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UNITED STATES DISTRICT COURT

DISTRICT OF OREGON

PORTLAND DIVISION

PRISON LEGAL NEWS, a project of the HUMAN RIGHTS DEFENSE CENTER, Plaintiff, v. COLUMBIA COUNTY; COLUMBIA COUNTY SHERIFF'S OFFICE; JEFF DICKERSON, individually and in his capacity as Columbia County Sheriff, Defendants.	No. CV 12-71-SI DECLARATION OF LUCY LENNOX In Support of Plaintiff's Motion for Preliminary Injunction

I, Lucy Lennox, declare and affirm as follows:

1. I am over the age of 18 and I am competent to testify. The statements of fact contained herein are based on my own personal knowledge and belief.

2. I am a resident of the state of Washington.

3. On December 15, 2011, I visited the Prison Legal News website (www.prisonlegalnews.org) and printed multiple copies of the same legal article titled "The Failed Promise of Prison Privatization" to send to prisoners at the Columbia County Jail. I enclosed the printed articles in separate envelopes and sent them to specific prisoners at the Columbia County Jail in standard sized #10 envelopes with appropriate postage affixed to each one.

4. The Columbia County Jail rejected the articles I mailed and returned the rejected mailings to me, as described below:

I. Exhibit I is an envelope I sent to prisoner Steven Adams at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "CONTRABAND."

II. Exhibit II is an envelope I sent to prisoner Arthur Bates Jr. at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. There is a sticker on the returned envelope stating: "As of April 1, 2010 The Columbia County Jail ONLY ACCEPTS POSTCARDS, This applies to ALL incoming and out going mail."

III. Exhibit III is an envelope I sent to prisoner Toni Bertasso at the Columbia County Jail on December 21, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. There is a sticker on the returned envelope stating: "As of April 1, 2010 The Columbia County Jail ONLY ACCEPTS POSTCARDS, This applies to ALL incoming and out going mail."

IV. Exhibit IV is an envelope I sent to prisoner Daniel Butts at the Columbia County Jail on December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," and "REFUSE/VIOLATES SECURITY."

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V. Exhibit V is an envelope I sent to prisoner Robert Clement at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. There is a sticker on the returned envelope stating: "As of April 1, 2010 The Columbia County Jail ONLY ACCEPTS POSTCARDS, This applies to ALL incoming and out going mail."

VI. Exhibit VI is an envelope I sent to prisoner Anthony Deherrera at the Columbia County Jail on December 22, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "REFUSE/VIOLATES SECURITY."

VII. Exhibit VII is an envelope I sent to prisoner Kenna Haynes at the Columbia County Jail on December 22, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "REFUSE/VIOLATES SECURITY."

VIII. Exhibit VIII is an envelope I sent to prisoner Scott Lavelle at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "REFUSE/VIOLATES SECURITY."

IX. Exhibit IX is an envelope I sent to prisoner Billy Nelson at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "CONTRABAND."

X. Exhibit X is an envelope I sent to prisoner Samuel Oester at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the

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envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "CONTRABAND."

XI. Exhibit XI is an envelope I sent to prisoner Cindy Seastone at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," and "REFUSE/VIOLATES SECURITY."

XII. Exhibit XII is an envelope I sent to prisoner Barry Shaft at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL" and "RETURN TO SENDER," with a handwritten note that states "no envelope mail."

XIII. Exhibit XIII is an envelope I sent to prisoner William Temple at the Columbia County Jail on or about December 15, 2011, and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL" and "RETURN TO SENDER," with a handwritten note that states "no envelope mail."

XIV. Exhibit XIV is an envelope I sent to prisoner Timothy Turner at the Columbia County Jail on December 20, 2011 and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL," "RETURN TO SENDER" and "CONTRABAND."

XV. Exhibit XV is an envelope I sent to prisoner Alisha Vandolah on or about December 15, 2011 and the seven-page article contained in the envelope. The Jail returned the article to me. The returned envelope is stamped and marked "INSPECTED BY COLUMBIA COUNTY JAIL" and "RETURN TO SENDER," with a handwritten note that states "no envelope mail."

