

**SYRACUSE UNIVERSITY  
MAXWELL SCHOOL OF CITIZENSHIP AND PUBLIC AFFAIRS**

PAI 735  
State and Local Government Finance  
Professor Yinger

**CASE:  
LOCKUP QUOTAS FOR PRIVATE PRISONS<sup>1</sup>**

**Introduction**

Established in 1983, Corrections Corporation of America (CCA) claimed an ability to build and operate state and federal prisons with the same quality of service provided in publicly operated prisons, but at a lower cost. One year later, CCA was awarded a contract for a facility in Hamilton County, Tennessee, the first instance of the public sector contracting management of a prison to a private company. In 1985, CCA attempted to assume management of the entire Tennessee prison system, but that offer was rejected by the state legislature after facing strong opposition over CCA's growing reputation for cost overruns and inmate escapes. Despite this setback, the company garnered additional contracts in Texas, Tennessee, and Kentucky by the end of 1987. Other startups and more established corporations, such as Wackenhut Corrections Corporation (now the GEO Group, Inc.), also entered into the prison business.

Today, CCA and GEO Group collectively manage over half of the contracts in the United States, which resulted in combined revenues exceeding \$2.9 billion in 2010. CCA, as the largest private prison company, manages more than 75,000 inmates and detainees in 66 facilities. GEO Group, as CCA's closest competitor, operates slightly fewer. Smaller companies, including Management & Training Corporation, LCS Correctional Services, and Emerald Corrections also hold multiple prison contracts throughout the United States.<sup>2</sup>

Figures 1 and 2 summarize the role of private prisons in the American prison system.

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<sup>1</sup> This case was written by Professor John Yinger solely for the purposes of class discussion.

<sup>2</sup> The first two paragraphs are taken directly from Cody Mason, "Too Good to be True," The Sentencing Project, January 2012. So are the first three paragraphs in the next section. Available at: [http://sentencingproject.org/doc/publications/inc\\_Too\\_Good\\_to\\_be\\_True.pdf](http://sentencingproject.org/doc/publications/inc_Too_Good_to_be_True.pdf).

### Cost Savings?

Private prisons supporters assert that the private sector saves resources through greater efficiencies. These claims are supported by some reports showing that private prisons produce cost savings, largely through lower salaries and benefits by employing mostly nonunion employees. It is also argued that governments can benefit in the short term through the direct sale of correctional facilities to private companies and can save money when constructing new facilities through public/private initiatives, rather than solely through government funding. However, studies have shown these benefits to be mostly illusory.

A 1996 report by the U.S. General Accounting Office (GAO) looked at four state-funded studies and one commissioned by the federal government. The methodologies and results varied across the studies, with two showing no major difference in efficiency between private and public prisons, a third showing that private facilities resulted in savings to the state of seven percent, and the fourth finding the cost of a private facility falling somewhere between that of two similar public prisons. Another study also found significant cost savings associated with private prisons, but the GAO criticized the report for using hypothetical facilities in its comparisons. The authors noted that they could not definitively conclude that privatization would not save money, but also established that, "... these studies do not offer substantial evidence that savings have occurred."

Similar conclusions were reached in a 2009 meta-analysis by researchers at the University of Utah that looked at eight cost comparison studies resulting in vastly different conclusions. Of the eight studies, half of them found private prisons to be more cost-efficient. The other four were evenly split between public facilities being more cost-efficient and finding both types of prisons statistically even. This information led the researchers to conclude that, "...prison privatization provides neither a clear advantage nor disadvantage compared to publicly managed prisons" and that "...cost savings from privatization are not guaranteed." While not directly resolving the question of whether private or public facilities are economically superior, the report did find the value of moving toward prison privatization to be "questionable."

Given the lack of clear evidence on cost savings, along with examples of fraud and abuse by private prison contractors, some groups are vehemently opposed to any form of private prisons. For example, Lee Sanders, president of the American Federation of State, County, and Municipal Employees (AFSCME), recently said: "When you privatize – and you entertain companies to come in and make money – then their ambition, it seems to me, would be to keep people incarcerated rather than looking for alternatives.... We really think it's unconstitutional – that is an inherent responsibility of government. You don't want to put the profit motive into the privatization of prisons."<sup>3</sup>

Nevertheless, private prisons are here to stay, and policy makers must decide on the circumstances under which private prisons make sense and on the provisions that are needed to protect the public interest in contracts with private prisons.

