FSC PRG Series

IMPLEMENTATION OF SOCIAL IMPACT BONDS TO ENCOURAGE SOCIAL INVESTMENT IN MAURITIUS

Financial Services Commission
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Introduction

In November of 2015, the Financial Services Commission of Mauritius (the “FSC”) launched a Policy Research Group (“PRG”) program to enhance its policy research agenda across several areas of interest.

Among the select research themes, we decided to focus on a feasibility study for a social investment market in Mauritius. Our objective has been to approach social investment market through the local implementation of Social Impact Bonds (“SIBs”) from both a theoretical and a practical aspect for the potential development of a social investment market in Mauritius.

Spread across three chapters we focused this report on three core topics: the Concept, whereby we detail the basis of our proposal, the origination of SIBs, and highlights of their mechanism and provision of an economic rationale for their development; the Research and Development which lays an overview of our findings from interaction with potential participants the ‘local social economy’; and the Recommendation for Implementation to provide a pragmatic approach in the potential development and implementation of SIBs in Mauritius.

When formulating policies for social investment, a bottom up approach is required. Policies must be crafted with feasibility in mind, that is, the tools that will be delivering the desired results must be able to function within the framework that will be established.

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1. Concept

1.1 Social Impact Bonds

A social investment or impact investing is defined as any investment activity, which has an expectation of both a social outcome and a financial return.

The biggest issue that we have to overcome when dealing with social investment is that: the majority of social ventures have no financial return. We can spend a million dollars to keep a dog shelter running, but those dogs will never be able to repay us. Social ventures are by their altruistic nature financial sinkholes that consume funds without being able to generate financial return to whomever is contributing financially to the social venture.

The solution that is being proposed to the above problem is the use of new financial instruments called Social Impact Bonds[1] to securitise social ventures. As financial instruments, SIBs have the ability to generate financial return where there is none. We proceeded with the theory that the implementation of Social Impact bonds might be the key to the creation of a viable social investment market in Mauritius.

Addressing the implementation of SIBs requires a common understanding of its theoretical conception, its mechanism, and the rationale that underpins its merit. A policy tool can only be proper to the extent that the participants implementing it understand its functionality. In this chapter, we will seek to introduce the concept of investing in social programs through the issuance of SIBs, and support the rationale to use SIBs for both social and economic development.

Theoretical Background

Social Impact Bonds are a variant of Social Policy Bonds ("SPBs") invented by Ronnie Horesh[2], a New Zealand economist. Horesh argued that many of the social issues plaguing society were unresolved largely because their solutions lied in the hands of local or central government bodies, whose programs suffered from a fatal flaw that almost guarantees they will be ineffectual and expensive: they reward people for undertaking activities, rather than for delivering desired outcomes.

His proposal was that a new financial instrument be created that rewards people only when they achieve targeted social goals. SPBs would be issued by entities commissioning the social target, and auctioned to the highest bidders. In principle, any problem that could be reliably defined and quantified could be resolved. The SPBs would create a group of people (Investors) who would have a strong interest in achieving the targeted social objective efficiently, or in paying others to do so.

This structural change would cause social investment to shift from input based financing to result orientated financing. Payment of the SPBs would be based on what the project or service has achieved, not the processes or work that has been done. For example, payments for a social impact bond would be based on whether or not the underlying project has achieved its required quantitative result, rather than the cost of the project or the number of people working on the project.

On the other side, the 'investors' would be at risk losing money if the service contracted under the SPBs did not achieve its desired outcomes. SIBs are not traditional bonds – they carry equity-like risk, meaning that the investor can be exposed to all the downside risk: e.g. they can risk losing part of the capital investment.

SIBs are relatively new policy instruments to influence investments from the private sector into social causes. There are limited case studies and even less academic research to sustain their use, with the first actual implementation dating 2010. However we rely on the quantitative and qualitative research that we have gathered to support our proposals.

1.2 SIB Mechanism

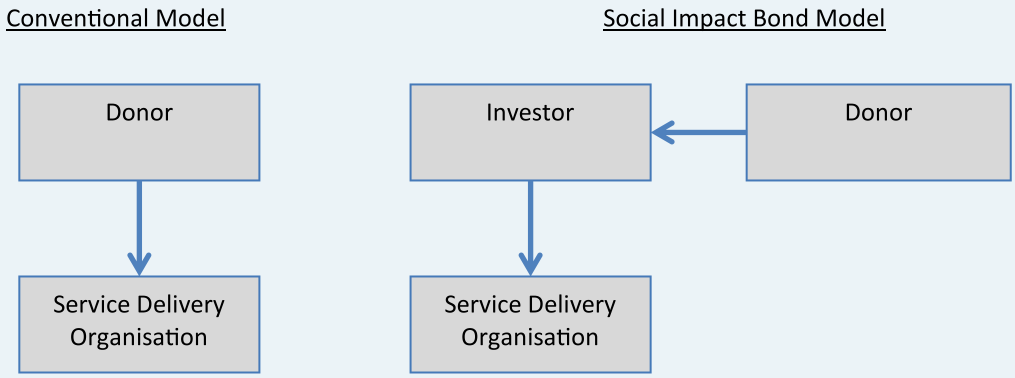

Chart 1: Conventional Model v Social Impact bond Model

In order to understand how SIBs will fit in Mauritius, we first needed to understand the mechanics of a SIB. This is achieved by comparing its functionality with that of a conventional social funding model.

Under a conventional model, capital is deployed directly to the Service Delivery Providers who undertake the social project. In contrast, the SIB model adds an additional layer of complexity, an Investor that provides investment capital in a social project in exchange for a performance related return paid by the donor.

This additional participant changes a simple process flow into a more complex one, that would unfold as follows:

- Project Commission - A social project would be commissioned to tackle a specific issue that is of the concern of the general public and the participants. A Service Delivery Organisation or a group of Service Delivery Organisations is selected to undertake a project with clearly defined measurable metrics to measure the success of the program.

  Donor Commitment – Donors are contracted to pledge funds to the effort of the social project. These funds are usually pledged in a trust or similar special purpose vehicle and may only be unlocked to pay the investors upon completion of the social project.

- Investor Commitment – Investors commit funds to the Service Delivery Provider(s). In exchange for funding the Service Delivery Organisation(s), the investor receives a 'bond' that will remunerate them based on the outcome of the social project.

- Project deployment, Assessment and Payoff – The funds are deployed by the Service Delivery Organisation and at the end of the project, the metrics are evaluated and the 'bond' investors remunerated or 'paid off' from the donor funds. In the event of a successful social project, the 'bond' investors are remunerated their capital and agreed upon return, but in the event of an unsuccessful project, they may only be remunerated part or forfeit the whole of their capital investment, depending on the pre agreed conditions.

All the participants must come to agreement on all the aspects of the SIB, that is: the operational structure; their legal relationships and duties; the financial risks involved and the quantitative objectives of the SIB. The above creates a slower hurdle to implementation as compared to the conventional model, making planning a crucial stage.

