

Public/Private Financing of California's Prisons and Jails

Mary Sutton

Antioch University Los Angeles

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President Obama recently acknowledged the mishap of the United States' incarceration policies that led to the incarceration of almost 2.5 million people, mostly poor people and/or people of color, over the last thirty years—"at a crippling cost to them, their families and communities, as well as to the taxpayers and society as a whole" (New York Times, 2015). Former President Clinton responded by admitting he played a role in the acceleration of incarceration rates, and that he was wrong when he signed the harsh anti-crime legislation into law in 1994 (Baker, P, 2015).

These public statements, none too soon, reflect the growing social awareness that mass incarceration has caused great harm to millions of people. Many reports and research generated over the last decade discuss methods and strategies to reduce incarceration, which are more humane, more cost effective, and increase public safety (Vera Institute, 2013; Public Policy Institute, 2015). Yet federal, state and local governments continue to disavow these reports and research and work closely with the public and private prison industry to propel the construction of prisons and jails forward without regard to the accumulating financial, environmental and human costs. This literature review will address the multi-faceted financial arrangements that the State of California and Counties across the State, specifically Los Angeles County, continue to maneuver to ensure that billions of dollars continue to flow into the construction and operation of prisons and jails—rather than investing in alternatives that support people coming home from prison or jail.

California built twenty-two new prisons between 1980 and 2005. The prison population in California reached its peak in 2007 when there were almost 180,000 people locked up in the

state's thirty-three massive cement and steel prisons. Each state prison was filled with twice the number of people that it was designed to hold. The "Golden Gulag" written by Ruth Wilson Gilmore and "Prison Profiteers," edited by Tara Herivel and Paul Wright, both published in 2007, offer detailed descriptions of how states around the country manipulated financing of public prisons and jails through private tax-free investments. The last time California taxpayers voted to fund new prison construction was in 1982 when they approved the sale of \$495 million in general obligation bonds (GOBs). Since that time, taxpayers have rejected legislation proposing to build new prisons and jails (Gilmore, 93). "No state has built a new prison with general obligation bonds since the turn of the century, and few have put the question to voters." In 2002, voters in Maine rejected a \$25 million prison plan; in 2006, California Governor Arnold Schwarzenegger did not receive support for a \$2.6 billion prison from his own party (Pranis, 38). In Kevin Pranis' "Doing Borrowed Time: The High Cost of Backdoor Prison Finance," he argues:

"Declining public enthusiasm for costly prison expansion plans has closed off traditional options for financing new prison construction...this trend has created new opportunities of a cottage industry of investment bankers, architects, building contractors, and consultants to reap large rewards with "backdoor" financing schemes. A review of recent prison, jail, and detention expansion initiatives shows that federal, state, and local governments are using backdoor financing mechanisms to borrow hundreds of millions of dollars to build facilities that the public does not want and cannot afford" (Pranis, 36).

Lease revenue bonds (LRBs) can be sold without public approval because, unlike GBOs. LRBs were originally designed to provide a source of funding for public projects that would

generate revenue to pay for themselves—like toll roads, hospitals, parking facilities or recreational projects (Pranis, 36; Gottschalk, 51).

While Gilmore states that “capitalists and statesmen (of California)” manipulated the LRB scheme, Pranis explains how New York State devised a similar backdoor finance plan earlier in the decade (Gilmore). “In 1980, New York Governor Mario Cuomo responded to voters’ rejection of a \$500 million prison bond referendum by turning to the state’s Urban Development Corporation (UDC). The UDC is a nonprofit corporation established after the assassination of Martin Luther King Jr. to expand access to affordable housing. Governor Cuomo used the UDC to issue revenue bonds to build upstate prisons” (Pranis, 37-38). In New York, the revenue from the sale of LRBs was backed by leases between the UDC and the Department of Correctional Services (Pranis, 38); In California, the State Public Works Board fronts the money for any prison or jail project. When the project is completed they sell the LRBs to cover the loan. The project is the security for the bondholders. Then the California Department of Corrections and Rehabilitation (CDCR), or Los Angeles County—in the case of the proposed women’s jail in Lancaster—pays rent, or leases the space from the Public Works Board. The “rent” comes from the County’s general operating budget. Alex Anderson explains the scam best in his article, “Hiding Out in Prison Bonds” published in Forbes magazine: “The state creates an entity or agency to build the prison. The agency floats bonds to the public to cover construction of the facility. The agency then leases the right to use the completed prison to the state. The state pays the entity lease payments. The entity uses the lease payments to service the bond debt. Essentially, the state takes money from one pocket... and puts it in another, and then the agency distributes the money to the bondholders” (Anderson, 2008). Once the issuing agency pays the debt in full, the ownership of the asset is returned to the jailer. The investors yield one and a half

