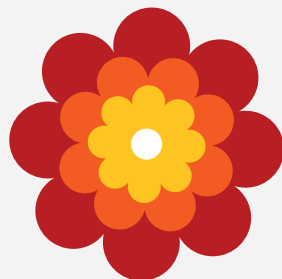


# SOCIAL IMPACT BONDS

Feasibility study on implementing  
Social Impact Bonds in Estonia

**FINAL REPORT AND LESSONS LEARNED**



HEATEO SIHTASUTUS

Tallinn, 2015



With financial support from the European Union

This analysis was financed by the European Union  
under the project "Preparatory Action for the Launch of the Social Impact Bonds in Estonia".

## FOREWORD

*“The state of Estonia is costly, and the state of Estonia is dear.  
Costly for the citizen’s wallet and dear to the citizen’s heart.”*

Lennart Meri, President of the Republic of Estonia, 2001

The Republic of Estonia is in a situation where expectations for government intervention to solve various social problems are ever increasing and the solutions to these problems are ever more complex. We are therefore in need of novel, more effective solutions and synergetic cooperation between the stakeholders of society – in other words, social innovation.

One of the prerequisites for social innovation is a society’s receptivity and readiness to establish various cross-sector cooperation models, involving the interaction of the public, private and third sectors. A number of synergetic models have already been designed and tested around the world. The *social impact bonds model*, first introduced in England in 2010, has since spread across the globe and is employed for social investments on an increasing scale.

Successfully implemented social impact bonds lead to new and improved public services that can help more people and save the taxpayers’ money. Although social impact bonds have their limitations, they could help introduce a new way of thinking and new solutions to Estonia’s social services sector.

It is our pleasure to note that the Good Deed Foundation has, during the past year, put its spirit and dedication into analysing the feasibility of launching the model in Estonia. We have actively engaged the representatives of the public, private and third sectors and established the first framework for implementing social impact bonds in Estonia.

We thank all contributors, supporters and partners without whom we wouldn’t be where we are today. We are especially grateful to Teele Raun and Anna Karolin, whose dedication made this project happen! We hope to see the launch of social impact bonds very soon. This time in Estonia!

**Maris Ojamuru**  
**Pirkko Valge**

Members of the Management Board  
The Good Deed Foundation

## SUPPORTERS



European  
Union



Estonian  
Development Fund

## PARTNERS



Estonian Social Enterprise  
Network



Praxis Centre for  
Policy Studies



PricewaterhouseCoopers



Borenium Law Firm

## CONTRIBUTORS

Pål Christian Bergstrøm, Francois de Borchgrave, Knut Gundersen, Ahti Heinla, Katrin Isotamm, Tarmo Jüristo, Heidi Kakko, Ly Kasvandik, Martin Kodar, Kai Liiva, Külli Lilleorg, Allan Marnot, Kati Nikopensius, Antti Perli, Vaiko Tammeväli, Gunnar Toomemets, Kristiina Treial, Margus Uudam, Kaido Veske, Taavi Veskimägi, Signe Viimsalu and Kaarel and Risto Oja who were the first to raise the topic of social impact bonds in Estonia.

## WE ALSO THANK

Aivar Pilv Law Firm  
Hedman Partners Law Firm  
Sorainen Law Firm  
Stibbe Law Firm  
BaltCap  
Estonian Unemployment Insurance Fund  
Estonian Business Angels Network  
European Venture Philanthropy Association  
Finance Estonia  
Ministry of Justice  
National Foundation of Civil Society  
KOIS Invest  
Crime Prevention Foundation  
Ministry of Finance  
RuaCrew NPO  
Ministry of Internal Affairs  
SmartCap  
Social Insurance Board  
Ministry of Social Affairs  
Swedbank  
Responsible Business Forum in Estonia  
Öökull NPO

## TABLE OF CONTENTS

<b>INTRODUCTION</b>	<b>7</b>
<b>1. SOCIAL IMPACT BONDS</b>	<b>8</b>
1.1 Origin and global practice	9
<b>2. TIMELINE FOR DEVELOPING THE MODEL</b>	<b>12</b>
<b>3. THE PARTIES AND THEIR PROFILES IN ESTONIA</b>	<b>14</b>
3.1 Public sector	14
3.2 Private sector	15
3.3 Third sector	17
<b>4. MAPPING AND SELECTION OF PROBLEM AREAS</b>	<b>19</b>
4.1 Approach	19
4.2 Outcome	20
4.3 Challenges and lessons learned	21
<b>5. MAPPING AND SELECTION OF INTERVENTIONS</b>	<b>22</b>
5.1 Approach	22
5.2 Outcome	23
5.3 Challenges and lessons learned	25
<b>6. MAPPING OF SERVICE PROVIDERS</b>	<b>26</b>
6.1 Approach	26
6.2 Outcome	27
6.3 Challenges and lessons learned	27
<b>7. MAPPING OF INVESTORS</b>	<b>28</b>
7.1 Approach	28
7.2 Outcome	29
7.3 Challenges and lessons learned	29
<b>8. IMPACT FRAMEWORK</b>	<b>31</b>
8.1 Approach	31
8.2 Outcome	31
8.3 Challenges and lessons learned	33
<b>9. FINANCIAL FRAMEWORK</b>	<b>34</b>
9.1 Approach	35
9.2 Outcome	35
9.3 Challenges and lessons learned	37

<b>10. LEGAL FRAMEWORK</b>	<b>38</b>
10.1 Approach	38
10.2 Outcome	38
10.3 Challenges and lessons learned	40
<b>SUMMARY</b>	<b>41</b>
<b>REFERENCES</b>	<b>43</b>
<b>ANNEX</b>	<b>45</b>

## INTRODUCTION

The Good Deed Foundation is the only organization active in venture philanthropy in the Baltic countries. The Foundation's mission is to find effective solutions for acute problems in Estonian society. During 12 years of activity, we have launched and developed a number of strong initiatives, including the Noored Kooli (Youth to School) Foundation, aimed at improving the quality of education in Estonia; NPO Uuskasutuskeskus (the Re-Use Center), the largest social enterprise in Estonia and operator of a chain of stores selling reused and redesigned goods; NPO Abikäsi (the Helping Hand), which counsels and supports persons with special needs and the long-term unemployed in seeking work on the open job market; and SOS Lasteküla, (SOS Children's Village) which provides for children without parental care.

The Good Deed team believes that social issues can be best solved in cross-sectoral cooperation. To achieve this, the organization has surrounded itself with an extensive network of volunteers and *pro bono* partners and philanthropists who contribute their professional skills and financial resources towards solving social issues. The Good Deed Foundation has close ties with the public sector as well, working together to promote social innovation and launch new initiatives. A good example and model is SPIN programm, a sports-based prevention program for youth, launched in cooperation with the Ministry of Internal Affairs in 2014.

In addition to launching influential initiatives and promoting cross-sectoral cooperation, the Good Deed Foundation has drawn Estonia's attention to a number of important areas and issues that contribute to a more effective resolution of social problems. This includes the introduction of the *social enterprise model* and the publication of a guidebook on social impact assessment. Within venture philanthropy, several new cooperation and financing models have been developed, which have caught the interest of philanthropists, socially responsible enterprises, funds and impact investors. One of these is the social impact bond model.

In 2014, Good Deed Foundation in cooperation with Estonian Social Enterprise Network initiated a feasibility study and cost-benefit assessment for launching Estonia's first social impact bond model. The sub-goals of the project were to increase public-sector awareness of impact investment; strengthen the credibility of social enterprises in the eyes of both private and public-sector investors; provide additional financing opportunities for social enterprises and disseminate and develop high-impact best practices in cooperation with the third sector and businesses.

The year-long project involved mapping the readiness of Estonia's public sector, investors and NGOs to implement the novel financing model, and preparing the impact, financial and legal framework for the first social impact bond. This report provides an overview of the model development process, the analyses and their results, and lessons learned through the activities.

Preparations for launching the social impact bonds model were carried out with support from the European Union and the Estonian Development Fund.

## 1. SOCIAL IMPACT BONDS

Social impact bonds (SIB) are a novel investment model aimed at increasing the effectiveness of solutions to social issues. The bond model enables the government to use private support in testing alternative services and, if successful, implementing these instead of services provided by the government.

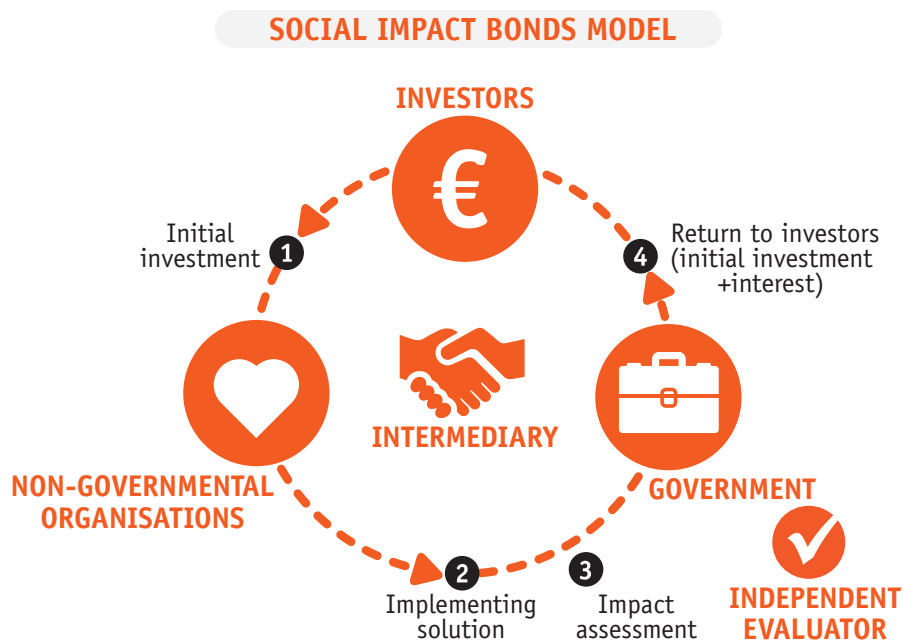


Figure 1. Social impact bonds model.

At the core of each bond is an agreement between the three parties – private investors, government and third sector organization(s) – to engage private investment in solving a specific social issue. The issue will then be tackled by a capable NGO that can provide an innovative and effective approach. If the proposed solution yields better results than the existing public service during an agreed period of time, the government shall reimburse the investment to the investor with interest. Reimbursements shall only be made if independent evaluation shows that the agreed-upon results and impacts have indeed been achieved.

