

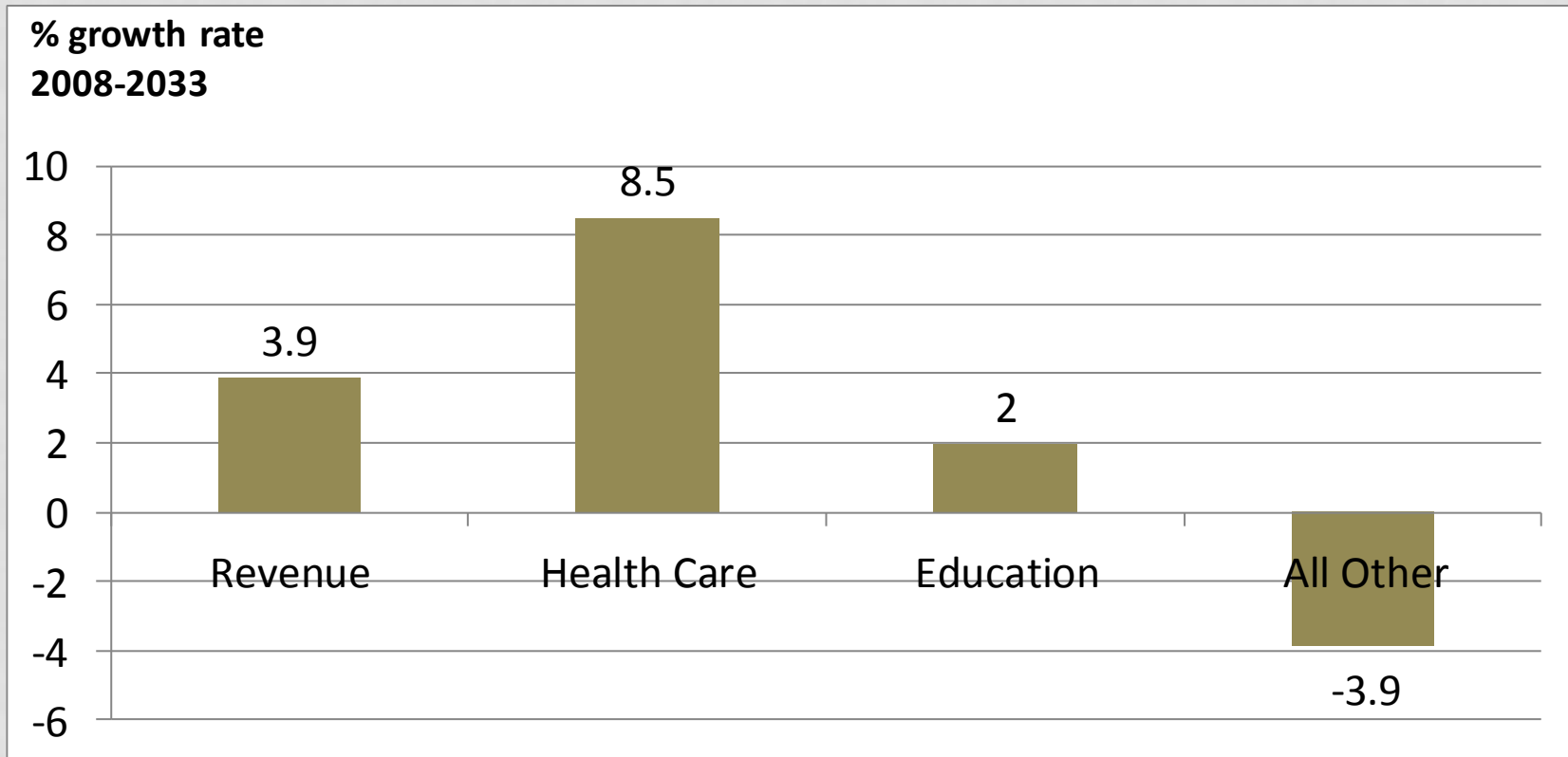
HUMAN CAPITAL PERFORMANCE BONDS(HUCAP)

