



State of Michigan

Social Impact Bonds: Pay for Success Based Financing

Request for Information

Project Number #0071141113B0000535

Applicant:

**Victory Social Capital, LLC
Durham, NC**



October 23, 2013

Victory Social Capital, LLC

201 West Main Street
Suite #200
Durham, NC 27701

Brandon Samuel

**Department of Technology Management and Budget
DTMB Procurement**

2nd Floor, Mason Building
530 West Allegan Street
Lansing, MI 48933

Subject: **Social Impact Bonds: Pay for Success Based Financing**
Request for Information
Project Number #0071141113B0000535

Dear Mr. Samuel,

Victory Social Capital, LLC (VSC) enthusiastically responds to the State of Michigan's Request for Information for *Social Impact Bonds: Pay for Success Based Financing*.

We believe that we are at a critical juncture in our country's history, where the traditional *ex ante* Pay for Promise system is inefficient and out of date. We believe that an *ex post*, evidence based Pay for Performance system is an innovative means to both transfer risk away from government and provide a market-based incentive for social delivery success.

We are excited about the prospect of working with the State of Michigan and look forward to hearing back from you. Please contact us if you have any questions concerning our submission.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Scott Lipinski", written over a horizontal line.

Scott Lipinski
Partner

Victory Social Capital, LLC

Table of Contents

Executive Summary 1
Targeted Service Area..... 5
Intervention Strategy 6

Executive Summary

Victory Social Capital brings economic solutions to social issues. Through an agreed upon performance-based service contract, VSC will leverage private capital and a proven non-profit therapeutic community model to build a free, sustainable treatment and prevention infrastructure throughout Michigan.

VSC differentiates itself from current social financing innovations and intermediaries by being:

- 1) **Simple** – Performance-based contracts are an established contracting vehicle designed to bring accountability to spending.
- 2) **Sustainable** – Social enterprise based program covers a significant portion of expenses by internal revenue generating businesses.
- 3) **Economical** – Intervention is one all-encompassing organization, not a network of providers.

The bottom line is that Michigan, like other governments, has invested in and built a social services infrastructure that has defined costs, outputs and outcomes. Michigan's current social systems are output (ability to put an offender through prison) oriented with costs and demand spiraling out of control. Outputs, like putting an offender through prison, have high return or recidivism rates. Return rates compound the demand on the system and continue the vicious cycle of not addressing the root cause of the return rate. Shifting the system to drive outcomes (offender does not return to jail) at scale is expensive and risky.

VSC is able to assume risk and create significant economic opportunity because our model focuses on program sustainability through social entrepreneurship and has a track record of superior outcomes which leads to a reduction in recidivism.

Complex issues require dynamic solutions. VSC correlates financial returns to social outcomes and in doing so, incentivizes private capital and government to work towards a shared goal, the betterment of people's lives.

Target Service Area

Untreated, chronic substance abuse among offenders has been a major impediment to significantly curbing prison populations and corresponding costs. Outside of increased prison populations, the frontline attack approach associated with the "War on Drugs" has had limited results reducing substance abuse. The recurring cycle of criminal offense, conviction, punishment, release, and recidivism is all too common.

Intervention

Victory Social Capital believes chronic substance abuse is a multi-faceted disorder that requires a comprehensive solution. This is why experts in the field laud the therapeutic community (TC) model. TCs provide one of the most effective interventions for reducing substance abuse and subsequently recidivism. The TC approach views substance abuse as a disorder of the whole person and is built upon the concept of the “community as the method of change.”

Victory Social Capital has partnered with TROSA (Triangle Residential Options for Substance Abusers), a Durham, North Carolina-based modified therapeutic community, to enhance and expand TROSA’s operational model. TROSA relies on several evidence-based therapies, including work therapy. TROSA uses its six businesses to (a) provide opportunities for residents to learn marketable job skills as well as create a sense of work ethic and responsibility and (b) generate revenue to cover nearly 80% of its annual expenditures.

TROSA is a proven model that can be scaled to address the rising and costly demand for effective substance abuse programs. VSC’s projections show that when scaled, the TROSA model is nearly self-sustaining, which enables the program to have lasting effects long after the initial contract.