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<sup>3</sup> <http://www.afscme.org/blog/for-profit-prison-lockup-quotas-put-taxpayers-on-the-hook-for-company-profits>

## Lockup Quotas

A controversial recent development is the use of “lockup quotas,” also called “bed guarantees,” which are provisions in a contract between a private prison company and a government that require the government to fill at least X percent of the prison beds in a private prison—or else pay the private prison company for empty beds to the extent that this quota is not met. The value of X varies from 50 to 100 percent in different contracts. Figure 3 shows the places with contracts in which X is 90 percent or more.

A recent study by In the Public Interest (ITPI), which is a non-profit organization that provides information on privatization and public contracting, examined the use of lockup quotas.<sup>4</sup> “Of the contracts that we reviewed,” the report says, “41 (65 percent) contained quotas. These occupancy requirements were between 80 percent and 100 percent, with many around 90 percent. The highest bed guarantee requirements were from Arizona, Louisiana, Oklahoma, and Virginia.... Arizona has three contracts that contain 100 percent occupancy guarantee clauses. Oklahoma has three contracts with a 98 percent occupancy guarantee provision, while a couple of Louisiana’s contracts contain occupancy requirements at 96 percent, and Virginia has one at 95 percent. All major prison companies, CCA, GEO Group, and Management and Training Corporation (MTC), have been successful in negotiating prison quotas in contracts.

“Interestingly, prison companies have also been successful at winning bed guarantee promises even after a contract that contains no such provision is executed. Many of these bed guarantee clauses were added after the initial contract was signed, usually in a contract amendment. This is consistent with the prison industry’s approach to revenue growth. In CCA’s 2010 Annual Report, the company explicitly cites ‘enhancing the terms of our existing contracts’ as one of the approaches it uses to develop its business. Additionally, bed guarantee clauses may be imposed completely outside the contracting process. [For example]..., CCA was able to insert a bed guarantee requirement for private facilities into the Colorado fiscal year 2013 state budget, completely circumventing the contract amendment process. The percentage of facilities that actually have bed guarantee requirements may be higher than an analysis of their contracts alone indicates.”

Key results from this report are summarized in Figures 3 and 4.

Virtually all the commentary on lockup quotas is negative. The report by ITPI argues that “These companies rely on occupancy guarantee clauses in government contracts to guarantee profits and reduce their financial risk, since the ability of private prison companies to ensure prison beds are filled generates steady revenues. These contract requirements are an important tool in private prison corporations’ efforts to maximize profits. Private prison companies have negotiated these clauses in both older existing contracts and newer amendments. They have even lobbied lawmakers to impose bed guarantees on prison facilities.... Private prison companies make no secret that high occupancy rates are critical to the success of their business. During a

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<sup>4</sup> In the Public Interest, “Criminal: How Lockup Quotas and “Low-Crime Taxes” Guarantee Profits for Private Prison Corporations.” Available at: <http://www.inthepublicinterest.org/sites/default/files/Criminal-Lockup-Quota-Report.pdf> .

2013 first quarter conference call, GEO Group boasted that the company continues to have ‘solid occupancy rates in mid to high 90s.’

“By contractually requiring states to guarantee payment for a large percentage of prison beds, the prison companies are able to protect themselves against fluctuations in the prison population. These provisions guarantee prison companies a consistent and regular revenue stream, insulating them from ordinary business risks. The financial risks are borne by the public, while the private corporations are guaranteed profits from taxpayer dollars.”

The ITPI report also is concerned that public officials often do not seem to be aware of the trade-offs involved between different types of contract provisions. “Private prison companies often attempt to lure governments into agreements with bed guarantee clauses,” the report says, “by promising a lower per diem cost. However, bed guarantees do not secure jurisdictions lower per diem rates, as evidenced by Arizona’s experience of per diem rates rising 13.9 percent even after the bed guarantee was added to the contracts. With better understanding of the per diem rates in private prison contracts in similar facilities in other jurisdictions, governments can negotiate reasonable per diem rates without resorting to bed guarantees.”

Finally, the ITPI report argues that “[b]ed guarantee provisions are also costly for state and local governments... [T]hese clauses can force corrections departments to pay thousands, sometimes millions, for unused beds — a ‘low-crime tax’ that penalizes taxpayers when they achieve what should be a desired goal of lower incarceration rates.” The ITPI report describes several cases of the “low-crime tax.” In Colorado, for example, lockup quotas for CCA were inserted as provisions in the state budget just when the prison population started to decline rapidly, in both public and private prisons, apparently with no change in the cost of the contracts. To be more specific, the ITPI report says that “In 2012, the state began a utilization study to analyze which facilities made the most sense to close, but did not want any to shut down any facilities until the formal analysis was complete. In response to these preliminary discussions, CCA threatened to close one of its private facilities. Behind closed doors and without any public hearings, CCA and the Governor’s Office and the Joint Budget Committee negotiated a deal. In exchange for keeping the facility open, the state agreed to a bed guarantee, which required Colorado to keep at least 3,300 prisoners in the three CCA facilities, at an annual rate of \$20,000 per inmate for the 2013 fiscal year. Instead of using empty bed space in its state-run facilities, the Colorado Department of Corrections housed inmates in CCA’s facilities to ensure they met the occupancy requirement. Colorado taxpayers must pay for the vacant state prison beds and for the per diem rate for inmates redirected to the CCA facility to fulfill the bed guarantee. The Colorado Criminal Justice Reform Coalition estimates that the deal cost the state at least \$2 million.”

