

Weighing the Watchmen: Evaluating the Costs and Benefits When Outsourcing Correctional Services

Part I: Employing a Best-value Approach to Procurement

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Introduction

Prison populations in the United States have swelled over the last 20 years. Fiscal constraints at the federal, state, and local levels have left few funds available for the accommodation of new prisoners, and overcrowding is a serious problem at many of the nation's jails and prisons. In response, correctional authorities have turned to the private sector by contracting for the construction, financing, and operation of private prisons.

Factors Behind the Privatization Decision

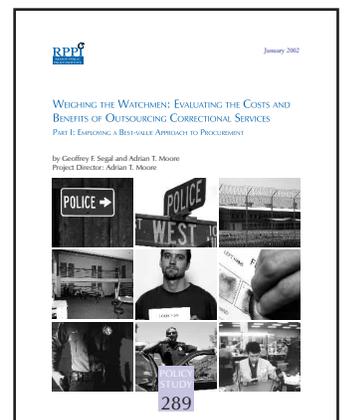
Traditionally the debate over privatization has been whether or not privatization saves money. This was particularly an issue with correctional services. The concept of cost is easy to grasp and the figures are

usually large, while other issues are more subtle and less sensational for either proponents or critics to use in arguments. However, research suggests that cost no longer is the dominant driver of privatization in corrections. Several other factors have become as important as cost savings in justifying privatizing, but they are harder to measure and even harder to hang an argument on in a political debate. These factors include:

- **Privatization to Achieve Improved Quality.** Quality outcomes from outsourcing arise from the appropriate safeguards that governments write into contracts. There is thus increased incentive for the contractor to produce high-quality work and to ensure proper performance. Contracts can be performance-based (focusing on outputs or outcomes) and can include quality assurances or quality-control assurances.
- **Privatization to Manage Capacity.** Prison overcrowding continues to

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plague many correctional facilities across the country. Because of the urgent need for new or expanded facilities, over 21 percent of state agencies say speedy project delivery is a key driver in the decision to privatize. Construction of a prison or jail takes governments an average of two and one-half years, while private firms complete the same type of project in about half the time.

- **Privatization to Improve Accountability and Better Manage Risks.** If written properly, a privatization contract gives policymakers more control and flexibility. To realize these benefits: 1) contracts have to be written with measurable criteria for success and mechanisms for termination where appropriate; 2) the government has to monitor compliance and be able to demonstrate non-compliance if it occurs; and 3) procurement laws have to allow selection criteria other than lowest bid so that a firm with a record of terminations can be excluded from bidding even if its bid is the lowest. Privatization allows governments to shift the risks to the contractors, which helps achieve both the most efficient risk allocations and allows risk to be used as a management tool. The power of the contract is often overlooked by public officials, who thus miss the opportunity to build quality assurances or quality controls into project delivery as a means of managing risk.
- **Privatization to Spur Innovation.** Competitive outsourcing can produce innovative solutions. The freedom to invent allows for new processes that integrate relevant technological advances.
- **Privatization to Gain Access to Expertise and Acquire New Services.** With the ability to draw inmates from a large population pool, private corrections companies can specialize in unique facility missions. Examples of unique private facilities include those devoted to geriatric inmates or terminal and chronically ill inmates, those devoted to teen offenders, or even regional jails that circumvent barriers to joint-operating agreements between governments. By privatizing, in effect, governments can purchase a service inherently different than what is provided by their own in-house resources. As such, policymakers can tailor their privatization initiatives to meet their specific goals and specific needs, and acquire services that are otherwise not available in-house.
- **Privatization to Improve Efficiency and Flexibility.** Private firms must compete to win the right to manage a facility or for contracts to house inmates. Thus, private

corrections firms have strong incentives to run efficient operations. Some means by which they improve efficiency include controlling legal liabilities, reducing use of overtime, managing to prevent injuries and workers' compensation liabilities, and improving labor productivity. Moreover, competition and the fear of privatization drive efficiency in both the public and private corrections marketplace, because government facilities are pressured to become more efficient and to provide better services to compete with private prisons.

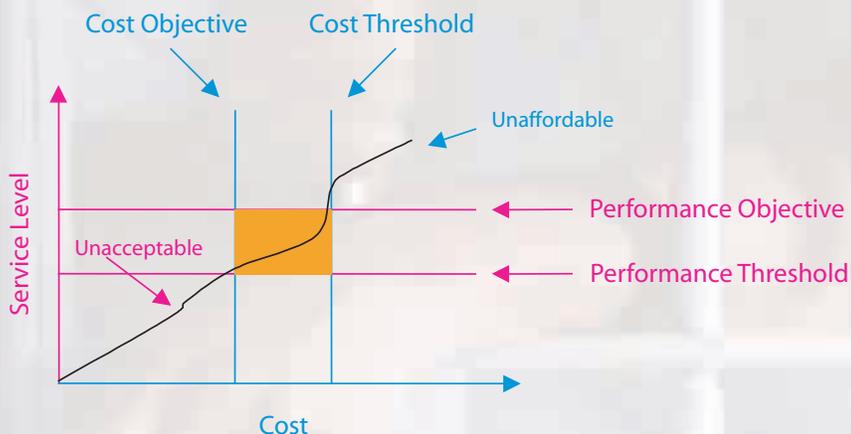
Cost Savings in Corrections Privatization

Even though cost savings is becoming less central to privatization decision-making, it nonetheless is important. A preponderance of evidence suggests that private prison facilities do create cost savings. We identified 28 studies that analyze cost data, and while none of these studies is without their flaws, many do a good job of achieving comparable results. Virtually all of the studies find private prison costs to be lower—on average between 5 and 15 percent.