The aim of social impact bonds is to achieve comprehensive change. By implementing the model, the public sector can invest in influential interventions and preventive activities and thus promote the creation of new services and improve the ability to solve social challenges. For non-profit organisations, this creates an opportunity to develop their services and expand activities. For investors, it provides a new financial instrument that can contribute to solving social challenges as well as creating conditions for earning a return on investment.<sup>1</sup>

<sup>1</sup> Bridges Ventures & Bank of America Merrill Lynch (2014). Choosing Social Impact Bonds: A Practitioner's Guide. <http://www.bridgesventures.com/wp-content/uploads/2014/12/SIB-report-DPS.pdf> (01.06.2015)



### SUCCESSFUL IMPLEMENTATION OF SOCIAL IMPACT BONDS INVOLVES:

- stronger positive impact for the target group;
- more effective and higher-quality public service;
- performance-based allocations from the state budget;
- more capable NGOs;
- return on investment for investors.

The bonds are issued by an organization that is capable of bringing together different parties involved in the project and also supporting the NGOs by improving their organizational capacity and managing the investment.

#### 1.1 GLOBAL PRACTICE

The idea of social impact bonds first emerged in 2010 in the United Kingdom in response to the issue of recidivism among offenders subjected to short-term imprisonment, i.e. up to 12 months. Sixty per cent of persons released from prison committed another offence during the first year after release. For many criminals, the prison system became a shelter and path to medical care, with the courts acting as a support system. Meanwhile, the incarceration and care of each prisoner cost the state around 80,000 pounds per year. When searching for solutions to rehabilitate the prisoners more successfully, an innovative solution was proposed by the third sector and financed through the social impact bonds model.

The first pilot project in the United Kingdom, and in the world, was launched in a cooperative venture between the UK Ministries of Justice and impact investment organization Social Finance. The goal was reducing repeat offences by persons released from short-term imprisonment by 7.5% during the first year after release, compared to a reference group. Social Finance raised 5 million pounds from 17 investors to finance a consortium of several organizations during six years as they worked with 3,000 persons released from Peterborough Prison. The program helped participants find permanent residence and jobs, offered drug and alcohol aversion therapy, psychological counseling and parenting support services. The parties agreed that if the established goal was reached, the government would reimburse the initial investment with 13% annual interest.

In the summer of 2014, the results of the first phase were published – the new intervention reduced reconvictions among persons released from short-term imprisonment by 8.6%. Although the project is still running, the UK government has officially acknowledged the piloted solution and is set to reform the national service on its basis.

## SOCIAL IMPACT BONDS IN BELGIUM:

### REDUCING UNEMPLOYMENT AMONG AT-RISK YOUTH

<b>PROBLEM:</b>	31.7% of youth in Brussels are unemployed
<b>GOAL:</b>	increase the employment level of at-risk youth by 35%
<b>POTENTIAL ECONOMIC ADVANTAGE FOR THE GOVERNMENT:</b>	approximately 33,000 euros per employed youth (unemployment benefit savings, revenue from social and income tax); employment of 1/3 of the target group youth would mean up to 2 million euros in government savings
<b>INTERVENTION:</b>	Duo for a Job, a 6-month mentoring program by local seniors in which an unemployed young person would be partnered with an experienced specialist who has recently retired
<b>TARGET GROUP:</b>	youth aged 18-30 arriving from outside the European Union; total of 180 young people
<b>RESULT INDICATOR:</b>	number of employed youth 12 months after the program's end (employed for more than 90 days during the period or working under long-term employment contracts)
<b>DURATION:</b>	3 years, 2014–2017
<b>INVESTMENT:</b>	234,000 €
<b>YIELD:</b>	up to 6%
<b>PARTIES:</b>	<p><b>Contracting authority:</b> Brussels Unemployment Office</p> <p><b>Service provider:</b> Duo for a Job</p> <p><b>Investors:</b> KOIS Invest, Bank Degroof Foundation and others</p> <p><b>Independent evaluation by:</b> Observatoire de l'Emploi Bruxellois</p>

By spring 2015, more than 30 social impact bonds have been launched across the globe, mostly in the UK, the United States and Australia. Several European Union member states, including the Netherlands, Belgium, Germany and Portugal, have also initiated their first social impact bond projects. The EU sees the model as an opportunity to approach a high-potential capital market with an innovative financing model.

The European Commission has pledged to support dissemination of the model by facilitating the pooling of member states' experience gained during implementation of the bonds model. The European Parliament has urged member states to employ innovative financing possibilities on a wider scale to help resolve social issues.<sup>2</sup>

Besides Estonia, around the world approximately 100 social impact bond model projects are currently in the works.

<sup>2</sup> European Parliament Think Tank. Davies, R. (August, 2014). Social impact bonds: Private finance that generates social returns. [http://www.europarl.europa.eu/thinktank/en/document.html?reference=EPRS\\_BRI\(2014\)538223](http://www.europarl.europa.eu/thinktank/en/document.html?reference=EPRS_BRI(2014)538223) (01.06.2015)

**COUNTRIES WHERE SOCIAL IMPACT BONDS HAVE BEEN LAUNCHED**

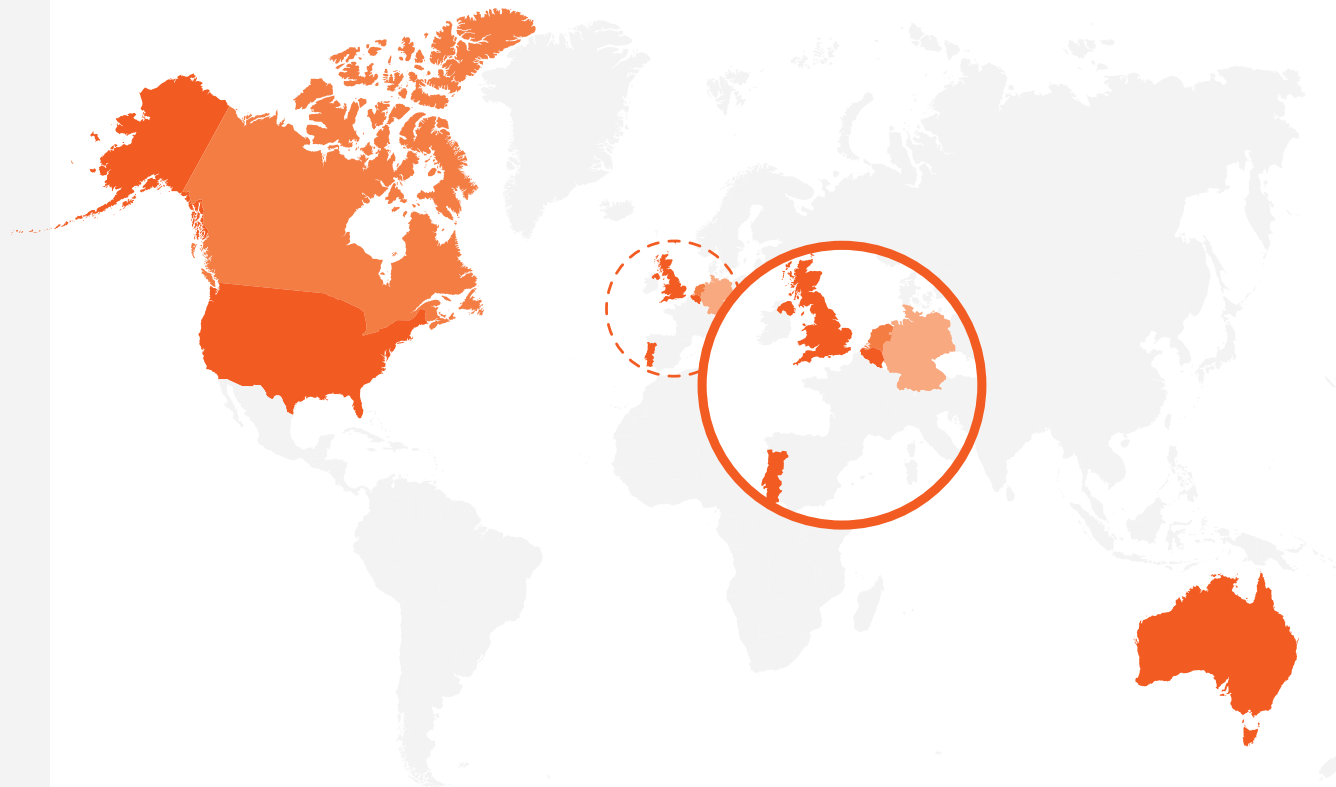


Figure 2. Countries where social impact bonds have been launched

## 2. TIMELINE OF THE PROJECT

The idea of social impact bonds was first presented to the Good Deed Foundation by Kaarel and Risto Oja, who got acquainted with the model in UK at the beginning of 2013. The first debate on whether and in which area Estonia should implement the bonds was held at the Festival of Opinion Culture in 2013. Inspired by the festival, the Good Deed Foundation summoned a working group for launching the model in Estonia. In the spring of 2014, both the European Union and the Estonian Development Fund decided to support the year-long project for developing the idea. Extensive research into implementation of the model started in the summer of the same year.

PROJECT STEPS:	June	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	March	April	May	June
Establishing and maintaining relationships with relevant parties													
Mapping and analysis of problem areas													
Mapping interventions and service providers													
Researching and developing an impact assessment framework													
Developing a legal framework													
Mapping state expenditures and financial analysis													
Dissemination of the results of the feasibility study													

Figure 3. Timeline of the project.

The project to prepare for the social impact bonds coincided with turbulent times in Estonian politics. During the spring of 2014 there was an unexpected change of government. Moreover, during the spring of 2015 general elections took place which were preceded by an active political campaign period. These events influenced the high official's willingness to take on new matters and therefore caused some delays in the project's schedule.

All in all, government officials responsible for the problem area became excellent partners starting from the first meetings and they participated actively in gathering information and cost data and developing the impact framework. Since changes and decisions on the political arena can have a strong influence on launching the model it was important to ensure the interest of the high officials in order to ensure the readiness to implement new models.

The biggest change compared to the initial project plan came from the assumptions used in planning. The initial project plan envisaged a step-by-step movement from one action to another, starting with analysis of problem areas and then proceeding to mapping service providers, creating an impact framework and launching social impact bond. Raising the awareness on impact investing and on social impact bonds was planned as a parallel work stream. The assumption behind the step-by-step approach was that each phase would end with a decision and proceeding to the next phase. In practice, however, the process diverged somewhat from the plan.

During the project it became clear that the prerequisite of deciding on a problem area was a complete understanding of the ecosystem surrounding the model. This included an overview of service providers already engaged in the area and their organizational capacity, the state's current expenditures and the budget of the new intervention. This required working on different work streams simultaneously which was challenging from the project management perspective.

As the development of the framework requires knowledge from different fields (e.g. financial- and judicial expertise, experience concerning evidence based programs and impact measurement) it was vital to establish a network of specialists whose expertise could be utilized in different phases of the project. The chance to work with leading experts offered Good Deed Foundation an opportunity to learn from the best. Cooperation with state officials helped achieve a clear understanding of their decision-making processes, priorities and logic of operation. Establishing contacts with investors gave a good overview of their expectations about the models implementation as well as impact investments in general. Inclusion of NGOs and state institutions offered in depth insight into the problem area and the target group.

