

Arizona Department of Corrections



JANET NAPOLITANO
GOVERNOR

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DORA B. SCHRIRO
DIRECTOR

February 8, 2006

The Honorable Janet Napolitano
Governor of the State of Arizona
1700 West Washington
Phoenix, Arizona 85007

Dear Governor Napolitano:

The Arizona Department of Corrections (ADC) retained MAXIMUS, Inc. an independent accounting firm with a national reputation for cost modeling, to review the department's preparation and applications of its Per Capita Operating Cost Report and Private Prison Cost Models and to provide recommendations for improvement.

MAXIMUS reviewed the department's preparation and utilization of its FY 2003 and FY 2004 Per Capita Operating Cost Reports and its methodologies for conducting cost comparisons to determine whether privatization provides a cost savings to the department prior to contracting for private beds.

The MAXIMUS report includes recommendations in three sections. First, MAXIMUS recommended improvements to the development of the Operating Per Capita Cost Report and restricting its usage solely to that purpose. Second, MAXIMUS recommended that the department adopt the State Versus Private Prison Cost Comparison report to determine retrospectively whether privatization provided a cost savings to the department per ARS 41-1609.01 (L). Third, MAXIMUS recommended the department discontinue use of the historical Private Prison Cost Model and improve the development of the projected Private Prison Cost Model to determine whether privatization provides a cost savings to the Department before contracting for permanent private beds per ARS 41-1609.01 (G). The department agrees with and is adopting all of the recommendations in the MAXIMUS report. Copies of the report and the department's response to MAXIMUS are attached.

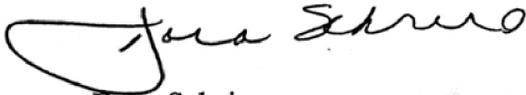
Further, the department has completed a comparison of public versus private bed costs for FY 2003 and FY 2004 establishing the ADC-operated, level 2 bed costs are appreciably lower than comparable in-state private beds. MAXIMUS has reviewed the department's comparisons of costs and concluded ADC continues to demonstrate ability to utilize the appropriate methodologies and procedures required to develop accurate, reasonable comparisons of cost to maintain male inmates in a State versus private prison.

The Honorable Janet Napolitano
February 8, 2006
Page 2

Copies of the department's FY 2003 and FY 2004 comparisons of public versus private bed costs and their review by MAXIMUS are provided as well.

If additional information is required, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Dora Schriro". The signature is fluid and cursive, with a large loop at the beginning.

Dora Schriro

Attachments

cc: The Honorable Robert Burns, Chair, Joint Legislative Budget Committee
The Honorable Russell K. Pearce, Chair, Joint Legislative Budget Committee

**REPORT ON THE EVALUATION OF
ARIZONA DEPARTMENT OF CORRECTIONS'
OPERATING PER CAPITA COST REPORT
AND
PRIVATE PRISON COST MODEL**

February 2006

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TABLE OF CONTENTS

SECTION	PAGE
I. Executive Summary	1
II. Operating Per Capita Cost Report	8
III. State Versus Private Prison Cost Comparison	17
IV. Private Prison Cost Model	23

Appendix A: Independent Evaluator - MAXIMUS, Inc.



SECTION I
EXECUTIVE SUMMARY



EXECUTIVE SUMMARY

This Report provides the findings and recommendations of an independent evaluation of the methodologies employed by the Arizona Department of Corrections (ADC) in the preparation and application of its Operating Per Capita Cost Report and Private Prison Cost Model. This Report and the evaluation upon which it is based were conducted and prepared at ADC's request by MAXIMUS, Inc. Information on MAXIMUS and the consultant assigned to conduct the evaluation is provided in Appendix A.

Operating Per Capita Cost Report

ADC annually prepares an Operating Per Capita Cost Report (Cost Report). The purpose of the Cost Report is to provide the average daily operating cost incurred by ADC during a fiscal year to incarcerate an inmate. Information provided in the Cost Report has also been utilized to compare state versus private prison costs. The Cost Report provides information on the average daily population and per capita operating cost of both ADC operated prisons and private contract prisons. In addition to providing information at the department level, the Cost Report provides information by security level, complex, and unit. The objective of the evaluation of the Cost Report is to ensure the methodology utilized by ADC to distribute direct and indirect costs accurately and reasonably reflects the operating costs incurred by ADC to perform its responsibilities.

Findings

In our opinion the methodologies utilized in the development of the FY 2003 Cost Report resulted in a reasonable cost analysis for FY 2003. Although recommendations for improvements have been identified, the application of the recommended improvements would result in less than a two percent (2%) decrease in the overall average daily operating costs of ADC operated prison and a decrease of approximately one percent (1%) in the overall average daily operating cost of a private prison.

Our review identified costs that had either been incorrectly classified or allocated that would have decreased the overall average daily operating costs for ADC operated prisons by approximately sixty-two cents (62¢). Costs that had been incorrectly classified were costs related to inmate intake and transportation. Based on the overall average FY 2003 ADC operated prison cost for all custody levels, this would have been an adjustment of less than two percent (2%). Costs that had been incorrectly allocated to private prisons would have decreased the average cost for contracted level 2 male inmate beds by less than forty-five cents (45¢) and increased ADC's overall average daily operating costs by approximately five cents (5¢). Based on the overall average FY 2003 private prison cost, this would have been an adjustment of approximately one percent (1%). The effect to ADC's overall average daily operating cost would have been less than one-tenth of one percent.



Although in our opinion the Cost Report presents a reasonable cost analysis, it does not enable the accurate comparison of ADC operated prison costs to private prison costs. The Cost Report only includes costs appropriated to ADC. It does not include costs of central support services provided by other Arizona state agencies in support of ADC operations or asset depreciation on ADC facilities. The Cost Report also includes costs of inmate intake, transportation, high health, and the work incentive pay plan only in the average daily cost of ADC operated prisons. These costs should be excluded from ADC costs in developing a cost comparison. Costs of inmate intake and transportation benefit both ADC and private prisons. Costs of inmate health are borne disproportionately by ADC operated prisons. Costs of the work incentive pay plan are borne solely by ADC operated prisons. In order to provide information on which a valid cost comparison could be made in response to ARS 41-1609.01 (L), a separate, distinct report should be developed that includes all costs, and appropriately allocates costs to both ADC and private prisons and/or excludes costs not borne by both ADC and private prisons.