Symbiotic Relationship

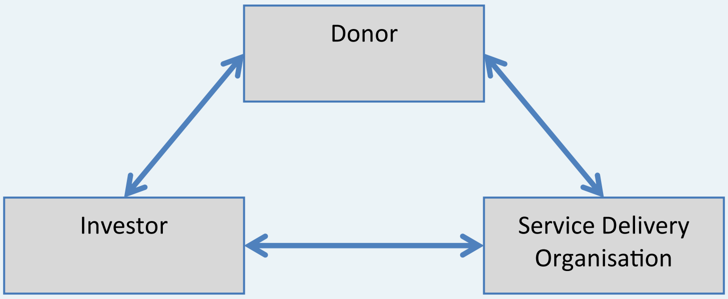

Chart 2: Balancing interests between Participants

While the additional complexity may not seem useful upfront, the greater purpose of the securitisation process is to create an imperative to succeed generated by self-interest from all three main participants by altering the perspective of the participants as follows:

- Donor Perspective – Institutional donors (e.g. governmental entities, non-governmental organisations and charitable trusts) are held accountable as to how their funds have been deployed and as to the effectiveness of their commitments. This reinforces due diligence on behalf of donors, but from the moment funds are committed, the donors have little to no control over the outcome of the project and bear the full financial and reputational risk of the project sub performing or failing. By shifting the actual payment in the future, and subjecting it to performance, the donors decrease their effective fund allocation to unsuccessful project and increase their effective allocation to successful project. This increases the flexibility for donors to commit to more bold social projects, while retaining an insured financial and reputational stance.

- Investor Perspective – As per the current status quo, there are no incentives for prospective investors to commit funds to social project, as there would not be any economic return. SIBs create an alternative and ethical investment market, uncorrelated with current macroeconomic factors, enabling investors to take on the risk in a social development projects and gaining an economic return. They would commit capital to projects that they believe will succeed, and be rewarded accordingly. A form of free market would drive capital into efficient social projects while reducing allocation to less efficient ones.

- Service Delivery Provider Perspective – The main hurdle to Service Delivery Providers is a lack of stability in fund commitment from donors. SIBs offer an opportunity for Service Delivery Providers to undertake grander scale projects that would require substantial financing by relying on investors through legally binding agreements. Similarly, professional and proficient Service Delivery Providers would be able to raise more funds for projects while underperforming ones would have their funding reduced.

1.3 The Peterborough SIB

Peterborough Social Impact Bond

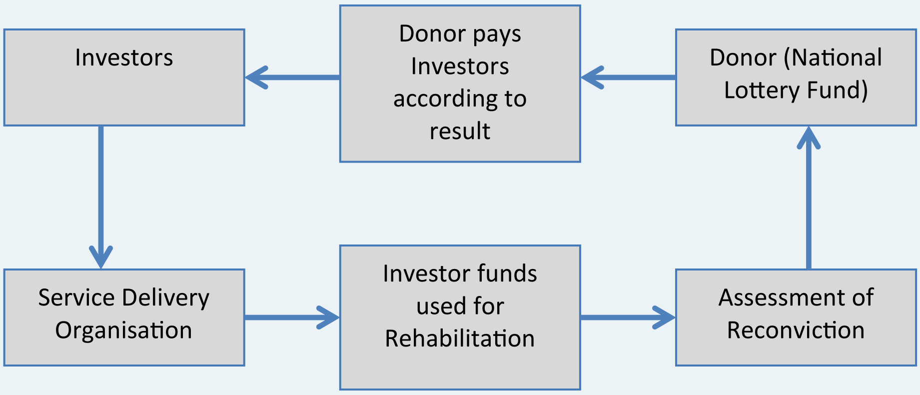

Chart 3: Peterborough Flowchart

The Peterborough Social Impact Bond[3] ("Peterborough SIB") was the first SIB to have been issued. In 2010, £5m was raised from private investors for a Social Impact Bond that was backed by the National Lottery fund in the UK. The aim was to innovate social work with 3,000 short-sentence offenders leaving Peterborough prison in the UK. The SIB was intended to fund an alternative wraparound support service designed to address the multiple and complex needs of the convicts.

The success of the project was measured by reductions in reconviction events, which was a proxy outcome for reductions in reoffending.

Defining Principles

The defining principles of the Peterborough SIB were that: when structured as a form of Payment By Results ("PBR"), an SIB has the following potential benefits for different stakeholders as follows:

- For the government – a SIB is a form of payment by results, which removes the upfront costs of service delivery from government and shifts the financial risk to private investors, who lose their investment if interventions do not improve outcomes.

- For service providers – unlike other Payment by Result mechanisms, service providers are not paid by results and do not bear the risk in the SIB. Providers are paid upfront, which provides opportunities for not-for-profit and third sector organisations, which could not bear the risk under traditional PBR arrangements, to deliver services. Another way in which SIBs are different from other PBR schemes is that under a SIB, several different providers can deliver services that contribute to improved outcomes.

- For investors – SIBs offer a new investment opportunity with a 'blended return' investors receive some financial return but also value the social returns on their investments.

- For society – SIBs may improve outcomes and quality of life by funding service provision where there previously was none. It is claimed that SIBs might be particularly used to fund preventative interventions, or other kinds of service delivery, which governments might not prioritise for funding – especially in a time of limited resources. In a SIB the government is not prescriptive as to the way in which services are delivered; it is hoped this may encourage innovation in service provision. Further, in some of the literature on SIBs, it is suggested that private donors and organisations may be willing to consider more innovative and/or riskier projects than government is likely to fund. Whether SIBs will encourage innovation is as yet untested, and is something which will be explored in later stages of this study.

- For service users – some groups, including offenders, may be less attractive beneficiaries for both charitable giving and government spending. SIBs may raise funding to deliver interventions to these groups.

Outcomes[4]

- Results for the first cohort of 1,000 prisoners on the Peterborough were as such: the SIB investment demonstrated an 8.4% reduction in reconviction events relative to the comparable national baseline. A team of independent assessor and the University of Leicester compiled the results for the Ministry of Justice.

- Nevertheless, after June 2015, five years after its launch, it was stated the intervention will not continue to be a SIB due to an a change in approach[5] to UK probation and rehabilitation services released by the Ministry of Justice called Transforming Rehabilitation ("TR"). TR will offer rehabilitation services to all offenders across the UK. Prior to the SIB, short-term male offenders did not receive rehabilitation services, a gap the SIB was able to fill. With the implementation of TR at the end of 2014, this contingent of offenders will no longer be left out by the UK's overarching strategy for rehabilitation.

- The end result from the SIB was one that benefited all parties to the social and financial experiment, with the government implementing working model into its own program.

1.4 An Economic Strategy for Mauritius

Whilst the primary focus of SIBs is to improve efficiency and transparency in the social investment market by introducing a market driven factor, we believe that SIBs may play greater role in the economic development of Mauritius. We identified three primary areas where we believe the implementation of SIBs could contribute to economic development: the local capital markets, attraction of international funding and professionalisation of social services.

