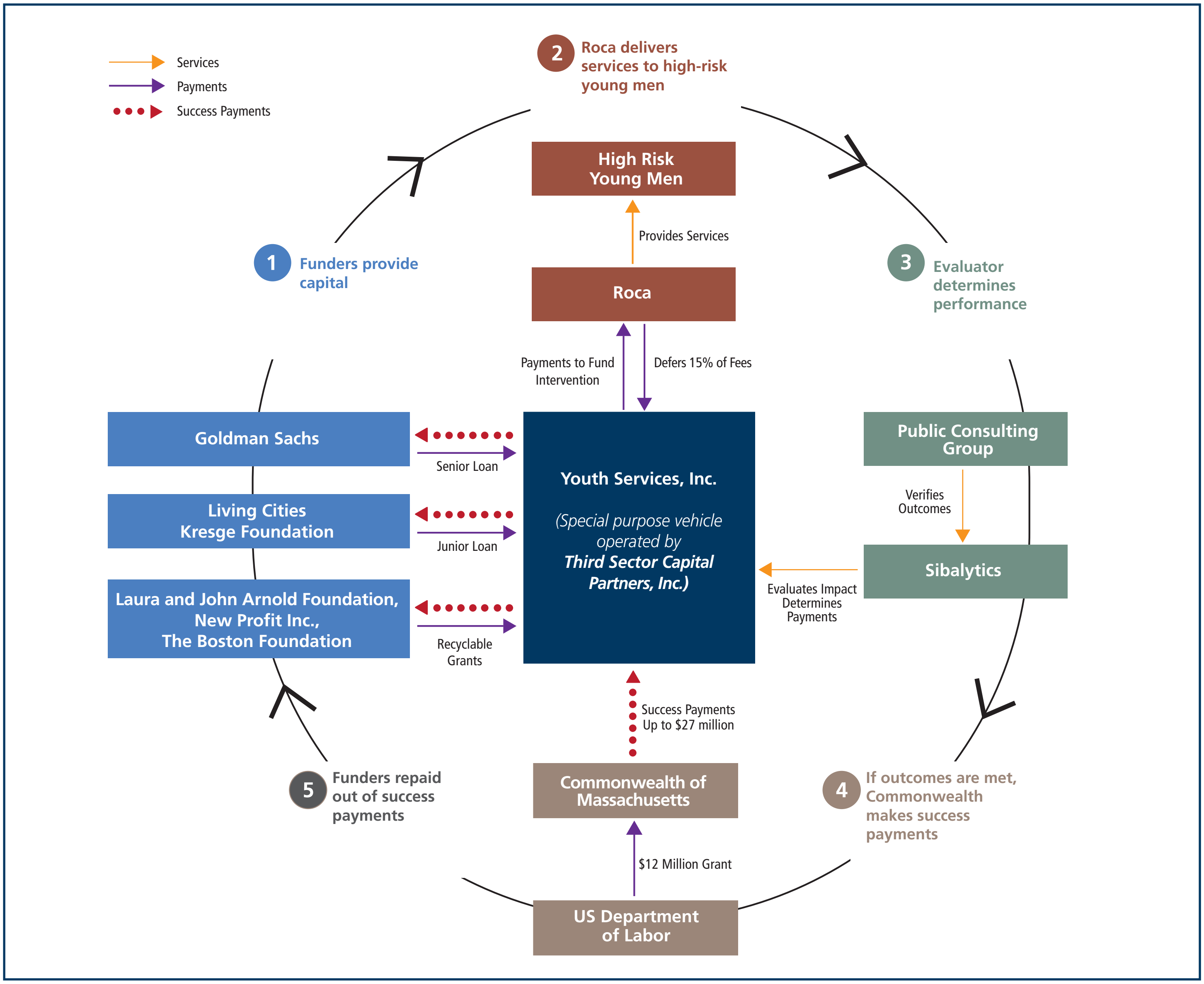
INTRODUCTION

In this case study, we review major lessons drawn from the Massachusetts Juvenile Justice Pay for Success Initiative ("the MAJJ PFS project"). The MAJJ PFS project aims to reduce recidivism and improve employment outcomes for young men at high risk of re-offending in the Boston, Chelsea, and Springfield, Massachusetts areas. The project will allow **Roca**, a service provider with a 25-year history serving this population, to provide its high-impact intervention to 929 at-risk young men aged 17 to 23 who are in the probation system or exiting the juvenile justice system.