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5. Other than the returned envelopes, I did not receive any communications from the Columbia County Jail about the mail I sent to prisoners or why the Jail rejected my mail. Nor did I receive any information about how to challenge the Jail's decision to reject the articles I sent.

I declare under penalty of perjury of the laws of the United States of America that the foregoing is true and correct to the best of my knowledge.

DATED this 25 day of January 2012, at Spokane, Washington.

Lucy Lennox

Lucy Lennox

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CERTIFICATE OF SERVICE

I hereby certify that on January 31, 2012, I electronically filed the foregoing to the Clerk of the Court using the CM/ECF system which will send notification of such filing to the following:

- **Marc D. Blackman**
  marc@ransomblackman.com,pat@ransomblackman.com
- **Gregory R. Roberson**
  grr@hartwagner.com,cej@hartwagner.com
- **Lance Weber**
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EXHIBIT I

TO

DECLARATION OF LUCY LENNOX

L Lennox
4128 S. Hatch
Spokane, WA
99203

UNITED STATES POSTAGE
PITNEY BOWES
02 1P $ 000.64[0]
0003048470 DEC 15 2011
MAILED FROM ZIP CODE 99201

RETURN TO SENDER

INSPECTED BY COLUMBIA COUNTY JAIL

Steven Adams 201100 2552
c/o Columbia County Jail
9
St

NIXIE 970 4E 1 01 12/28/1
RETURN TO SENDER
ATTEMPTED - NOT KNOWN
UNABLE TO FORWARD
BC: 99203624428 *2029-10539-20

97051 99202 06244

The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

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competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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- The Failed Promise of Prison Privatization by Richard Culp, Ph.D. We have been experimenting with prison privatization in the U.S. now for over ...

or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT II

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4128 S Hatch
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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.

In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.

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The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

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Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT III

TO

DECLARATION OF LUCY LENNOX

L Lennox
4128 S Hatch
Spokane, WA
99203

SPOKANE WA 992
PM
21 DEC
2011

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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TO

DECLARATION OF LUCY LENNOX

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99203

RETURN TO SENDER

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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The Failed Promise of Prison Privatization

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The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

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competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue..

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT VI

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

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The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

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The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT VII

TO

DECLARATION OF LUCY LENNOX

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

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Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

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Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT VIII

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

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CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT IX

TO

DECLARATION OF LUCY LENNOX

L Lennox
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Spokane, WA
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INSPECTED BY COLUMBIA COUNTY JAIL
RETURN TO SENDER X
PERSON NOT HERE
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St. Helens, Oregon 97051

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning. Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

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After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT X

TO

DECLARATION OF LUCY LENNOX

9870.05 fa246305

L Lennox
4128 S. Hatch
Spokane, WA
99203

RETURN TO SENDER

UNITED STATES POSTAGE
PITNEY BOWES
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INSPECTED BY COLUMBIA COUNTY JAIL
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PERSON NOT HERE
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REFUSE/VIOLATES SECURITY

Samuel Bester 2011002123
c/o Columbia County Jail

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

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competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
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The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

EXHIBIT XI

TO

DECLARATION OF LUCY LENNOX

L Lennox
4128 S. Hatch
Spokane, Wa
99203

RETURN TO SENDER

UNITED STATES POSTAGE
PITNEY BOWES
$ 000.64⁰
0003048470 DEC 15 2011
MAILED FROM ZIP CODE 99201

INSPECTED BY COLUMBIA COUNTY JAIL
RETURN TO SENDER
PERSON NOT HERE
CONTRABAND
WSP FACILITY
MAIL VIOLATES SECURITY X

Cindy Seastone
c/o Columbia Co. Jail
90 [illegible]
S [illegible]

NIXIE 970 DE 1 00 12/20/11
RETURN TO SENDER
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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

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competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
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Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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EXHIBIT XII

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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EXHIBIT XIV

TO

DECLARATION OF LUCY LENNOX

L Lennox
4128 S. Hatch
Spokane, WA
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RETURN TO SENDER

SPOKANE WA 992
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C/O Columbia County Jail

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competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

Origins of the Artificial Market

Contracting out of noncustodial prison services such as medical care, food service, maintenance, education and mental health services has been practiced for a long time and with little controversy. Contracting out of custody services, for which there is no free market analogue, is much more controversial. The deinstitutionalization movement in juvenile corrections during the 1970s initiated a number of experiments in privatized services and custody for juveniles. A major step toward contracted custody of adults occurred when the Immigration and Naturalization Service (INS), the forerunner to today's Immigration and Customs Enforcement (ICE), decided in 1983 to partially outsource the detention of undocumented immigrants in its custody. In the summer of 1983, the INS issued a request for proposals and the newly-formed Corrections Corporation of America (CCA) submitted the winning bid.