Recommendations Related to Cost Report

As a result of our review, MAXIMUS has identified the following recommended improvements to the format of the Cost Report and methodologies utilized to develop information presented in the Cost Report:

- Additional Narratives - Narratives should be added stating the objectives of the Cost Report, clarifying the methodologies, and describing the purpose of and the information presented on each exhibit.
- New and Reordering Exhibits - Current Cost Report exhibits are not conducive to presenting a clear cost analysis or presented in an order that provides key information for readers with limited time. Exhibits should be developed and presented in an order that supports the objectives of the Cost Report.
- Redesign Exhibit - Exhibits should be either redesigned or new exhibits added that present direct costs by major cost components. The average daily costs should also be presented by major cost components. This will allow a reader to better analyze ADC costs and enable ADC to document their costs and validate their appropriation requests. Exhibits presenting information on private prisons should identify costs by permanent and emergency beds, and by major cost components.
- Classifying Costs - Currently costs associated with inmate intake and transportation are classified as direct costs of the ADC prison unit or complex incurring the expenses. These costs should not be direct costs utilized in the development of a unit's per capita cost. These costs benefit both ADC and private prisons, and should be tracked and identified as a separate cost category in the Cost Report.
- Indirect Cost Allocations - Review of the responsibilities and duties of the units currently classified as indirect costs identified costs that are inappropriately allocated to private prison or for which a more appropriate allocation base should be utilized.



Due to the relatively small costs of these services, the total estimated effect of recommended changes to the overall average daily operating cost for ADC prisons would be an increase of less than five cents (5¢). The estimated effect to the overall private prison operating cost would be a reduction of less than forty-five cents (45¢).

- ❑ Documentation of Procedures - A comprehensive manual should be developed that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data presented in the Cost Report.

Recommendations Related to Development of a State Versus Private Prison Cost Comparison

As previously stated, in order to provide information on which a valid comparison could be made in response to ARS 41-1609.01 (L), a separate, distinct report should be developed that includes all costs, and appropriately allocates costs to both ADC and private prisons and/or excludes costs not borne by both ADC and private prisons. The report should provide comparison exhibits for each custody bed level being compared. Exhibits should provide the average per capita cost based on the total costs incurred by the State to incarcerate an inmate in the custody level being compared. Total costs should include appropriate ADC operating costs, asset depreciation, and costs of services provided by other state agencies in support of ADC. State and private prison costs associated with the same custody level beds should be used to develop the comparison. For example, a cost comparison of private prison level 2 male permanent inmate beds should use the costs associated with ADC level 2 male permanent inmate beds for comparison. Following are recommendations for the development of a state versus private prison cost comparison report (Comparison Report).

- ❑ Report Format - The Report should include narratives clearly stating the objective(s) of the Comparison Report, and provide descriptions of the methodology and exhibits; and exhibits presenting costs by custody level by major cost components.
- ❑ Cost to be Included - The comprehensive costs of each custody level should be comprised of three principal components: ADC direct and indirect operating costs, asset depreciation, and costs of central support services provided by other Arizona state agencies in support of ADC operations. ADC direct and indirect operating costs should be acquired from and reconciled with the Operating Per Capita Cost Report for the fiscal year on which a comparison is being developed. Costs of current period improvement and equipment should be deducted and depreciation on the original construction, improvements and equipment should be added. Costs of central support services identified in the statewide cost allocation plan should also be included.
- ❑ Costs to be Excluded - The Cost Report includes costs of inmate intake, transportation, high health, and the work incentive pay plan (WIPP) only in the average daily cost of ADC operated prisons. These costs should be excluded in developing a cost comparison. All inmates, whether incarcerated in ADC or private prisons, are processed through ADC inmate intake. Transportation costs are related



to transporting inmates between intake and their assigned prison (both ADC and private), ADC prison to ADC prison, and ADC prison to private prisons. In most private prison contracts health cost are capped at \$10,000 per inmate. In addition, inmates identified as high health risk are not sent to private prisons. WIPP costs are payments to inmates for services.

- ❑ Documentation of Procedures - A comprehensive manual should be developed that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data presented in the Comparison Report.

Private Prison Cost Model

ADC contracts with private operators to incarcerate certain inmate populations. Prior to contracting with private prison operators, ADC is required per ARS 41-1609.01 (G) to conduct a comparative analysis between ADC's projected operating costs and bids submitted by private prison operators to determine whether cost savings through privatization may be achieved. ARS 41-1609.01 (G) states: "A proposal shall not be accepted unless the proposal offers cost savings to the state. Cost savings shall be determined based upon the standard cost comparison model for privatization established by the Director." In order to comply with ARS 41-1609.01 (G), ADC has developed a Private Prison Cost Model (Cost Model) that is intended to provide a consistent, reasonable cost comparison and determine whether cost savings through privatization may be achieved. The objective of the evaluation of the Cost Model is to ensure the methodologies incorporated within the Cost Model result in an equitable and reasonable cost comparison.

Findings

Cost models have been developed on historical costs and on projected costs. The historical Cost Model developed by the Arizona Office of Excellence utilizes average daily per capita cost information from the most recently published Operating Per Capita Cost Report and projected facility construction costs to develop costs used in the analysis. The projected Cost Model developed by ADC utilizes projected average daily operating costs and facility construction costs to develop costs. In our opinion neither methodology currently results in an equitable cost comparison analysis or reasonably determines the potential cost savings to be achieved through privatization.

Historical Cost Model

In our opinion, the Cost Model based on historical costs should not be utilized in the development of a privatization analysis. The utilization of ADC historical costs and a private contractor bid based on new construction results in an inequitable cost comparison and may result in an inappropriate decision to privatize. This Cost Model does not allow ADC to properly project costs of building and operating a new state owned facility with enhanced security designs and technology. Although the current historical Cost Model does utilize projected new facility construction costs, it does not include any allowances for improved facility operating and



maintenance or security. A new facility should have significantly lower operating and maintenance costs than an older, existing facility, especially during the first ten to twenty years.

Projected Cost Model

In our opinion, cost models utilizing projected costs for developing comparative analyses provide the most appropriate cost comparisons. The ADC-developed Cost Model based on projected costs should be modified and utilized for developing cost comparison analyses. In effect, ADC should develop their costs as if they were bidding on providing the requested services.

ADC's current projected Cost Model attempts to compare the additional costs that ADC would incur in operating a new facility to the additional cost that would be incurred through service contracting. However, the current projected Cost Model could potentially result in an understatement of ADC costs and an overstatement of contractor costs. Potential understated ADC costs include construction, start-up, and some operating costs. Potential overstated contractor costs include costs associated with ADC central support costs that have been added to the contractor bid for comparison purposes.