Capital Markets

Developing the capital markets is a strategic priority to Mauritius, however the growth potential of the local capital market is foremost limited by the size of our local economy. In small countries, the number of economic ventures that meet the criteria to raise funds on the public market are numbered, and therefore there is limited scope for current capital to grow much faster than the domestic GDP growth rate

The solution that SIBs bring to the above problem is to increase capital market instruments through their inclusion as non-traditional instruments. Similar to equities or bonds, they are contracts that give rise to a financial assets and liabilities, and therefore have the potential to be securitised. They can therefore be adapted for most scenarios whereby a donor would commission an undertaking to achieve a social outcome.

For example:

Incremental Gain/Loss Model	Savings Model
Principle – The SIB would pay the investor an incremental point of return on capital for each point of incremental outperformance over the benchmark; or subtract a basis point of return from capital over each basis point of incremental underperformance under the benchmark.	Principle – The SIB would pay the investor to commission and invest in a Service Delivery Organisation that can deliver a similar service at a lower cost.
Application – This SIB would be implemented in cases where donors have previously allocated funds to specific quantifiable result social investment, but are seeking to increase the efficiency of funds deployed.	Application – This SIB would be implemented in cases where funds for specific social investments are being reduced and the donor is seeking to achieve the same social result but with lower costs.
Case – A current social program increases primary school pass rate at in a ZEP school from 40% to 60% at the rate of MUR 10,000 per year per student. The donors are willing to pay investors and additional MUR 100 for each percentage increase in school pass rate.	Case – A current social program provides basic transportation services for 100 cancer patients to hospitals for treatment at the rate of MUR 5,000 per patient per year, but is facing pressure to reduce spending by 10%. The donors allocate 90% of the original budget to the SIB to achieve the same target.
Success Payoff – Should the SIB bring the pass rate from 60% to 70%, investors would receive a return of 10% on investment while the donor would increase the efficiency of his donations by 50% by increasing his commitment by only 10%.	Payoff – To generate a payoff, the investor needs to invest in a Service Delivery Provider that will achieve the target for less than the allocated amount and take the difference as profit.
Failure Payoff – Should the SIB lower the pass rate from 60% to 58%, they would face a loss of 10% on their capital equivalent to the decrease in efficiency.	

Table 1: Securitisation Models

International Funding

In 2014, over USD 44 billion in Official Development Assistance ("ODA") was distributed to Sub Saharan countries from Development Assistance Committee countries ("DAC"), out of which USD 49 million was allocated to Mauritius. These figures give Mauritius a receipt per capita of USD 38.80 which is lower than the 2014 average of USD 45.44. This can be attributed to the relative economic and political success of the country which makes Mauritius less attractive to foreign aid.

Our view is that traditional international funding to Mauritius will keep decreasing as long as the country keeps outperforming its sub Saharan neighbours at both a social and economic level; and that we will not be able to retain or increase net DAC funding without reforming our approach.

As per the UNDP Millennium Goals Development report of 2015[6]:

"Mauritius has achieved or nearly achieved a number of the fundamental Millennium Development Goals (MDGs) relating to poverty, education, health, gender and global partnership for development."

As a recipient country, we need to compete on a different level, by proving that we are more committed to transparency and efficiency[7]. Implementation of

SIBs at a local level would very likely achieve the desired outcome by providing more information on the social projects being undertaken, and subsequently increasing the amount of discretionary donations that we can receive.

	1998-1999 Average	2003-2004 Average	2011	2012	2013	2014
Angola	570	1 036	192	243	283	230
Benin	303	444	666	519	660	596
Botswana	119	50	120	74	107	99
Burkina Faso	604	767	961	1 156	1 044	1 115
Burundi	115	382	560	527	556	499
Cabo Verde	204	189	241	255	245	229
Cameroon	703	1 082	597	609	748	842
Central African Republic	173	102	258	230	202	607
Chad	270	377	451	479	458	386
Comoros	45	33	50	69	79	74
Congo	163	117	256	142	151	106
Côte d'Ivoire	1 061	270	1 409	2 712	1 272	917
DR Congo	202	4 799	5 472	2 898	2 583	2 373
Djibouti	112	90	136	147	148	164
Equatorial Guinea	34	33	24	15	4	1
Eritrea	244	381	129	135	81	82
Ethiopia	993	2 190	3 461	3 243	3 885	3 540
Gabon	71	17	70	75	90	111
Gambia	54	78	130	139	115	98
Ghana	916	1 488	1 781	1 802	1 330	1 119
Guinea	434	337	201	342	473	561
Guinea-Bissau	112	151	116	80	104	109
Kenya	515	744	2 467	2 676	3 312	2 637
Lesotho	68	111	253	279	320	103
Liberia	125	205	751	573	535	744
Madagascar	614	1 137	438	380	499	580
Malawi	649	653	790	1 174	1 130	926
Mali	527	748	1 252	1 012	1 398	1 233
Mauritania	283	290	372	415	293	257
Mauritius	62	10	184	185	148	49
Mayotte (a)	165	240	-	-	-	-
Mozambique	1 449	1 497	2 049	2 105	2 315	2 096
Namibia	278	206	281	262	261	223
Niger	358	659	634	908	797	914
Nigeria	259	545	1 756	1 922	2 515	2 437
Rwanda	547	525	1 251	889	1 086	1 024
Saint Helena	20	25	85	169	139	123
Sao Tome and Principe	44	46	70	50	52	39
Senegal	774	958	1 027	1 084	992	1 104
Seychelles	28	13	21	36	25	10
Sierra Leone	137	449	414	443	447	882

	1998-1999 Average	2003-2004 Average	2011	2012	2013	2014
Somalia	160	262	1 084	998	1 054	1 106
South Africa	809	824	1 399	1 091	1 295	1 061
South Sudan (b)	-	-	432	1 192	1 400	1 945
Sudan	360	1 039	1 733	1 371	1 503	867
Swaziland	44	41	122	90	116	85
Tanzania	1 517	2 249	2 417	2 842	3 431	2 629
Togo	144	74	530	244	224	207
Uganda	955	1 412	1 562	1 656	1 701	1 622
Zambia	735	1 203	1 028	964	1 142	984
Zimbabwe	374	238	718	1 008	824	745
South of Sahara, regional	603	1 796	2 571	3 071	2 444	3 459
OVERALL TOTAL	20 104	32 611	44 969	44 977	46 014	43 950

Table 2: Net Disbursements of ODA to Sub-Saharan Africa by Recipient[8]

Professionalisation of Social Services

By incorporating a result-oriented model in the social services industry, we aim to foster competition and incubate a generation of professional social workers that have the capacity to innovate to deliver better social services. Diversification of the local economy may not only arise from the development of new industries; but from the innovation and reform of existing ones, such as the social services industry.

While the current state of the local social services industry is too nascent to make long-term economic predictions, we have a positive outlook on its future development. Especially when Mauritius is geographically located next to the biggest aids recipients in the world; the possibility of creating an exportable business model reliant on a skilled workforce, is a national economic strategy to be considered.