Likewise, the community corrections movement in the adult system involved contracting out of the custody function in many low-security adult facilities. Minnesota passed the Community Corrections Act in 1971, and 25 states followed suit with similar legislation over the next 12 years. Community corrections legislation transferred funding from state-level departments of correction to local governments which, in turn, used the funds for halfway house programs and other services for lower-level offenders. Many jurisdictions turned to private contractors to operate these facilities.

In 1986, Management and Training Corporation (MTC) secured a contract to operate a community corrections facility in Eagle Mountain, California. Also in 1986, the State of Kentucky contracted out the development and operation of a 200-bed minimum-security facility in Marion County. Another newly-formed company, the U.S. Corrections Corporation, was awarded the contract. Similarly, the U.S. Bureau of Prisons (BOP) began contracting out the operation of low-security halfway house programs to the private sector during this time. Another early private prison company, Correctional Services Corporation, originally Esmor Correctional Corp., began business in 1989 with two contracts from the BOP to operate halfway houses in New York City.

These early entrants to the incarceration services market found a political climate supportive of privatization in several states, including Kentucky, Tennessee, Texas, Florida, Arizona, New Mexico and Louisiana. By 1994 there were approximately 20 companies actively seeking contracts to either build and manage company-owned prisons or manage existing facilities owned by federal, state and local jurisdictions.

The Supply Side of the Incarceration Services Industry

The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

The decade of the 1990s witnessed the rapid growth of prison privatization, consolidation of the industry and the cooling off of growth rates as the decade ended. The industry moved through the traditional life cycle stages of fragmentation to maturity during this period. The industry experienced tremendous growth from 1992 to 1998, averaging an increase in capacity of 36% each year. But from 1999 to 2006, growth declined to an average rate of under 4% per year. As market maturity is commonly defined as reaching a state of equilibrium marked by the absence of significant growth or innovation, the industry reached maturity as the new millennium began.

The shakeout stage of the industry is reflected in the difference between the companies doing business in 1996 and those doing business in 2011. In 1996, there were 14 companies with private prison contracts in the United States. Table 1 lists these companies, their rated capacity and their market share of U.S. private prison business. A common measure of the dominance of companies in a given market is the market concentration ratio (CR), or the percentage of total industry sales (or capacity, or employment, or value added

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.
In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.
At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

Richard Culp is an Associate Professor of Public Administration at John Jay College of Criminal Justice in New York City and the Coordinator of the Bachelor of Science in Criminal Justice Management program. He is also a member of the doctoral faculty in Criminal Justice at the Graduate Center of the City University of New York and serves as Deputy Executive Officer of the CUNY Criminal Justice Doctoral Program. Professor Culp's research has been published in Justice Quarterly, Journal of Contemporary Criminal Justice, Criminal Justice Policy Review, The Prison Journal and the Journal of Public Affairs Education.

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Contemporary Reader (pp.183-209). Boston: Jones and Bartlett Publishers (2010).

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The Failed Promise of Prison Privatization

by Richard Culp, Ph.D.

We have been experimenting with prison privatization in the U.S. now for over twenty-five years. The privatization idea originated out of a notion that the private sector, with its competition-driven efficiency and innovation, could operate prisons of higher quality and lower cost than the public sector. Create a market for incarceration services, the argument ran, and the market will work its magic, improving prison conditions and rehabilitative outcomes while saving the taxpayers millions of dollars. That market has effectively been created over the past quarter century and we have now arrived at a place where prison privatization has been studied extensively and evaluated rigorously.