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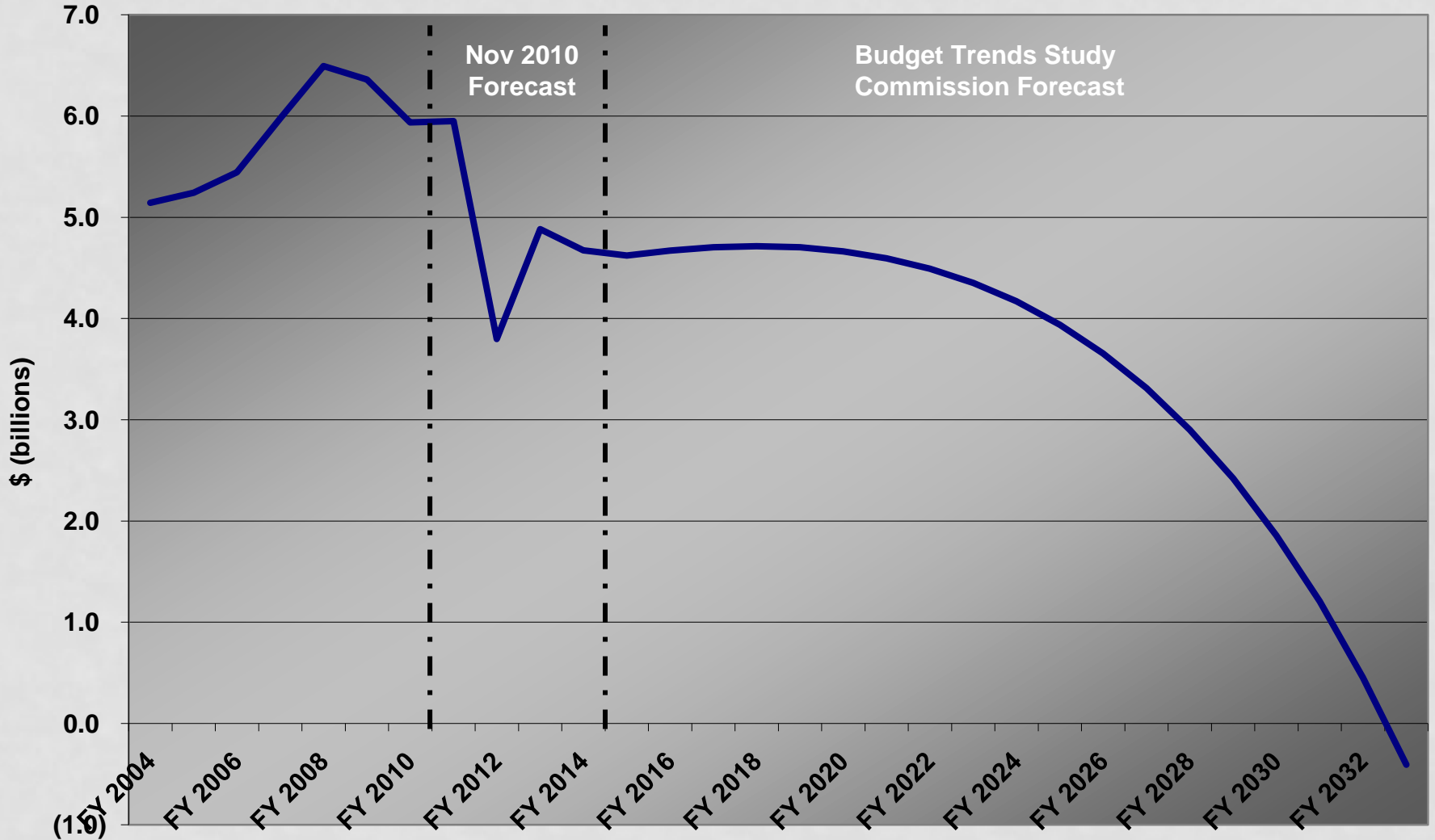
Agenda