THE MASSACHUSETTS JUVENILE JUSTICE PAY FOR SUCCESS INITIATIVE STRUCTURE



Roca's programming aims to reduce recidivism and increase employment through intensive street outreach and targeted life skills, education, and employment programming. The Roca intervention is delivered over an intensive two-year period followed by two years of follow-up engagement. Funders, including **Goldman Sachs, Living Cities, the Kresge Foundation, Laura and John Arnold Foundation, New Profit, Inc.** and **the Boston Foundation**, are providing a combination of loans and grants to pay for Roca's services. **The Commonwealth of Massachusetts** will repay funders only if Roca's services are proven to produce positive societal outcomes and savings for the Commonwealth. Massachusetts will make up to $27 million in success payments for this seven-year project, which is the largest investment in a PFS initiative in the U.S. to date. **Third Sector Capital Partners, Inc.** served as the intermediary organization and assisted project parties in developing and launching the project, and will serve as the ongoing project manager.

This project was one of the first state-level PFS projects in the United States and the largest PFS project by amount of upfront funding to-date. Over the 1.5-year development process of this innovative project, we learned several critical lessons about PFS project development and management. While the PFS sector is still in its infancy and no "cookie cutter" deal yet exists, we believe that these lessons are immediately relevant for all PFS projects regardless of the ultimate financing or governance structure.

With the completion of the MAJJ PFS project, we believe it is critical to disseminate these lessons in order to inform future projects. Our goal is simple: to help all stakeholders execute *quality* PFS projects *efficiently.*

THE FOLLOWING FIVE LESSONS HAVE BECOME OUR GUIDEPOSTS TO ACHIEVE OUR GOAL:

Lesson #1: **The Intermediary Works for the Project, Not Just One Stakeholder**

Lesson #2: **We Must Find Mechanisms to Accelerate the Pace of Negotiations**

Lesson #3: **All Parties Must Have a High Level of Commitment to the Pay For Success Model**

Lesson #4: **A Funding Tool for PFS Project Development is Needed**

Lesson #5: **Early Projects Should Consciously Set an Example for the Field**

In this document, we set out an abbreviated project timeline, and then discuss these lessons from our perspective serving as intermediary for the MAJJ PFS project. We hope these lessons prove helpful for all organizations interested and/or involved in this growing sector, and assist in current and future PFS project development.

PROJECT TIMELINE

JUNE 2011	Third Sector (in partnership with New Profit) and Roca submit responses to the Commonwealth of Massachusetts' Request for Information on PFS.
JANUARY 2012	The Commonwealth issues Requests for Responses on PFS Project to intermediary organizations and to service providers.
MARCH 2012	Third Sector (in partnership with New Profit) and Roca respond to the Commonwealth's Request for Responses as an intermediary and service provider, respectively.
AUGUST 2012	The Commonwealth names Third Sector and Roca as the successful bidders in the procurements for intermediary and service provider, respectively.The Commonwealth passes legislation authorizing PFS contracting and backing obligations with its full faith and credit.
OCTOBER 2012	Third Sector develops a preliminary information memorandum for prospective funders. The Commonwealth, Roca and Third Sector clarify the contingent payment structure and identify avoided bed-days (rather than reduced recidivism) as an outcome metric.
NOVEMBER 2012	Third Sector, with assistance from Roca, begins reaching out to foundations for early expressions of interest or verbal pledges.
DECEMBER 2012	The Commonwealth formally applies to the Department of Labor (DOL) for grant funding. The submission requires technical details and letters of intent/interest from New Profit (for a $1 to $2 million grant) and from debt funders, including Goldman Sachs.
FEBRUARY 2013	The Commonwealth and Third Sector negotiate a Memorandum of Understanding, enabling Third Sector to negotiate for the project, as well as a clear method of payment for Third Sector's provision of intermediary services. The first draft of the PFS contract is circulated to all parties.
APRIL 2013	The Commonwealth issues a Letter of Intent to contract with Third Sector and Roca. Living Cities holds a convening for financial institution, philanthropic and program-related investment stakeholders, where Third Sector and Roca present the MAJJ PFS project. This directly leads to funding commitments from Living Cities and the Kresge Foundation.
MAY 2013	A majority of funders have made contingent financial commitments.
JUNE-AUGUST 2013	Financial structure is further refined, including agreements on funding disbursement, paying for success, and distribution of success payments.
SEPTEMBER 2013	Most funders receive approval from their respective investment committees. Concurrently, the DOL announces nearly $12 million in supplemental funding for the MAJJ PFS project.
NOVEMBER-DECEMBER 2013	Additional agreements are negotiated, including the fiscal services and management agreements, as the financial model and loan agreements are refined.
JANUARY 2014	Publicity protocols are negotiated and enacted; loan and grant agreements are finalized; final contracts are signed; the MAJJ PFS project launches on January 29, 2014.