Although hyperbole continues to propel prison privatization policy along, research findings are incontrovertible: even in the best private prisons, quality of prisoner care is no better than in public prisons and the cost advantage of privatization, which initially accounted for minimal savings, is steadily eroding as the private prison industry matures.
The big promises of prison privatization – less cost, higher quality – have simply not materialized. Despite these disappointing results, prison privatization advocacy maintains traction in diverse jurisdictions as policymakers from Ohio to Florida and from Maine to California seek expedient solutions to budget shortfalls triggered by a lingering great recession.

In retrospect, it should come as no surprise that prison privatization would fail to live up to its promises. There are several reasons for this. First, free market solutions to social problems like crime assume, after all, that there are "free" markets for appropriate services. However, there is no such thing as a natural market for the services provided by private prison companies. On the contrary, the marketplace for incarceration services is created by the government, for the government. It is an artificial market. Many of the services that have been privatized by government (e.g., custodial services, food preparation, medical care) are provided by the private sector independently of the government's decision to privatize or not. There is a free market analogue for many kinds of services that governments routinely provide. Other fields such as education and health care, for example, have an active market of existing nonprofit and for-profit providers willing to sell educational and healthcare services to a huge market of potential buyers that includes both individuals and governments.

The prison business is fundamentally different in that no one can freely purchase incarceration services as a private individual. There is no natural market for incarceration services. The power to incarcerate someone – to hold a person against his or her will – is a defining characteristic of the state. The government holds a monopoly over the legitimate use of physical force and the power to incarcerate. Only the government has the legitimate power to restrict a citizen's liberty; individuals are prohibited by law from incarcerating another person under "false imprisonment" statutes. The government can delegate this power on a limited basis – for example, "shopkeeper's privilege" allows merchants to temporarily detain suspected shoplifters. But long-term incarceration is a different matter. The only potential buyers who can legally purchase incarceration services are the government jurisdictions that have custody over indicted, convicted or detained persons. In order to privatize its incarceration function, the government has had to create a market since one does not and cannot exist without its direct intervention.

Secondly, the development of the private prison industry has resulted in a highly concentrated producer market where only four companies control over 90% of the incarceration services business. Economic theory tells us that when production is highly concentrated in very few companies, the market becomes an oligopoly, a market situation that is inherently less competitive and innovative than a market with more broad-based representation. An oligopoly is characterized by interdependence, avoidance of

competition and a rigid attachment to the status quo among the leading firms.

A third part of the story is that government itself unwittingly stifles innovation in the private prison industry. Since the only legitimate customers of prison companies are the jurisdictions that can indict, convict or otherwise detain people, the potential customer base for incarceration services is very limited. In practice, this has led to a situation where only a handful of customers, an oligopsony in economic terms, has come to dominate the customer base. The limited number of customers serves to dissuade private prison companies from conducting research and development into innovative correctional programming, as the tiny customer base tends to demand only those services that mimic what the governments themselves are accustomed to providing.

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The traditional industrial life cycle model suggests that new markets move through a process marked by four stages: fragmentation, shakeout, maturity and decline. The fragmentation period occurs when the industry is new, many entrepreneurs enter the market, and they operate at low volume and tend to serve narrow geographic areas. Eventually, a shakeout period occurs as some companies become more efficient and the less efficient ones fail to stay in business. Growth and competition are strongest during this period, as are the profits of the largest companies. The industry reaches maturity when growth slows and surviving companies try to solidify their positions in the industry. At some later time, the industry moves into decline as the demand for the product or service drops and companies seek new ways to recover profitability.

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or physical output) contributed by the four leading firms ranked in order of market share. A market is considered to have a high CR when the four leading firms control over two-thirds of market share, a moderate concentration when the ratio falls between one-third and two-thirds, and a low concentration when the top four companies control less than a third of total market share.

The four-firm market concentration ratio of the private prison industry was 86% in 1996, a significantly high level of concentration. But by the end of 2011 only seven companies remained in the private prison business, and the market share of the top four firms increased to 92% (see Table 2).