The extent and complexity of the project have given Good Deed Foundation a valuable experience in cross-sector project management and the opportunity to establish important new contacts for solving societal problems on a wider scale.

### 3. THE PARTIES AND THEIR PROFILES IN ESTONIA

An important condition for the successful launch of social impact bonds is the parties' interest and readiness to test the model. Firstly, state authorities should be motivated to seek opportunities for solving issues in their field of administration more effectively, and reduce the cost base. Secondly, investors' interest in investing into social impact is necessary. And thirdly, capable third-sector organizations with motivation to develop and offer new services need to be in place.

#### 3.1 PUBLIC SECTOR

The public sector's role in launching social impact bonds is to point out a problem area and order services.

Since the restoration of Estonia's independence, the country has pursued a balanced state budget and low taxes; state intervention in the economy is maintained at a low level and the economic and social well-being of citizens depends largely on each person's own activity. The "thin state" implies, among other things, fewer levels of decision-making and fewer public servants.

According to a 2014 study by the Praxis Centre for Policy Studies, local governments have a more important role than the state in providing everyday services to citizens.<sup>3</sup> According to Praxis, 62.9% of local governments had delegated the provision of some of their public services to non-profit organisations during 2013–2014.<sup>4</sup>

In view of the upcoming social and economic changes, local governments should employ creativity for providing the appropriate level and quality of public services to citizens. Increasing attention needs to be paid to social innovation and social enterprise, engaging the public in various phases of policymaking and policy implementation, co-creation of services and partnerships involving different sectors and citizens. All this should help meet the challenges of a modern society, introduce new solutions to the public sector and enable the provision of an adequate level of services while improving their quality and cost-effectiveness. Many countries have developed concepts and measures for implementing innovative forms of cooperation for the provision of services on national and local levels. As noted in the Praxis report, the methods of service provision need to be reconsidered or reinvented also in Estonia in order to create a favorable environment for social innovation.<sup>5</sup>

3 Uus, M., Tatar, M., Vinni, R. (2014). Avalike teenuste delegeerimine vabaihendustele. Tallinn: Poliitikauuringute Keskus Praxis. <http://www.praxis.ee/wp-content/uploads/2014/12/teenuste-delegeerimine.pdf> (1.06.2015)

4 Ibid.

5 Ibid.

Accession to the EU and the related changes have significantly influenced and guided the national and social development of Estonia. The amount of EU support for Estonia has consistently increased and accounts for an ever-larger proportion of the state budget, currently at around 15%. According to the professor of international entrepreneurship Urmas Varblane, Estonia has developed a dependence on support and Estonia needs a comprehensive plan of action for coping in an environment of decreasing foreign support.<sup>6</sup> Implementation of social impact bonds could be one of the solutions to cut public expenditure and engage the private sector in solving social problems.

### 3.2 PRIVATE SECTOR

The private sector's role in implementing social impact bonds is to provide primary financing for the launch of a novel service aimed at solving a social problem.

Since the restoration of independence, Estonia's priority has been the creation of a competitive and stable business environment. Today, Estonia stands high in freedom of enterprise rankings. According to the World Bank's Doing Business 2015 report, Estonia is currently 17<sup>th</sup> in the world in terms of ease of doing business.<sup>7</sup> In the global Index of Economic Freedom compiled by the Heritage Foundation and the Wall Street Journal, Estonia climbed from 11th place to 8th in 2015, and is now the highest-ranking European country after Switzerland.<sup>8</sup> At the same time, Estonia's start-up community is steadily developing and able to successfully raise capital on the local level as well as from various accelerators, incubators and private investors across the world. The state has plans to continue the development of the business environment by investing more than 140 million euros in 2015–2020 to provide better access to capital and credit insurance for businesses.

According to the Ministry of Economic Affairs and Communications, Estonia has more than 60,000 registered companies, though only approximately 150 are large enterprises (i.e. with 250 or more employees).<sup>9</sup> The main sectors of the economy (by employment levels) are manufacturing, commerce, education, construction and logistics. The internal market of less than 1.3 million consumers is too small for many companies, who have therefore sought expansion abroad. A high level of openness also means that the Estonian economy is susceptible to global changes and the economy and the labor market have experienced major fluctuations in recent years. Nevertheless, Estonia has closed in on the EU's more

6 Varblane, U. (2015). Euroopa raha võlu ja valu. <http://www.riigikogu.ee/rito/index.php?id=16676> (01.06.2015)

7 World Bank Group (Oct, 2014). Doing Business 2015 Going Beyond Efficiency. <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB15-Full-Report.pdf> (01.06.2015)

8 The Heritage Foundation (2015). 2015 Index of Economic Freedom: Estonia. <http://www.heritage.org/index/country/estonia> (01.06.2015)

9 Majandus- ja Kommunikatsiooniministeerium (2015). Majandusanalüüs. <https://www.mkm.ee/et/tegevused-eesmargid/majandusareng-ja-ettevotlus/majandusanaluus> (01.06.2015)

developed economies relatively quickly, although a significant gap still remains: according to Eurostat, Estonia's GDP at purchasing power parity was 47% of the EU average in 2001 and 73% in 2013. The development of Estonia's productivity has been similar. The goal is to achieve 80% of EU's average productivity by 2020.

Despite the satisfactory outlook for Estonia's economy, mostly due to positive developments in household consumption, investment statistics have been unsatisfactory for the past few years. According to data from the Bank of Estonia, corporate investment in Estonia was down from 2.6 billion euros in 2013 to 2.4 billion euros in 2014.<sup>10</sup> The investment activity and boldness of Estonian enterprises is dampened by geopolitical tensions, notably the Russia-Ukraine conflict, which has directly affected the demand for Estonian goods and services in those countries.<sup>11</sup>

Meanwhile, adherence to the *corporate social responsibility* (CSR) principles is gaining much attention across the world. Corporate social responsibility stands for economically, environmentally and socially responsible enterprise. In Estonia, CSR principles and related goals are included in the corporate strategies of local branches of large foreign corporations and are therefore increasingly implemented in Estonia.

The Responsible Business Forum in Estonia currently has 39 members, including both large and small enterprises. Responding to a United Nations survey, 93% of company managers across the globe mentioned corporate social responsibility as one of the key factors in the success of their organization, while a poll conducted by KPMG Baltics indicated that just 56% of Estonian entrepreneurs and managers mentioned corporate sustainability as part of the strategy and daily activities of their company. However, 6% of Estonian entrepreneurs considered CSR activities to be merely a public relations stunt, while 5% thought CSR was nothing more than an irrational fad.<sup>12</sup> This shows that it is important to raise awareness on how to link corporate social responsibility with corporate strategy.

The CSR Index compiled annually by the Forum is currently the only survey in Estonia that provides an in-depth assessment of the local businesses contribution to the society. The index shows that strategic contributions to the community are underdeveloped (scoring 63 points out of 100) in comparison to the businesses' other activities. The main ways of contributing were sponsorships and single charitable actions. Civil society therefore loses hundreds of thousands of euros per year and, more importantly, valuable knowledge that could be obtained through strategic and well-reasoned cooperation with the private sector.

10 Eesti Pank (2015). Eesti majanduse aastanäitajad. <http://statistika.eestipank.ee/?lng=et#treeMenu/MAJANDUSK00ND> (01.06.2015)

11 Eesti Konjunkturiinstituut (2015). Konjunktuur, nr 1 (192), lk 7. [https://www.mkm.ee/sites/default/files/konjunktuur\\_nr\\_1\\_192\\_marts\\_2015.pdf](https://www.mkm.ee/sites/default/files/konjunktuur_nr_1_192_marts_2015.pdf) (01.06.2015)

12 Vastutustundliku Ettevõtluse Foorum. Uuringud ja statistika. <http://www.csr.ee/uuringud-ja-statistika/> (01.06.2015)



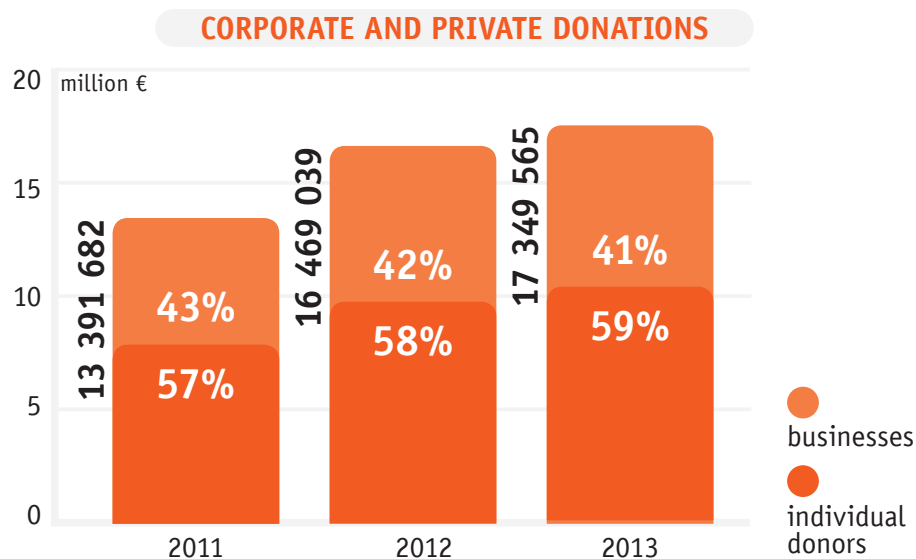


Figure 4. Corporate and private donations.<sup>13</sup>

Although donation culture is on the rise and the number of donations has increased from year to year, Estonia has practically no knowledgeable impact investors nor local impact investment foundations. The largest financial investments, approximately 1 million euros, are managed by the Estonian National Culture Foundation. Only around 50 charities have declared profits from financial investments, the SEB Charity Fund being the most profitable with 38,000 euros.<sup>14</sup>

### 3.3 THIRD SECTOR

The role of NGOs in the social impact bonds model is to develop and implement a novel intervention. This provides an opportunity for the third sector to show itself as a capable partner for the state as well as for investors and gain long-term financing for its services.

A democratic country is characterized, among other things, by a strong and functional civil society, or third sector. The development of civil society in Estonia began in the years after restoration of independence. Independent statehood was influenced by domestic change as well as external factors, while the attitudes of the people were shaped by financial and political support from the United States, Europe and Scandinavia. As of today, Estonian civil society is considerably more organized, organizations are more capable of standing up for their interest groups, and legislation concerning civic initiatives has been improved significantly. Nevertheless, the partnership between public authorities and the civil society is

<sup>13</sup> Ibid.