Although the majority of the commentary on lockup quotas is negative, a large number of state and local governments have decided to include some form of lockup quota in their contracts with private prisons. The ITPI report contracts with 62 private prison facilities and, as noted earlier, found these quotas in 65 percent of them. This outcome may reflect lobbying by private prison providers, who are profitable enough to conduct extensive lobbying efforts and to provide large campaign contributions, but many governors support these quotas, ostensibly on the grounds that they make for good public policy. However, the National Governor’s Association

(NGA) has not taken an official position on this issue.

One foundation, the Prison Reform Advocacy Group, PRAG, thinks these quotas can save governments a considerable amount of money.<sup>5</sup> Frederick McHenry, president of PRAG, agrees with ITPI that lockup quotas shift some of the financial risks away from the private prison companies and onto taxpayers. However, McHenry argues that this is precisely the point: “Because lockup quotas lower a company’s financial risk,” McHenry says, “they lower the cost of providing private prisons and hence lower what a government has to pay for a private-prison contract. This is a fundamental market principle. People are willing to accept a lower average return in exchange for lower risk. The expected return on a low-risk asset such as a U.S. Treasury Bill, for example, is much lower than the expected return on a municipal bond issued to help fund a new elderly housing project with tenuous financial prospects. If lockup quotas do not save the government money, as appears to have been the case in some states, the problem is with the contract, not with the quota concept.”

“It is no wonder,” McHenry concludes, “that so many states and the federal government often include lockup quotas in their contracts with private prison companies. By lowering the risk for the private company, these provisions lower the cost to the associated government.” Mr. McHenry also has a very different interpretation of the events in Colorado than the version presented in the ITPI report. “The point of a lockup quota,” McHenry emphasizes, “is to shift the risk away from the contractor onto the contracting government. A government cannot on the one hand accept the risk and then, on the other hand, be upset when one of the possible outcomes in this risky situation, namely, empty beds in public prisons, actually comes to pass. Governments do not have to take on this risk, but if they do, they must live with the consequences.” McHenry’s recommendation is for governments to make sure that the price of a private prison contract is commensurate with the governmental risk imbedded in it. “The difference in price between a contract without and with lockup quotas, McHenry says, “should be equal to the cost of insurance against the risk that the quotas impose on the contracting government.”

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<sup>5</sup> PRAG and its president exist only in Professor Yinger’s imagination.

### **The Decision**

You have been appointed to chair a U.S. Justice Department Task Force on the use of lockup quotas. You have convened a meeting to discuss this topic, and have invited representatives from NGA, AFSME, ITPI, PRAG, and CCA to participate.

The objective of this meeting is to discuss the analytical issues connected with lockup quotas. These quotas obviously raise important political issues, as well. Many people are upset, for example, about the lobbying for lockup quotas conducted by the private prison companies. This meeting is not about these political issues. Moreover, many people do not believe that private prisons should be used at all. For the purposes of this meeting, however, the use of private prisons is not up for debate. Many state and local governments use them, and they appear to be here to stay.

Instead, this meeting is intended to produce guidance for elected officials who are thinking about contracts for private prisons by answering the following questions. Are lockup quotas a good idea? If so, under what circumstances? If not, why not? If a state or local government decides to use lock-up quotas, what provisions should be included in the contract?

You may, if you wish, prepare a brief (two-page) memo stating your views on this topic.

Figure 1.

**Prisoners Held in Private Prisons in the United States<sup>2</sup>**

	1999	2010	Change 1999-2010
Total Prison Population	1,366,721	1,612,395	+18%
Total Private	71,208	128,195	+80%
Federal Private	3,828	33,830	+784%
State Private	67,380	94,365	+40%

Source: Cody Mason, “Too Good to Be True,” The Sentencing Project, January 2012. So are the paragraphs in the next section. Available at:

[http://sentencingproject.org/doc/publications/inc\\_Too\\_Good\\_to\\_be\\_True.pdf](http://sentencingproject.org/doc/publications/inc_Too_Good_to_be_True.pdf).