Acquisitions and Ethical Challenges

The rise in concentration ratio means that the industry as a whole has become less competitive. Five of the companies that disappeared between 1996 and 2011 (U.S. Corrections Corporation, Correctional Services Corporation, Cornell Corrections, Inc., Fenton Security, Inc. and Correctional Systems, Inc.) were acquired by larger companies. Four other firms went out of business (Bobby Ross Group, Capital Correctional Resources, Dove Development Corporation and Maranatha Production Company, LLC). Three newcomers, LaSalle Southwest Corrections, Louisiana Corrections Services and Emerald Companies, are small and regionally-based in Texas and Louisiana. A review of the ongoing concentration in the market is illustrative of shakeouts in the industry and of some of the ethically-challenged behavior that can attend to the process of profit seeking. The largest company – Corrections Corporation of America – acquired the third-ranked company, U.S. Corrections Corporation, in 1998. U.S. Corrections, based in Kentucky, had much in common with Tennessee-based CCA. Both companies were founded by entrepreneurs who were well connected with the political establishment in their state. One of CCA's founders, Thomas W. Beasley, was a former chair of the state Republican Party and managed the successful 1978 gubernatorial campaign of Lamar Alexander. Honey Alexander, the governor's wife, was an early investor in CCA. U.S. Corrections Corporation, based in neighboring Louisville, did all of its business in Kentucky prior to 1995. Executives of the company contributed over $77,000 to political campaigns in the state between 1987 and 1993, including $23,000 to Governor Wallace G. Wilkinson and his wife Martha.

Clifford Todd, the CEO of U.S. Corrections, was implicated in a payoff scandal involving the company's contract to run the county jail in Louisville. He was arrested by the FBI in 1994, pleaded guilty to mail fraud and was sentenced to 6 months in jail and fined $250,000. He sold his stake in the company for $15 million in 1994. At the time of the buyout by CCA, U.S. Corrections owned a total of four facilities in Kentucky, Ohio and North Carolina with a capacity of 5,275 beds, and had contracts to manage publicly-owned facilities in Kentucky, Florida and North Carolina with a capacity of 5,743 beds.

The second-largest company in 1996, Wackenhut Corrections Corporation (WCC), was formed in 1984 as a subsidiary to security firm Wackenhut Corporation, which was founded by George Wackenhut, a former FBI agent. Over the ensuing years, WCC grew to become one of the largest private prison companies in the world. The company began providing residential services for at-risk juveniles and young adults under the Job Corps program. WCC went public in 1994 (with Wackenhut Corporation as the majority shareholder). In 2002, the Danish company Group 4 Falck merged with the Wackenhut Corporation and, indirectly, became the owner of 57% of WCC's stock. In 2003, WCC bought out Group 4 Falck's interest in the company and changed its name to the GEO Group, Inc. The GEO Group acquired the industry's seventh-largest company, Correctional Services Corporation (CSC), in 2005 and Cornell Corrections, the fifth-largest company, in 2010.

Founded in 1989, CSC operated under several different names, including Esmor Correctional Services, Inc. The company was founded by the owners of a welfare hotel in New York City and began its prison business operating halfway houses under contract with the BOP. CSC also managed the INS Detention Center in Elizabeth, New Jersey, remembered best for a June 1995 riot in which 300 detainees took over the facility in protest of poor conditions of confinement. Esmor staff fled from the detention center, leaving order to be restored by federal, state and local law enforcement officers. The INS closed the facility after the riot, noting that CSC guards had abused detainees, gave them spoiled food and deprived them of sleep. The facility was reopened in 1997.

Later, in 2003, CSC was fined $300,000 by the New York State Lobbying Commission for failing to report free transportation, meals and gifts given to a dozen state legislators from Brooklyn and the Bronx. The fine was the largest the state had ever imposed on a company for violating the state's lobbying laws. In May 2008, the Securities and Exchange Commission (SEC) filed charges against three Fort Lauderdale, Florida physicians, alleging insider trading in GEO Group's 2005 acquisition of CSC. According to the complaint, one of the three worked as a consultant to GEO and had a son who worked in GEO's finance department, where he allegedly learned of the pending deal. The three were charged with illegally purchasing $390,000 in CSC stock before the acquisition. Two of the defendants entered into settlement agreements while the third was cleared of the charges.