<sup>14</sup> Kübar, U., Rammo, A. (2014). 23 küsimust Eesti vabakonna kohta ja vastused, nii hästi, kui neid leida oskasime. Hea Kodanik, nr 5 (63), lk 21-28. [http://issuu.com/emsl/docs/hea\\_kodanik\\_talv\\_2014](http://issuu.com/emsl/docs/hea_kodanik_talv_2014)

ever stronger and citizens are increasingly involved in the decision-making processes. Meanwhile, the stable long-term cooperation ties between NGOs and all their usual partners have weakened significantly.<sup>15</sup> Although the number of various civic initiatives has increased and the public image of social activism has improved, there is still a long way to go.

Social entrepreneurship in Estonia essentially began in 2004 with the founding of Estonia's first social enterprise – Uuskasutuskeskus (The Re-use Center). In the decade that followed, the sector has been growing in Estonia as well as in other countries. Interest in social entrepreneurship has increased and social enterprises are now active in a variety of areas, bringing excluded target groups back to the job market, creating innovative educational models and providing innovative solutions for social care. In 2012, the Good Deed Foundation founded the Estonian Social Enterprise Network in cooperation with other organizations. The network aims to increase the number, influence and capability of social enterprises and represent their interests.

---

<sup>15</sup> Tallinna Ülikool, Kodanikuühiskonna Sihtkapital (2015). Kodanikualgatuse institutsionaliseerumine Eestis 2014. <http://www.kysk.ee/failid/Upload/files/KUAK%2014%20raport.pdf> (01.06.2015)

## 4. MAPPING AND SELECTION OF PROBLEM AREAS

The social impact bonds model has been applied around the world to solve a variety of social problems like facilitating the employment of vulnerable groups, strengthening families by improving parenting skills, rehabilitation of homeless persons and helping children overcome educational lags.

However, it should be noted that all social problems cannot be solved through social impact bonds. The model is based on a transparent impact assessment model (including data about the problem area) and a readiness of the parties to contribute to solving the problem.

### 4.1 APPROACH

Possible problem areas which could benefit from the application of social impact bonds were mapped by the Praxis Centre for Policy Studies. Problems were mapped on the basis of existing studies and overviews concerning Estonia, in relation to the problem areas in which social impact bonds have been used in other countries. Lasting from August to February, this was also the longest phase of the project as it was dependent on establishing relationships with different public-sector organizations. To introduce the model and map the possible problem areas, several meetings with the representatives of different state agencies were held. The meetings involved representatives of the Ministry of Social Affairs, the Ministry of Justice, the Ministry of Internal Affairs, the National Institute for Health Development, the Social Insurance Board and the Estonian Unemployment Fund. Mapping was followed by an in depth analysis based on the criteria below.

#### THE FOLLOWING CRITERIA WERE USED FOR SELECTING PROBLEM AREAS:

- the existence of a distinct target group,
- availability of data and indicators describing the area,
- availability of data regarding the effectiveness and impact of earlier interventions,
- public financing for the area or significant public expenditure to address the problem,
- availability of a potentially better and more influential intervention,

- the existence of capable third-sector organization(s) able to provide an intervention,
- motivation on the part of the state and possession resources to implement a better solution,
- high likelihood of cost savings by a successful intervention for the state,
- the significance of the area and its attractiveness for investors.

The problem analysis consisted of desk-top study, based on a thorough list of existing research material on the identified social issues, including reports commissioned and undertaken by government agencies, academic research and public databases.

In order to clarify specific questions and for updating information, requests for obtaining further data were sent to agencies that are responsible for collecting the data. Several interviews were made with specialists working on the issues, and regular dialogue was established with key specialists in government institutions, relevant to the shortlisted issues.

## 4.2 OUTCOME

After consulting with officials and specialists and analyzing the issues raised, three potentially suitable problem areas were established – juvenile delinquency, domestic violence and mistreatment of newborns (parental misbehaviour). After the assessment against established criteria, the decreasing of juvenile delinquency was selected as the most suitable area for Estonia's first social impact bonds project.

According to estimates, juvenile offenders constitute approximately 1-2% of each youth age group. Estonia applies various intervention to juvenile offenders, including community work, rehabilitation services, a variety of social programs or specialized classes. For the more complicated target group, schools for juvenile delinquents have been created. Nevertheless, almost 1,500 minors appear in front of juvenile misconduct committees each year, half of whom are repeat offenders. A majority (81%) of youth discharged from specialized schools commit another offence within two years.<sup>16</sup>

The indicators describing the field are gathered on the national level and can be used to create performance indicators (e.g. number of repeat offences and youth recidivism) and measure the effectiveness of different intervention models (recidivism rates among juvenile offenders released from prison, recidivism rates among youth discharged from specialized schools).

---

<sup>16</sup> Riigikontroll (2010). *Erikoolide ja alaealiste komisjonide järelaudit*. <http://www.riigikontroll.ee/DesktopModules/DigiDetail/FileDownloader.aspx?FileId=11171&AuditId=2163> (01.06.2015)

Intervention programs for juvenile offenders involve significant public expenditures related to financing the work of juvenile misconduct committees, schools for juvenile delinquents and rehabilitation programs. The cost of investigation and legal proceedings is also significant.

Because of the costliness of the problem the state is actively interested in and ready to apply more effective interventions.

The full report by the Praxis Centre for Policy Studies on possible problem areas for social impact bonds (“Ühiskondliku mõju osakute võimalike probleemvaldkondade analüüs”) is available at [www.sib.ee](http://www.sib.ee).

### 4.3 CHALLENGES AND LESSONS LEARNED

#### **AVAILABILITY OF DATA REQUIRED FOR THE SELECTION OF A PROBLEM AREA**

One of the main challenges in mapping the problem area was related to the availability of the data. This means that data is either unavailable or that information on the single target is gathered by different agencies using different methods. Another problem is that systematic performance evaluation of services is not yet applied in Estonia. This makes analysis complicated and time-consuming as it requires manual processing of the data provided by different agencies.

#### **IMPLEMENTATION OF THE MODEL IN A FIELD THAT FALLS IN THE AREA OF RESPONSIBILITY OF MULTIPLE STATE ACTORS**

One of the first steps should be the mapping of all stake-holders associated with the specific problem. In order to get a full overview of the field, its status quo and main problems, including only one main partner is not enough. It is important to understand which agency deals with which aspect of the problem. Detailed play field mapping in the early stages of the project enables for more smooth communication in later stages. Also, early inclusion of the state helps to prevent situations where the chosen problem is not a priority for the government at the time or the administrations responsible for the social issue do not have the capacity to take on new projects.

## 5. MAPPING AND SELECTION OF INTERVENTIONS

An intervention applied in the framework of a social impact bonds must be more effective than previously used solutions. This requires knowledge of how the model works, how well it works and how can it be adapted and implemented.<sup>17</sup> The choice of intervention is influenced by a number of factors such as measurability of results, whether the intervention is evidence-based, availability of potential service providers and the cost and time frame of the intervention. Importantly, a successful intervention should create cost savings for the state in the near future. An intervention may be rather simple (single activity) or very complex (comprehensive approach involving many different activities), depending on objectives and the model being applied.

### 5.1 APPROACH

Estonian Social Enterprise Network mapped the possible interventions for the social impact bond program. As a major input for intervention analysis, the Praxis Centre for Policy Studies had previously prepared an analysis of problem areas. Existing international surveys and reports of different intervention programs were analyzed to establish an effective method for influencing the target group of juvenile offenders. Information was also gathered from agencies, organization and service providers active in the selected problem area in Estonia. The capability of service providers was analyzed separately.

#### THE FOLLOWING CRITERIA WERE USED IN SELECTING THE INTERVENTION PROGRAM:

- maximum duration of the program is 2–3 years;
- maximum cost of the intervention is around €200,000;
- the intervention is consistent with the new Estonian child welfare policy;
- availability of impact measurement methods and their feasibility;
- availability and capability of service providers;
- future cost savings for the state as a result of a successful implementation of the program.

17 Bridges Ventures (Oktoober 2014). Choosing Social Impact Bonds: A Practitioner's Guide. <http://www.bridgesventures.com/wp-content/uploads/2014/12/SIB-report-DPS.pdf> (01.06.2015)

The limited duration of the program was set due to the state’s budget policy according to which the state can take on obligations for up to four years. This means that the period should accommodate the implementation of the intervention as well as the performance evaluation required for reimbursement. On the other hand, this approach was also supported by early feedback from potential investors who recommended to test the first projects on a smaller scale.

## 5.2 OUTCOME

By engaging specialists and officials and analyzing the established criteria, the choice was narrowed to two potential programs: ART (Aggression Replacement Training) and MultifunC (Multifunctional Treatment in Residential and Community Settings). Interested parties existed for both ART and MultifunC. Both programs were also generally consistent with the selection criteria listed above.

### MODEL OF ART’s LOGIC

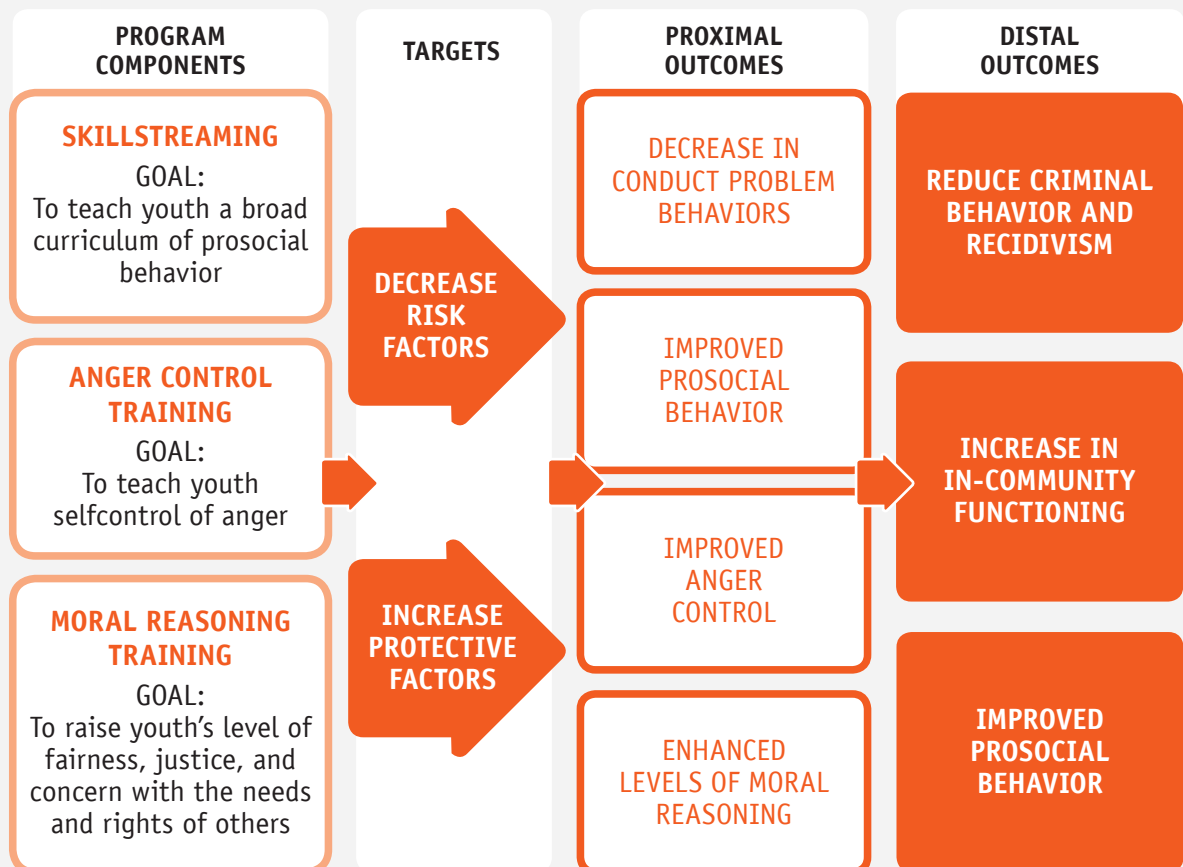


Figure 5. Model of ART’s logic.<sup>18</sup>

18 EPISCenter. ART Logic Model. [http://www.episcenter.psu.edu/sites/default/files/ebp/ART\\_Logic\\_Model.pdf](http://www.episcenter.psu.edu/sites/default/files/ebp/ART_Logic_Model.pdf) (01.06.2015)

