

## The Opportunities and Challenges of Pay for Success in the Philadelphia

In Winter 2014, the City of Philadelphia procured Social Finance to assess the feasibility of implementing a Pay for Success (PFS) project. In particular, the City was focused on using PFS to reduce recidivism of citizens returning from jail or prison and limiting out-of-county placements of system-involved youth. The study sought to understand the potential for PFS financing to complement ongoing efforts by driving public resources toward evidence-based, outcomes-driven programs. Social Finance focused on two agencies: the Philadelphia Prison System (PPS) and the Department of Human Services (DHS).

The Philadelphia Prison System – a complex of county jails, despite its name – housed approximately 8,300 individuals in the winter of 2015, bursting at the seams to accommodate high incarceration rates. While the recidivism rate has decreased in recent years below the national average, it is still troublingly high: 40% of individuals return to PPS within one year of release and close to 60% return to PPS or prison within three years.<sup>1,2</sup> Reducing recidivism was an important piece of Mayor Nutter’s agenda to make Philadelphia safer and to improve the wellbeing of all citizens.

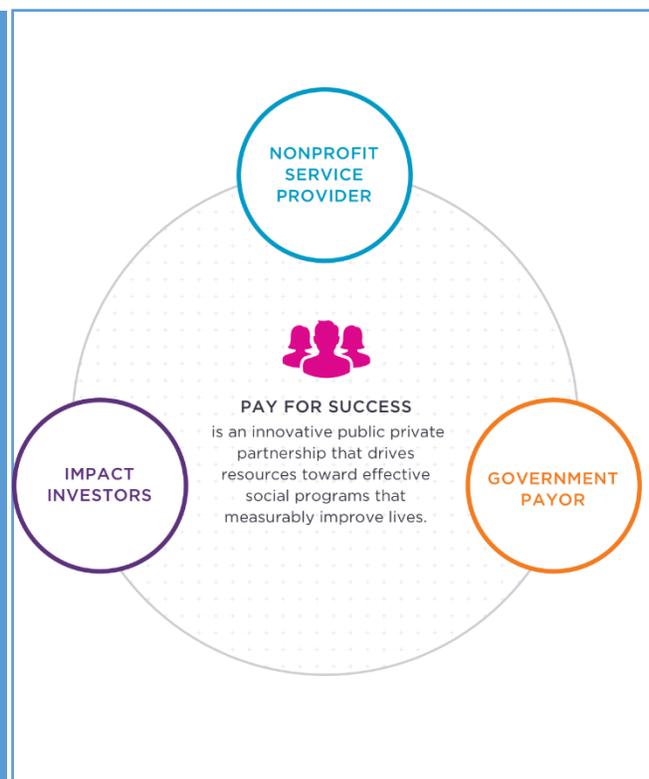
For years, the Department of Health and Human Services had focused on reducing the use of congregate care, recognizing wide-spread evidence that children in family settings have better long-term outcomes than those in group or institutional settings. DHS established Improving Outcomes for Children, a system-wide reform to assess program strengths and weaknesses and improve data collection. DHS now wanted to reduce congregate care placements outside of Philadelphia, where children’s outcomes were worst and costs to the

### WHAT IS PAY FOR SUCCESS?

Pay for Success (PFS) is a financing tool designed to measurably improve the lives of people most in need by driving resources toward better, more effective programs.

PFS builds public-private-partnerships that expand funding for high-quality social services through performance-based contracts. PFS projects enable federal, state, and municipal governments to partner with high-performing service providers by tapping private investments to cover the up-front costs of programs. If, following a rigorous evaluation, the program is successful in reaching pre-determined outcomes, then government repays the original investment. If the program exceeds those outcomes, the government pays a small return on the investment; if it does not achieve its target results, government pays nothing.

In this way, this model ensures that taxpayer dollars are being spent only on programs that actually work and expanding access to services for those who need them the most.



<sup>1</sup> City of Philadelphia - Five Year Financial and Strategic Plan for Fiscal Years 2015-2019

<sup>2</sup> Durose et al, 2014

system were highest.

The feasibility study explored whether Pay for Success could be part of an integrated effort to reduce recidivism and reduce out-of-country placements for youth in the foster care system. In late 2014, a committee including the Mayor's Office, DHS, PPS, the Departments of Finance and Law, and the School District of Philadelphia selected Social Finance to conduct a four-month study to assess the feasibility of implementing a PFS project to improve outcomes for these two vulnerable populations.

## Three Themes in PFS Exploration

PFS forces jurisdictions to break with the status quo and consider difficult questions. Is PFS a good fit for my jurisdiction? What are the legal hurdles in implementing a performance-based contract? What kind of data will I need to provide? Do we have the capacity to implement a PFS project?