Figure 2.

**Inmates held in custody in state or federal prisons or in local jails, 2000 and 2011–2012**

Inmates in custody	Number of inmates			Average annual percent change, 2000–2011	Percent change, 2011–2012
	2000	2011	2012		
<b>Total</b>	1,938,500	2,240,600	2,228,400	1.3%	-0.5%
<b>Federal prisoners<sup>a</sup></b>	140,100	214,800	216,900	3.9%	1.0%
Prisons	133,900	206,000	208,000	3.9	1.0
Federal facilities	124,500	176,200	176,500	3.2	0.2
Privately operated facilities	9,400	29,800	31,500	10.5	5.7
Community corrections centers <sup>b</sup>	6,100	8,800	8,900	3.3	1.1
<b>State prisoners</b>	1,177,200	1,290,200	1,267,000	0.8%	-1.8%
State facilities	1,101,100	1,197,800	1,170,200	0.8	-2.3
Privately operated facilities	76,100	92,400	96,800	1.8	4.8
<b>Local jails<sup>c</sup></b>	621,100	735,600	744,500	1.5%	1.2%
<b>Incarceration rate<sup>d</sup></b>	680	720	710	0.5%	-1.4%
Adult incarceration rate <sup>e</sup>	920	940	920	0.2	-2.1

Source: Lauren Glaze and Erinn J. Herberman, “Correctional Populations in the United States, 2012,” U.S. Department of Justice, Bureau of Justice Statistics, December 2013. Available at: <http://www.bjs.gov/content/pub/pdf/cpus12.pdf> .



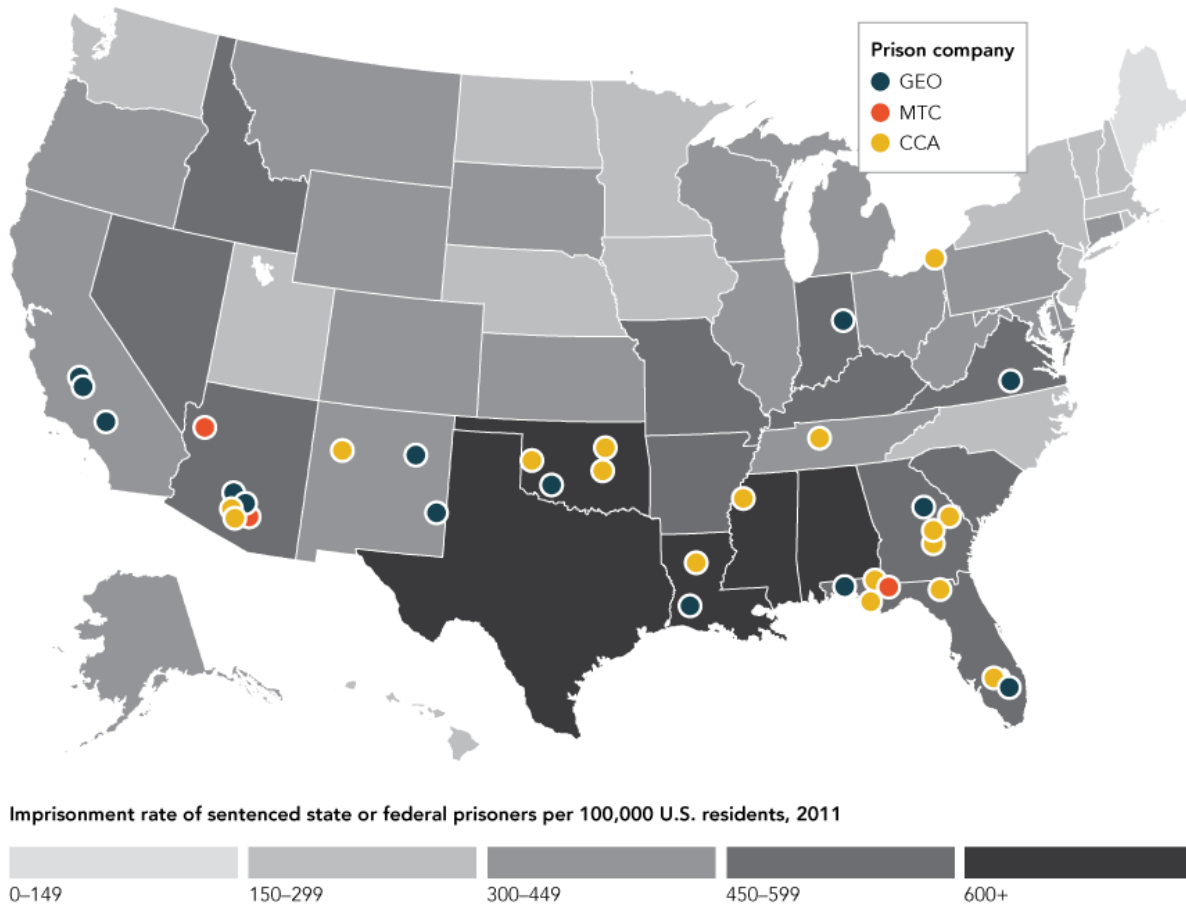
Figure 3.