Pay for Performance

VSC’s business model builds on traditional alternative investment disciplines like venture capital and private equity but also incorporates recent impact investment innovations like Pay-For-Success (PFS) financing. VSC monetizes the economic value of positive social impact from prevention compared with the cost of operating remedial programs. VSC’s core activities are to create performance-based social service contracts and perform project management functions for non-profit service providers to drive the best possible outcomes.

Technical Requirements

Availability of performance measures for assessing outcomes

The criminal justice system has been an early target for Pay for Performance for good reasons, the direct relationship between performance and cost savings. We have identified several key metrics that can be used:

- (1) Recidivism
- (2) Sobriety
- (3) Job Placement
- (4) Homelessness
- (5) Education
- (6) Health Care

A strong evidence base indicating that the intervention model is likely to achieve the outcome targets

In addition to empirical evidence based support for therapeutic communities, TROSA leverages additional evidence based methods, including group therapy, Women in Recovery, educational workshops, DBT, anger management, Seeking Safety, peer mentoring, and individual counseling.

A sufficient and well defined participant base

Chronic substance abuse is rampant in the criminal justice system. The TROSA model specializes in helping individuals with chronic substance abuse recover from their addictions. TROSA partners with convicted offenders, judges, and public defenders to arrange treatment at TROSA as an alternative to incarceration. Approximately 40% of TROSA residents are either on probation or probated to TROSA. Sex offenders, arsonists, and individuals with certain serious physical and/or mental illness are the only offender segments that TROSA screens out of its program.

Ability to take the initiative to scale if results show that the initiative is working

Therapeutic communities have a track record of being replicated. The TROSA model has the ability to be replicated and scale according to demand. It is our mission to use the private sector model of injecting capital to catalyze growth. We believe pairing this model with a nearly self-sustaining social delivery, social enterprise is a synergistic combination that will truly revolutionize the way our country attacks some our most pressing social issues.

Clear and identifiable state budgetary savings

The costs and second and third order effects associated with chronic substance abuse are well documented.ⁱ Prison, court, and health care costs are good examples of the direct cost savings Michigan will realize when implementing VSC's offering. In addition, there are several other areas where the State will benefit that are more difficult to quantify, such as savings on foster care, added tax revenue, Medicare savings, etc.

Using Michigan's average daily cost to incarcerate an offender, average sentence served length, as well as published recidivism rates, we have estimated potential savings associated with diverting 1,000 offenders to a TROSA facility for 2 years (Table 1.). Assuming a 20% reduction in recidivism with the TROSA based intervention, our proposal suggests a savings of over \$100,000,000. This figure only represents the direct cost associated with incarceration.

Table 1. Potential Savings – 1,000 Substance Abuse Offenders Diverted to Treatment



Targeted Service Area

Recidivism & Chronic Substance Abuse

The dramatic growth of America's prison population is an all too familiar issue. The PEW Center on States reported in 2011 that one in 33 Americans is currently incarcerated, on probation or parole. The costs associated with this growth have been well documented. The states and the federal government spend approximately \$74 billion a year on corrections, the bulk of which is spent on prisons. State spending on corrections quadrupled during the past two decades, making it the second fastest growing area of State budgets, trailing only Medicaid.

Governor Snyder and U.S. Attorney General Holder have both recently acknowledged that smarter solutions to this epidemic are long past due:

*It is simply a better, smarter solution for Michigan to address offenders early on by **providing alternative treatment programs to those who commit crimes as a result of underlying addiction or mental health issues**.*

- Rick Snyder, Governor of the State of Michigan 3/12

*Today, a **vicious cycle of poverty, criminality, and incarceration traps** too many Americans and weakens too many communities. And many aspects of our criminal justice system may actually exacerbate these problems, rather than alleviate them.*

- Eric Holder, Attorney General of the United State 8/13

Chronic substance abuse has plagued our criminal systems for decades. The closed-loop cycle of substance abuse, crime, and incarceration has been well established. While policy makers have been overwhelmingly aware of this growing epidemic and have attempted to craft policies and invest in interventions to curve it downward, little progress has been made. We are faced with a challenge that cannot be addressed with a single silver bullet solution. A comprehensive solution that addresses all the hurdles associated with recovery (treatment, education, training, employment, housing, etc.) is needed.