Lesson 1: THE INTERMEDIARY WORKS FOR THE PROJECT, NOT JUST ONE STAKEHOLDER

As we move forward, one of most critical lessons we take with us is a deeper understanding of our role as an intermediary in PFS projects and in building this nascent sector. The initial proposal for a PFS project with the Commonwealth of Massachusetts was modeled on what might be characterized as a "privatization" model that positioned Third Sector as the sole negotiator with the Commonwealth as to the choice of population served, success metrics, payment schedules and financing cost and structure. Third Sector would then contract privately, independently of the government, with Roca (and others) for program services and would go on to contract separately with funding partners and philanthropists for financing. Under this model, all parties would negotiate opposite to Third Sector and Third Sector's obligation to negotiate the best possible deal that it could persuade all parties to agree to would be evident. No party would have a reason to believe that Third Sector was uniquely aligned with it.

It soon became clear, however, that the "privatization" approach was not the right model for this project, and that it was more important for all parties to work together to resolve issues and create contracts that would spell out their mutual obligations. As a result, we arrived at a more collaborative, multiparty contracting approach, where multiple parties in the MAJJ PFS project brought different interests, levels of familiarity with PFS, technical skills and capacity to dedicate to negotiations. Given the multi-party complexities, it soon became clear that the project would fail to move forward unless Third Sector played a highly active project manager role by setting joint agendas, meeting frequently with all parties, raising and resolving issues and generally driving constant progress on the project.

As we took on multi-party project management, our role became less clear. Now who was our client in these projects? To whom did Third Sector owe a fiduciary duty? The Commonwealth, which ultimately provides success payments and initially named us as the intermediary through a competitive procurement process? The funders, who will actually pay our fees, at least unless and until the Commonwealth makes success payments in five to seven years? Roca, who relied on us for deal construction? We believe that the answer to this question will provide guidance as to the role of the intermediary in the PFS sector.

Through the long negotiating process with multiple parties, **we have come to believe that—whatever the structure—the essential intermediary role in these projects is to understand the perspectives and motivations of each stakeholder and utilize any and all commonalities across stakeholders to drive the project forward. Essentially, as an honest broker, it is best that intermediaries report to the project and thus work with all parties who join the project.**

By serving the project, we were required to be highly sensitive to all stakeholders' needs and continually work towards consensus. An implication of this perspective is that although MAJJ PFS project included a small number of initial stakeholders, Third Sector needed to anticipate the needs of future stakeholders. As new partners joined the project, Third Sector's roster of clients expanded.

We believe that these motivations will be similar in future PFS projects and being sensitive to them will allow for more proactive engagement on potential issues or stumbling blocks to project execution. PFS projects are consensus-building exercises. Intermediaries should build necessary insight on stakeholders' motivations in order to execute projects better and faster and be clear that their obligation is not to any individual stakeholder but to the project. This allows intermediaries to serve their ultimate clients better: the community of people the projects seek to help and taxpaying citizens that the projects serve.