Based on mapping results, ART was chosen as the most suitable intervention for the first model. ART is a cognitive-behavioral intervention program for training social skills such as empathy, anger management and problem-solving, and supports the making of ethical decisions. The main target group for ART are children and youth, but the program has been successfully applied to adults as well. The program is based on group exercises conducted by two trainers. Practical training of the above skills takes place during 10 consecutive weeks, 3 hours per week. In international practice, a suitable size for the group is 6-10, depending on the background of the participants.

In the United States, ART is one of the evidence-based programs which has resulted in measurably lower recidivism among youth participants. A 2004 study by the Washington State Institute for Public Policy showed a 24% decrease in repeat offences during the 18 months after the program.<sup>19</sup> The cost-benefit analysis of the program indicated that each dollar invested in the program saved the state an average of 6–11 dollars, considering the state's expenditure forecast without the program.

A knowledge-based version of the program, developed further by Norwegian specialists, has been applied in Europe and Russia. In those countries, surveys have focused on direct impact assessment, i.e. measuring changes in the youth's attitudes, skills and behavior patterns after completing the program. It should be noted that different organizations have used different questionnaires and protocols to measure the same aspects, i.e. the program has no single impact assessment protocol, which has to be developed for Estonia by using available Estonian-language questionnaires and models.

In conclusion, implementation of the ART program is compatible with the time constraints – given the short duration of the intervention – and financially feasible as the Norwegian version is not subject to license fees and the main expenditure would be the cost of training ART trainers. The ministry and officials responsible for the field have strong motivation to test the model as it complies with the updated Estonian child welfare strategy and the program is evidence/knowledge-based. Furthermore, implementation of the ART program is one of the prerequisites for future implementation of the MultifunC programme.

A survey of potential service providers indicated that strong service providers have notable experience from working with the target group and conducting similar programs and are interested in program implementation. For more information on service providers, see Section 6.

---

<sup>19</sup> Washington State Institute for Public Policy (Jan 2004). Outcome evaluation of Washington State's research-based programs for juvenile offenders. [http://www.wsipp.wa.gov/ReportFile/852/Wsipp\\_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders\\_Full-Report.pdf](http://www.wsipp.wa.gov/ReportFile/852/Wsipp_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders_Full-Report.pdf) (01.06.2015)



## 5.3 CHALLENGES AND LESSONS LEARNED

### **PREFERENCE FOR EVIDENCE-BASED PROGRAMS IN ESTONIA**

In the case of international social impact bond projects, third sector organizations have often developed novel programs by themselves, engaging various parties and different service providers. In Estonia, the state currently has strong preference for evidence-based programs with proven effectiveness. This results in limited flexibility the program must be implemented according to established protocols in order to obtain results. It also results in potentially higher set-up costs related to purchasing licenses, translating program manuals and importing program-related knowledge.

The Scandinavian version of ART is a knowledge-based program that can be imported at a lower cost, but as the program does not include a uniform impact assessment method, the cost of its development must be added.

### **ENSURING THE QUALITY AND SUSTAINABILITY OF THE INTERVENTION PILOTED THROUGH THE SIB PROGRAMME**

In case where interventions based on the ART-method are critical for the Estonian state in the long term and the effectiveness of the ART-trainers increases over time, then the state should consider opportunities for continuing with the intervention after the SIB programme. This is critical develop the skills and competencies of the ART-trainers. Furthermore, the Norwegian experts stressed the need to create a local center of competence that would train new ART trainers and provide supervision and master trainer training for existing trainers.

## 6. MAPPING OF SERVICE PROVIDERS

A vital necessity for implementing social impact bonds is the existence of capable NGOs that can provide a new intervention in high quality. For service providers, the implementation of social impact bonds means a possibility for launching novel solutions and demonstrating their capability to the state. To obtain an overview of existing service providers, the Estonian Social Enterprise Network analyzed organizations that had previous contacts with the target group and were providing services similar to the ART program.

Mapping was based on evaluation criteria developed for service providers and followed by an analysis of the capability of organizations which had conducted programs among at-risk youth in recent years.

### 6.1 APPROACH

The objective of the mapping of service providers was to find capable organizations with the interest and potential to implement evidence-based intervention programs for juvenile offenders. A desktop survey was conducted to find organizations that have previous experience and have lead large scale projects with juvenile delinquents. Information was gathered from networks, experts, previous studies and the web. In the second phase, selected organizations were contacted and interviews with their representatives were held.

#### CRITERIA USED FOR MAPPING SERVICE PROVIDERS:

- **Management capability** – motivated managers who base their activities on the organization's strategy,
- **Financial capability** – the budget size, systematic financial planning and no history of overdue liabilities,
- **Operational capability** – the organization is reliable and sustainable, has consistently offered services to the target group and has conducted large scale projects,
- **Social impact** – the organization is involved with an important social problem and its activity has impact.

## 6.2 OUTCOME

Ten potential service providers were found as a result of the desktop survey. All organizations are financially viable, have sufficient staff and have regularly and consistently carried out large-scale programs targeted at juvenile offenders in recent years. On the basis of further analysis, four of the ten potential service providers were selected for interviews, one of whom declined the interview due to ongoing large-scale projects.

The aim of the interviews was to gather additional information for assessing the capability of service providers and validate the information obtained from the secondary sources. The interviews also served to introduce the objectives and activities of social impact bonds to potential service providers and to check whether they are interested in participating in the model.

As a result, all three interviewed organizations proved to have sufficient long-term experience in working with juvenile offenders in accordance with the established criteria. According to the results, Estonian NGOs are competent in the area and interested in implementing the evidence-based ART program and participating in the social impact bond model.

## 6.3 CHALLENGES AND LESSONS LEARNED

### **SIMULTANEOUS APPLICATION OF SEVERAL EU-FUNDED PROGRAMS AND A LIMITED SCOPE OF THE SECTOR IN ESTONIA**

Analysis done by the Estonian Estonian Social Enterprise Network established four eligible service providers, one of whom declined due to ongoing large-scale commitments. Although the list of potential service providers is not final, finding capable service providers and excellent trainers could be problematic in a situation where several programs are launched and extended simultaneously. Therefore the timing of the launch of the social impact bonds as well as a good relationship with the service providers are essential.

### **LIMITED EXPERIENCE WITH IMPLEMENTING EVIDENCE-BASED INTERVENTIONS**

Estonian organizations have only limited experience with implementing evidence-based interventions and impact assessment. Many organizations use story-telling to describe the impact of their activities, but actual impact is not systematically measured.

For this reason, the role of the mediator of social impact bond model increases. The task of the mediator should also be to engage a research organization and improve service providers' capabilities (including measuring impact).

## 7. MAPPING OF INVESTORS

The European Venture Philanthropy Association (EVPA) is an umbrella organization for foundations that invest into social enterprises to achieve double profits - social impact and financial revenue. According to EVPA the sector has attracted 5 billion euros in investments since it came into being.<sup>20</sup> In the global arena, these investors include charity and/or impact investment funds, state-controlled funds, private persons and institutional investors. The range of investors is the same for social impact bonds.

Family offices hold a prominent place on the global level, but the personal wealth of Estonian philanthropists is smaller compared to those in Western Europe or North America. Therefore, Estonia lacks the infrastructure of local foundations to build upon. Wealthier individuals decide their philanthropic investments case-by-case and, in Good Deed Foundation's experience, the investments usually remain below 20,000 euros.

Meanwhile, the number of companies wishing to move beyond simple sponsorships or visibility measures and contribute to solving social issues has grown in recent years. The scale of their investments is similar to that of philanthropists' investments.

Today, the main organization investing in NGOs in Estonia is the state-funded National Foundation for Civil Society, established in 2008. In 2014, they published several calls for proposals and invested a total of 2.7 million euros in NGOs.<sup>21</sup>

### 7.1 APPROACH

To test the readiness of investors, the Good Deed Foundation first approached the active philanthropists and organizations who invest in social change. At the same time, GDF met with different financial investors, venture capital investors, and umbrella organizations (Finance Estonia, Estonian Business Angels Network), fully or partly state-owned foundations (National Foundation for Civil Society, SmartCap), the Responsible Business Forum in Estonia and their members and people and organizations recommended during earlier meetings. In all, about 50 organizations and private persons were approached during the analysis to discuss impact investing and social impact bond programme.

<sup>20</sup> European Venture Philanthropy Association (Dec 2014). European Venture Philanthropy and Social Investment 2013/2014 | The EVPA Survey <http://evpa.eu.com/publication/european-venture-philanthropy-and-social-investment-20132014-the-evpa-survey/> (01.06.2014)

<sup>21</sup> Kodanikuühiskonna Sihtkapital. SA Kodanikuühiskonna Sihtkapitali majandusaasta aruanne 2014. [kysk.ee/failid/Upload/files/aastaruanded/SA\\_Kodanikuühiskonna\\_Sihtkapitali\\_majandusaasta\\_aruanne\\_2014.pdf](http://kysk.ee/failid/Upload/files/aastaruanded/SA_Kodanikuühiskonna_Sihtkapitali_majandusaasta_aruanne_2014.pdf) (01.06.2014)

## 7.2 OUTCOME

Investors expect the model, during the first years at least, to be a new philanthropic tool which is attractive mostly due to the fact that the investment can later be recovered and reused.