Recommendations for Improvements

Our review has identified the following recommended improvements that should be incorporated into the projected Cost Model:

- ❑ **Costs to be Included** - In developing a privatization analysis only additional costs should be included in the analysis. Costs attributed to an ADC operated facility should only include additional ADC costs that may be incurred as a result of operating a new facility. Also, only additional costs associated with a new private contract facility should be added to a private contractor's bid.
- ❑ **Construction Costs** - In order to develop a projected construction cost and annual depreciation, a construction cost estimate should be developed for the size of facility being analyzed.
- ❑ **Start-Up Costs** - The construction and opening of a new ADC operated facility would require the employment and training of staff prior to the acceptance of inmates. These start-up costs should be estimated and included in ADC's costs.
- ❑ **Operating Costs** - In order to develop a valid estimate of operating costs, a budget should be developed for the size of facility and the specific site being analyzed.
- ❑ **Central Administrative Support** - A cost estimate for any additional central administrative costs that may be required as a result of opening a new state operated facility should be developed and included in the cost analysis.
- ❑ **Contractor Support** - Currently in the projected Cost Model, costs have been added to the private contractor's bid for support provided by central office units. The method



utilized to determine these costs was to utilize one seventh of the total current costs of applicable services. This could result in an overstatement of the contractor's bid. Only additional costs that may be incurred by ADC should be added.

- Documentation of Procedures - A comprehensive manual should be developed that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data utilized in the Cost Model.

Report Format

In addition to the Executive Summary, the Report is comprised of the following three sections:

- Operating Per Capita Cost Report
- State versus Private Prison Cost Comparison
- Private Prison Cost Model



SECTION II
OPERATING PER CAPITA COST REPORT



OPERATING PER CAPITA COST REPORT

MAXIMUS has reviewed and evaluated the FY 2003 Operating Per Capita Cost Report (Cost Report). The purpose of the Cost Report is to provide the average daily operating cost incurred by ADC to incarcerate an inmate. The FY 2003 Cost Report is based on financial and prisoner data incurred during the fiscal year ended June 30, 2003. ADC's Bureau of Planning, Budgeting and Research prepared the FY 2003 Report.

ADC annually prepares a Cost Report. The Cost Report provides information on the average daily population and per capita operating cost of both ADC operated prisons and private contract prisons. Costs included in the Cost Report are only costs incurred by ADC and do not include the costs of any services provided by other state agencies in support of ADC operations. In addition to providing information at the department level, the Cost Report provides information by security level, complex, and unit.

The objective of the evaluation of the Cost Report is to ensure the methodology utilized by ADC to distribute direct and indirect costs accurately and reasonably reflects the operating costs incurred by ADC to perform its responsibilities. Application of the Cost Report's methodologies should result in a reasonable cost analysis of the average daily operating cost incurred by ADC to incarcerate an inmate during the year on which the Cost Report is based.

Findings

In our opinion the methodologies utilized in the development of the FY 2003 Cost Report resulted in a reasonable cost analysis for FY 2003. Although recommendations for improvements have been identified, the application of the recommended improvements would result in less than a two percent (2%) decrease in the overall average daily operating cost of ADC operated prison and a decrease of approximately one percent (1%) in the overall average daily operating cost of a private prison.

Our review identified costs that had either been incorrectly classified or allocated that would have decreased the overall average daily operating costs for ADC operated prisons by approximately sixty-two cents (62¢). Costs that had been incorrectly classified were costs related to inmate intake and transportation. Based on the overall average FY 2003 ADC operated prison cost for all custody levels, this would have been an adjustment of less than two percent (2%). Costs that had been incorrectly allocated to private prisons would have decreased the average cost for contracted level 2 male inmate beds by less than forty-five cents (45¢) and increased ADC's overall average daily operating costs by approximately five cents (5¢). Based on the overall average FY 2003 private prison cost, this would have been an adjustment of approximately one percent (1%). The effect to ADC's overall average daily operating cost would have been less than one-tenth of one percent.



All cost information in the Cost Report reconciles to ADC's actual financial information as recorded on the Arizona Uniform Statewide Accounting System. Both direct and indirect costs incurred by ADC are included in determining the average daily cost. Direct costs are those costs directly incurred by and/or for the benefit of an ADC prison unit or private contract prison. Indirect costs are costs of Department administration and support units, and program operational support units that benefit multiple prison units. Indirect costs are allocated to benefiting prison units serving the same population utilizing an allocation base, usually either average daily population (ADP) or number of assigned full-time equivalent positions.

The annual number of prisoner days for each unit is determined by multiplying a unit's ADP by 365 or in leap years by 366. The ADP is developed using both the inside and outside inmate counts obtained from ADC's "*Institutional Capacity and Committed Population*" reports. Dividing total unit costs by the annual number of prisoner days provides an average daily operating cost per prisoner.

Although in our opinion the Cost Report presents a reasonable cost analysis, it does not enable the accurate comparison of ADC operated prison costs to private prison costs. The Cost Report only includes costs appropriated to ADC. It does not include costs of central support services provided by other Arizona state agencies in support of ADC operations or asset depreciation on ADC facilities. The Cost Report also incorrectly includes costs of inmate intake, transportation, and health costs only in the average daily operating cost of ADC operated prisons. Costs of inmate intake and transportation benefit both ADC and private prisons. Costs of inmate health are borne disproportionately by ADC operated prisons and should not be included in a cost comparison. In order to provide information on which a valid comparison could be made in response to ARS 41-1609.01 (L), a separate, distinct report should be developed that includes all costs, and appropriately allocates costs to both ADC and private prisons and/or excludes costs not borne by both ADC and private prisons.

Extent of Review

The review of the Cost Report included a complete review of all narratives and exhibits comprising the Cost Report, FY 2003 organizational charts, duties and responsibilities of organizational units, methods for identifying and allocating costs, and meetings with ADC staff. The work program consisted of the following tasks:

❑ ***Task 1: Obtain Key ADC Information***

The FY 2003 Operating Per Capita Cost Report, FY 2003 organization charts, and FY 2003 Annual Report were obtained.

❑ ***Task 2: Reviewed Annual Report and Organization Charts***

The ADC's FY 2003 Annual Report was reviewed in conjunction with the Department's FY 2003 organization charts. The intent of the review was to



understand ADC's organizational structure, and the responsibilities and duties of each organizational unit.

❑ ***Task 3: Reviewed Operating Per Capita Cost Report***

The FY 2003 Operating Per Capita Cost Report was reviewed in relation to the purpose of the Cost Report, the exhibits and data presented, and the applicability of the assignment of costs in relation to items reviewed in Task 2.