EXAMPLE: "REPORTING TO THE PROJECT": MITIGATING SHUTDOWN RISK

The challenge of mitigating shutdown risk in the MAJJ PFS project highlights why intermediaries need to take an "honest broker" role in PFS project negotiations. On one hand, there was a reluctance to construct a project that could not guarantee that it would deliver the promised four years of service to each Roca enrollee. An early shutdown would also greatly undercut the goal of receiving a full set of data to support a rigorous and conclusive evaluation. At the same time, funders indicated that they wanted to see a mechanism that would avoid "throwing good money after bad" if there were compelling early indications that the project was unlikely to meet its objectives of reducing incarceration and increasing employment.

The ultimate solution to these issues was resolved by both parties' proposing project innovations and agreeing to compromise as long as critical risks were mitigated. By working with the ultimate goal of the project launch in mind, Third Sector was able to broker a solution: funding would be based on "conditions precedent" that had to be met in order to draw down funds.

Lesson 2: WE MUST FIND MECHANISMS TO ACCELERATE THE PACE OF NEGOTIATIONS

In Third Sector's role as project manager, we found it difficult to set deadlines that were enforceable, which slowed down project development. There were several reasons for the slow pace: stakeholders often needed the approval of decision makers at their organization who were not involved in day-to-day negotiations; project parties needed to work across silos at their own organizations; and stakeholders often lacked the capacity to dedicate significant daily resources to PFS project development. How can PFS project parties speed up the process going forward? Some lessons Third Sector seeks to incorporate going forward include:

- A commitment on the behalf of government and all project parties to dedicate a staff person to the PFS projects who is authorized to make decisions.
- Intermediary organizations should utilize an all-party memorandum of understanding expectations at the start of any PFS project. This can include agreements on a shared financial model, decision rights, expected roles and responsibilities, timeline and publicity protocols.
- "Forcing functions" such as the Department of Labor grant application deadline and the Living Cities convening drove MAJJ PFS project development. **These deadlines or events were inflection points that truly drove progress on the project, whether it was clarifying evaluation or obtaining investor commitments.** In the future, we hope to identify opportunities to utilize similar events to facilitate project execution or even to artificially create them through financial incentives tied to timing or "exploding offers." We believe that any stakeholder may be in a position to insist on deadlines and to accelerate progress. An intermediary could also potentially set deadlines "with teeth," but this would require a willingness to walk away from a slow-moving project and/or perhaps pre-negotiate penalties with project stakeholders that would compensate the service provider or intermediary if delays take place.

- Utilize shared, transparent tools to work towards consensus. To manage multi-party financing negotiations, Third Sector developed a shared economic model that allowed all parties to coalesce around a unified set of cost, scale, payment structure, financing structure and impact assumptions. This model became the centerpiece for how the deal was negotiated across multiple parties. Several times throughout the process, an individual party would approach Third Sector with an idea for how the deal might be structured, or the terms/assumptions changed. Third Sector would work privately with the party and then nominate the changes to the rest of the parties for incorporation into the shared model. This single model, shared and used by all funding partners, was critical to ensuring that negotiations were couched in the same financial understanding of the project. The model quantified capital requirements for all stakeholders and provided a shared framework for negotiation.

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Lesson 3: ALL PARTIES MUST HAVE A HIGH LEVEL OF COMMITMENT TO THE PAY FOR SUCCESS MODEL

Given the novelty of the Pay for Success contracting model, Social Innovation Financing and the multi-party collaboration that will be necessary on most early PFS projects (as it was on the MAJJ PFS project), these projects will require extraordinary levels of commitment, creativity and cooperation on the part of providers, government, funding partners, evaluators and intermediaries. We believe the following characteristics for project parties are also non-negotiable in the early days of PFS project development.

GOVERNMENT CHAMPIONSHIP

Having a government champion actively promoting PFS is essential. Governor Deval Patrick's public support of PFS was necessary for the project's success. Secretary of Administration and Finance Jay Gonzalez was the original and enthusiastic sponsor of PFS and his successor, Glen Shor, continued to prominently support the project.