2. RESEARCH AND DEVELOPMENT

Given the novelty of SIBs, we believed that the foundation for implementation would be based on adapting the concept to local participants. In this chapter we explored the concept with potential SIB participants so as to better determine the feasibility of implementation. Our prerogative was as follows:

- To introduce the concept of Social Impact Bonds and result based financing;
- To help localise each participants in the SIB model;
- To review the relevance SIBs in current operational requirements; and
- To explore prospective conflicts in the prospective implementation.

The goal we set was to generate constructive feedback that would provide a clearer insight as to the caveats and impetus for SIBs implementation the local context.

2.1 Research Methodology and Limitations

Methodology

The research was conducted primarily through individual interviews. The process was more laborious that initially anticipated; most potential participants had no knowledge with respect to Social Impact Bonds, and had limited understanding of the financial markets.

We conducted the research by prioritising the introduction of the concept of social impact bonds as a tool to help potential participants achieve their respective goals. From thereon, the participants were able to determine whether they would have any interest in developing or using such a tool. Interviews with potential participants were made on a recommendation basis whereby each potential participants we interviewed redirected us to other potential participants that they believed would be most appropriate to help develop the SIBs.

Limitation

The research phase of the study was primarily focused on obtaining qualitative data. Therefore we set several limitations to our interactions to avoid any misinterpretation of our research.

- We followed the guidelines of the Income Tax Act 1995 by limiting our definition social investment as any undertaking that would directly concern, poverty alleviation, educational support, social housing, supporting persons with severe disabilities, dealing with health problems resulting from substance abuse and poor sanitation; and family protection.

- We classified social investment into 2 categories, 'quantifiable result' and 'non-quantifiable result'. 'Quantifiable result' social investment has the underlying effect of achieving a measurable effect on society, while 'non-quantifiable result' social investment effect would not be measurable. For example, increasing literacy, decreasing obesity and improving participation of disabled people in the work force would be classified as 'quantifiable result' social investment. Research was conducted strictly in the applicability of SIBs for 'quantifiable result' social investment.

- We were not able to interview the full spectrum of local potential participants in our SIB models. At the current stage of the research, some categories of participants were left out due to practical constraints.

2.2 Interaction with Potential Participants

Overall, we received generally favorable response with potential participants, providing clearer insights as to the status of the social industry. We regrouped out results under three groups, in line with the SIB concept: potential Donors, potential Investors and potential Service Delivery Providers.

Donors

From our interviews we identified that locally, the biggest potential donor participants in a hypothetical SIB implementation were as follows: the government of Mauritius, Non-Governmental Organisations, and Corporate Social Responsibility (CSR) Donors.

- Government[9] - The biggest source of social spending in Mauritius is from the local government. The government has a budget that is dedicated to the provision of social services to the local population. On its own the government of Mauritius has the capacity by itself to kick-start the Social Impact Bond industry. In addition, the government had access to international grants that other local organisations are not eligible for.

- Non-Governmental Organisations[10] – These organisations range from: well known international names such as the United Nations, Development Programme (UNDP), the World Bank the Global Environmental Facility (GEF), the African Bank to smaller private charitable organisations.

  These organisations have been in operation in Mauritius for years. They have access to international funding that exists as: non-discretionary funding (funding that have been committed to a specific country for a specific cause) and discretionary funding (funding that are committed to a country at the discretion of the donors).

- Local Donors and Corporate Social Responsibility – CSR donors are empowered through the implementation of Corporate Social Responsibility law. The mandatory tax has forced the private sector to contribute a stable flow of funds into local social causes, but mostly it has allowed the private sector to direct funds to social ventures of their choice. In contrast with government or Non-Governmental donors, CSR donors have a relative flexibility to channel their funds freely.

We identified that this combination of legal obligation, but discretionary choice, made private sector CSR donors, ideal donor participant in the SIBs, and pursued our research accordingly.

Sector of Intervention	Jan-Dec 2010	Jan - Dec 2011	Jan - Dec 2012	Jan - Dec 2013
Socio Economic Development	256,120,318.77	103,008,742.69	142,251,939.26	115,951,134.84
Health	37,462,705.07	28,149,372.66	17,743,103.10	17,832,727.40
Leisure and Sports	31,787,488.91	27,876,688.11	23,639,711.00	34,412,763.41
Environment	16,068,023.24	21,940,015.85	26,525,824.00	26,478,712.99
Education and Training	64,001,254.55	86,253,045.45	61,158,024.50	85,286,930.26
Calamities	721,680.00	0.00	0.00	22,600,098.55
Total	406,161,470.54	267,227,864.76	271,318,601.86	302,562,367.45

Table 3: Summary of CSR Funds disbursed sector wise between 2010 – 2013[11]

Key Findings

Segment	Preferred Funds Distribution Methodology	Interest in SIBs
Large Scale Donors (LSD)	Most LSD developed "subsidiary organisations"[12] capable of receiving and deploying funds for specific goals in alignment with the donor goals.	Limited interest in SIB as they have an existing functioning system to effectively deploy available funds.
Medium Scale Donors (MSD)	Have mostly adopted a “parrainage style”[13] for select organisations that receive approval of management.	Moderate interest in SIBs.
Small-Scale Donors (SSD)	Use the “parainage” Style, but a significant portion of small-scale donors opt to transfer the money to the Mauritius Revenue Authority.	Interested in the ability to participate in bigger controlled projects subject that project is CSR approved.

Table 4: Comparison of Local donor profiles

While we received mostly positive feedback from CSR Donors towards the implementation of SIBs, we also noticed several patterns that were of relevance to our model:

A. CSR donors were stratified in 3 segments: large scale donors, medium scale donors and small-scale donors;

B. Potential donor participants in each segment tended to adopt CSR strategies similar to other participants in their segments; and

C. The interest with respect to SIBs for potential participants converged for each segment.

However, the most notable finding was that a significant amount of funds that were available from small scale donors were directed to the Mauritius Revenue Authority. Repeated feedback from small scale donors were that CSR approval system for Mauritian NGOs were unclear and that they did not have the resources nor were they willing to take on the administrative burden of assessing whether a project would be approved CSR approved by the Mauritius Revenue Authority.

These strata of donors were the most interested in having a ‘click and drop’ platform of pre-approved project whereby they could direct their funds, and would support a CSR approved SIB.

Year	2010	2011	2012	2013	2014
Unspent CSR Funds (Rs Millions)	149.5	116.40	130.0	124.7	166.5

Table 5: Unspent CSR funds as collected by the MRA[14]

Investors

In fulfilling the role of investor participants, we considered two categories of potential investor participants in SIBs in Mauritius; retail investors and institutional investors.

- Retail Investors – Generally speaking, investment options for retail investors in Mauritius are currently very restricted.

  We approached prospective retail investors by introducing the concept of Social Impact Bonds. The idea of supporting and participating in a social cause while generating financial return was very appealing to this segment of investors. The key aspect was that SIBs would act as a conduit for them to participate into crowd funded social ventures.

- Institutional Investors – Institutional investors were inclined to investing in SIBs subject to the investments being transparent and clear. Current market conditions in Mauritius have an excess of liquidity chasing limited available locally denominated investments, which creates a natural demand for investments. Under the guise of state funds or insurance funds, institutional investors would be the primary buyers of SIBs.