❑ ***Task 4: Met with Report Preparer***

A meeting was held with the ADC staff person in the Bureau of Planning, Budget and Research responsible for the preparation of the FY 2003 Cost Report. All exhibits, methodologies and financial information were reviewed. An ADC staff contact was identified for any questionable costs, services, or issues.

❑ ***Task 5: Clarification of Issues***

ADC staff was contacted to acquire additional information, clarify organizational unit responsibilities, and costs. Meetings were held with the Director of the Support Service Division, Administrator of the Administrative Services Bureau, the Director of the Program Services Division, and the Operations Director of the Contract Beds Bureau.

❑ ***Task 6: Detailed Review of Financial Information and Methodologies***

Reviewed all financial information and methodologies utilized to assign or allocate costs in relation to information acquired in previous tasks. The review focused on their compliance with generally accepted accounting principles and best business practices.

❑ ***Task 7: Preparation of Report***

Based on the previous task, a report was prepared presenting findings and recommendations for improvement.

Recommendations for Improvements

As a result of our review, MAXIMUS has identified improvements to the format of the Cost Report and methodologies utilized to develop information presented in the Cost Report. Recommended improvements to the format and information presented should enhance the value of the Cost Report to ADC management, the Governor and Legislature, and the citizens of Arizona. Methodology recommendations should enhance the validity of the data and findings presented in the Cost Report.



Report Format

Recommendations related to the Cost Report's format are intended to assist ADC in providing a report that both presents factual performance information, and enhances a reader's ability to analyze ADC costs. Recommendations include adding narrative information, creating new and reordering existing exhibits, and redesigning current exhibits.

Additional Narratives

Currently the Cost Report only provides a one-page methodology narrative that very briefly describes the methodologies utilized to develop the per capita operating costs presented in the Cost Report. It is recommended that narratives be added stating the objectives of the Cost Report, clarifying the methodologies, and describing the purpose of and the information presented on each exhibit.

- ❑ Objectives - The inclusion of a narrative clearly stating the objectives of the Cost Report would assist in clarifying to a reader the intent and the value of the information presented. Based on information currently presented in the Cost Report, the objective would be to provide the average daily operating costs incurred by ADC to incarcerate an inmate. Statement of this objective in the Cost Report would clarify to the reader that information is provided related to both ADC operated and contracted prisons, and only presents ADC operating costs.
- ❑ Clarify Methodology - The brief narrative on the methodologies currently presented in the Cost Report provides only minimum information. The narrative should be enhanced to clearly state the source of financial information; expenditures not included in the analysis and the reason for their exclusion; the methods and procedures utilized to identify direct unit costs, complex costs, and indirect costs; a description of the responsibilities and duties of each unit classified as an indirect cost; the method and allocation base utilized to allocate indirect and complex costs; and the method for determining ADP.
- ❑ Exhibit Descriptions - Currently the Cost Report provides no explanation of the purpose or the information provided on the exhibits. A narrative or narratives should be provided that clearly states the purpose of each exhibit. If an exhibit is utilized to support another exhibit and/or it reconciles to another exhibit, the narrative should so state. A brief description of the purpose and costs included in each column of an exhibit should also be provided.

New and Reordering Exhibits

Current Cost Report exhibits are not conducive to presenting a clear cost analysis or presented in an order that provides key information for readers with limited time. Exhibits should be developed and presented in an order that supports the objectives of the Cost Report. If the objective of the Cost Report is to provide the average daily operating costs incurred by ADC,



the first exhibit in the Cost Report should provide this information. Currently an exhibit providing daily per capita information is provided as the third exhibit beginning on page 6 of the FY 2003 Per Capita Cost Report. Although providing per capita information, this exhibit does not provide a reader with valuable information. A more applicable first schedule would present ADC operated prison costs by security level, not by complex. The objective is to focus on costs per level.

Redesign Exhibits

Exhibits should be redesigned or added to present information that is more conducive to analyzing ADC costs. Currently exhibits present for each ADC complex and unit the ADP, the total direct and indirect costs, the annual per capita total operating direct and indirect costs, and the average daily per capita operating cost. Although exhibits are presented that provide information on indirect costs, exhibits providing information on the type of costs classified as either unit direct or complex direct are not provided. The lack of information by type of costs does not allow ADC to inform readers on the costs that drive their average per capita costs.

Exhibits should be either redesigned or new exhibits added that present direct costs by major cost components. The average daily per capita costs should also be presented by major cost components. This will allow a reader to better analyze ADC costs and validate their appropriation requests. Costs should be grouped and presented by the following components:

- Facility Administration - Personal services, equipment depreciation, and other costs associated with the prison warden and other administration staff and services.
- Facility Operating - Costs of personal services, equipment depreciation, utilities, preventive maintenance, repairs and maintenance, insurance, and other costs associated with operating and maintaining facilities.
- Inmate Transportation - Personal services, equipment depreciation, and other costs associated with the transportation of inmates.
- Inmate Security - Personal services, equipment depreciation, and other costs associated with inmate security.
- Inmate Programs - Personal services, equipment depreciation, and other costs associated with the provision of treatment, education, recreation and other inmate programs.
- Inmate Medical - Personal services, equipment depreciation, drugs, hospital, and other costs associated with the provision of medical services for inmates.
- Inmate Food - Personal services, equipment depreciation, food, and other costs associated with the preparation and serving of food to inmates.



- ❑ Work Incentive Play Plan – Costs of the work incentive pay plan payments to inmates and associated administrative costs.

Exhibits presenting information on private prisons should identify costs by permanent and emergency beds, and by major cost components, notably inmate medical costs. Currently the exhibit providing the average daily cost for private prisons does not distinguish between permanent beds and emergency beds. The costs of emergency beds are considerably less than permanent beds because they are basic beds with none of the services of permanent beds. Although the average cost may be correct, it does not allow a valid analysis of private prison costs. By breaking out costs between permanent and emergency beds, a more valid cost analysis can be made of permanent, long-term private prison contract costs. All costs for private prisons should be presented utilizing the same major cost components selected for ADC prisons.

Methodology Improvements

Recommendations related to the methodology are intended to assist ADC in properly identifying the costs incurred by ADC, and in properly classifying and allocating costs to enhance the validity of the information presented in the Cost Report. Recommendations include reclassifying costs and utilizing bases to allocate indirect costs that better reflect services and their beneficiaries.

Classifying Costs

Currently costs associated with inmate intake and transportation are classified as direct costs of the ADC prison unit or complex incurring the expenses. These costs should not be direct costs utilized in the development of a unit's per capita cost. These costs benefit both ADC and private prisons, and should be tracked and identified as a separate cost category in the Cost Report. All inmates, both those at ADC and private prisons, must come through intake. Transportation costs are related to transporting inmates between intake and their assigned prison (both ADC and private), ADC prison to ADC prison, and ADC prison to private prisons.