Beyond executive level support, it proved essential that the government was able to allocate dedicated personnel to the development of the project. For the first year of project development, a fellow from the Harvard Kennedy School's Social Impact Bond Technical Assistance Lab ("SIB Lab") provided this support, replaced by a fellow from the Harvard Business School. The administration also assigned a first-tier manager on a close to full-time basis to the project and secured pro bono legal assistance developing the contract from Nixon Peabody. Future projects cannot expect as much technical government support; as PFS and SIF become more routine, the level of day-to-day government involvement needed will likely diminish and/or the intermediary will have to assume greater responsibilities. However, a government champion that is firmly committed to PFS contracting will remain essential to launch any PFS project.

CATALYTIC PHILANTHROPY

From the beginning, the MAJJ PFS project capital structure was a split between philanthropy and debt. Commercial funding partners were expected to contribute senior debt, program-related investments from foundations would constitute junior debt and philanthropic grants could serve as first-loss capital to encourage investment. As presented in the timeline, with the exception of an early commitment of time and capital from New Profit, initial commitments to the project came primarily from debt providers. Despite efforts to solicit grant funding, commitments from philanthropists were generally slowest to materialize.

This seemed puzzling; compared to traditional grant-making, the advantages of funding PFS projects are tremendous. First, rather than funding initiatives in a silo, philanthropies can receive funding leverage from commercial funders. Second, successful projects can allow for return of grant funds (essentially making them program-related investments without interest) or a recycling of grant funding into continued service delivery in order to sustain positive outcomes. Third, PFS projects have an advantage over traditional grant making even in the event of failure: philanthropies can utilize PFS projects' built-in rigorous impact evaluation to inform their future grant-making activities.

In larger terms of sector building, philanthropies also play a vital catalytic role: we firmly believe that the early days of SIF financing will require more subsidization than what will ultimately be required. By providing a "wean-able" subsidy, philanthropists act as a catalyst to transformative change. Also, philanthropists play a vital signaling role that lends unique legitimacy to SIF projects: funder seats at the table that are unambiguously focused on social benefits combined with institutional constancy that spans across political cycles.

The philanthropies that ultimately committed to the MAJJ PFS project made funding commitments for one or more of the above reasons, but on the whole, the philanthropic sector remains cautious of PFS projects. More accustomed to direct grant or lending requests, many philanthropies struggled to decide whether a potential MAJJ PFS project investment should be seen as a traditional grant opportunity or as a program-related investment loan. The pure investment side of foundations (who would make MRIs) found the risk-reward characteristics of the PFS investment opportunity unappealing, as did even most of their colleagues responsible for socially motivated PRIs. At the same time, the grant makers at foundations often were reluctant to be seen as subsidizing commercial funders. As fundraising efforts progressed for the MAJJ PFS project, obstacles in raising philanthropic funds took many project partners by surprise.

How can Third Sector and other intermediaries "sell" philanthropies on these advantages and involve philanthropies earlier in the deal process? From the MAJJ PFS project development, we take away one possibility for future projects: **convene early and often**. Given that many funders prefer participating in an iterative process before agreeing to invest in any project, Third Sector has started to convene local funders early and often in current PFS projects. Establishing an "investor council" in deal development is one method for engaging a diverse pool of interested funders. This allows funders to do due diligence and express interest and commitment early, while also enabling project partners to incorporate funder feedback in initial deal construction. This type of structure may enable parties to mitigate significant time delays in negotiating and contracting late in the project's development.

A "philanthropic champion" or lead grantor can also assist by creating forcing functions for philanthropic commitments. In the MAJJ PFS project, Living Cities' convening of philanthropies in April 2013 provided an important formal opportunity for philanthropic organizations to seriously consider the MAJJ PFS project as a grant-making or lending opportunity. Ultimately, the convening was a catalyst for obtaining philanthropic commitment. In the future, a philanthropic champion could help bring other philanthropies on board by hosting a convening or a similar forcing function.

COMMERCIAL LENDING EXPERTISE

While philanthropies catalyze project development to help build a sustainable PFS sector, commercial funding partners also add critical value to early PFS projects beyond their evident role of providing capital.

We found in the MAJJ PFS initiative that in addition to providing capital, commercial funding partners served two important roles: (1) they made contingent commitments to participate in projects early, legitimizing the project for other potential funders and all project parties, and (2) they brought market discipline to project development, especially with project timelines and the design of project financing structures. Their insistence on continual progress was critical in driving project development forward. Moreover, the technical input and assistance that commercial funding partners provide is invaluable, especially as early PFS projects can and should experiment with innovative financing structures.