Comparing the cost of privatized services relative to government services is a complex undertaking that requires making initial assumptions that partly shape the outcome. The simple fact is that cost comparison is more an art than a science—a fact that pains many who would prefer cost comparisons to be simple matters of data analysis. It is a fundamental tenet of cost comparisons that the work requirements, physical plant, quality measures, etc. must be identical for a cost comparison to be accurate. This means ignoring different factors that may include inmate population characteristics, facility age, design, and layout, to name but a few. In order to eliminate the situation of “comparing apples to oranges,” specific adjustments must be made to cost comparisons that take these differences into account.

Not only is comparing identical facilities, populations, and conditions impossible, but postulating identical situations puts the cart of cost comparison before the horse of motivations for privatization in the first place. If a government prison and a private prison are identical in every detail that could affect cost, what is the point of privatizing? Many of the driving factors for privatization (such as quality, innovation, and cost savings) are necessarily lost in this postulation. Arguably, no pure “apples to apples” comparison is possible.

Cost vs. Service: Understanding that cost is only one variable, but an important one, contracting agencies need to identify a range of acceptable costs and a desired service level.



The shaded area is where both service performance level and acceptable costs can be achieved. The areas in which the line extends outside the box are considered unacceptable because they represent ranges that do not fall within the desired service level or within the cost threshold.

Source: Lt. Col. Casey Blake, "Cost-effective PBSA," *Contract Management*, May 2001, pp 28-32.

Other examples of cost distortions appear during the contract-award process. Contracting agencies often micro-manage service delivery, dictating staffing patterns, prison design, style and type, the wages employees are to be paid, and other details. This level of input may appear to give the contractor more control, but it also directly raises the costs of the outsourced services and at the same time slams the door on opportunities to do things in new ways that save money.

Quality: The Flip Side of Privatization?

The major charge against privatization is that quality and security are sacrificed by reducing costs. Yet there is clear and significant evidence that private facilities provide at least the level of service that government-run facilities do. Private correctional facilities have measured well against government-run facilities in almost all criteria of quality, including:

- **Quality-comparison Studies.** We identified 17 quality-comparison studies, and all but two found the private

facilities to perform as well or better than government-run facilities. Overall, the research supports a pattern of high-quality services in private facilities.

- **American Correctional Association (ACA) Accreditation.** Independent accreditation by the ACA designates that a facility meets nationally accepted standards for quality of operation, management, and maintenance. There are currently 5,000 government and privately managed detention facilities located around the United States. Only 532 are accredited by the ACA—465 of 4,800 government-managed facilities (10 percent ACA accredited) and 67 of 150 privately managed facilities (44 percent ACA accredited).
- **Contract Terminations and Renewals.** As Dr. Charles Thomas wrote, "This indicator evaluates quality by measuring the willingness of contracting agencies to renew existing contracts. The hypothesis behind this first indicator is that contracts would

be terminated for cause or not renewed if the contracting agency was dissatisfied with the caliber of services they received." Since the first modern private prison opened in 1985, there have been only a handful of contract terminations and virtually every contract has been renewed.

- **Court Orders and Prisoner Litigation.** In 2001, of the 50 state correctional departments, 13 entire departments were under a court order to relieve unsatisfactory conditions, and 15 states had at least one facility under court order. In comparison, no privately operated prison has ever been placed under a court order for problems with conditions. In fact, several states have had tremendous success in getting facilities out from under court orders by contracting with a private firm to run it, and incorporating the court-imposed standards into the terms of the contract. At the same time, while private prison companies and correctional officers are much easier for inmates to sue than are governments and public employees, they appear to suffer fewer lawsuits.

Policy Alternatives to Cost Comparisons

Correctional-services privatization needs to catch up with best practices of privatization of other services nationwide by adopting a “best-value selection” criteria. “Best value” is rooted in the simple concept of value—selecting firms to provide services or projects based on qualifications and technical merits, not just on lowest cost—as long as the price is the true value of what is promised. Governments are becoming better shoppers and realize that the best value is not always the cheapest. Selecting simply the cheapest alternative assumes all other things are equal, which they rarely are.

The more complex the privatization process is, the more important a best-value selection criterion is. When the goal of privatization is a mix of cost savings and other objectives, best-value procurements still allow all factors to be weighed appropriately in making the privatization decision. Policymakers now recognize that with privatization they are often buying something different from the services traditionally provided in-house. Best-value selection allows these differences to be properly weighed in context of desired outcomes.

Performance-based Contracting

Performance-based contracts are a key way to capture the broad range of privatization goals that go beyond simple cost savings. Performance-based contracts clearly spell out the desired result expected of the contractor; while the manner in which the work is to be performed is left to the contractor’s discretion. These contracts allow governments to purchase results, not just process, and reward the private firm only if specified quality and performance goals are met. This makes privatization even more dramatically a case of purchasing something fundamentally different from in-house government services, which are often guided by nothing more than the goals of simply building and staffing.

To date, the most advanced use of performance-based contracting in corrections occurs in Australia. Using a set of performance measures to govern the contracts and structure payments to private firms, private operators receive three revenue streams from the government: an accommodation service fee, a corrections service fee, and a performance-linked fee.

Conclusion

Cost comparisons are only part of the data needed to evaluate the merits of privatization, and the measur-

able data alone cannot paint the complete picture. The full measure of worth of privatization has to be assessed in a policy context, with full due given the broader goals that can be achieved, including quality and performance. Most important is recognizing that cost savings from privatization is itself a product of competition, and that competition has beneficial effects on the entire system.

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