to three times their original investment depending on the length of the bond agreement.

California taxpayers did not want to see higher taxes for any reason in the early 80s, and conservative politicians did not want to appear to raise tax rates (Pranis, 38; Gilmore). In 1982, California needed much more than \$495 million to complete the prison construction plan that was on the table. The lease revenue bond scheme solved that dilemma. A 1984 memo from Daniel J. McCarthy, Director of the California Department of Corrections, indicates that the reason to use LRBs was to speed up the process because overcrowded state prisons, filled at 147% capacity, were hazardous for staff and prisoners (McCarthy). "Currently authorized and available funds for the construction program are not adequate to support completion of the required building program... the Department was asked by the Legislature to investigate the advisability of using lease or lease-

purchasing financing arrangements. This report explores this subject and identifies and recommends an approach to lease-purchase financing that would permit the Department to continue its current efforts to reduce the overcrowded conditions by bringing new prison facilities online as soon as possible" (McCarthy).

LRBs are tax-free and have higher interest rates because they are high risk. The government entity cannot

NEW BOND ISSUE IDENTIFY ONLY **ATTENTION:** (See "NOTES" herein)

In the opinion of Shelley Horn Corbett, J. Board, a Professional Corporation ("Bond Counsel"), under existing law, regulations, rulings and judicial decisions, and assuming certain representations and conditions with respect to certain tax-exempt and requirements described herein, interest (and original issue discount), on the Bonds as outlined from gross income for federal income tax purposes and in no way on any other basis, for purposes of payment of individual state income tax on the Bonds as excepted from State of California personal income tax. See "TAX" and "NOTES" herein.

\$22,270,000	\$22,200,000	\$22,200,000
Lease Revenue Bonds (Department of Corrections and Rehabilitation) 2010 Series A (Various Jails)	Lease Revenue Bonds (Judicial Council of California) 2010 Series B (Los Angeles Courthouse)	Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series C (Valley State Prisons)
\$18,960,000		\$11,000,000
Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series D (Kern Valley State Prisons)		Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series E (Continental and California State Prisons)

State Public Works Board of the State of California

State: State of California **Date:** As shown on the table hereover

The Official Treasurer describes the State Public Works Board of the State of California (the "Board") and its issue on new bonds regional (hereinafter, the "Bonds"). The Board's Lease Revenue Bonds (Department of Corrections and Rehabilitation) 2010 Series A (Various Jails) (the "2010 Series A"), the Board's Lease Revenue Bonds (Judicial Council of California) 2010 Series B (Los Angeles Courthouse) (the "2010 Series B"), the Board's Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series C (Valley State Prisons) (the "2010 Series C"), the Board's Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series D (Kern Valley State Prisons) (the "2010 Series D") and the Board's Lease Revenue Refunding Bonds (Department of Corrections and Rehabilitation) 2010 Series E (Continental and California State Prisons) (the "2010 Series E") are each referred to herein as a "Series" of Bonds. Details of anticipated issues listed on the face hereof of the Official Treasurer have the meanings stated herein.