DATA-FLUENT SERVICE PROVIDERS

While Third Sector was selected independently of Roca to develop a PFS project, **a key factor to the success of the project was Roca's pre-existing operational sophistication and comfort with data-driven program evaluation.** The evaluation component of the MAJJ PFS project required intensive use of government databases and careful tracking of participant data points. Roca's comfort with collecting and analyzing data made the development of the PFS project evaluation much easier. A less sophisticated provider would have faced significant hurdles in implementing the necessary outcome-tracking systems and infrastructure required to meet the evaluation standards of a PFS project, and would have caused significant delays in project implementation. Providers must also have strong administrative and financial capacity to get through a negotiation process and to help determine what outcomes can be achieved. Indeed, Roca played an in-depth role in designing the deal terms, and their strong organizational capacity was a major key to success.

In the future, we expect that PFS projects will continue to place a strong premium not only on government administrative databases, but also on providers who are comfortable with working with data to develop and inform their programs. First, a service provider with existing evaluations of its programs can demonstrate to the government and potential funders that it has a track record of creating social impact. Second, existing provider-level data also furnishes valuable information needed to construct economic models and guide the design of evaluation mechanisms. Lastly, service providers that have the capacity to track and analyze data shorten the time needed for data analysis in the preliminary phases of the project.[1]

[1] Like government, service providers also need to dedicate resources and time to project development. Undertaking a PFS project requires intensive amounts of performance analysis, budgeting, operations management and efforts across the entire provider's organization. A deep commitment from the service provider is essential for project success.

Lesson 4: A FUNDING TOOL FOR PFS PROJECT DEVELOPMENT IS NEEDED

The longer-than-expected deal development process stretched out the implementation timeline for the MAJJ PFS project. As a result, Roca had to limit the number of new participants it enrolled prior to the PFS project start date to ensure that its staff had sufficient capacity to increase its scale when the project actually launched. Furthermore, since Roca was relying on the MAJJ PFS project to cover a significant portion of their operational expenses, delays created financial pressure on the organization. Likewise, the delayed start date also impacted Third Sector, since our 19 months of intensive work prior to the project's launch date were uncompensated before the project launched. While we were compensated after the project launched, it is not currently practical to expect non-profit service providers or intermediaries to be able to continue to develop projects without compensation at the time.

Future PFS projects need to remediate this funding gap. We may be able to do so with upfront partial funding from philanthropic organizations or other project stakeholders that can be reimbursed upon project close or converted to a loan to the project. As the PFS sector develops and organizations build cash balances to mitigate project payment schedules, the importance of interim funding will hopefully diminish, but at the moment it remains critical for intermediary and service provider operations.

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Lesson 5: EARLY PROJECTS SHOULD CONSCIOUSLY SET AN EXAMPLE FOR THE FIELD

All parties were highly conscious throughout the MAJJ PFS project development that it would be one of the first to launch in the United States and likely the largest to-date. We believe that the additional efforts and challenges in project negotiations were worth the development of project features that are replicable for future projects. As more projects launch and project development becomes standardized, this effort will grow less important. However, we strongly urge all project parties in the PFS sector to be thoughtful about project development and structures. These early projects set a critical example for the PFS sector at-large. Below, we outline some project parameters and structures that we believe are replicable on an ongoing basis.

THOUGHTFUL USE OF FIRST-LOSS CAPITAL

Risk structuring in a PFS project can take many different forms. In Massachusetts, a conscious decision was made to insist on philanthropic grants serving as first-loss capital in the capital stack, as opposed to using philanthropic funds to guarantee repayments of loan principal. There were three reasons for this:

1. By using philanthropic grants to mimic the role of equity in traditional project finance, we hope to create a replicable financing structure to grow the PFS market. With philanthropic grants as first-loss capital, we hope to both encourage all funders to view PFS as analogous to private sector investment opportunities and to create a demonstration effect, where return-seeking funders will grow more comfortable with PFS projects in the future and then invest in the place of philanthropy.