Social impact bonds are not considered a regular investment as the risk level of the investment is very difficult to determine. The investment area and the parties involved are new to most investors. Also the success and future payouts depend on the effectiveness of parties and the adherence to the agreements. As the yield does not compensate for the risk it is not the deciding factor in favor of making the investment. The investors stressed that the first social impact bonds would benefit from some level of state guarantees to the initial investment.

Investors will see the model as a potential financial investment when several bond projects have already been launched and there is a track record of successful projects available.

In June 2015, four private persons and organizations confirmed their interest in investing in SIBs. Number private persons and organizations who are ready to continue discussions after the first public procurement for contracting services under the social impact bond model has been announced. On the basis of existing agreements and meetings, we are certain that conditions for impact investment are favorable in Estonia and the likely first investors are corporations and persons who have already invested or contributed towards social change by other means.

## 7.3 CHALLENGES AND LESSONS LEARNED

### **LOW INVESTMENT VOLUMES AND LACK OF CHARITY FOUNDATIONS INFRASTRUCTURE**

After consulting with investors and their representatives a conclusion was reached that the duration of the first projects should rather be shorter time-wise and the total investment in the project should stay around 200 000 euros. Low investment volumes and the lack of supporting infrastructure of foundations might become a limiting factor for engaging in larger long-term projects. A continuous dialogue with the investors should be maintained to raise the awareness on impact investing further.

### **HIGH RISK AWARENESS OF INVESTORS**

Social impact bonds are a new and innovative financial instrument that involves several parties from different sectors, who have had no previous cooperation in investing into social change. Investors have difficulties assessing the risks involved and thus they rate the risks high. It is important for the investors to see that the project will be carried out by a capable team and the payout is based on solid agreements with the state. Therefore it is important to create trust between the parties involved and discuss the readiness of the state to guarantee a proportion of the investment in the first SIB projects.

## 8. IMPACT FRAMEWORK

A number of factors are to be taken into account when developing the impact framework. The project's goals and assessment indicators should be objective, transparent, measurable and clearly understandable for all parties. This requires attaching a numerical value to each goal, including clear definition of the target group, establishing primary indicators, mapping of the state's costs relating to the target group and agreeing upon the expected target level. To establish specific indicators, it is important to determine the results that are achievable, which the investors are willing to invest in and which the state is willing to reimburse in the case of success. A reasonable balance between the aforementioned aspects is necessary for the setting of the final result indicators.

Results and impact can only be assessed within a specific time-frame and in comparison with existing data.<sup>22</sup> The impact of the specific intervention and the influence of external factors must be clearly distinguished during evaluation. It is also important to establish the likely course of development without the intervention.

Controlled measurement instruments and methods (data gathering logic, description of the measuring process and research plan) are critical, as well as access to personal data in the state's databases and finding a competent research institution/independent evaluator.

### 8.1 APPROACH

Research on the impact framework of the ART program was conducted by the Estonian Social Enterprise Network. Description of the impact framework is based on problem area mapping, desk research of international impact surveys and interviews with Estonian and Norwegian experts.

### 8.2 OUTCOME

In the United States, ART is one of the evidence-based programs which have resulted in measurably lower recidivism among youth participants. A 2004 study by the Washington State Institute for Public Policy showed a 24% decrease of repeat offences during the 18 months after the program.<sup>23</sup> The updated ART methodology, developed in Norway, is a new knowledge-based program used in Scandinavia. As the program has been used for a shorter

<sup>22</sup> UK Cabinet Office: Centre for Social Impact Bonds (April 2013). A measurable outcome. [http://data.gov.uk/sib\\_knowledge\\_box/measurable-outcome](http://data.gov.uk/sib_knowledge_box/measurable-outcome) (01.06.2015)

<sup>23</sup> Washington State Institute for Public Policy (Jan 2004). Outcome evaluation of Washington State's research-based programs for juvenile offenders. [http://www.wsipp.wa.gov/ReportFile/852/Wsipp\\_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders\\_Full-Report.pdf](http://www.wsipp.wa.gov/ReportFile/852/Wsipp_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders_Full-Report.pdf) (01.06.2015)

period of time than in the US than evidence-based surveys have not yet been conducted. The current surveys of the updated methodology have focused on direct impact assessment, i.e. measuring changes in attitudes, skills and behavior patterns after completing the program.

**An analysis of impact surveys of ART programs indicated that different countries have used different methods to assess the program's impact:**

1. Effectiveness of the program according to the participants' own assessment. Those surveys are based on questionnaires concerning the participants' behavior and attitudes before and after the program. Impact and effectiveness are measured on the basis of participants' answers.
2. Effectiveness according to the participants' and third parties' evaluation of change. Such surveys involve the participants as well as their parents and/or teachers.
3. Reduction of recidivism. Official statistics on offences are reviewed 12/18/24 months after the completion of the program.

According to the survey, the same criteria were measured using different models developed by the implementer and/or researcher in accordance with the needs of the specific program. Program enrolment criteria, the parties involved in direct impact assessment and methods, and assessment of recidivism rates have differed case by case. This means that Estonia needs to create its own evaluation model and protocol and engage a research institution to conduct the evaluation.

After consulting with specialists and state experts, it was concluded that the social impact bond model would be best served by a combined performance indicator covering both the assessment of social skills immediately before and after the program as well as an analysis of registered offences during the 18 months after the program. A reference group should be established to eliminate the impact of external factors.

In general principle the implementation of the SIB model requires the selection of goals that would lead to a reduction of public sector costs. To this end, it is important to monitor repeat offences by juvenile offenders participating in the program, as those give rise to investigation, proceedings and other costs. Committed offences and changes in patterns can be analyzed on the basis of information from state databases.

Evaluation of social skills offers an additional picture of the program's impact and has globally been the main method for assessing the program's effectiveness. Various methods have been employed to evaluate social skills. With regard to the existing Estonian-language questionnaires, Norwegian experts recommended the use of SDQs Strengths and Difficul-



ties Questionnaire, containing questions for the youth, the teacher and the parent, thus enabling researchers to obtain both the participant's and the other parties' assessment of changes in behavior and attitudes. Furthermore, this assessment method has already been tested by the National Institute for Health Development during the 2014–2015 pilot year of the Good Behavior Game Program.

### 8.3 CHALLENGES AND LESSONS LEARNED

#### CREATING A DETAILED MODEL OF IMPACT

In a situation in which Estonia has limited experience with developing evidence-based models and there is a lack of impact measurement experts, creating a detailed impact model with research methodology and protocol is a challenge. It is important to establish contacts with universities and state institutions who are familiar with the research methodology and also interested in engaging in the field of impact assessment. To ensure the quality of the impact model it is necessary to create a task-force and engage existing experts as advisers to help ensure the quality of the research methodology.

#### ESTABLISHING TARGET LEVELS FOR REDUCTION OF RECIDIVISM

In a situation where the ART program has not yet been launched and the effectiveness of programs similar to ART have not been previously measured in Estonia it is difficult to set target levels. It is especially difficult in regards to decrease in recidivism since there are a very few evaluations done in that field in the world. The evaluation methods used are more often used to measure the increase of psycho-social skills, not changes in the criminal behavior. It is important to set conservative goals and to use combined result indicators which are comprised of change in recidivism and other changes in psychosocial skills compared to the control group.

#### THE COST OF IMPACT MEASUREMENT

Performance analysis might become rather costly as the measurement methods are resource-consuming and might therefore increase the investment needs. It is important to consider possibilities of cooperation with other state agencies and specialists. It is important in regards to the projects sustainability. In order to pre-evaluate and invite participants to the program cooperation with organizations and specialists already involved with the target group (e.g. Social Insurance Board, the police, hospices, special schools) should be established.

## 9. FINANCIAL FRAMEWORK

The logic of social impact bonds requires the contracting party to pay for the service if the novel intervention has been proven more effective than the service previously provided by the state itself and has created costs savings for the state. Financial analysis and a working business model are therefore critical for successful implementation of the bonds.

### TO PERFORM FINANCIAL ANALYSIS, WE ESTABLISHED:

- the state's current costs relating to the problem and target group;
- the expected effect of the intervention;
- the cost of implementing the intervention (including impact assessment and support for organizational capacity);
- the expected rate of return for investors.

To conduct the financial analysis it is important to map and analyze the state's current expenditures relating to the problem area and assess future expenditures in the case of no intervention. Then assess the intervention's impact on future costs and calculate potential savings resulting from the impact.

### STATE SAVINGS ON IMPLEMENTING THE SOCIAL IMPACT BONDS

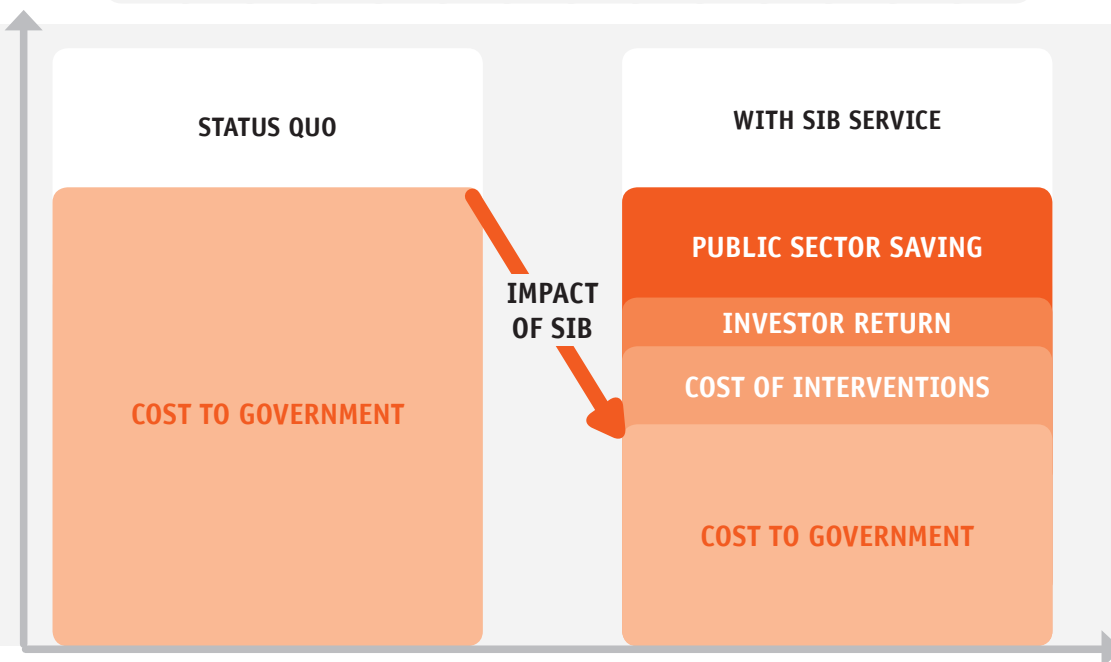


Figure 6. State savings on implementing the social impact bonds.<sup>24</sup>

<sup>24</sup> Mars Centre For Impact Investing (Nov 2013). Social Impact Bond Technical Guide for Service Providers. [http://www.marsdd.com/wp-content/uploads/2013/11/MAR-SIB6939\\_\\_Social-Impact-Bond-Technical-Guide-for-Service-Providers\\_FINAL-ELECTRONIC1.pdf](http://www.marsdd.com/wp-content/uploads/2013/11/MAR-SIB6939__Social-Impact-Bond-Technical-Guide-for-Service-Providers_FINAL-ELECTRONIC1.pdf). (01.06.2015)

According to the logic of the model, the savings created can be channeled towards reimbursement of the initial capital contributed by the investors (i.e. the cost of the intervention), a risk premium (interest on the initial investment) and, subject to agreement, a bonus to service providers and/or intermediaries for achieving the results. The remaining amount will be recorded as savings in the state budget. In this context, it is important for the parties to negotiate the terms for reimbursing the investment with interest and the period of reimbursement.