Currently ADC does not track inmate intake or transportation costs as cost centers in their accounting system. These costs should be tracked in the future. Based on brief cost analysis, the estimated cost of inmate intake is approximately five million to six million dollars for FY 2003. If deducted from ADC overall average daily cost, this would have resulted in a forty-nine cent (49¢) to fifty-nine cent (59¢) reduction in the overall average daily operating cost of ADC prisons. The estimated cost of inmate transportation for FY 2003 is seven to eight hundred thousand dollars. If deducted from ADC overall average daily operating cost, this would have resulted in a seven cent (7¢) to eight cent (8¢) reduction in the overall average daily cost of ADC prisons.

Indirect Cost Allocations

Indirect costs are allocated to ADC prisons and contract prisons based on either ADP or number of assigned full-time equivalent (FTE) positions. Review of the responsibilities and



duties of the units currently classified as indirect costs identified costs that are incorrectly allocated to private prison or for which a more appropriate allocation base should be utilized. Due to the relatively small costs of these services and the large ADP, the total estimated effect of recommended changes to the overall average daily operating cost for ADC prisons would be an increase of less than five cents (5¢). The estimated effect to the overall average private prison operating cost would be a reduction of less than forty-five cents (45¢). Following are the recommended improvements:

- ❑ Labor Relations - Costs of the Labor Relations unit are currently being allocated to both ADC and private prisons based on ADP. This Unit's costs should only be allocated to ADC operations based on FTEs. The estimated effect of this recommendation would be an increase of less than one cent (1¢) to ADC's overall average daily operating cost and a decrease of less than five cents (5¢) to the overall average daily private prison operating cost.
- ❑ Information Technology Services - All costs of the Information Technology Section (ITS) are currently being allocated to both ADC and private prisons based on ADP. Although ITS does support systems benefiting or utilized by private prisons, many ITS services are only utilized and for the benefit of ADC staff and facilities. ITS costs should be classified as either ADC support or inmate systems support. ADC support costs should only be allocated to ADC operations based on either ADP or FTEs. Inmate systems support should be allocated to both ADC and private prison on ADP. The estimated effect of this recommendation would be an increase of less than two cents (2¢) to ADC's overall average daily operating cost and a decrease of less than twenty cents (20¢) to overall average daily private prison operating cost.
- ❑ Administrative Services - All costs of the Administrative Services Bureau are currently being allocated to both ADC and private prisons based on ADP. Bureau services include procurement, financial services, and fleet and facilities maintenance. Although these services may benefit both ADC and private prisons, they are primarily benefiting ADC operations. A more appropriate base for procurement would be number of purchase orders processed or dollar volume of procurement. Financial services should be allocated on transactions processed or other bases that reflects effort. Fleet and facilities management should be allocated on square footage or number of FTEs served. The estimated effect of modifying the allocate bases for these services would be an increase of less than two cents (2¢) to ADC's overall average daily operating cost and a decrease of less than twenty cents (20¢) to the overall average private prison operating cost.

Documentation of Procedures

MAXIMUS recommends the development of a comprehensive manual that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data presented in the Cost Report. Detailed work papers are currently developed and maintained supporting all costs in the Cost Report. However, there is minimal written documentation on



methodologies, assumptions, or procedures utilized to develop the Cost Report. Sound management practices support the development and maintenance of documentation on ADC policies and procedures that assist preparers and auditors in ensuring the Cost Report is prepared in compliance with ADC policies. Documentation should also permit efficient, consistent preparation of Cost Reports in subsequent years.

This concludes MAXIMUS, Inc. comments on the Arizona Department of Corrections Operating Per Capita Cost Report.



SECTION III
STATE VERSUS PRIVATE PRISON COST COMPARISON



STATE VERSUS PRIVATE PRISON COST COMPARISON

Per ARS 41-1609.01, ADC is required to periodically conduct a cost comparison of services provided by private prison vendors and the State to determine if anticipated costs savings materialized. Although in our opinion the Operating Per Capita Cost Report (Cost Report) presents a reasonable cost analysis, it does not enable the accurate comparison of ADC operated prison costs to private prison costs.

The Cost Report only includes costs appropriated to ADC. It does not include costs of central support services provided by other Arizona state agencies in support of ADC operations or asset depreciation on ADC facilities. The Cost Report also includes costs of inmate intake, transportation, high health, and the work incentive pay plan only in the average daily cost of ADC operated prisons. These costs should be excluded from ADC costs in developing a cost comparison. Costs of inmate intake and transportation benefit both ADC and private prisons. Costs of inmate health are borne disproportionately by ADC operated prisons. Costs of the work incentive pay plan are only borne by ADC operated prisons.

In order to provide information on which a valid cost comparison could be made in response to ARS 41-1609.01 (L), a separate, distinct report should be developed that includes all costs, and appropriately allocates costs to both ADC and private prisons and/or excludes costs not borne by both ADC and private prisons. The report should provide comparison exhibits for each custody bed level being compared. Exhibits should provide the average per capita cost based on the total costs incurred by the State to incarcerate an inmate in the custody level being compared. Total costs should include appropriate ADC operating costs, asset depreciation, and costs of services provided by other state agencies in support of ADC. State and private prison costs associated with the same custody level beds should be used to develop the comparison. For example, a cost comparison of private prison level 2 male permanent inmate beds should use the costs associated with ADC level 2 male permanent inmate beds for comparison. Following are recommendations for the development of a state versus private prison cost comparison report (Comparison Report).

Recommendations for Improvements

Report Format

Recommendations related to the Comparison Report's format are intended to assist ADC in providing a report that both presents factual performance information, and enables a reader's to analyze ADC costs and conduct valid comparisons. Format recommendations include developing narratives that clearly state the objective(s) of the Comparison Report, and provide descriptions of the methodology and exhibits; and the development of exhibits presenting costs by custody level and major cost components.



Narratives

It is recommended that narratives be developed stating the objectives of the Comparison Report, clarifying the methodologies, and describing the purpose of and the information presented on each exhibit.

- Objectives - The inclusion of a narrative clearly stating the objectives of the Comparison Report would assist in clarifying to a reader the intent and the value of the information presented.
- Methodology - A narrative should be developed clearly stating the source of financial information; expenditures included and not included in the comparison, and the reason for their exclusion; the methods and procedures utilized to identify direct and indirect costs; the methods and allocation bases utilized to allocate indirect costs; and the method for determining ADP.
- Exhibit - A narrative or narratives should be provided clearly stating the custody level and purpose of each exhibit. If an exhibit is utilized to support another exhibit and/or it reconciles to another exhibit, the narrative should so state. A brief description of the purpose and costs included in each column of an exhibit should also be provided.