2. The utilization of a partial or full loan guarantee removes capital from being placed at-risk in PFS projects. In the MAJJ PFS project, while philanthropic grant capital provides a buffer against losses, 100% of the loan capital is at risk.

3. This first-loss role for philanthropic funds provides an attractive proposition for philanthropic donors, as discussed previously. This allows philanthropies to leverage their grant-making with commercial capital, have the opportunity for grant replenishment to sustain funding and builds in a rigorous impact evaluation of the services they are funding- three features that are not present through traditional grant-making.

FINANCE INNOVATIONS

We highlight several finance innovations below. The majority of these arose out of necessity, whether due to the Commonwealth's requirements or funders' needs. However, we believe these innovations will prove desirable and replicable in other PFS projects.

The Success Payment Schedule.

- The original model suggested that the Commonwealth would pay a flat rate for each incarceration avoided. This had the considerable merit of simplicity. This mechanism, however, discounted that the Roca model anticipates "relapse" through short-term incarcerations for less serious offences and sees these incarcerations as a way to dissuade the young men they serve from risking more serious – and longer – incarcerations. As a result, the "all or nothing" incarceration metric would fail to reflect the benefits of shorter sentencing and less serious infractions among the young men being served. These problems were addressed by shifting the primary outcome variable to "bed-days avoided" in incarceration instead of "number of incarcerations."

- Detailed cost-benefit analysis conducted by Harvard's SIB Lab revealed that the amount of savings per avoided bed-day that can be captured by the Commonwealth will depend strongly on the overall scale of impact. We therefore adjusted the payout schedule to initially reflect only the marginal cost of incarceration and to gradually grow to reflect the average cost as the overall reduction in bed days increases. This projection was based on a sophisticated probabilistic model built by the Commonwealth's advisors at the Harvard SIB Lab to reflect the likelihood of capturing and sustaining savings as the number of bed days avoided increases.

- As a compromise between providing ongoing success payments to funders, but also ensuring that the Commonwealth has not overpaid for preliminary promising outcomes that may be revised through later data, 20% of the payments are withheld until wind-up.

- The Commonwealth agreed to a mechanism that would allow payments to be made in the project's final quarter based upon the projections of outcomes among young men who had not been observed for a full five years. This means the project can wind-up 25 quarters after beginning, which appears to be a more investable proposition than only winding up some time in the ninth year of the project after a full observation period for all participants.

- In order to make the project use capital as efficiently as possible and create a more attractive proposition to funding partners, the loans can be paid back as early as Quarter 18 if the project is able to reduce bed days of incarceration at a high enough level (and as late as Quarter 25 – or even never -- at lower levels of impact). The effect is that funding partners' capital is exposed for less time, the project pays as little interest as possible, and the project is able to offer the promise of a higher IRR without actually paying out any additional funds simply by re-paying loans it no longer needs instead of holding onto the money and paying it back only at the end of the project.

Recyclable Grants.

Depending on the level of impact, the project may have leftover funds to distribute back to the grantors. These funds will be recycled consistent with the direction of each grantor. This is important for several reasons:

- *PFS Innovation:* These grants illustrate the potential for return-seeking funding partners to eventually move into the place of the grantors in the capital stack; it also creates an exciting new class of philanthropy that bridges the gap between PRI and irrevocable grants.

- *Service Provider Compensation:* Because these funds may be allocated to Roca, their presence increases the expected value of the project to Roca, which compensates Roca for the considerable risk it has taken on.

Remedy for Commonwealth Default.

The Commonwealth agreed early on that if it defaulted on its obligations it would owe damages equal to the amount expended to date by the project. This provided an important financial protection to other stakeholders, as well as a powerful alignment of interests towards avoiding unnecessary premature shutdown.

"OPEN SOURCE" PROJECT CONTRACTING

Many parties were initially unsure about whether to keep project documents such as loan agreements confidential. After all, to openly share the lessons and intellectual property that were developed after a tremendous amount of upfront investment in this project could compromise a "first mover's advantage" in the PFS ecosystem, and may even hinder Third Sector's efforts to establish a sustainable business model that could help the sector at large.

