ISSUE BRIEF: PAY FOR SUCCESS

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.

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 determining 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 delivery 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. 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.

**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

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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:

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

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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