Issues on the 2010 Series A, 2010 Series B, 2010 Series C and 2010 Series D are payable on June 1 and December 1 of each year, commencing on December 1, 2010. Issues on the 2010 Series E are payable on September 1 and March 1 of each year, commencing on September 1, 2010. The Bonds may be redeemed for the principal amount of \$200,000 and any unpaid interest at any time, but only for the full amount of the principal amount of \$200,000. The Bonds may be redeemed prior to their respective stated maturities as described herein. See "TERMS OF THE 2010 SERIES - Redemption Provisions of 2010 Series A," "TERMS OF THE 2010 SERIES - Redemption Provisions of 2010 Series B," "TERMS OF THE 2010 SERIES - Redemption Provisions of 2010 Series C," "TERMS OF THE 2010 SERIES - Redemption Provisions of 2010 Series D" and "TERMS OF THE 2010 SERIES - Redemption Provisions of 2010 Series E."

The Bonds of each Series are special obligations of the Board, payable solely from certain revenues and other assets pledged under the Indenture for each Series. The holders of a Series of Bonds shall have no claim on the property or assets of the Board, nor shall they have any right to vote on any other issue of the Board, or any right to be heard on any other issue of the Board. See "RIGHTS OF THE HOLDERS OF PAYMENT FOR EACH SERIES OF BONDS - Bonds are Limited Obligations."

THE BOARD DOES NOT REPRESENT OR WARRANT THE CREDITWORTHINESS OF THE STATE OF CALIFORNIA, AND POLITICAL RISK IS NOT COVERED. THE BOARD OR ANY PARTICIPATING AGENCY WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY LIMITATION OR A PLEDGE OF THE FULL FAITH AND CREDIT OF THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF. THE OWNERS OF THE BONDS SHALL HAVE NO RIGHT TO BE HEARD OR TO BE PAID FOR THE PAYMENT OF ANYTHING DUE ON THE BONDS. NEITHER THE BOARD NOR ANY PARTICIPATING AGENCY HAS ANY POWER TO MAKE THE CREDIT OR TO BE PAID FOR THE STATE OF CALIFORNIA.

This one page contains information for general information only. It is not a summary of the terms of the Bonds. Investors must read the entire Official Treasurer's Report and the Indenture to which they are referred for complete details.

REGISTER, PRINCIPAL AGENCIES, INTEREST PAYERS, TERMS AND CURE:
See Inside Front Cover

The Bonds are offered to the general public by the Underwriters, subject to certain conditions, including the approval of selling by the Honorable David L. Harman, Attorney General of the State of California, by counsel to the Board, and by Shelley Horn Corbett, J. Board, a Professional Corporation, Bond Counsel to the Board. Certain legal matters will be passed upon by the Participating Agencies by their respective counsel, and by the Underwriters by Honorable David L. Harman, J.P. He represents only the interests of the Board, RFB Public Finance, a Member of Citicorp Financial Group, California, in serving as Honorary Advertiser of the State Treasurer. RFB Public Finance, L.P. is serving as Co-Underwriter Counsel to the Board. David J. Harman, J.P. and Shelley Horn Corbett, J. Board, a Professional Corporation, are serving as Co-Underwriter Counsel to the Board of California regarding the Bonds. It is required that the Bonds will be available for delivery through the jurisdiction of RFB, on or before 12:00 P.M., EST, 2010.

Honorable John Chiang
Treasurer of the State of California

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Based on Official Treasurer Report, 2010.

be held liable. Official statements from bond sales clearly state the following.

“The bonds do not represent or constitute a debt of the state of California, and political subdivision thereof, the board or any participating agency (devined herein) within the meaning of any constitutional or a pledge of the faith and credit of the state of California or any political subdivision thereof. The owners of the bonds shall have no right to have excises or taxes levied for the payment of amounts due on the bonds. Neither the Board nor any participating agency has any power to pledge the credit or taxing power of the state of California. (SPWB, 2015).”

Yet, the State Public Works Board has made payments and debt service to investors, in good faith, so as not to ruin their credit or lose their good standing with investors (Gilmore, 2007; Gottschalk, 2015).

