SOCIAL FINANCE

ISSUE BRIEF 7

IS THE PRICE RIGHT?

Pay for Success (PFS) projects are built around specific, measurable outcomes—each with an associated dollar value unlocked through demonstrated performance. In this brief, we share strategies to determine prices for project outcomes.

ABOUT THIS ISSUE BRIEF SERIES

This issue brief is one of a 10-part series written **for government officials interested in learning how to use Pay for Success tools and principles.**

The series summarizes best practices and lessons learned at Social Finance from a decade of designing, launching, and managing Pay for Success projects. It includes guidance on each step of the process, from deciding whether Pay for Success is a good fit to actively managing a project post-launch.

See here to access the complete issue brief series on our website.

OUTCOME PRICES SIGNAL "PERCEIVED" VALUES

THE OUTCOMES SELECTED for a PFS project help to signal *what* the outcome funder cares about; the prices assigned to each outcome signal *how much* it cares about them. In PFS projects, the goal is to choose prices that appropriately reflect the fiscal and social value of each outcome while also taking into account the realities of local and political context. In this brief, we share methods for achieving that goal. (The contents of this brief assume project developers have already selected project outcomes and agreed upon measurement methodologies to assess the achievement of those outcomes; see *Issue Brief 5 – Defining Success* and *Issue Brief 6 – Measuring Success* for more information.)

PARAMETERS THAT INFLUENCE PRICING MODELS

There is no single formula to determine outcome prices. Rather, the inputs for establishing outcome prices differ based on the project's design. Below, we discuss different variables that may impact pricing and how they can be used to model outcome prices.

The **fiscal and social value of project outcomes** represents the theoretical best answer for how much an outcome is worth. Government entities enter into contracts with social service providers because they seek to generate ***fiscal and community value***. ***Fiscal value*** refers to budgetary impact on government (e.g., reduced emergency room costs resulting from a prevention-focused intervention); ***community value*** refers to broad benefits for constituents (e.g., quality-of-life improvements for individuals who spend less time in the emergency room).

Different outcomes vary widely in the amount of fiscal and community value they generate. One method for quantifying and comparing the value of different outcomes is to conduct a ***cost-benefit analysis (CBA)***. A CBA measures the total possible benefits (both fiscal and social) of achieving project outcomes, versus the costs required to achieve them. An outcomes funder likely wouldn't be willing to pay more for an outcome than the total fiscal and community value it generates, so a CBA can help project partners understand the ***maximum price*** for project outcomes.

While CBAs may seem like precise estimates that can translate directly into outcome prices, they aren't. The benefits resulting from an intervention often accrue to multiple entities, not all of which are involved in the project. Outcomes values themselves are often imprecise. And of course, benefit calculations are predicated on unreliable estimations of impact (see sidebar). So while calculating the fiscal and social value of different outcomes is a helpful starting point, it is rarely the end point in determining outcome prices for PFS contracts.

Provider costs for delivering services are also an important parameter for determing outcome prices. Providers cannot sustainably offer services for less money than it costs to deliver them, so project partners need to ensure that PFS outcome prices are high enough to cover deliver costs. Therefore, the provider costs for delivering services helps project partners understand the ***minimum price*** for project outcomes. (This is not to say that outcomes funders will always pay *more* than the cost of service delivery; they might not pay at all, if positive results aren't achieved. But if projects are successful at getting good outcomes, they should never be funded at less than their costs.)

Considering the **outcomes funders' willingness to pay** ultimately guides project designers between these two poles. Outcomes funders, guided by the above analyses and grounded in local political realities, cannot budget an unlimited amount for outcomes payments, so they typically put aside a fixed pool of funds. In other words, the ***total available outcomes dollars*** is a constraint on the amount that can be paid for the achievement of each outcome.[1] This parameter should be used to help project partners determine and negotiate outcome prices that fall between the maximum price derived from a CBA and the minimum price derived from provider costs to deliver services.

PREDICTING OUTCOME PERFORMANCE

It is nearly impossible to predict exactly how well an intervention will work in a given time and place; therefore, PFS projects need to attempt to link payment and performance along a continuum of possible outcomes. To do this, one of the inputs project developers need for pricing outcomes is the range of ***expected outcomes performance***. Past performance or historical data of the intervention or program can be used as a starting point, but project partners should ensure that any historical evidence used is relevant to the current project in terms of intervention specificity, outcome specificity, geography, target population, time, and delivery mechanism.

For more discussion on this topic, see Issue Brief 5 – Defining Success

PFS IN PRACTICE: EXAMPLE PRICING APPROACH FOR EMPLOYMENT OUTCOMES

To illustrate how project parameters influence pricing models, we share an example below of how project developers calculated outcome prices for a project focused on improving workforce outcomes.

The outcomes funder's goal for the project was to incentivize service providers to achieve client employment outcomes that were "above and beyond" contractual obligations. For example, service providers' contracts required them to achieve a

[1] See *Issue Brief 8 – Pay for Success Contracting* for different types of legal mechanisms to ensure that outcomes funding is available over the entire duration of a multi-year PFS project.

certain number of job placements, but the outcomes funder was willing to pay more for job placements with higher wages.

This project was designed as an ***outcomes rate card (ORC),*** a PFS tool in which outcomes funders contract directly with service providers to achieve specific outcomes at pre-set prices.[2]

To determine the price paid for each outcome on the ORC, the project partners:

1. **Determined outcomes funder's willingness to pay**. The outcomes funder decided that payments should be capped at 5 percent of provider costs. Across all four service providers contracted under the rate card, 5 percent of costs equaled $137,000.
2. **Modeled performance scenarios** to predict a range of expected outcomes for the performance period of the rate card (one year) based on data from the prior three years.
3. **Conducted a CBA** to help determine the relative value of the four outcomes included in the rate card. For example, "*job placement at $15/hour"* had higher fiscal and social value than *"job placement at $12/hour*," so it was determined that it should have a higher price.
4. **Calculated outcome prices using all of the above inputs,** ensuring (i) that the $137,000 reserved for outcomes payments would not run out even if providers overperformed the modeled performance scenarios by 20%, and (ii) that higher prices were assigned to outcomes with higher fiscal and social value.

The resulting outcome prices for the project were:

Outcome	Price per outcome
Client enrolls in program	$25
Client obtains job placement at $12/hour	$150
Client obtains job placement at $15/hour	$200
Client's earnings over the year after program exit are greater than earnings over the two years before enrollment	Up to $1,500, depending on level of earnings increase

For this project and others, outcomes pricing is an inexact exercise. But unlike traditional budgeting, it makes explicit the assumptions and values underlying program goals—which helps outcomes funders get more precise over time.

[2] See *Issue Brief 2 – The Pay for Success Toolkit* for an explanation of outcomes rate cards.

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ABOUT SOCIAL FINANCE

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