A HUFFINGTON POST GRAPHIC



## Where Prisoners Are Guaranteed

Lockup quotas ensure that private prisons turn a profit. If a certain number of beds aren't filled, states must pay the prison companies for the unused beds — leaving taxpayers footing the bill for lower crime rates. Here are prisons with contracts that guarantee occupancy of 90 percent or more.

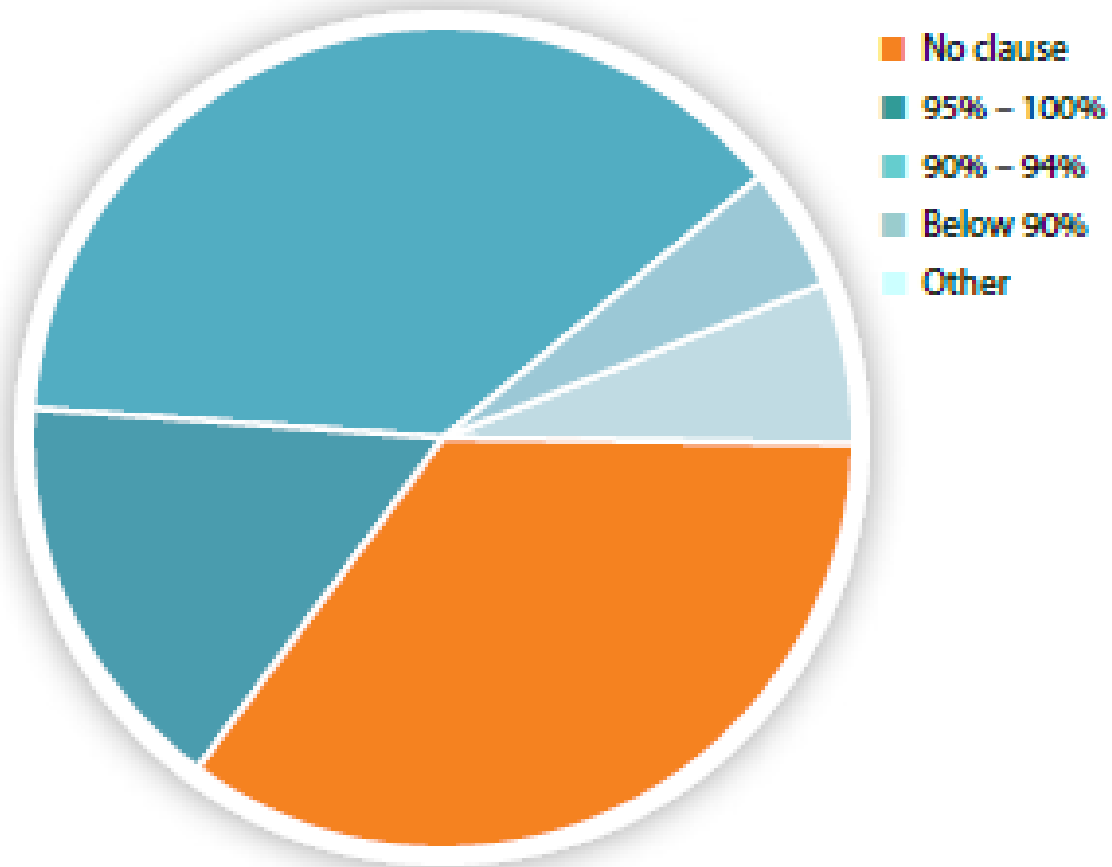


Sources: In The Public Interest, Bureau of Justice Statistics

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Figure 4.

### Occupancy Guarantee Provision



Source: In the Public Interest, “Criminal: How Lockup Quotas and “Low-Crime Taxes” Guarantee Profits for Private Prison Corporations.” Available at: <http://www.inthepublicinterest.org/sites/default/files/Criminal-Lockup-Quota-Report.pdf>