Key Findings

SIBs as an alternative investment product has the ability to easily attract capital; which also implies that there is room for abuse. We strongly emphasise that SIBs issuance must be monitored and the relevant regulatory authorities must issue proper directives.

Service Delivery Organisations

As of date, the social ecosystem supports only two types of Service Delivery Organisations: governmental entities, and charitable organisations and Special Purpose Vehicles (SPVs).

- Governmental Entities[15] – As previously stated, the biggest source of social spending in Mauritius from the local government, which through its execution arms provide social services to the population.

- Charitable Organisations – They form the backbone of the social economy. They greatly vary in size and objectives, but they all compete on a daily basis for funding. They were the most receptive of SIBs as their implementation would promote greater transparency, and give them access to much needed funding.

Key Findings

The addition of new funding through the CSR laws created a spike in local NGOs and charitable Special Purpose Vehicles (SPVs). Over the period of 2009 to 2013, the number of charitable NGOs and SPVs tripled in number[16]. Increased funding availability came with increased competition.

There were concerns were that bogus institutions being set up to siphon CSR funds as well as third parties providing access to CSR funding in return for high commissions. The general perception was that: if a charitable organisation was not a “subsidiary organisation” nor did it manage to get a “parrainage” there was a cutthroat competition for funding in an opaque environment.

However, it was the absence of a centralised platform that prevented funds from being efficiently connected to donors. As a result, those ‘orphan’ entities were working with a very a short vision as any project had high chances of being underfunded. Service Delivery Organisations strongly supported SIBs as tool to increase funding and transparency.

Year	2009	2010	2011	2012	2013
Total NGOs	232	454	510	538	561
Total SPVs	0	0	37	76	84

Table 6: No. of NGOs & SPVs accredited with the CSR from October 2009 to December 2013[17]

2.3 Notable Findings

From our research, several findings came into emphasis that warranted the implementation of Social Impact Bonds.

Underutilisation of CSR Funds

Two issues currently plague the field of the local CSR industry:

- There is lack of clear guidance that encourages many small scale donors to transfer their CSR funds to the Mauritius Revenue Authority, rather than disburse it for Social Causes to charities; and
- Small size charities are not able to secure funding due to increased competition, lack of exposure and transparency.

In other words, there is a mismatch between donors and Service Delivery Providers; the flow of funds is not efficient. Our view is that in the current situation, the mismatch will not auto-regulate itself without external intervention. There is a need for reform in the social services industry.

The Future of International Aid is Transparency

There has been a recent change in the way in which international aid is dispensed as more empirical data is being gathered to support some of the destructive effects of unbridled donations. With 2010 Haiti earthquake[18] as an example, the dearth consequences of aid were as follows:

- Orphans – A massive surge in donations for Haiti orphanage created a seven-fold surge in “orphans” being placed in the system. Children were separated from their family and placed in institutions where they would be vulnerable to abuse and exploitation because there were economic incentives for them to be orphaned.
- Economic Disruption – The free flow of food, water, medication, construction materials and other items while relieving the population destroyed all the trade economy. Businesses were forced to go under, as they could not

compete with donations, jobs were lost and the economy was irreversibly damaged. Once the free flow of donation was halted, the economy went into shock, as there was no one to fill the gap.

Donor fatigue is weighting in as many donors start to rein in donations when faced with the possibility of their donations being more destructive than constructive. Going forward, only transparent[19] programs will be able to compete for funding.

Disruptions in CSR Laws

On the 29th of July 2016 major changes were announced in the 2016/2017 budget[20], namely the compulsory attribution of CSR funds to a national CSR foundation. This was subsequently reflected in the Finance (Miscellaneous Provisions) Act 2016. These changes will strongly impact CSR donors by severely affecting the funding mechanism of both large donors and small donors.

The destabilisation of current social programs will create a need for alternative funding mechanisms.

3. RECOMMENDATIONS FOR IMPLEMENTATION

The social investment market has so far remained the most difficult financial innovation to implement. As initially stated, the majority of social ventures have no financial return, which is why we experimented with Social Investment Bonds: SIBs enabled us to securitise the risk element in social ventures and transfer it for a financial return.

We studied several models of implementation and case scenarios, but the most informative part of our research remained the interactions with participants in the local social economy. It provided us with a clear rationale for implementation and helped us define a proper guideline for prospective implementation: Social Investment is a means to an end, but not an end in itself; it is a policy tool that needs to be adapted and used according to the needs of the current social economy.

On the long term, our approach is that SIBs may only operate upon the implementation of clear Regulatory Framework, Conceptual Framework, and Operational Framework.

3.1 Legislative Framework

Our recommendations for a legislative framework is based on an in-depth analysis of the Social Impact Bond Act[21] submitted by Representative Todd Young from the United States House of Representatives. Any potential legislation encompassing SIBs would require: a structured purpose for a unified long-term goal; and clear guidance on SIB award and transparent monitoring.

Structured Purpose

Our first legislative recommendation is to reorient the current CSR purpose guidance under the Income Tax Act 1995 so that the goals have a structured purpose. To support the previous statement, we contrast the purposes between the Mauritian Act and the proposed US bill:

Mauritian Legislation	US Legislation
PRIORITY AREAS OF INTERVENTION - Dealing with health problems resulting from substance abuse and poor sanitation. - Educational Support targeting families in the Social Register of Mauritius - Family protection – protection to victims of domestic violence. - Poverty alleviation targeting families listed in the Social Register of Mauritius - Social Housing targeting families in the Social Register of Mauritius. - Supporting persons with severe disabilities. **ACTIVITIES WHICH DO NOT QUALIFY UNDER CSR** - Activities discriminating on the basis of race, place of origin, political opinion, colour or creed. - Activities targeting shareholders, senior staff or their family members. - Activities which are against public safety and national interest. - Religious, political, trade union, self-financing, staff welfare and marketing activities.	To qualify as a social impact bond project under this subtitle, a project must produce a measurable, clearly defined outcome that results in social benefit and Federal savings through any of the following: (1) Increasing work and earnings by individuals who have been unemployed in the United States for more than six consecutive months. (2) Increasing employment and earnings of individuals age 16 to 24. (3) Increasing employment among individuals receiving Federal disability benefits. (4) Reducing the dependence of low-income families on Federal means-tested benefits. (5) Improving rates of high school graduation. (6) Reducing teen and unplanned pregnancies. (7) Improving birth outcomes among low-income families and individuals. (8) Reducing rates of asthma, diabetes, or other preventable diseases among low-income families and individuals. (9) Increasing the proportion of children living in two-parent families. (10) Reducing incidences of child abuse and neglect. (11) Increasing adoptions of children from foster care. (12) Reducing recidivism among individuals released from prison. (13) Other measurable outcomes defined by the State or local government that result in positive social outcomes and Federal savings.