## 9.1 APPROACH

Financial analysis of the model for reducing juvenile offences through the ART program was conducted by PricewaterhouseCoopers, with help from the Praxis Centre for Policy Studies to map the state's expenditure.

The aim of the analysis was to establish the state's cost base relating to juvenile offences and analyze possible cost savings created for the state and taxpayers by the ART program. Initial data and information for the analysis was gathered from public sources, earlier surveys and by enquiries to institutions related to the field. Input from different parties who participated in earlier meetings (including the opinions of representatives of ministries, Norwegian experts and investors) was also taken into account.

The analysis was based only on direct costs relating to offences during a period of 12/18 months. It did not account for the long-term costs/benefits of (not) returning the offender to the proper path. In the worst-case scenario, the youth commits one or two offences per year, ends up in a specialized school and subsequently in an adult prison, is unable to find work after release and continues in a vicious circle. In a situation where the young offender is prevented from entering the vicious circle he or she starts to generate tax revenue after entering the job market.

## 9.2 OUTCOME

Mapping of the state's direct costs indicated that the state's costs relating to juvenile offenders were about 13.7 million euros per year, most of which relates to registering and investigating the offence and damage caused to the victim.

## STATE'S COSTS RELATING TO JUVENILE OFFENDERS

DESCRIPTION	COSTS
Cost of registering and investigating the offences	6,4 mln EUR
Cost of juvenile offenders in specialized school	1,6 mln EUR
Cost of juvenile offenders in prison	0,5 mln EUR
Cost of proceedings (prosecutor)	0,2 mln EUR
Damage to victims (property)	3,3 mln EUR
Damage to victims (lost income)	1,4 mln EUR
Other costs	0,3 mln EUR
<b>Total costs</b>	<b>13,70 mln EUR</b>

Table 7. State's costs relating to juvenile offenders.<sup>25</sup>

According to a U.S. study on the feasibility of an ART program, repeat offences by participants decreased by 24% during 18 months after the program and each dollar invested in the program saved the state an average of 6–11 dollars.

In Estonia, the feasibility study conducted by PwC showed that if the rate of offences among ART participants would decrease by 22% during the 12 months after the program or 16% for 18 months after the program, the state's costs and benefits would be in balance. If those numbers could be exceeded, the state would achieve further savings. As the current analysis only accounts for direct costs, it is likely that scenarios with lower offence reduction rates as a result of the ART program would also be beneficial for the state in the long run.

Calculations are based on the assumption that the program will be carried out in one year during which 128 young people will complete the program; the entire cost of the intervention is around 200 000 euros and the expected return for the investors is 5%.

<sup>25</sup> PwC (2015). Ühiskondliku mõju osakute tasuvusarvutused.

## 9.3 CHALLENGES AND LESSONS LEARNED

### **INCONSISTENCY AND UNAVAILABILITY OF DATA**

Similarly to the mapping of the problem area the collecting of data was challenging due to the discordance in their availability. The analysis was based on different sources – this included prior studies, national databases, agency based knowledge and expertise. Regardless, it was necessary to rely on numerous assumptions due to the limited availability of the data.

### **ASSESSING AND PRICING THE ADDED VALUE CREATED FOR THE STATE**

As a result of the development and implementation of the SIB model, the state acquires a considerably better overview of the problem area and the need to gather specific data (including quantified costs and impact assessment) which the state would probably not have gathered itself at such scale. As a result of detailed impact and effectiveness measurement during the pilot project, the state will hopefully begin to conduct a similar measurements and implement the same principles in financing other problem areas.

### **LONG-TERM FINANCING AND SCALING OF THE PROGRAM AFTER SIB**

An ART program covering 128 persons of a target group of around 1400 (i.e. 9%) does have a limited reach. If the same program were later to be applied to the whole population, the anticipated impact and effect would be much higher due to the elimination of one-off expenditures. Therefore it is important to consider and discuss with the government the programs scalability and sustainability after the SIB project.

## 10. LEGAL FRAMEWORK

The structure and framework of social impact bonds largely depends on the laws of the state concerned, as well as the needs and preferences of participants of the specific project.

In international practice, three main structures have been employed for social impact bonds. Twenty-five per cent (25%) of all projects use the “project leader model” in which one party assumes leadership (and responsibility for ensuring effectiveness), raises investment capital and concludes agreements with all parties. This structure also enables “sub-contracting” of services from several providers. In 33% of the cases, representatives of the public sector, investors and service providers conclude a trilateral agreement without intermediaries, leaving the service provider solely responsible for ensuring effectiveness. In 42% of cases, investors founded a special purpose vehicle (SPV) to implement a project, which then concludes an agreement with the service provider and the party responsible for effectiveness.<sup>26</sup>

### 10.1 APPROACH

Developing the legal framework involved consulting specialists from various areas, including tax law, business law, state budget, public procurement and investments. Possible legal frameworks were mapped on this basis and a round table was held to analyze the mapped structures. On the basis of input from meetings, and having regard to potential investors’ preferences, Borenius Law Firm prepared a comprehensive analysis of the Estonian model.

### 10.2 OUTCOME

To launch the first social impact bond model project in Estonia, the state needs to announce a public procurement and conclude a performance-based agreement with the successful bidder. Because the state budget strategy does not allow ministries to assume responsibilities beyond the ongoing four-year period, the duration of any procurement contract may not exceed four years.

In view of the Estonian context and the readiness of the parties, an SPV would be optimal for submitting a tender at the public procurement. As a legal entity, this SPV would be a non-profit organization established to act as an intermediary in the project, connect the other parties of the project, conclude the contracts needed to implement the project and act as a project manager and coordinator.

---

<sup>26</sup> Bridges Ventures (Oct 2014). Choosing Social Impact Bonds: A Practitioner’s Guide. <http://www.bridgesventures.com/wp-content/uploads/2014/12/SIB-report-DPS.pdf> (01.06.2015)

The state will sign a contract with the intermediary that will be selected through the public procurement process. To carry out the project, the intermediary would then conclude:

- a) loan agreements with investors providing initial investment for the project,
- b) contracts with the service provider(s) who would carry out the agreed-upon intervention,
- c) jointly with the state, an agreement with an independent evaluator to assess whether the agreed-upon results have been achieved and the prerequisites for the reimbursement have been fulfilled.

### LEGAL STRUCTURE OF SOCIAL IMPACT BONDS

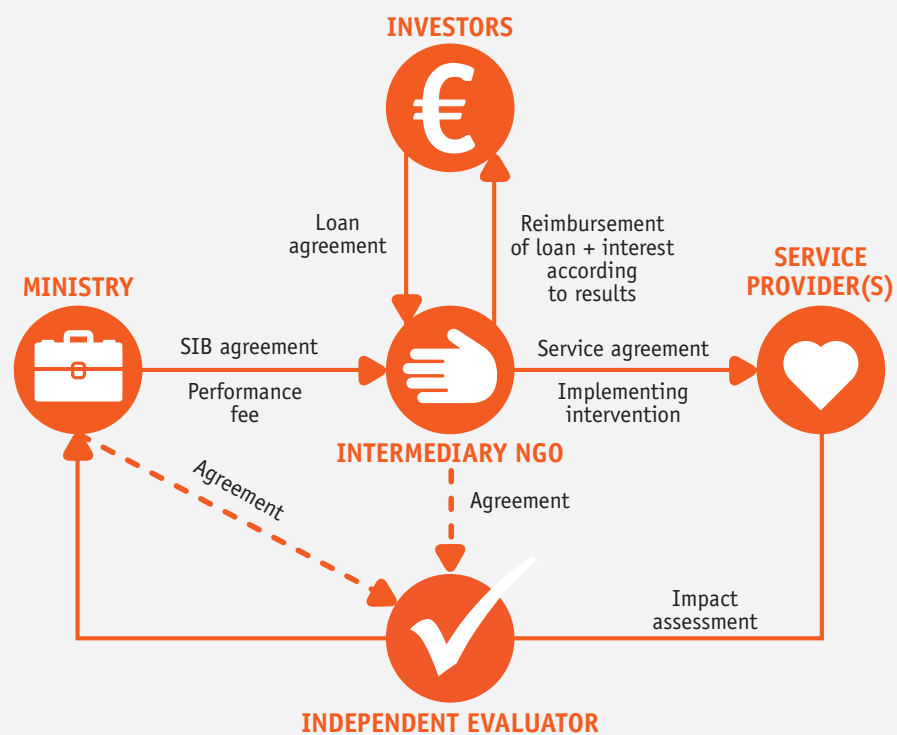


Figure 8. Legal structure of social impact bonds

The choice of financing method depends on the specific social impact bond model (including the legal form of the recipient) and investors' preferences (including the level of active engagement of the investors in the SIB project). Private sector financing will be involved in the form of loans, as this was deemed most suitable in the given framework. Depending on the structure of future projects and the participants' preferences, financing may also take the form of convertible loans, convertible bonds, options or holdings.

### 10.3 CHALLENGES AND LESSONS LEARNED

#### **LIMITATIONS OF THE STATE BUDGETARY POLICY**

The limited duration of the program was set due to the state's budget policy according to which the state can take on obligations for four upcoming years which might become a limiting factor in upcoming larger and more long-term projects. It is important to start discussions on opportunities to create supporting legislation for the social impact bond model.

#### **LEGAL FRAMEWORK FOR THE MODEL SHOULD BE DEVELOPED AT THE STARTING PHASE OF THE PROJECT**

Development of the project's legal framework was initially planned for a later phase, but senior officials voiced concerns about the possibility of implementing the model according to Estonian law already at the very first meetings. As a result, input from the representatives of the Ministry of Finance and lawyers was sought during the initial phase of the project. Both parties ensured that SIB model is feasible, but needs further analysis.