- The Problem
- What's Required
- A New Idea
- Implications for Budget and Policy
- Goals/Status/Plans

Implications of Continued Health Care Trends Plus CPI Inflationary Increase for Education in Minnesota



General Fund Spending Not Attributable to K-12 Education, Health Care Grants/Admin and Continuing Care Grants/Admin: FY 2004-FY2033



WHAT'S NEEDED

- Greater Productivity
- New Investors
- Additional Investment

ASSUMPTIONS

Quality Nonprofits Create Social Value



Social Value Equates to Economic Value



Economic Value Equates to Cash Flow

Twin Cities RISE! *example*

- “Pay for Performance” contract established by Mn. Legislature in 1997
- Based on economic value established by higher tax receipts and lower government subsidies from increased incomes
- \$10,000 increase in income assumed \$3,800 cash value/yr. and p.v. of \$31,000 (actual is \$50,000)
- TCR! paid \$9k at placement, \$9k at retention
- State’s 13 year ROI= 624% (\$33.4M benefit for \$4.6M investment)

HUMAN CAPITAL PERFORMANCE BOND

- **WHAT IS IT :**

Market Rate, State AA bond that funds high performing human services

- **WHO INVESTS:**

Private investors, financial institutions, banks seeking a market rate of return; social investors

- **WHY DOES IT WORK:**

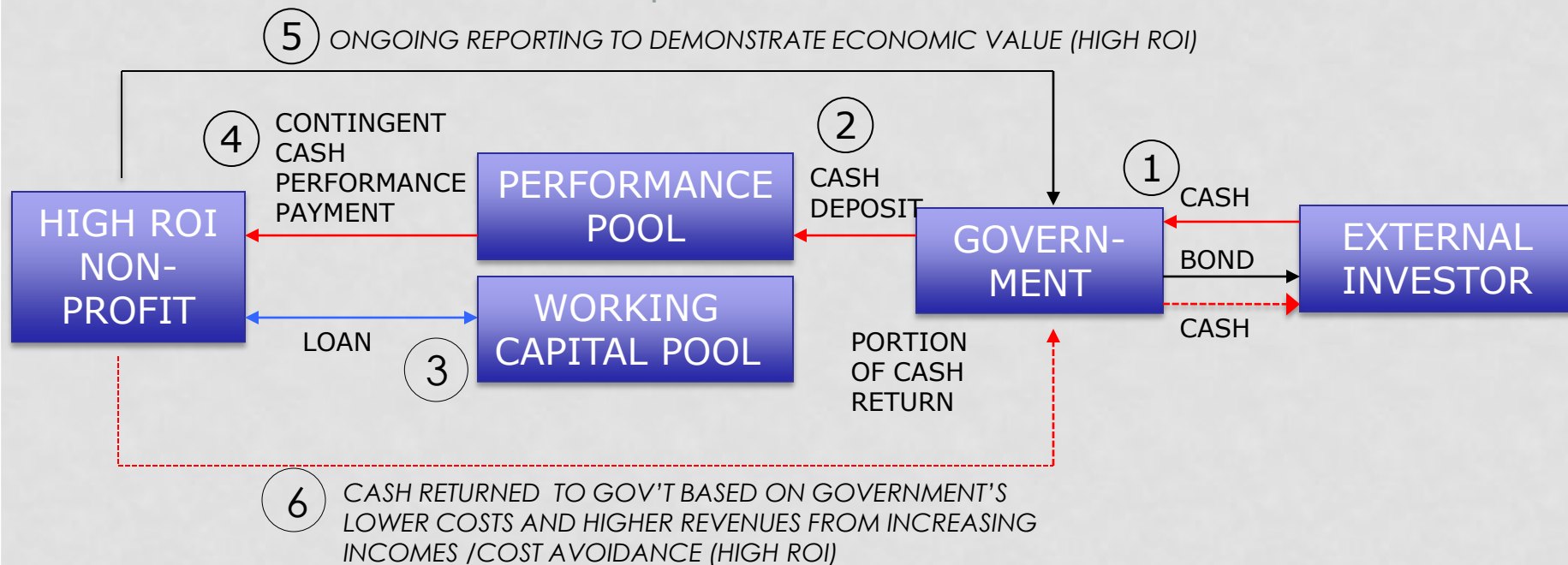
Economic return (ROI) of providers exceeds the state's cost of borrowing