Exhibits

Exhibits should be developed presenting direct and indirect costs by major cost components or service. Total annual costs and the average daily per capita cost should be provided for each direct and indirect cost component. This will allow ADC to identify costs and present justification for their costs; and improve comparisons with private prisons and other incarceration options. Costs could be grouped and presented by the following components:

- Facility Depreciation - The annual depreciation of the original cost of a facility and any subsequent improvement costs.
- Facility Administration - Personal services, equipment depreciation, and other costs associated with the prison warden and other administration staff and services.
- Facility Operating - Costs of personal services, equipment depreciation, utilities, preventive maintenance, repairs and maintenance, insurance, and other costs associated with operating and maintaining facilities.
- Inmate Security - Personal services, equipment depreciation, and other costs associated with inmate security.
- Inmate Programs - Personal services, equipment depreciation, and other costs associated with the provision of treatment, education, recreation and other inmate programs.



- Inmate Medical - Personal services, equipment depreciation, drugs, hospital, and other costs associated with the provision of medical services for inmates.
- Inmate Food - Personal services, equipment depreciation, food, and other costs associated with the preparation and serving of food to inmates.
- Department Administration - Costs of ADC central administration and support services.
- Statewide Central Support - Costs of central support services provided by other state agencies in support of ADC operations.

Exhibits information on private prisons should also identify costs by permanent and emergency beds, and by major cost components. The cost of emergency beds is considerably less than permanent beds because they are basic beds with none of the services of permanent beds. By breaking out costs between permanent and emergency beds, a more valid comparison can be made between ADC's costs and the permanent, long-term private prison contract rates. Where possible, private prisons costs should be presented utilizing the same major cost components selected for ADC prisons.

Cost Identification

Recommendations related to cost identification are intended to assist ADC in identifying the full or comprehensive costs incurred in support of ADC inmates, and properly classifying costs to enhance the validity of the information presented in the Comparison Report.

Costs to be Included

The comprehensive costs of each custody level should be comprised of three principal components: ADC direct and indirect operating costs, asset depreciation, and costs of central support services provided by other Arizona state agencies in support of ADC operations. Following is a brief description of each component:

- ADC Direct and Indirect Operating Costs - ADC direct and indirect operating costs and ADP information should be acquired from and reconciled with the Operating Per Capita Cost Report for the fiscal year on which a comparison is being developed. Cost Report costs are the base costs to which appropriate non-operating ADC costs should be added or from which inappropriate costs should be deducted. The utilization of Cost Report data ensures the data is in accordance with ADC financial records and auditable.
- Asset Depreciation - Currently ADC does not include any asset depreciation costs in the Cost Report. Original prison costs are depreciated for State financial purposes but are not recorded on ADC's financial records or included in the Cost Report. Costs of prison improvements and equipment incurred by ADC are treated as current period expenses. The lack of inclusion of depreciation on original prison costs,



improvements, and equipment purchased in prior years understates ADC's current year costs. The treatment of the total cost of improvements and equipment as current period expenses results in an overstatement of ADC's current year costs. Original prison costs should be depreciated over the expected life of each prison and the annual amount included for each prison. Costs of prison improvements should be deducted and an annual depreciation costs included. Depreciation should be based on the expected useful life of the improvements. Equipment costing over \$5,000 should be deducted, depreciated over its expected life, and the annual amount included for each prison. Due to the age of ADC's prisons and the ADP, the potential impact of this recommendation is estimated to add less than two dollars to ADC's average daily costs for a custody level two bed.

- ❑ Central Support Services - Costs of central support services provided by other Arizona state agencies in support of ADC operations should be included. The Arizona Department of Administration (DOA) annually prepares a statewide cost allocation plan (SWCAP) that identifies the costs of state central support services and allocates them to state agencies. Services allocated in the SWCAP include general accounting, procurement, risk management, mailroom, legal, treasury, records management, equal opportunity, budget, and occupancy. Costs allocated to ADC for FY 2003 totaled \$2,864,748. If allocated on ADC's ADP, ADC average per capita costs for a custody level two bed would have been twenty-five cents (25¢).

Costs to be Excluded

The Cost Report includes costs of inmate intake, transportation, high health, and the work incentive pay plan only in the average daily cost of ADC operated prisons. These costs should be excluded in developing a cost comparison.

- ❑ Intake - Currently costs associated with inmate intake are classified as direct costs of the ADC prison unit or complex incurring the expenses. All inmates both those incarcerated in ADC and private prisons are processed through inmate intake. Intake costs should be excluded in the development of cost comparisons. The inclusion of these costs only in ADC's average per capita cost results in an invalid cost comparison. Based on a cursory cost analysis using available information, the estimated cost of inmate intake was approximately five million to six million dollars for FY 2003. If deducted from ADC overall average daily cost, this would have resulted in a reduction of forty-nine cents (49¢) to fifty-nine cents (59¢) in ADC's overall average daily operating per capita cost.
- ❑ Transportation - Currently costs associated with inmate transportation are classified as direct costs of the ADC prison unit or complex incurring the expenses. Transportation costs are related to transporting inmates between intake and their assigned prison (both ADC and private), ADC prison to ADC prison, and ADC prison to private prisons. The inclusion of these costs only in ADC's average per capita cost results in an invalid cost comparison. Based on a cursory cost analysis



using available information, the estimated cost of inmate transportation for FY 2003 was seven to eight hundred thousand dollars. If deducted from ADC overall average daily operating cost, this would have resulted in a reduction of seven cents (7¢) to eight cents (8¢) in ADC's overall average daily per capita cost.

- ❑ High Health - In most private prison contracts health cost are capped at \$10,000 per inmate. In addition, none of the private prisons accept inmates identified as high health risk. Costs of inmates with high health risk/costs (costs exceeding \$10,000 annually) are borne disproportionately by ADC operated prisons and should not be included in a cost comparison. In FY 2003 the cost of high health included in ADC average per capita cost for custody level 2 male inmates was \$4,634,615. If deducted from ADC custody level 2 average daily per capita costs, this would have resulted in a reduction of one dollar and eighty-eight cents (\$1.88) in the average daily operating per capita cost.
- ❑ Work Incentive Pay Plan - Costs of the work incentive pay plan (WIPP) are borne disproportionately by ADC operated prisons and should not be included in a cost comparison. WIPP costs are payments to inmates for work they perform. Costs of WIPP are not included in private prison costs. In FY 2003 the cost of the work incentive pay plan included in ADC average per capita cost for custody level 2 male inmates was \$2,696,065. If deducted from ADC custody level 2 average daily per capita costs, this would have resulted in a reduction of one dollar and nine cents (\$1.09) in the average daily operating per capita cost.

