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Correction Privatization Memo

Introduction

Private prison, which is also called for-profit prison, is the correction facility operate by the third party that is contracted out by government agencies. There are two types of privatization: fully privatization and private-public partnership. With fully privatization, which only happened in the U.S, the U.K and Australia, the private companies have 100% control of the prisons and they are also in charge of supervising the inmates. For the private-public partnership, private companies provide peripheral services such as building maintenance, catering, and inmate training, about 20% of France prisons are considered public partnership. Despite the private prison could save state government million dollars a year, there is strong disapproval on private prison in New York State because of the negative reputation of private firms on maximizing profits while degrading the correction service. This paper, stands solely for economic development purpose, will discuss some economic concepts that helps to explain the motivation to allow private prison in New York State, then will examine the condition that makes it feasible for the New York State to introduce and regulate the private correction service in New York State.

Historical Context and Current State

The early history of private prison could be dated back to the Reconstruction period (1865-1876), after the Civil War, businessmen in the south seek for replacement of their slave labor force, the convict leases supplied those businessmen with prisoner labor until the early 20th century. In the 1980s, due to the rapidly expanding prison population, state and federal governments seek for a cost saving way to solve the overcrowding and rising cost problem, which is, allowing the private sector to get involve in prison service. The first US modern fully privatized prison was established in 1984 by CCA, the Correction Corporation of America. The first private prison locates in Hamilton County, Tennessee. Today, 30 state governments use private prisons¹. According to the *U.S. Department of Justice: Prisoners in 2014*, seven states held at least 20% population in private facilities. Since 1999, the uses of private prisons grew 90%. The overall private prisoner population constitute 9% of the total U.S. prisoner population.² By the end of 2010, an average government spending outside the state budget on correction in 40 states are 13.9%, New York spends 22.8% more on correction.³⁴ State correction expenditures were increasing during 1982-2001, but fluctuated between \$53.4 billion and \$48.4 billion in the last decade.⁵ Although many reports point out that there are no direct

¹ 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

² Prisoners in 2014, available at <http://www.bjs.gov/content/pub/pdf/p14.pdf>

³ Alaska, Oregon, Wyoming, South Dakota, New Mexico, Michigan, Tennessee, South Carolina, Mississippi, Massachusetts did not participate in survey.

⁴ The Price of Prisons: What Incarceration Costs Taxpayers, available at <http://www.vera.org/sites/default/files/resources/downloads/price-of-prisons-updated-version-021914.pdf>

⁵ State Corrections Expenditures, FY 1982-2010 available at <http://www.bjs.gov/content/pub/pdf/scefy8210.pdf>

evidences to prove the private prison contract saves the government spending on correction, coincidentally, the fluctuated period matches the private prison burgeoning period.

Economic Assumption and Implications

In the economic theory of competition, business operates more efficiently under privatization than under public ownership in competitive market. In a competitive market, there are many firms providing similar products and everyone in the market is price taker. Within a fix price range, consumers choose the most perfect product; When choosing from identical products, consumers choose the lowest price one. To win a market share, firms sell at the lowest price they can afford. To survive in such situation, firms attract consumers by innovating and differentiating their products. Here, state and local governments are the buyers and private firms looking for a contract are sellers. The idea to contract out partial government services to the private sector is based on the competition theory. When there is only one producer in the market, this is a monopoly market. A monopoly market absorbs consumer surplus and discourage innovation and development. To become more responsible to taxpayers and switch from a monopoly, governments decide to let more firms in the public service and produce together, here is how public services privatizing starts. Over recent decades, governments around the world successfully implemented several privatization policies in order to reduce budget deficits and increase efficiency. So far, we have mature private school system and private medication care services, both making profits under government regulations. Furthermore, governments are also contracting out garbage collection and weapon procurement.⁶ The weapon procurement privatization are alike the prison privatization case: both are superiority of privatization, and both are criticized by a lower quality outcome initially. Since the weapon procurement privatization is continuing to mature, introducing prison privatization into New York State is not impossible under a competition hypothesis.

The Opposition and Concerns

The in class case study on lockup quota almost come to a negative conclusion on private prison, but the prison privatization is not a bad project eventually. Most opposing news and reports of the private prison criticizing the high profit private companies earn and low quality service they provided.

1. High profit

People are over ignited by the high profit those private companies earn. As of 2015, the two largest private prison management corporations in the US, the CCA and the GEO Group together control over half of the private prisons. It is not difficult for us to find a news or review that is not emphasizing how CCA and other correction companies try to maximize profit and how much they earned: the occupancy guarantee requirement, which could lead to mass incarceration. However, a high profit does not necessarily relate to low quality service. In contrast, firms earning high profit now is evidence to prove that, they are able to provide a higher quality service and survive.

2. Low quality service

As other for-profit services, to maximize their profit and reduce cost, the private companies have strong incentive to sell low quality goods and services to customers in

⁶ The Proper Scope of Government, available at <http://www.jstor.org/stable/2951268>

order to cut the cost. In the private prison cases, the unqualified services are inhuman prisoner treatment, building insecure fence, and hired less professional handlers.

3. Staff turnover rate

Similar stories we could hear from other government contract services, the private prisons hire staff at the lower wage rate, they use mostly nonunion labor and control wages in order to save the cost by 20%, indirectly causing the former state-own prison officers unemployed.⁷ The employee turnover rates were 50% to 100% higher in private prisons than in public facilities.