These considerations were outweighed, however, by our collective belief that "open source" of the MAJJ PFS project legal language and other insights were critical to the growth of the PFS/SIF ecosystem. We concluded that the development of SIF and PFS will be better served by an open-source philosophy. Moreover, the Commonwealth's disclosure obligations combined with its involvement in all facets of deal construction led to a mandate that the vast majority of final documents are available upon request.

In future projects, we will recommend to governments that they establish from the outset that projects will be open-source: that all final contracts will be posted to a website. There will likely have to be some agreement as to how each party will characterize the others and describe the project and a protocol for tracking publicity opportunities, but the project will be well served by simplifying these issues and addressing them early.

We believe that the extra effort and difficulty in project negotiations was worth the development of project features that are replicable for the future.

EVALUATION: CREATIVE RCT IMPLEMENTATION

The ultimate goal of PFS is to incorporate a permanent "feedback loop" into governmental procurement processes, so government can rigorously understand what is working in social services on an ongoing basis. Rather than blindly funding what may or may not have worked in the past, governments can allocate resources better and fund measurable social impact. To that end, all parties viewed the MAJJ PFS project's evaluation design as absolutely essential to the future success of PFS projects. To us, the "gold standard" of evaluation is the accurate reflection of the counterfactual in impact assessment: what would have happened to those served had they not been served? Usually, the most powerful way to properly assess impact against a compelling counterfactual is the utilization of a randomized control trial (RCT). However, designing an RCT for social services presents several challenges. Below, we detail three creative solutions that enabled the MAJJ PFS project to utilize an RCT evaluation design.

No Denial of Service.

In the past, all efforts to design an RCT at Roca had been determined to be too difficult due to the logistical and ethical problems they presented.[2] A traditional RCT would require that youth placed in the control group explicitly be barred from being served by Roca, an unacceptable ethical proposition for Roca. The SIB Lab created a sophisticated evaluation design that included a "no denial of service" policy but could tolerate considerable levels of "contamination" of members of the control group receiving Roca services. This design required the overall sample size for the project to be increased significantly – but the ethical dilemma was resolved.

Back-Up Evaluation Plan.

However, stakeholders were also concerned that implementation problems, the "no denial of service" contamination and other logistical obstacles could potentially render the RCT inconclusive. To address this risk, the project developed a back-up evaluation plan that would use a difference-in-differences approach comparing Roca cities to matched cities that were not served. To the extent that the RCT results lost statistical power, the difference-in-differences approach could be blended in as the official way to measure impact and drive PFS payments.

[2] It is worth noting that a collateral benefit of the project is the RCT itself. A crucial impediment to previous efforts by Roca to construct an RCT was the need for government cooperation. The existence of the PFS project aligned the Commonwealth's and Roca's interests sufficiently to commit to this evaluation.

CONCLUSION

The MAJJ PFS project required a substantial investment of capital, resources and time. Due to the sector's early stage of development, first deals like this one often require an outsized amount of resources. Third Sector relied on various sources of support for this deal, ranging from philanthropic support for our internal operations to pro bono legal counsel. We expect that a reliance on "predevelopment" subsidies will be necessary going forward until the sector develops more fully. In particular, we believe that outside technical assistance for government will continue to be absolutely critical for project development. Going forward, intermediaries may need to perform more of a technical assistance role.

On the other hand, compared to the MAJJ PFS project experience, we expect to see a significant decrease in the amount of upfront investment of time for future PFS/SIF projects. Most of the processes and intellectual property developed during this project can be leveraged to help future projects proceed more smoothly. These include the project timeline, the documentation of stakeholder roles and responsibilities, the publicity protocol, the project governance model, the design of capital structure, techniques for assessing and managing shut down risk, frameworks for establishing orders of repayment across stakeholders, methods for setting funding partners exit thresholds and language for more clearly communicating propositions to stakeholder prospects, to name just a few.

The amount of time and effort required to negotiate and close the next PFS transactions should be greatly reduced as a result of the templates created by the MAJJ PFS project. Ultimately, we believe our experience with the MAJJ PFS project will actively inform the creation of a sustainable PFS sector that transforms government's procurement of social services and delivers real results to our communities.

Most profoundly, we have moved past the "blank slate" starting point in our development of the deal points and legal language that will undergird future PFS/SIF transactions.

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