Another GEO acquisition, Cornell Corrections, Inc., had been the third-largest private prison company in 2006, with 8% of industry market share. Incorporated in 1994, the company built its business primarily with youth services and community-based rehabilitation programs for

adults. Pirate Capital, LLC, a hedge fund firm, acquired a 13% interest in Cornell in 2004, becoming the company's largest shareholder, and replaced several board members and the company's CEO with financiers more oriented toward short-term growth. Pirate Capital unloaded its shares of Cornell in 2006 in the midst of an SEC investigation over its stock sales practices, several bad investment decisions and company downsizing. The company warned its stockholders in 2009 of looming problems in managing indebtedness of some $303 million. GEO Group bought Cornell, along with its debt, in 2010.

Management and Training Corporation (MTC) is the third-largest company currently providing incarceration services. MTC is a privately-held Utah-registered company that gained expertise in working with at-risk young people as a major provider of Job Corps programs. The company first entered the private prison market in 1987 when it received a contract to manage the Eagle Mountain Community Correctional Facility in Desert Center, California (which experienced a major riot that resulted in the deaths of two prisoners in 2003). MTC expanded slowly and steadily since 1987 and now runs a total of 20 correctional facilities in Arizona, California, Florida, Idaho, New Mexico, Ohio and Texas.

The company's generally positive reputation as a job training provider has been tarnished by its corrections experience. In 1997, MTC hired the former director of the Utah Department of Corrections, Lane McCotter, as Director of Corrections Business Development. McCotter was well connected in pro-privatization states, having served as director of both the Texas Department of Criminal Justice and the New Mexico Corrections Department before serving as the corrections head in Utah. He left the Utah DOC job in the midst of an investigation over the death of a prisoner with schizophrenia who had been shackled to a hard plastic chair for the final sixteen hours of his life.

In 2003, MTC's Santa Fe, New Mexico facility was under investigation by the U.S. Justice Department for unsafe conditions and poor quality prisoner medical care while McCotter was employed with the company. Nonetheless, that same year he was appointed by Attorney General John Ashcroft to serve on a U.S. Department of Justice team commissioned to assess and implement a plan for rebuilding Iraq's criminal justice system. The team's final act before leaving Iraq was to conduct a ribbon cutting ceremony at the refurbished Abu Ghraib prison, a centerpiece of their corrections planning.
Although the facility was empty when McCotter left Iraq, the work of the committee of experts was indelibly stained by the infamous events that subsequently occurred at the prison and from on-going human rights abuse allegations in prisons under the direct supervision of other committee members.

MTC was also involved in a failed experiment in prison privatization in Canada. In 2001, the company won a five-year contract to operate the Central North Correctional Centre (CNCC) in Ontario as part of a pilot project to compare operations of the CNCC facility with a similar publicly-run prison, the Central East Correctional Centre. The government hired PricewaterhouseCoopers to evaluate the two prisons across a variety of dimensions. The evaluation found that the public prison outperformed the MTC facility overall. While the MTC prison was cheaper to operate and provided a greater variety of programming than the government facility, the public prison rated significantly better on security, recidivism rates, health care and community impact. Based on the results of the experiment, Ontario decided to turn management of the privatized facility over to the public sector.

Community Education Centers (CEC), incorporated in 1996, rounds out the quartet of companies that control 92% of the current incarceration services market. Like MTC, CEC is a privately-held company whose finances and governance structure are much less transparent than is the case with publicly-held companies. Until a few years ago, CEC's business was concentrated in providing community-based residential, re-entry and rehabilitative services to offenders, mostly in New Jersey and Pennsylvania, but the company moved into the secure incarceration services business with its acquisition of CiviGenics in 2007.

CiviGenics was founded in 1995 in Marlboro, MA by Roy Ross, the former president of Spectrum Health Systems, Inc., a nonprofit company that provided drug and alcohol treatment services for prisoners in the Massachusetts Department of Corrections. Ross arranged a contract for CiviGenics to provide management of Spectrum's Massachusetts in-prison treatment programs. In 1996, CiviGenics acquired Fenton Security, Inc., a small company that had management contracts to operate two county jails in Colorado. Tom Rapone, a former Secretary of Public Safety in Massachusetts, joined CiviGenics as the firm's Chief Operating Officer. CiviGenics expanded its secure custody operations and by 1998 operated several small jail facilities, employed more than 1,000 staff and had revenues of more than $30 million.