As the nation's slumping economy continues to force States to do more with less, policy makers and tax payers are asking what the real outcome of corrections is. A key element of that analysis is the measurement of recidivism, or the rate at which offenders return to prison. The national recidivism rate is around 40%.ⁱⁱ That means that more than four out of 10 adult American offenders return to prison within three years of their release. Unchecked recidivism rates have caused the prison population and corresponding cost of care to spiral out of control.

The only way to break the costly cycle of recidivism is to break the strangle hold of addiction.

Over 70% of those in our national correction system have a substance abuse issue or were under the influence when committing the crime. Only 11% of those identified to have substance abuse issues received treatment while in the correctional system.ⁱⁱⁱ

Intervention Strategy

Victory Social Capital, LLC has partnered with TROSA , modified therapeutic community to combat this pressing need for chronic substance abuse treatment.

Therapeutic Communities (TC)

The first therapeutic communities were started in the United States during the 1940s and gained momentum, in part, due to the criticism of the existing mental health system. In the 1960s and 1970s, many within the psychiatric community adopted the concept for the treatment of substance abuse and interrelated mental health issues. The TC approach views substance abuse as a disorder of the whole person and is built upon the concept of the “community as the method.” Within these programs, the goals of the TC were “to promote freedom from alcohol and illicit drug use, to eliminate antisocial behaviors, and to affect a global change in lifestyle” (Sacks, Sacks, Harle, & De Leon, Homelessness Prevention Therapeutic Community (TC) for Addicted Mothers, 1999).

Triangle Residential Options for Substance Abusers (TROSA)

TROSA is a **modified substance abuse therapeutic community** based in Durham, North Carolina. Started in 1993 by Kevin McDonald, TROSA is a licensed, comprehensive, two-year residential substance abuse recovery program currently serving over 400 men and women located in Durham, North Carolina. TROSA has been recognized nationally, regionally, and locally for their innovative approaches to curing substance abuse.

TROSA operates a highly structured and disciplined program from several facilities in Durham and accepts substance abusers with one condition: they must have a strong desire to change their lives. Key elements of the program include vocational training, education, communication, peer counseling, mentoring, leadership training and aftercare. The program is provided at no cost to the individual. Graduates who remain in this area benefit from TROSA’s reputation and are respected for their accomplishment by neighbors and employers in addition to being mentors and guides to current TROSA residents. TROSA’s positive effects are compounding throughout Durham and North Carolina.

TROSA has 15 years of data that has demonstrated proven success. TROSA currently follows its graduates for one year after completion of the program although graduates are supported for life through outreach and job placement services. While government estimates predict that between 40 to 60% of substance abusers will relapse during the first year after treatment^{iv}, only 15% of graduates relapse during that time period and less than 5% receive new criminal charges. Additionally, 95% remain employed and 90% remain in housing (do not re-enter homelessness). These figures demonstrate that TROSA’s social enterprise model of substance abuse treatment provides an innovative, scalable, and effective method in helping address one the most significant challenges facing America.

Program activities are focused on four key areas:

- Vocational Training
- Clinical Services (group therapy, *Women in Recovery*, educational workshops, DBT, anger management, *Seeking Safety*, peer mentoring, individual counseling)
- Education (adult literacy, GED classes, college classes, computer training)
- Aftercare (resume building, interview skills, job search & placement, low-cost transitional housing, 1-year job-related transportation, select clinical services).

The cornerstone of TROSA's treatment philosophy is its vocational training program. Under its Organizational Motto of empowerment, ***"Each one, teach one"***, through a series of businesses (Residential Moving, Commercial Cleaning, Lawn Care, Catering, etc.), TROSA is able to train residents with marketable job skills as well as provide opportunities for residents to create a sense of work ethic and responsibility. TROSA is consistently voted best of the Research Triangle for moving companies. These newly developed skills and work ethic contribute to **100% full-time job placement** for program graduates. In addition to providing job skills, the revenue generated from its businesses covers nearly 80% of TROSA overall annual expenditure, leaving approximately 20% derived from cash donations, grants, and government contracts.

ⁱ National Center on Addiction and Substance Abuse at Columbia University

ⁱⁱ www.pewtrusts.org

ⁱⁱⁱ Substance Abuse and Mental Health Services Administration's (SAMHSA's) National Survey on Drug use and Health

^{iv} National Institute on Drug Abuse (NIDA)