Table 7: Contrasting Mauritian and US targets for social development goals

To highlight the difference: under the Mauritian model, a social program to provide psychological support to the unemployed poor would be warranted, while under the US model it would not be, as it would not resolve the problem of unemployment under any of the qualified purposes.

While Mauritian guidance recommends a vague remedial stance for general social ills, the proposed US bill is geared towards planned constructive actions that have proven long-term direct social and economic outcomes. It is the specificity of the US bill ensures that all subsequent implementation of SIBs will have a correlated result in line with national priorities.

3.2 Conceptual Framework

In many ways, SIBs will appear as an alien concept to both the general public and the potential participants. And though the proposed legislative framework may provide for clear guidance, practical implementation will have to be developed on the basis of a universal simplified structure that can be made clear and understandable to the layman. For that objective we proposed an archetype built on the Template Trust Mechanism, and the Five-Phase Delivery System.

Template Trust Mechanism

Based on the preliminary model presented throughout our research, we proposed a localised model that would be more approachable to local participants, a Template Trust Mechanism (**"TTM"**).

Under the TTM, the tripartite model that encompasses Donors, Investors and Service Delivery Providers is expanded to include two minor participants, the Intermediary and the Arbitrator. Those two additional participants independently, reinforce the functional aspect of the SIB that will be built around a purpose trust.

- The Intermediary – In a practical scenario, it is unlikely that the three main participants would naturally converge into an SIB arrangement. Each will operate in their distinct industry and would not have the relevant know how to lead on an SIB.The idea behind using an Intermediary is to have a third party promote and control the SIB by pushing for the creation of the SIB, through the selection of a suitable project and finding the complementary participants to the SIB. This would create the foundation for the social investment to build upon. A promoter can originate from any of the 3 main participants: donors trying to increase the output of the funds they commit to social investment; financial institutions or professional investors willing diversify into social venture capitalism; current service delivery organisations looking to expand their current business model to undertake projects on a bigger scale; or simply social entrepreneurs.

- The Arbitrator – As stated in the previous section, transparency would be an essential pillar of the development SIB. With huge funds being at stake, the role of the Arbitrator would be to act as an auditor or safeguard against potential fraud that may occur in any SIB. In that view, we are concerned with the following potential issues:

  1. Participants setting up bogus SIBs;
  2. Investors or Donors reneging on their commitments; or
  3. Collusion between Participants to falsify results.

With only those few potential issues as example, the requirement for an independent third party becomes a necessity, as are auditors in the corporate world.

Qualitative v/s Quantitative Aspect of SIBs

SIBs only caters for quantitative metrics for measurements for assessing success. As legal and financial agreements there is no room for interpretational ambiguity. While some projects will fall out of the scope of SIBs, other projects can seek inclusion by restating their goals. For example a cancer awareness campaign can be restated to focus on increasing detection rates and participation rates for testing.

Template Trust Mechanism

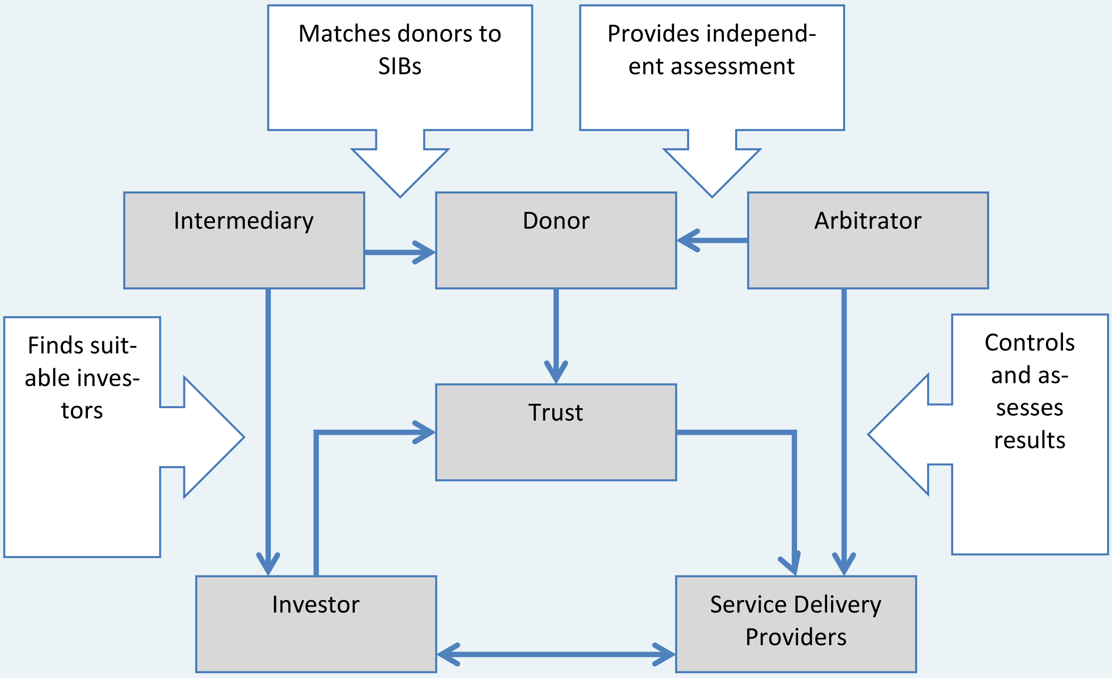

Chart 4: Template Trust Mechanism

<u>Five Phase Delivery System</u>

In light of the proposed TTM Model we are recommending a Five-Phase Delivery System that would define guidelines for execution aspect of SIBs.

Phase 1 – Project Viability Study

An SIB project can only be deemed to be viable if it can sustain interest from the three main participants. In a Mauritian TTM, the commissioning of a project would most likely be initiated either from Voluntary, Community and Social enterprises (“VCSE”), regrouping to summon funds for a bigger initiative, or from the private sector pushing forward a project.

Phase 2 – Trust Construction and Pledging

The main purpose of the trust would be to act as a special purpose vehicles to which the donors would pledge their funds. This would create a binding legal commitment from the donors so that the trust will be acting as guarantor to the investors who will be risking the funds in the project.

Phase 3 – Investment and Securitisation

Once a project is completely structured and the funds pledged, the intermediary will require funds to deploy the project. The investors would then legally commit to transferring the agreed funds directly to the service delivery organisation.

Phase 4 – Deployment and Control

Once phase 1 through 3 is cleared the project is actually executed. Funds are released by the investors to the service delivery organisation are deployed as agreed in it the viability study. Funds can be released as per Key Performance Indicators achieved or be left to the discretion of the intermediary or the investors.

Phase 5 – Result Assessment and Payoff

With the project reaching its completion of the end of the social investment, the arbitrator’s final role comes into play. They assess the result of the project in line with what was commissioned. Assessment is not subjective as the outcome has been pre-defined: a successful result is rewarded, and a failed project is not.