In July 1999, the Ohio Department of Rehabilitation and Correction (ODRC) awarded CiviGenics a $14.9 million contract to operate the newly-built North Coast Correctional Treatment Facility (NCCTF) in Grafton. However, the ODRC elected not to renew its contract with CiviGenics when the contract expired in July 2001, citing problems with high staff turnover (including five different wardens in its first 18 months), repeated failure to maintain minimum staffing levels and problems with over-billing the state for positions that remained uncovered. The ODRC subsequently awarded the contract to MTC, which continues to operate the NCCTF facility.

In 2004, the Massachusetts State Auditor completed an audit that found Spectrum Health Systems had misused $17.4 million in state money, with $10.2 million of the total amount involving excessive payments to CiviGenics. The matter was settled in January 2007 in an agreement that required CiviGenics to repay the state $3.4 million and Roy Ross to repay $650,000. With its acquisition of CiviGenics in 2007, CEC became the fourth largest private prison company in the U.S.

The Demand Side of the Incarceration Services Industry

The demand side of prison privatization, like the oligopoly of private prison companies, is also highly concentrated. The potential customers in the private prison market are government agencies at the federal, state and local level that operate jail, prison and detention programs. At the federal level, the Bureau of Prisons, the U.S. Marshals Service and Immigration and Customs Enforcement all manage a variety of custody facilities. The four branches of the military also operate facilities for military personnel sentenced under the Uniform Code of Military Justice. Of course, the 50 states and the District of Columbia each have departments of correction.

According to the Bureau of Justice Statistics, there are some 1,821 state and federal correctional facilities, not counting facilities operated by the U.S. Marshals Service and ICE. At the local level, counties and cities operate about 2,875 jail facilities in the United States. In sum, the potential consumer base of the private prison industry numbers somewhere in the area of 4,700 facilities.

After over 25 years of correctional privatization, there are fewer than 200 private correctional facilities in the United States – only about 4% of all facilities. The federal government is the most actively involved in privatization, with 16.3% of federal prisoners serving time in private facilities. State governments are next, with 6.6% of state prisoners in private facilities. However, whereas 60% of all correctional facilities in the United States are at the local level, only about two dozen city and county jurisdictions (1.7% of the total) contract with private companies to operate their jails and detention centers.

In practice there are very few buyers of privatized incarceration services, and the federal government is the largest single customer. Between 2000 and 2008, the number of state prisoners placed in private prisons increased by about 25%, from 75,018 to 93,537. In the federal system, however, the number increased from 15,525 to 32,712, or about 110%. During the same period, the number of states placing some portion of their prisoners in private facilities actually declined from 30 states to 27.

There are in practice only fifty-four "customers" buying incarceration services from the private prison industry – the three federal agencies, twenty-seven state departments of correction and two dozen local jurisdictions. Within this small customer base, the federal government plus eight states (Texas, Florida, Arizona, Oklahoma, Colorado, Tennessee, California and Mississippi) collectively account for more than 70% of all private prison business. In effect, the market of buyers constitutes an oligopsony, or a market form in which only a few customers buy a certain good and therefore possess the power to affect pricing. The two largest publicly-traded private prison companies recognize their dependency on a limited number of governmental customers as a threat to their profitability and include a warning to stockholders to that effect in their annual reports.

At CCA, just three federal government agencies, the BOP, ICE and the U.S. Marshals, accounted for 43% of the company's total revenue for fiscal year 2010, or $717.8 million. The state of California, which is placing thousands of prisoners out-of-state in an effort to reduce in-state prison populations, provided 13% of CCA's total revenue for fiscal year 2010, or $214 million. GEO Group reports that while they have a total of 45 governmental clients (customers), 4 of those clients accounted for over 60% of their U.S.-based revenue (BOP, ICE, U.S. Marshals and the State of Florida). Among those, the three federal agencies combined are responsible for 53% of GEO Group's total U.S. revenue.

The oligopsony of governmental consumers serves to discourage innovation. In practice, government purchasers of incarceration services have required that private prison companies simply duplicate policies and procedures practiced in public prisons, to the effect that the standard operating procedures of most private prison programs closely mirror those of public prisons in the same state. Notably, none of the companies have distinct and viable research and development departments as would be expected in an industry that values innovation. Private prison companies encourage the adoption of public prison practice, rather than the development of innovative practice, by actively recruiting management-level staff from within the public sector.