Documentation of Procedures

MAXIMUS recommends the development of a comprehensive manual that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data presented in the Comparison Report. Sound management practices support the development and maintenance of documentation on ADC policies and procedures that assist preparers and auditors in ensuring the Comparison Report is prepared in compliance with ADC policies. Documentation should also permit efficient, consistent preparation of Cost Comparisons in subsequent years.

This concludes MAXIMUS, Inc. comments on the development of a State Versus Private Prison Cost Comparison.



SECTION IV
PRIVATE PRISON COST MODEL



PRIVATE PRISON COST MODEL

MAXIMUS, Inc. has reviewed and evaluated two private prison cost models. The cost models are utilized to conduct comparative analyses of ADC's projected operating costs and bids submitted by private prison operators to determine whether cost savings through privatization may be achieved. ADC's Administrative Services Bureau is responsible for performing the comparative analyses.

ADC contracts with private operators to incarcerate certain inmate populations. Prior to contracting with private prison operators, ADC is required per ARS 41-1609.01 (G) to conduct a comparative analysis between ADC's projected operating costs and bids submitted by private prison operators to determine whether cost savings through privatization may be achieved. ARS 41-1609.01 (G) states: "A proposal shall not be accepted unless the proposal offers cost savings to the state. Cost savings shall be determined based upon the standard cost comparison model for privatization established by the Director." In order to comply with ARS 41-1609.01 (G), ADC has developed a Private Prison Cost Model (Cost Model) that is intended to provide a consistent, reasonable cost comparison and identify any potential savings from privatization. The objective of the evaluation of the Cost Model is to ensure the methodologies incorporated within the Cost Model result in an equitable and reasonable cost comparison.

Findings

Cost models have been developed on historical costs and on projected costs. The historical Cost Model developed by the Arizona Office of Excellence utilizes average daily per capita cost information from the most recently published Operating Per Capita Cost Report and projected facility construction costs to develop costs used in the analysis. The projected Cost Model developed by ADC utilizes projected average daily operating costs and facility construction costs to develop costs. In our opinion neither methodology currently results in an equitable cost comparison analysis or reasonably determines the potential cost savings to be achieved through privatization.

Historical Cost Model

In our opinion, the Cost Model based on historical costs should not be utilized in the development of a privatization analysis. The utilization of ADC historical costs and a private contractor bid based on new construction results in an inequitable cost comparison and may result in an inappropriate decision to privatize. This Cost Model does not allow ADC to properly project costs of building and operating a new state owned facility with enhanced security designs and technology. Although the current historical Cost Model does utilize projected new facility construction costs, it does not include any allowances for improved facility operating and maintenance or security. A new facility should have significantly lower operating and maintenance costs than an older, existing facility, especially during the first ten to twenty years. New facility designs and technology should also assist in reducing security related costs.



In addition to our overall concerns about using historical costs, the following issues were identified with ADC historical Cost Model:

- ❑ **Operating Per Capita Cost Report** - The Cost Model utilizes the average daily per capita cost of a comparable ADC prison unit or units to determine ADC operating costs. A Cost Report utilized by ADC may be one to two years old and may not reflect current year operations. Even a \$1 variance in the average per capita cost on a unit with 1,000 beds could result in an annual variance of \$365,000. Also, most department indirect costs will not increase or decrease as a result of adding a 1,000 beds. The average per capita cost includes indirect cost allocation that may be reduced if indirect costs are allocated over a larger ADP without significant increases in indirect costs.
- ❑ **Projected Construction Costs** - The Cost Model projected per bed construction costs based on a construction estimate provided by the Arizona Department of Administration for a facility with 1,100 beds. An average per bed cost is determined by dividing the Total construction costs by 1,100. The average cost is subsequently divided by the number of prisoner days to be incurred over twenty years to determine an average daily per prisoner cost. This method does not result in an appropriate construction or depreciation estimate.

Construction costs for many areas of a new prison may not be affected by a reduction in beds. Facility costs related to water and sewage, administrative offices, food preparation, guard towers, and other common areas may remain the same. In order to develop a projected construction cost and annual depreciation, a construction cost estimate should to be developed for the size of facility being analyzed and be site specific.

- ❑ **Start-Up Costs** - The Cost Model does not include any costs associated with the start-up of a new facility. The opening of a new facility may require the employment and training of staff prior to the acceptance of inmates. It is common to employ and begin training staff sixty to ninety days prior to accepting inmates. These start-up costs should be estimated and included in ADC's costs.

Projected Cost Model

In our opinion, cost models utilizing projected costs for developing comparative analyses provide the most appropriate cost comparisons. The ADC-developed Cost Model based on projected costs should be modified and utilized for developing cost comparison analyses. In effect, ADC should develop their costs as if they were bidding on providing the requested services.

ADC's current projected Cost Model attempts to compare the additional costs that ADC may incur in operating a new facility to the additional cost that may be incurred through service contracting. However, the current projected Cost Model could potentially result in an



understatement of ADC costs and on overstatement of contractor costs. Potential understated ADC costs include construction, start-up, and some operating costs. Potential overstated contractor costs include costs associated with ADC central support costs that have been added to the contractor bid for comparison purposes. Further discussion of issues and improvement recommendations on the projected Cost Model are provided in a subsequent section titled "Recommendations for Improvements."

Extent of Review

The review of the cost models included a complete review of all narratives and exhibits comprising the cost models, methods for identifying and determining costs, and meetings with ADC staff. The work program consisted of the following tasks:

❑ ***Task 1: Obtain Private Prison Cost Models***

Copies of the private prison cost model based on historical costs and the cost model based on projected costs were acquired.

❑ ***Task 2: Reviewed Private Prison Cost Models***

Cost models were reviewed to determine the source and applicability of financial information, and the justification for inclusion or exclusion of costs. The review focused on compliance with generally accepted accounting principles and best business practices.

❑ ***Task 3: Met with Cost Model Developer***

A meeting was held with the ADC staff person in the Administrative Services Bureau responsible for the development of the cost models and their use in performing private cost analysis. All exhibits, methodologies and financial information were reviewed.

❑ ***Task 4: Clarification of Issues***

ADC staff was contacted to acquire additional information, clarify organizational unit responsibilities, and costs. Meetings were held with the Director of the Support Service Division, the Director of the Program Services Division, and the Operations Director of the Contract Beds Bureau.