By 2007, all thirty-three state prisons were filled to almost 200% capacity, compared to 147% in 1984, which was considered an overcrowding crisis at that time. Governor Arnold Schwarzenegger, Republicans, and liberal Democrats alike responded to the last decade of prison overcrowding with AB900, the world's largest prison and jail expansion project in history. AB900, passed in Spring 2007, originally authorized more than \$7 billion in lease revenue bond sales to construct 53,000 new prison and jail beds across the state of California—to relieve overcrowding. Funds were allocated “for state prison projects, reentry facilities, and local jail beds to ease the overcrowding in California's prisons and local jails.” A 2011, AB 900 Construction update states that seven health care facilities were underway, and three local jail projects had broken ground. The report also points out that the department was reassessing the number of additional beds needed considering the implementation of Realignment Assembly Bill 109 (AB 109) which had the potential to lower the state prison

population by as much as 30,000 people over the next few years. As of 2015, the State Public Works Board is still waiting to issue more AB900 lease revenue bonds to build more county jails, including \$100 million for the new women's jail in Los Angeles County. The women's jail is one of two facilities that are part of LA's multi-billion dollar jail project that was approved in September 2015.

From 1991- 2007, Bank of America, Goldman Sachs, and Morgan Stanley purchased over \$2 billion in lease revenue bonds for the construction of California prisons (Petrella, C. 2011). Since that time, AB900 was passed, and several prison projects have been completed and others are underway. One of those projects is the 2500 bed hospital prison in Stockton, California, where sick, physically challenged, and dying prisoners will spend their last days. Official statements, dated between 2007 and 2015 reveal over \$2.5 billion in lease revenue bonds that were issued by the State Public Works Board of California for the construction of correctional facilities (SPWB, 2007, 2011, 2012, 2013, 2014, 2015; EMMA). As recently as November 2015, the State Public Works Board sold almost \$224 million in LRBs to Morgan Stanley & Co. LLC for multiple buildings at Corcoran State Prison. In April 2015, California sold over \$221 million in LRBs to Goldman Sachs for four prison expansion projects—Valley State Prison, Kern Valley State Prison and Centinela and Calipatria State Prisons—and for the Solano Jail. In November 2014, the state sold \$137,750,000 in prison bonds to J.P. Morgan, and in October 2014, they sold \$172,770,000 in prison bonds to Barclays. (California State Treasurer; EMMA). Investors are buying and selling these bonds on Wall Street with the potential to double and triple their investments over 20-30 years California taxpayers will pay this massive debt to wealthy financiers without even knowing it (EMMA).

Lease Revenue Bonds issued by the State Public Works Board of the State of California—2007 - 2015		
12-Jun-07	\$33,310,000	CDCR -California Men's Colony Wastewater Collectiona and Treatment Plant
20-Nov-07	\$37,545,000	CDCR (Various Correctional Projects)
12-Oct-11	\$151,825,000	CDCR- California State Prison, LA (Various Buildings)
19-Apr-12	\$267,625,000	CDCR - California State Prison—Kern County at Delano II
18-Oct-12	\$65,485,000	CDCR - California State Prison - Susanville
19-Mar-13	\$15,105,000	CDCR - Stanislaus - Juvenile Facility
2-Oct-13	\$135,995,000	CDCR - Various Correctional Facilities
2-Oct-13	\$161,115,000	CDCR - Wasco State Prison: Various Buildings
26-Mar-14	\$794,710,000	CDCR - Various Correctional Facilities
10-Apr-14	\$152,420,000	Kern State Prison: Various Buildings
16-Oct-14	\$108,185,000	CDCR - (Various Correctional Facilites)
16-Oct-14	\$64,585,000	CDCR - Pleasant Valley State Prison
6-Nov-14	\$137,750,000	CDCR - California Substance Abuse Treatment Facility and State Prison at Corcoran (Corcoran II)
9-Apr-15	\$52,270,000	CDCR - Solano Jail
9-Apr-15	\$19,650,000	CDCR - Kern Valley State Prison
9-Apr-15	\$45,300,000	Valley State Prison
9-Apr-15	\$103,990,000	Centinela and Calipatria State Prisons
19-Nov-15	\$223,800,000	California State Prison, Corcoran: Various Buildings
TOTAL	\$2,570,665,000	

In 2014, the California state legislature approved another \$500 million LRB sales, through SB1022, for county jail beds. SB863, passed in 2015, “allows for the sale of \$500 million in lease-revenue bond financing authority for the acquisition, design, and construction of

adult local criminal justice facilities in California” (The State of California). Despite the reduction in the California prison population, due to Realignment and Prop 47, the 2015-2016 operating budget for the California Corrections Department (CDC) is over \$10 billion.