- **HOW DOES IT WORK:**

1. State sells bonds
2. Proceeds to “performance pool”
3. Providers that create economic value share in value at performance

Human Capital Performance Bond

Proposed Structure for State



- ① External investor buys state appropriation bond that is linked to specific economic criteria established by government; structured as normal, market rate of return
 - ② State deposits investor funds in "Performance Pool" where it's held until payout terms are met by pre-certified non-profit.
 - ③ Non-profit qualifies for working capital loan from pri's ,cdc's, performance pool, other.
 - ④ Pool pays out to non-profit based on non-profit meeting government performance goals.
 - ⑤ Non-profit/pool oversight board annually validates performance value (ROI) to state.
 - ⑥ If performance targets are met, government receives high ROI and cash flow to fund principal repayment and interest.
If performance targets are not met, state has use of funds for principal repayment, interest or other purposes until bond period terminates.
- Structure term ends at end of bond term. Alternatively, performance pool continues operating, funded by cash returns re-invested by government

HUCAP ACCOUNTING

- Individuals tracked through their Social Security #
- Incremental taxes and entitlement savings “booked” where benefit occurs (e.g. revenue, human services budgets)
- Cash benefit kept in Finance dept. account
- All Interest, Principal and Administrative Costs paid from Finance Dept account.

POLICY AND BUDGET IMPLICATIONS

- Neutral or Positive Cash Flow to State
 - Cost of Debt @14% (4% interest, 8% Principal, 2% admin)
 - Provider Cash return above 14%
- Annual Appropriation Bond Constitutional and Accepted in Marketplace
- State Bonding Not Required Long-Term To Fund Bond
- Establishes Framework for Allocating Appropriations

CONTINUUM OF SOCIAL INVESTING

No Financial Return

Billions Invested
No Cost of Capital

Examples:

- Government Appropriations
- Philanthropy

Below Market Return

Millions Invested
High Cost of Capital

Examples:

- Social Venture Capital
- Program Related Investments
- SOCIAL IMPACT BOND

Market Return

Trillions Invested
Low Cost of Capital

Examples:

- Government Bond for Building and Equipment
- HUMAN CAPITAL PERFORMANCE BOND

STATUS

- Legislature passed HUCAP in government finance bill vetoed by governor.
 - Governor indicated interest in HUCAP in veto letter
- Economists completed workforce program feasibility. Adult day care, supportive housing, addiction treatment, disability employment next.
- Evaluation protocol being developed
- Planning underway for relationships with state agencies, foundations, banks, business.

PLANS

- Pass Law
- Finalize economic values, bond structure and pilot areas
- Determine technical and contractual terms with Government
- Fundraise to support development and evaluation
- Execute pilot

CONCERNS & HOPES

CONCERNS:

- Fidelity of model
- Supplant instead of supplement appropriations

HOPES:

- Execute pilot in 2012
- Demonstrate feasibility in many human service areas
- Interest others

SUMMARY

- Systems change for government and non-profit sectors
 - “pay for performance” based on economic value
 - ROI allocates capital to best social performers
- Generates incremental investment for human services at no cost to Government
- Encourages more strategic investing by providers
- Cuts across structural issues in all major spending areas of government.
- Tests possible new approach for appropriations