Thorough analysis indicated that a public procurement is needed to launch the bonds. Announcing a new procurement requires thorough preparation on behalf of the interested state agencies which in the context of Estonia might take roughly a year starting from the finalization of the implementation study.

Good Deed's experience showed that complex issues relating to different parties might be encountered during preparation of the framework and a long time may be needed to solve these issues. Legal issues should therefore be resolved at the early stages of a project, by engaging experts from various fields. Once the terms of reference have been established, it is vital to find a dedicated legal advisor.



## SUMMARY

In 2014, the Good Deed Foundation in cooperation with the Estonian Social Enterprise Network and the Praxis Centre for Policy Studies initiated a feasibility study and cost-benefit assessment for launching Estonia's first social impact bond model initiative. The year-long project involved mapping the readiness of Estonia's public sector, investors and NGOs to implement the novel financing model and preparing the impact, financial and legal framework for the first model.

Good Deed Foundation's and its partners have learned a lot during the process. The project team's experience showed that as the creation of the model's framework requires knowledge of various fields (including financial and legal expertise, knowledge of evaluation of evidence-based programmes and impact assessment), it is vital to compose a team of experts and professionals for involvement in different phases of the project. It is also important to involve opinion leaders of different sectors to introduce and explain the issue in their communities. This increases the credibility of the project and facilitates the engagement of new partners.

The project revealed close interconnections between different activities, which require working with various issues in parallel and could prove a challenge in terms of project management. For example, final selection of a problem area required a broad understanding of the whole ecosystem surrounding a model, including an overview of service providers active in the area and their capabilities, the state's current expenditure and the cost of the new intervention. Furthermore, the public sector and the potential contracting entity should be strongly motivated by the selected issue. It is therefore important to involve responsible state agencies at an early stage of the project and ensure the interest of high officials in order to ensure their readiness to work towards novel intervention and financing models.

In the longer term, scalability of the bonds requires further analysis of market obstacles and possibilities of overcoming them from the perspective of different parties. Today, the state can assume obligations for up to four consecutive fiscal years, which could limit the implementation of longer-term and larger-scale projects. As investors' awareness of impact investment is currently rather low, the launching of new projects would require active communication and dialogue in that area. As for service providers, the capability for implementing evidence-based practices should be improved. It is also necessary to create a line-up of organizations able to assume the role of intermediary and coordinator in the development of future projects.

In conclusion, the year-long preparatory project showed that the Estonian state, investors and NGOs are ready for testing social impact bonds as a novel performance-based financing model. In cooperation with the experts from various fields, a framework has been created for implementing a pilot project. The feasibility study and cost-benefit assessment provide a strong base for launching the first social impact bonds project in Estonia, but the actual launch requires further efforts by all interested parties.

**We thank all partners, supporters and contributors for assistance on this journey. Good Deed Foundation will continue work towards launching the first Social Impact Bond in Estonia in 2016.**

## REFERENCES

Bridges Ventures and Bank of America Merrill Lynch (2014). Choosing Social Impact Bonds: A Practitioner's Guide. <http://www.bridgesventures.com/wp-content/uploads/2014/12/SIB-report-DPS.pdf> pp. 6 (01.06.2015)

Eesti Konjunktuurinstituut (2015). Konjunktuur, nr 1 (192), pp. 7. [https://www.mkm.ee/sites/default/files/konjunktuur\\_nr\\_1\\_192\\_marts\\_2015.pdf](https://www.mkm.ee/sites/default/files/konjunktuur_nr_1_192_marts_2015.pdf) (01.06.2015)

Eesti Pank (2015). Eesti majanduse aastanäitajad. <http://statistika.eestipank.ee/?lng=et#treeMenu/MAJANDUSKOOND> (01.06.2015)

European Parliament Think Thank. Davies, R. (August 2014). Social impact bonds: Private finance that generates social returns. [http://www.europarl.europa.eu/thinktank/en/document.html?reference=EPRS\\_BRI\(2014\)538223](http://www.europarl.europa.eu/thinktank/en/document.html?reference=EPRS_BRI(2014)538223) pp. 1 (01.06.2015)

European Venture Philanthropy Association (December 2014). European Venture Philanthropy and Social Investment 2013/2014 | The EVPA Survey <http://evpa.eu.com/publication/european-venture-philanthropy-and-social-investment-20132014-the-evpa-survey/> (01.06.2014)

Kodanikuühiskonna Sihtkapital. SA Kodanikuühiskonna Sihtkapitali majandusaasta aruanne 2014. [kysk.ee/failid/Upload/files/aastaruanded/SA\\_Kodanikuuhiskonna\\_Sihtkapitali\\_majandusaasta\\_aruanne\\_2014.pdf](http://kysk.ee/failid/Upload/files/aastaruanded/SA_Kodanikuuhiskonna_Sihtkapitali_majandusaasta_aruanne_2014.pdf) (01.06.2014)

Kübar, U., Rammo, A. (2014). 23 küsimust Eesti vabakonna kohta ja vastused, nii hästi, kui neid leida oskasime. Hea Kodanik, nr 5 (63), pp. 21-28. [http://issuu.com/emsl/docs/hea\\_kodanik\\_talv\\_2014](http://issuu.com/emsl/docs/hea_kodanik_talv_2014) (01.06.2015)

Majandus- ja Kommunikatsiooniministeerium (2015). Majandusanalüüs. <https://www.mkm.ee/et/tegevused-eesmargid/majandusareng-ja-ettevotlus/majandusanaluus> (01.06.2015)

Mars Centre For Impact Investing (November 2013). Social Impact Bond Technical Guide for Service Providers. [http://www.marsdd.com/wp-content/uploads/2013/11/MAR-SIB6939\\_\\_Social-Impact-Bond-Technical-Guide-for-Service-Providers\\_FINAL-ELECTRONIC1.pdf](http://www.marsdd.com/wp-content/uploads/2013/11/MAR-SIB6939__Social-Impact-Bond-Technical-Guide-for-Service-Providers_FINAL-ELECTRONIC1.pdf). (01.06.2015)

Riigikontroll (2010). Erikoolide ja alaealiste komisjonide järelaudit. <http://www.riigikontroll.ee/DesktopModules/DigiDetail/FileDownloader.aspx?FileId=11171&AuditId=2163> (01.06.2015)

Social Finance UK (November 2011). A Technical Guide to Commissioning Social Impact Bonds. <http://www.socialfinance.org.uk/a-technical-guide-to-commissioning-social-impact-bonds/> (01.06.2015)

Tallinna Ülikool, Kodanikuühiskonna Sihtkapital (2015). Kodanikualgatuse institutsionaliseerumine Eestis 2014. <http://www.kysk.ee/failid/Upload/files/KUAK%2014%20raport.pdf> (01.06.2015)

The Heritage Foundation (2015). 2015 Index of Economic Freedom: Estonia. <http://www.heritage.org/index/country/estonia> (01.06.2015)

UK Cabinet Office: Centre for Social Impact Bonds (April 2013). A measurable outcome. [http://data.gov.uk/sib\\_knowledge\\_box/measurable-outcome](http://data.gov.uk/sib_knowledge_box/measurable-outcome) (01.06.2015)

Uus, M., Tatar, M., Vinni, R. (2014). Avalike teenuste delegeerimine vabaihendustele. Tallinn: Poliitikauuringute Keskus Praxis. <http://www.praxis.ee/wp-content/uploads/2014/12/teenuste-delegeerimine.pdf> (1.06.2015)

Varblane, U. (2015). Euroopa raha võlu ja valu. <http://www.riigikogu.ee/rito/index.php?id=16676> (01.06.2015)

Vastutustundliku Ettevõtluse Foorum. Uuringud ja statistika. <http://www.csr.ee/uuringud-ja-statistika/> (01.06.2015)

Washington State Institute for Public Policy (January 2004). Outcome evaluation of Washington State's research-based programs for juvenile offenders. [http://www.wsipp.wa.gov/ReportFile/852/Wsipp\\_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders\\_Full-Report.pdf](http://www.wsipp.wa.gov/ReportFile/852/Wsipp_Outcome-Evaluation-of-Washington-States-Research-Based-Programs-for-Juvenile-Offenders_Full-Report.pdf) (01.06.2015)

World Bank Group (October, 2014). Doing Business 2015 Going Beyond Efficiency. [http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB15-Full-Report.pdf](http://www.doingbusiness.org/~/media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB15-Full-Report.pdf) (01.06.2015)

## **ANNEX. PROPOSAL FOR THE FIRST SOCIAL IMPACT BOND IN ESTONIA**

### **REDUCING THE NUMBER OF JUVENILE OFFENCES IN ESTONIA THROUGH THE ART PROGRAM**

**PROBLEM:** Estonia applies various interventions to juvenile offenders, including community work, rehabilitation services, a variety of social programs and specialized classes. For the more complicated target group, specialized schools for juvenile delinquents have been created. Nevertheless, almost 1,500 minors appear before juvenile misconduct committees each year, half of whom are repeat offenders. A majority of youth discharged from specialized schools continue to commit offences. According to specialists, Estonia needs more effective interventions for influencing the juvenile delinquents.

**INTERVENTION:** ART (Aggression Replacement Training) is an internationally acknowledged cognitive-behavioral intervention program for training social skills, anger management and problem-solving and supporting ethical decisions. The main target group for ART are children and youth, but the programme has been applied to adults as well. The program involves teamwork conducted by two trainers. The practical training for the above skills takes place during 10 consecutive weeks, 3 hours per week. In international practice, the suitable size of the group is considered to be 6–10 participants.

**POTENTIAL IMPACT:** In the United States, ART is one of the evidence-based programs used for lowering recidivism among juvenile offenders. A U.S. study showed a 24% decrease of repeat offences during the 18 months after the program. According to calculations, each dollar invested in the program saved the state an average of 6–11 dollars, considering the state's expenditure forecast without the program.

**POTENTIAL TARGET GROUP IN ESTONIA:** In 2014, 1,400 offenders appeared before juvenile misconduct committees, almost half of them repeat offenders. In the same year, specialized schools had 56 students, 33 minors were in prison and 168 minors under probation.

**TARGET GROUP FOR THE INTERVENTION:** approximately 128 offenders with aggressive behavioral patterns, aged 14–17

**DURATION:** 3 years, including 1 year for program implementation and 1.5 years for impact assessment

**COST OF INTERVENTION:** approximately EUR 200,000

**IMPACT ASSESSMENT:**

Two indicators are used to evaluate the effectiveness of the program: improvement of social skills and reduction of registered offences.

Improvement of social skills (including anger management, problem-solving skills, making ethical decisions) is measured on the basis of the internationally standardized and Estonian-tested *Strengths and Difficulties Questionnaire (SDQ)*, which contains questions for the young person, teacher and parent. Skills are evaluated immediately before and after the program.

Reduction of recidivism is measured according to official databases by comparing the number of registered offences by participants during the 18 months after the program.

**MODEL STRUCTURE:**