In a 2011 article, “Leasing Through the Back Door: The Private Financing of “Public” Prisons,” Christopher Petrella points out that, while public attention has been focused on the growing number of private prison facilities owned by Corrections Corporation of America and The GEO Group, “scant attention has been paid to the private financiers of “public” prison projects.” Petrella continues by stating that “the public must be made to know that although financial institutions like Bank of America, Goldman Sachs, and Morgan Stanley do not profit directly by exploiting prison labor or by operating private penal facilities, they nonetheless realize exorbitant annual revenues by propping up a “prison industrial complex” by way of “leasing through the back door.” And to paraphrase 16th-century Dutch polymath Balthazar Gerbier, too many back doors make thieves” (Petrella).”

In her recent book, *Caught: The Prison State and the Lockdown of American Politics*, Marie Gottschalk cites many of the same aforementioned sources in her discussion about the financing of correctional facilities in Chapter Three, “Squaring the Political Circle.” She states that LRBs obscure the full cost of prison construction as payments and debt service are not itemized in the state budget and can only be found in separate documents. She emphasizes the role of neoliberal forces in manipulating prison financing schemes that remain quite stable, even during the 2008 financial downturn. She says, “They built a carceral state that has been hiding in plain sight. They also emboldened certain interests that have become major impediments to dismantling the carceral state.” Gottschalk implies that it will not be enough to fight prison and jail expansion by focusing on “recidivism, reentry, and justice reinvestment, but that it will be

necessary to change 'social, political, and economic structures (Gottschalk, 78)."

Indeed, the construction of prisons, jails and detention centers across the United States, and California, is kept in motion through a variety of public and private finance strategies and partnerships, including builders, planners, architects and private prison corporations. In 2007, AB900 also approved contracts with the private prison industry to house up to 9,000 California State prisoners in out-of-state private prisons. As of September 9, 2015, individuals are held in out-of-state private prisons in Arizona, Mississippi, and Oklahoma. This number is going down. On July 29, 2015 there were 6508 in these facilities. Today, the state has almost 11,000 state prisoners in private facilities. California and Los Angeles are increasing their collaborations with private prison corporations right under the nose of California taxpayers. As public opinion is swayed toward anti-incarceration sentiment, the GEO Group is making millions through their "GEO Continuum of Care" programs, providing housing, employment assistance, rehabilitation and substance abuse counseling, and vocational and education programs" (GEO, 2014); they have scooped up control of 24 day reporting centers across the state of California. They also sell electronic monitoring devices, and provide transportation for state and local correctional facilities (GEO, 2014). The Los Angeles County Sheriff is expanding their capacity by utilizing bed space in seven city jails that are run by The GEO Group. The company's 2015 2nd quarterly publication for employees and their families, "GEO World," features an article highlighting a meeting they sponsored about AB109 Realignment. A photo taken at a re-entry forum focused on AB109 Realignment shows, Assistant Sheriff of LA County, Terri McDonald, along with representatives from CDCR, the state Legislature, and the California State Association of Counties (GEO WORLD).

Whether state or local entities or a private prison corporation runs California's prisons

and jails, private investors finance the construction of new facilities. Through “backdoor” financing schemes and privatization, California taxpayer dollars are being sucked into the coffers of the 1%. With the entrenchment of neoliberal mechanisms to fund correctional facilities and re-entry services, as Gottschalk suggests, depending on growing investment in community solutions to undo mass incarceration may be a false solution (Gottschalk, 78).

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