3.3 Operational Framework

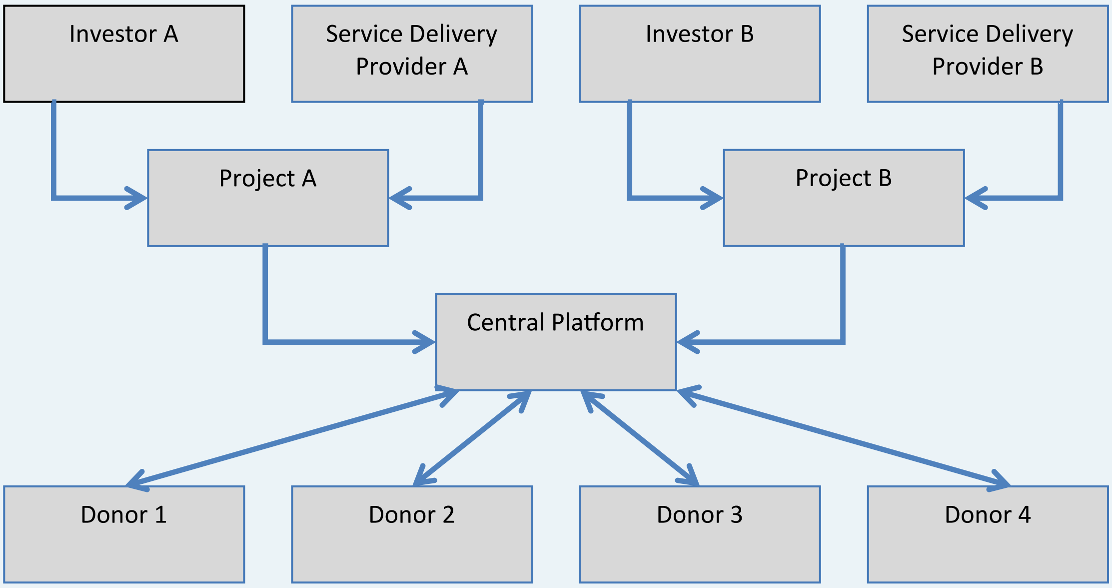

Chart 5: Schema for a centralised Platform

With the legislative and the conceptual aspect covered, in the last leg of this section we will explore two ideas that would be most constructive in implementation of SIBs: the use of a centralised electronic platform and the creation of a regulatory sandbox.

Using a Centralised Platform

Our proposition for a centralised platform is derived from the current development of crowd funding models. The last few years have given rise to the social sharing economy such as UBER, Air BnB, and Kickstarter, the innovations in such ventures do not lie in the revolutionary inventions but in connecting users and service providers efficiently. This part of the submission will seek to provide a concept based to develop a viable platform in line with our recommendation.

As a tool of the future, we believe SIBs would most likely see its operation take place on a modern platform. In our SIB promotion we propose the following:

- A centralised electronic platform would be created to manage all issuance of SIBs;
- Service Delivery Providers would provide a detailed plan, budget and objective for their project and list it on the platform;
- Prospective investors would be invited into providing financial backing to the projects, and structure the terms and conditions of the bonds, this exercise would encourage the investor to help charities plan their project, an subsequently screen out bad projects;
- Private donors (such as NGOs or private charities), and CSR Donors would send their funds to the centralised platform in exchange for SIB credits;
- The finalised projects would be listed on the platform jointly by the investor and the charity, and the donors would distribute their SIB credits accordingly.
- Once the project would reach enough donor commitment, the funds would be transferred into an escrow account and a 'bond' would be issued to the Investor.
- The investor would deploy its funds, and upon the completion and assessment of the project, the

funds would be disbursed from the escrow account to repay the investor accordingly.

Regulatory Sandbox[22]

In the current local regulatory context we are likely to encounter several regulatory obstacles to the implementation of SIBs. Be it expensive regulatory licensing fees, or the lack of an appropriate regulated party to undertake the securitisation; we do not see the implementation of SIBs from a regulatory perspective as straightforward.

In early 2016, the Financial Conduct Authority of the United Kingdom committed to the creation of a Regulatory Sandbox, a segregated regulatory environment from which new financial innovations would be allowed to operate, relatively free from burdensome regulations. The rationale was that financial industry was facing a wave of disruptions from the technology sector, financial technology (“fintech”) and regulatory technology (“Regtech”), which were coming to displace traditional businesses.

Financial rules that predate the creation of smartphones and the Internet would very likely be inappropriate to protect and regulate a whole new market built on block chains and biometric identification. A lack of foresight would cause these new businesses to either operate outside regulations or against them. This would only lead to the suppression of innovation and drag the UK further behind in the tech upheaval.

The regulatory sandbox provides for new business that intend to pioneer new financial services and tools that would benefit the consumers, to float their ideas with the regulators who would exempt from certain regulations, until proper regulation can be crafted to cover the new businesses.

Such an approach would be highly recommended to support Social Impact Bonds.

3.4 Expectations on the Implementation Process

Subject to the implementation of the above-mentioned frameworks, we hold expectations on the local development of SIBs as follows:

Quantitative v/s Quantitative Aspect of SIBs

The concept of SIBs revolves on catering strictly for quantitative metrics to assess success; the rational being that SIBs as legal and financial agreements should leave no room for interpretational ambiguity.

It is an unavoidable eventuality that some projects will fall out of the scope of SIBs due to their qualitative nature. However other projects would be able to seek inclusion by restating their goals. For example a cancer awareness campaign can be restated to focus on increasing detection rates and participation rates for testing.

This being said, we do not see the definition for the quantitative metrics to be affixed to general measurements or indexes. In the particular case of Mauritius, setting rigid barometers for the general implementation of SIBs would be counter productive to the required flexibility. A good analogy would be comparing SIBs to over-the-counter derivatives: the market is structured in such a way that you can enter into contracts on anything, but you need to adhere to the guidelines of the International Swap and Derivatives Association[23] (**“ISDA”**). The first step will be to focus on an equivalent of an ISDA for SIBs, which is to build guideline methodologies for building SIBs, and let the market determine itself its metrics.

Product and Market Development

As a new concept we do not expect, multi million dollar publicly listed issuances for SIBs at the development stage.

The way we foresee and recommend initial development is through a multitude of short term mini-bond[24] strictly for local projects. Issuances would range between 5 and 10 million Mauritian rupees, privately placed, whereby buyers will be buying to hold to maturity, all issued within the recommended regulatory sandbox. Secondary market transactions would remain the domain of private sales.

As the market develops, we will have: more organised, and proven service delivery organisations, which can undertake bigger projects; experienced underwriters for those SIBs; and a proper regulatory framework. From thereon we could be expecting bigger projects and more long term to be proposed for SIBs, and eventual public placements with the possibility of an active secondary market on a listed stock exchange.

Mauritius as a Global Hub for SIBs

On a long-term basis, we made consideration for the potential establishment of Mauritius as a global hub for SIBs issuance, given its strategic location.

As discussed in the paper, SIBs currently have a very novel and private nature with the earliest records dating 2014. There are limited examples on which to rely for SIBs development, which makes for the creation of a SIBs hub a pioneering endeavor at the national level that would echo on an international scale.

This would require cooperation at the international level, for which Mauritius will have to bring solid evidence that SIBs can work at the international negotiating table, hence the imperative to fist develop a solid and sustainable domestic market that can thereon be replicated at an international level.