In a rational view, private companies earning high profit should not be our first concern. The low quality service is our concern. Inmates receiving worse services in private prison lead to the discussion of prohibiting private prison in New York State. However, private prison does not cause the inhuman treatment, the incomplete contract establishment does. Government had a long history of contracting out relevant prison service to private firms including medical services, food preparation, vocational training, and inmate transportation. The services mentioned above eventually became mature and saved cost, so does the private prison service. To adopt the private prison, state and local governments need to have a complete and comprehensive contract with private firms to achieve the same outcome as government did before. If contracts are incomplete, the incentive for private firm to engage in cost reduction is typically too strong because he ignores the adverse effect on non-contractible quality. And the problem for government side is, the quality of service government wants, is hard to be fully specified.⁸ Having a complete contract stating a clear quality service private firms need to provide may solve this two-way problem.

Reasons for Prison Privatization

The state government contracts out prison services, not the justice decision. Under the condition when the contract controls quality and reduce cost, or in the situation where there is competition among the private firms, private prison does provide the society considerable extra benefits.

Reasons for introducing private prison are listed below:

1. Privatizing prison could serve at a lower cost, it reduces the resources needed to complete such job, saving us from bureaucracy, corruption, and human capital wasting. No matter who finally get the share of the profit from cost reduction, at least it lowers the resources input. For instance, to produce same quality service, government spend \$10 input to get \$10 outcome, a private company is able to provide same service at \$8 cost. Eventually, it cost the whole society \$2 less to get the same service.
2. Private enterprises are more vulnerable but stronger than state-owned enterprise. In one side, to win the government contract, private company needs to be highly competitive in the market; In the other side, it has to be more compliance to the regulation to maintain its "government membership". In other words, while pleasing the government, the contracted private company should also please the tax payers at the same time. One evidence is that, now more and more people draw attention on private prison industry,

⁷ The Danger of Private Prisons, available at <http://www.outsiderclub.com/the-dangers-of-private-prisons/215>

⁸ Hart, Oliver, Andrei Shleifer, and Robert W. Vishny. "The Proper Scope of Government: Theory and an Application to Prisons." *The Quarterly Journal of Economics* 112.4 (1997): 1127-61. Web

voices from tax payer drives the development of private prison company to a fair and transparent direction. Decades ago, inmates encounter unfairness or adversity in public prison was less likely able to complain. Nowadays, state government got the back of family and friends of prisoners in private facility, anything the private facility done imperfectly could be the excuse for government to penalize the private firms or suspend the contract, which builds a counterbalance environment relationship among taxpayer, government, and the private companies.

3. Privatizing public service in long run is good for technology innovation. Though in short turn, the high staff turnover rate in private sector terrifies current state employees, once a mature private correction industry integrates, the longer private sector workforce specialized on correction service, the lower wages they request for this job by exploiting the economies of scale.
4. State prisons have been financed through tax-exempt general obligation bonds, which request complex procedure and longer time to process in a democracy, but private firms usually financed from private revenue. State government avoid the finance risk in this segment.

Recommendations

In summary to the reasons above, it should be benefit to NYS to carry the proposal of introducing private prison operation under certain conditions.

1. Start with adopting the public-private partnership. The public-private partnership gives the state government some control of the prison, but it need not to care about all qualifications and responses to operate a prison. Contracting the catering and maintenances jobs out is less risky and less costly. Catering and maintenance services require little prison operation background for the contractors. And this half private method gives government a kind of retreat if decides to take the whole prison service back.
2. Prepare job retraining program for those state employees who will lose their jobs when private companies take over the prison. Wages difference between two sectors contribute to 15% of cost saving, thus, it is unlikely for the private enterprise to hire the state employee at the former rate. All the government need to do is to relocate and retrain the former employees.
3. Increase the prison industry competitiveness within the states. For example, before decide which firm to operate the prison, welcome every possible firm to turn in proposals. Firms compete to win the contract would try to provide identical service at lower price or better service within the same price range. Secondly, choose more than one companies to operate private prisons in the NYS, the one with better performance award privileges like partial tax exemption or priority to next contract renewal.
4. As contract cannot specify what to be done in every possible contingency, and at the time of contracting, future contingencies may not even be describable. In this case, government need is hard to define, and private firm lack of prison management experience is not as responsive as government prison management expert, to avoid current and future problems caused by incomplete contract, government list the services and quality that regular public prisons provide such as size of cell, frequencies of routine inmate medical care, daily nutrition, solidness of the fence, and career background of

chief handlers in the contract. The more detail the contract is, the easier for private prison to follow the rule and clearer for taxpayer to evaluate the private prison service when comparing to the public prison services.

5. Separate the jurisdiction decision with the prison location decision would lower the mass incarceration problem. Courts are independent when decide whether a person is guilty, and not affect by the contract.

Conclusion

In sum, a thorough prison privatization project seems difficult to implement in short time because of its complexity to define the government's need. But keep opposing to the privatization is not a solution. In a democracy, wealthy businesses are all politically active: ESMOR Correction Corporation evidently lobbied politicians and makes political contributions to receive contracts⁹ (*The New York Times*, July 23, 1995). In a condition that corruption and lobbying are unavoidable, getting prepared for privatization is more important than speaking for the state-own prison. To have a successfully introduction for private prison in to the New York State, governments should focus on the incomplete contract problem and have the cost reductions to be controlled through contract or competition.

⁹ A Prison Empire: How It Grew -- A special report.; Parlaying the Detentions Business Into Profit available at <http://www.nytimes.com/1995/07/23/nyregion/prison-empire-it-grew-special-report-parlaying-detentions-business-into-profit.html?pagewanted=all>