As a case in point, a review of the background of CCA's facility management staff suggests a widespread practice of mining the public corrections system for managers. Among the wardens of 63 of the company's correctional facilities, nearly two-thirds formerly worked in state departments of correction (36 wardens) or the federal BOP (5 wardens). The most warden-rich jurisdiction was the Texas Department of Criminal Justice, from whence 28% of all CCA wardens were recruited. These experienced staffers bring a degree of order and control to the company's private prisons, but they are not likely to be hired for their spirit of experimentation and innovation.

Arguably, private prisons are not looking to be innovative unless it is a way of cutting costs. The most common way for these companies to make money from government contracts is

by reducing personnel expenses. Because labor represents about 80% of the operating cost of a prison, much of the cost savings in private prisons results from paying private correctional officers less than comparable public correctional officers. But this advantage begins to erode in a market where private companies are dependent upon contract renewals (with more experienced staff) rather than new facilities (with new, entry-level staff). Even as labor rates vary among the states, public sector correctional officer starting salaries average $28,000 across all states with a (one standard deviation) range between $23,000 and $34,200. By comparison, the Bureau of Labor Statistics reports a mean annual salary of $42,270 for all occupations in the United States (in May 2008). Public sector prison staff salaries are very low already, suggesting that it is not easy for the private sector to continue to undercut the government in personnel costs.

Conclusion

The increasing concentration of market share among the top four companies and the declining number of companies in the incarceration services market mean that governments considering the privatization option will find a decreasing competitive environment when seeking contract bids. In 1995, for example, a total of seven companies submitted bids in response to a Arkansas Department of Corrections request for proposals for two new privately-operated prisons. In contrast, a 2006 request for proposals to manage a private prison in Pennsylvania yielded only two bidders. With market maturation and increased concentration, it is increasingly difficult for new companies to get into the business and for marginal performers to stay afloat.

Oligopoly theory and industry life cycle theory suggest that the remaining companies will be less competitive overall, seeking interdependent relationships with their competitors to help secure their position now that industry growth rates have cooled. As this scenario continues to unfold, any possibility of meaningful cost savings from privatization will decline over time. A recent study of private prison costs in Arizona found that this has already occurred, as the cost of incarcerating minimum-security prisoners has reached parity between state prisons and private prisons while the cost of housing medium-security prisoners is now actually lower in state prisons than in private facilities.

The private prison industry bears a fair share of the responsibility for not registering a better showing in research results. Despite the fact that it has hired away from the public sector many "best and brightest" correctional staff, the industry's penchant for financially rewarding its executives and top managers has drained resources that could have been devoted to program research and development.

Governments have also played a role in the failure of private prisons to perform better, particularly in the area of program quality. As an oligopsony, governments hold the power to be more demanding in the area of performance yet have systematically failed to do so. In the main, contracting governments have simply abdicated demand for increasing program quality, settling for an illusory decrease in program costs. Given the history of "iron triangle" relationships that intertwine the private prison industry and government officials, this failure is perhaps not surprising.

One of the more depressing statistics to emerge in criminal justice in recent years is the fact that two-thirds of released prisoners are re-arrested within three years. Enlightened government officials around the country have realized that they can reduce correctional expenditures only by focusing their efforts on reducing recidivism, not by building or contracting for more prison space. Government jurisdictions that are having the greatest success in reducing correctional expenditures are those that are turning to evidence-based practice to guide sentencing decisions and devoting correctional resources toward programs proven to reduce recidivism. Prison is not one of them. In enlightened jurisdictions, incarceration rates are beginning to decline.

As this trend continues, the private prison industry will eventually enter the fourth stage of the industrial life cycle – decline – and will begin shedding some of its capacity. Some companies have already sighted this trend on the horizon and have begun developing alternative business opportunities in areas such as electronic monitoring and prisoner health care. For those government agencies with heavy reliance on private prisons, decline in the industry will pose new problems as companies shed unprofitable contracts and simply walk away. Albert Einstein suggested that insanity is doing the same thing over and over again and expecting different results. If a quarter century of experience with prison privatization has not led to better quality and cost outcomes, it is time to take a more sane approach.

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