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LEGISLATION

- The Income Tax Act 1995
- The Trust Act 2001
- The Securities Act 2005
- The Finance (Miscellaneous Provisions) Act 2016

NORTH AMERICAN CASE STUDIES

Rikers Island SIB 2012	**Sector** – Recidivism **Overview** – Preventive services to reduce re-incarceration rate among adolescent at Rikers Island Prison, modeled after the Peterborough SIB.
Utah SIB 2013	**Sector** – High Quality Preschool Program **Overview** – Early specialised education at Kinder garden level to reduce costs of special education requirement at primary and secondary levels.
New York State SIB 2013	**Sector** – Recidivism and employment **Overview** – Reduce recidivism and increase employment prospects for convicts.
Massachusetts SIB 2014	**Sector** – Recidivism **Overview** – Reduce recidivism and increase employment prospects for convicts for young men between 17 and 23.
Sweet Dreams SIB 2014	**Sector** – At-risk single mothers **Overview** – Support for single mothers to reduce future cost to the government in the future.

EUROPEAN CASE STUDIES

Peterborough SIB 2010	**Sector** – Short sentence offenders **Overview** – Preventive services to reduce re-incarceration rate.
Links4Life SIB 2012	**Sector** – Unemployment/NEETs **Overview** – Support for 14 to 19 years old to avoid disengagement from society.
ThinkForward SIB 2012	**Sector** – Unemployment/NEETs **Overview** – Improving school attendance, social behavior and progress to higher education.
GLA Homelessness SIB 2012	**Sector** – Homelessness **Overview** – Increase access to public services to homeless to reduce homelessness.
It’s All About Me (IAAM) SIB 2013	**Sector** – Adoption services **Overview** – Provide support for adoption to increase integration into new families and reduce social rejection.
Manchester City Council SIB 2014	**Sector** – Children in residential care **Overview** – Focus on foster care children to reduce risk of social rejection.
Juvat SIB 2014	**Sector** – Unemployment/NEETs **Overview** – Increasing employability of youngsters.
Belgium SIB 2014	**Sector** – Workforce empowerment **Overview** – Reduce unemployment among young immigrants in Brussels.

AUSTRALIAN CASE STUDIES

Newpin SIB 2013	**Sector** – Complex families & child welfare **Overview** – Reduce and prevent children from having to be placed in out of home care.
Benevolent Society SIB 2013	**Sector** – Complex families & child welfare **Overview** – Reduce and prevent children from having to be placed in out of home care

RESPONDENT PROFILE

Sector of Employment	Number
Finance	8
Industrial & Services	4
Social Services	8
International NGOs	3
Government	0

Professional Position	Number
Financial Controller	8
Non-Financial Managerial	7
Executive	3
Non Executive	5

The interviews were conducted among a cohort of 23 individuals representing the various potential participants in an experimental Social Impact Bond implementation. The respondents' profiles generally covered professionals with reliable academic and professional background, currently engaged in a variety of local industries that could be classified as follows:

- Professionals directly involved in the social services industry;
- Professionals indirectly involved in the social services industry;
- Financial controllers that controlled CSR allocation;
- Prospective local institutional and private investors; and
- Financial Service professionals.

End Notes

[1]Social Impact bonds and Social policy bonds form part of the Impact Bond family, i.e investment tools that have a social impact.

[2]Ronnie Horesh, 'Injecting incentives into the solution of social problems: Social Policy Bonds', 2000.

[3]Peterborough SIB is the first social impact bond that was implemented.

https://www.gov.uk/government/publications/social-impact-bond-pilot-at-hmp-peterborough-final-report

[4]Outcomes for Peterborough

https://www.gov.uk/government/publications/social-impact-bond-pilot-at-hmp-peterborough-final-report

[5]Takeover by the Ministry of Justice and transition to transformative rehabilitation.

https://www.theguardian.com/voluntary-sector-network/2014/may/01/social-impact-bonds-funding-model-sibs-future

[6]Millennium Development Goals Report 2015,

http://www.mu.undp.org/content/dam/mauritius_and_seychelles/docs/Procurement/Government-Report/Millenium%20Development%20Goals%20Final%20National%20Report%202015%20pdf.pdf

[7]Cost benefit of aid transparency – this report details how donors are looking for more transparency and efficiency in dollar deployment.

http://www.aidtransparency.net/wp-content/uploads/2010/06/1140-100407-Framework-for-Costs-and-Benefits-of-transparency-with-Annexes.pdf

[8]Figures from OECD that show a year on year decrease in funding for Mauritius.

http://www.oecd.org/dac/stats/statisticsonresourceflowstodevelopingcountries.htm

[9]Government Donors - At this stage of the development it was deemed better to focus on CSR donors who were smaller but more versatile in funding arrangements. We did not interview government donors, but did research their methodologies.

[10]International NGO Donors - At this stage of the development it was deemed better to focus on CSR donors who were smaller but more versatile in funding arrangements. We did not interview International NGP donors, but did research their methodologies.

[11]Data from the Corporate Social Responsibility Committee.

[12]We classify "Subsidiary organisations" as legal entities, incorporated by the donors or their affiliates to receive the CSR funds from the donors themselves and their affiliates.

[13]"Parrainage Style" refers to donors establishing a long-term relationship with particular charitable organisations, sponsoring their program and getting involved with the activities of the organisations beyond providing funding.

[14]Record of unspent CSR funds that are sent to the MRA consolidated fund.

http://defimedia.info/corporate-social-responsibility-rs-8904-million-unspent-private-sector

[15]Government Entities - At this stage of the development we have not considered government arms that carry social work as eligible service delivery participants in SIBs.

[16]Data from the Corporate Social Responsibility Committee.

[17]Data from the Corporate Social Responsibility Committee.

[18] Haiti Orphanage system after a surge in donations following the 2010 earthquake

https://www.ft.com/content/53536acc-ac60-11e6-9cb3-bb8207902122

[19]The United Nations has established a new fund, United Nations Social Impact Fund, which would make locally implemented SIBs eligible.

http://un.socialimpact.fund/

[20]Data from Budge Speech 2016/2017

[21]Proposal for a Social Impact Bond Act by representatives Young an Delaney of the US House of Representatives

https://www.congress.gov/bill/113th-congress/house-bill/4885

[22]Regulatory Sandbox – The regulatory sandbox aims to create a 'safe space' in which businesses can test innovative products, services, business models and delivery mechanisms in a live environment without incurring all the normal regulatory consequences of engaging in the activity in question.

https://www.fca.org.uk/firms/project-innovate-innovation-hub/regulatory-sandbox

[23]Interenational Swaps and Derivatives association – The non-profit association provide for guidelines to regulate swaps and derivatives.

http://www2.isda.org/

[24]Mini-bond – Mini bonds refer to corporate securities offered on a much smaller scale compared to regular securities, catering for smaller size issuers.

http://www.telegraph.co.uk/investing/bonds/what-you-need-to-know-about-mini-bond-problems/

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