While the answers vary by jurisdiction, in the below section we describe three themes that we developed for Philadelphia, but which we see replicated in many jurisdictions as they consider PFS.

### A. Defining value

Philadelphia needed to understand the value generated by an intervention in order to assess the feasibility of a PFS project. We quantified the value of reducing recidivism in terms of direct economic savings to the City, such as reduced bed days at PPS, direct economic savings to the State, such as reduced bed days at the state prisons, and societal benefits for the community, such as improved public safety.

We reviewed over 50 criminal justice programs and shortlisted three evidence-based interventions which we believed would have a meaningful effect on recidivism rates in Philadelphia.<sup>3</sup> For these interventions, we reviewed four potential outcome metrics - bed days in jail or prison, reduced public safety costs, increased employment and earnings, and the value of the transitional labor itself.

Each outcome creates economic and societal benefit for the City. To estimate these benefits, we compiled administrative data from PPS, the State Department of Corrections (DOC), APPD and public reports to better understand the costs averted by each outcome, such as the cost of a bed day at PPS.

The average cost of a bed day at PPS—the total PPS budget divided by the number of inmates—includes fixed costs such as building maintenance, salaries and administration, in addition to marginal costs, such as food, clothing and medical care. A marginal cost approach looks only at the latter costs, or the variable costs associated with each incremental bed day. There is a significant difference between the average and marginal cost of a day in incarceration: DOC estimated that the average daily cost per inmate is \$116<sup>4</sup> while the marginal daily cost per inmate is only \$15.<sup>5</sup> Marginal costs are smooth; average costs change as step

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<sup>3</sup> In order to shortlist the top three interventions for PFS, we used the following criteria: 1) Service provision to the identified target population; 2) Services fill an unmet need for the target population; 3) Rigorous evidence base for treating a directly similar population; 4) Proven impact on relevant outcomes (e.g. congregate care reduction and recidivism reduction); and 5) Provision, or potential for provision, by local service providers with the capacity to scale operations.

<sup>4</sup> <http://www.vera.org/files/price-of-prisons-pennsylvania-fact-sheet.pdf>

<sup>5</sup> Interview with DOC official, 2014

functions—such as when PPS can close a wing or avoid building a new wing. There is no simple way of estimating the value created by reducing incarceration but often the best way is to blend marginal and average costs for prison and jail days.<sup>6</sup>

In Philadelphia, due to the limited capacity of PPS facilities, PPS pays neighboring counties approximately \$60 per day to house an overflow population of nearly 600 inmates, based on a contract that could be renegotiated annually. If a program reduced recidivism rates, it would reduce the overflow population, saving PPS \$60 per inmate per day in next year's contract. In addition to the savings at PPS, DOC would see reduced bed days if recidivism rates declined. More than 70% of PPS' population is being held pre-trial,<sup>7</sup> and a percentage will be convicted to serve a sentence at a DOC facility. In our analysis, we blended the costs of a bed day at DOC and PPS to calculate the cost of a bed day in incarceration.

It quickly became clear, in our conversations with the City, that valuing these outcomes was a balance of art and science. While we did rigorous data analysis and extensive research to identify costs associated with outcomes, we also had to make significant assumptions. Where data were not available, we developed assumptions through a combination of third-party research and conversations with PPS, APPD, and others who best understood where and how meaningful value would be created for Philadelphia.

## B. Understanding funding streams

Assessing the value created by an intervention's outcomes for a jurisdiction is only the first step of a Pay for Success cost-benefit analysis. The next step is understanding what value is captured by the jurisdiction's agencies in order to identify a potential payor for the PFS project. While some of the value goes directly to individuals and communities, such as increased wages or lower crime rates, a portion accrues to government budgets, such as reduced bed days at PPS. Since social services are financed through a web of local, state and federal funding sources, understanding which agency budget benefits from avoided service costs can be complicated.

DHS wanted to use PFS to reduce the percentage of system-involved youth placed in out-of-county residential facilities. After reviewing dozens of programs which focus on reducing out-of-home placements, we prioritized Functional Family Therapy (FFT). FFT is an intensive, family-driven therapy which works with youth and their families and can be used as an alternative to incarceration or out-of-home placement. DHS already offered FFT to a small number of Philadelphia youth, but PFS could expand access to FFT as a way to reduce days in foster care, congregate care and detention centers, and to improve educational attainment. After estimating a value for these outcomes—as described in the previous section—we attempted to identify where this value would accrue. For each youth averted from out-of-home placement, which government entities benefit?

To answer that question, we looked beyond DHS to ten agencies across the county, state and federal levels. The flow of costs between agencies in such a complex system is, of course, complex. Police costs are borne by the Philadelphia Police Department. Adjudication costs are borne by the court system. Juvenile detention costs are split between the State and City DHS. The group home costs are covered by Pennsylvania's IV-E Waiver and therefore the daily cost for room and board is split between the Federal government (who covers 53.5%), State DHS (who covers 37.1%) and City DHS (who covers 9.30%).<sup>8</sup> Education services at the group

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<sup>6</sup> Santora, Marc, "City's Annual Cost Per Inmate is \$168,000, Study Finds," *New York Times*, August 23, 2013

<sup>7</sup> Pew Charitable Trust Report

<sup>8</sup> Pennsylvania's Title IV-E Waiver Demonstration Project allows the State more flexible use of federal funds in order to test new approaches to service delivery and financing structures.

home are paid for by the School District of Philadelphia (SDP), and behavioral health services by the City's Department of Behavioral Health (DBH)—which, for its part, is reimbursed by Medicaid dollars, split between the State and Federal government according to the Federal Medical Assistance Program (FMAP) percentage for Pennsylvania.

Ultimately, our payor analysis of FFT suggested that its value flows primarily to the State, rather than to the City—suggesting that it is not a strong candidate for a Philadelphia-based project. In some cases, however, it may be possible to overcome these kinds of “wrong pockets” problems, in which one level of government invests and another benefits.

### C. Data, data, data

In our very first meeting with the City we raised the topic of data, and data was raised in almost every subsequent meeting. We used data not only to understand the child welfare and adult jail populations of Philadelphia, but also to evaluate whether sufficient data would be available to design, manage, and evaluate a successful PFS project. For many jurisdictions, data availability and data sharing are major hurdles, so a city's ability to generate and share data is in itself a critical part of assessing feasibility for PFS.

In the first weeks of our study, we sat with the data team at PPS to answer two questions: Who would a PFS project serve, and what would be the financial impact of a successful PFS project for PPS? Specifically, we requested de-identified, individual-level data on the PPS population, including demographic traits, the number and length of encounters with the criminal justice system and geographic identifiers, as well as associated operational costs for the target population – all in keeping with our signed data sharing agreement.

PPS provided three data sets on the previous year's inmate population. The first described the demographic characteristics—age, gender, race, educational attainment—of the jail population, aggregated by Philadelphia zip code. It also included the average number of PPS encounters for each of these demographic subgroups. The second data set included an inventory of all PPS programs and services offered within the walls, the total number of participants in each service and their average one-, two- and three-year recidivism rates upon release. Finally, the third contained a list of all vendor contracts including vocational training, education and re-entry services and their associated costs to PPS. (This dataset was also where we discovered PPS' contract with neighboring county jail facilities to house its overflow population.)

We are often unable to access all of the data we would like, because an agency doesn't track the breadth of data we request or they are limited in sharing data. For instance, PPS does not track inmates' employment or housing status upon release, because its responsibility ends with release. Data sharing restrictions limit PPS, and many other agencies, from reporting inmates' path to incarceration (i.e., pre-trial, probation, parole, or sentenced) or charge type (i.e., property, person, drugs, weapons, vehicle or other). These data points help us to better understand the target population, assess their service needs upon release, and refine the assumptions underlying our cost-benefit analysis. Where local historical data were not accessible, we relied on group-level data or PPS' expertise on the target population, as well as state and national cost data.

Beyond understanding how individuals flow in and out of PPS, we also focused on interactions with other agencies—APPD and the Philadelphia Police Department, and for many, the Department of Behavioral Health, the Office of Supportive Housing and the emergency medical systems. Ideally, we'd be able to track an individual through each of these systems but like many jurisdictions, Philadelphia does not have an integrated data system to track individuals. Instead, we worked with other agencies directly to estimate the

number of active parolees from PPS, as well as their service needs around substance abuse, mental health and homelessness. Combined with PPS data, this gave us a more holistic understanding of the target population.

The ability to track individuals through different agencies—rather than to make assumptions based on aggregate level data—strengthens PFS projects. Integrating data systems across agencies requires significant commitment from senior government officials and dedicated resources to implement. Other jurisdictions have leveraged resources, such as local academic research centers or quasi-governmental state longitudinal databases, to decrease the costs of aggregating data.

As part of our recommendation, we advised the city to pursue legal avenues for increasing data sharing among agencies. For example, it may be possible for PPS to share data with a nonprofit service provider as long as they are considered an extension of the criminal justice system. Another avenue may be to request a letter from the Pennsylvania Attorney General's office allowing the instance of data-sharing.