❑ ***Task 5: Detailed Review of Cost Models***

Reviewed all financial information and methodologies utilized to assign or allocate costs in relation to information acquired in previous tasks.



❑ *Task 6: Preparation of Report*

Based on the previous task, a report was prepared presenting findings and recommendations for improvement.

Recommendations for Improvements

As previously stated, MAXIMUS recommends the projected Cost Model be utilized by ADC for developing comparative analysis. However, our review has identified improvements that should be incorporated into the projected Cost Model. In addition we recommend the development of a comprehensive manual on the projected Cost Model.

Recommended Improvements

- ❑ ***Costs To Be Included*** - Currently the projected Cost Model includes both estimates for additional costs and allocations of existing costs. In developing a privatization analysis only additional costs should be included in the analysis. Costs attributed to an ADC operated facility should only include additional ADC costs that may be incurred as a result of operating a new facility. Also, only additional costs associated with a new private contract facility should be added to a private contractor's bid.

- ❑ ***Projected Construction Costs*** - The projected Cost Model projects per bed construction costs based on a construction estimate provided by the Arizona Department of Administration for a facility with 1,100 beds. An average per bed cost is determined by dividing the Total construction costs by 1,100. The average cost is subsequently divided by the number of prisoner days to be incurred over twenty years to determine an average daily per prisoner cost.

This method does not result in an appropriate construction or depreciation estimate. Construction costs of many areas of a new prison may not be affected by a reduction in beds. Facility costs related to water and sewage, administrative offices, food preparation, guard towers, and other common areas may remain the same. In order to develop a projected construction cost and annual depreciation, a construction cost estimate should be developed for the size of facility and the actual site being analyzed.

- ❑ ***Start-Up Costs*** - The projected Cost Model does not include any costs associated with the start-up of a new facility. The construction and opening of a new facility may require the employment and training of staff prior to the acceptance of inmates. It is common to employ and begin training staff sixty to ninety days prior to accepting inmates. These start-up costs should be estimated and included in ADC's costs.
- ❑ ***Operating Costs*** - Currently in the projected Cost Model, average per prisoner day costs for some operating costs were projected based on a budget estimate developed for a facility with 1,100 beds. An average per prisoner cost was determined by



dividing the annual budgeted costs by 1,100. An average cost per prisoner day was determined by dividing the average cost by 365. A significant cost estimated utilizing this method was personal services.

This method does not result in an appropriate estimate for most operating costs. For example, personal services costs associated with the warden, administrative staff, security management, and maintenance staff may be relatively the same for a facility with 1,000 beds as for a facility with 1,100 beds, not 10/11 of the costs. In order to develop a valid estimate of operating costs, a budget should be developed for the size and the site of the facility being analyzed.

- ❑ **Central Administrative Support** - Currently the projected Cost Model does not include any additional central support costs related to operating a new state facility. A cost estimate for any additional central administrative costs that would be required as a result of opening a new state operated facility should be developed and included in the cost analysis. Only the personal services costs of additional staff and other operating costs should be developed. There would be no additional costs for the Department Director or management staff. However, it could require the addition of facility maintenance, procurement, personnel, and/or other staff impacted by the additional workload associated with a new facility.
- ❑ **Contractor Support** - Currently in the projected Cost Model, costs have been added to the private contractor's bid for support provided by central office units. The method utilized to determine these costs was to utilize one seventh of the total current costs of applicable services. This could result in an overstatement of the contractor's bid. Only additional costs that may be incurred by ADC should be added. ADC should analyze the workload of staff providing contractor support and determine if staff or costs would need to be added as result of the contract. The full cost of these services should be determined and added for determination of the potential cost savings through contracting.

Comprehensive Manual

MAXIMUS recommends the development of a comprehensive manual that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data utilized in the Cost Model. Currently there is minimal written documentation on methodologies, assumptions, or procedures utilized to develop the Cost Model. Sound management practices support the development and maintenance of documentation on ADC policies and procedures that assist preparers and auditors in ensuring cost analyses are prepared correctly and in compliance with ADC policies. Documentation should also support efficient, consistent preparation of cost analyses.

This concludes MAXIMUS, Inc. comments on the Arizona Department of Corrections Private Prison Cost Model.



APPENDIX A
INDEPENDENT EVALUATOR - MAXIMUS, INC.



INDEPENDENT EVALUATOR - MAXIMUS, INC.

MAXIMUS, Inc. was selected by ADC through a competitive bid process to conduct an evaluation of ADC's Operating Per Capita Cost Report and Private Prison Cost Model. MAXIMUS is a nationally recognized professional services firm established in 1975 that is currently traded publicly on the New York Stock Exchange. Corporate offices are located in Reston, Virginia. Information on MAXIMUS and its services are available on the Internet at <http://www.maximus.com>.

The Cost Services Division of MAXIMUS through its Phoenix office was responsible for conducting the evaluations and preparing this Report. MAXIMUS has prepared thousands of studies that have determined the total costs, both direct and indirect, of government services. Study results have been utilized to establish fees for services, establish performance measures, assist in privatization decisions, and recover costs from other governmental entities.

The MAXIMUS consultant assigned to conduct the evaluation was Joel E. Nolan, a Vice President of the Cost Services Division located in Phoenix, Arizona. Mr. Nolan is a Certified Government Financial Manager with over twenty-five years of experience in analyzing and costing government services. His state prison experiences have included the preparation of cost of services studies for the Alaska Department of Corrections and the Louisiana Department of Corrections. He has also prepared jail per-diem rate studies for local governments in Arizona, Colorado, Louisiana, and Texas. These studies provide the average cost of booking a prisoner and the average daily costs of housing prisoners. Counties utilize study results to recover costs from the U.S. Marshall's Office, the U.S. Bureau of Prisons, and state correctional agencies. Study methodologies have been challenged and successfully defended in court actions in Louisiana and Texas. Recent local government jail studies have been completed for the Arizona counties of Apache, Cochise, and Pinal; and Texas counties of El Paso, Galveston, Harris, San Patricio, Smith, and Tarrant.

Mr. Nolan also has extensive experience in assisting local and state governments in assessing the potential cost savings of privatizing services. He assisted in the development of a service costing methodology that was adopted by the Texas Council on Competitive Government for use by state agencies in determining privatization benefits. He has also developed methodologies and prepared privatization analysis for local and state equipment services, data processing services, facility operations, security services, telecommunication services, and printing services.



THE END

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February 7, 2006

Mr. Doug MacFarlane
Division Director, Support Services
Arizona Department of Corrections
1601 West Jefferson, MC 328
Phoenix, Arizona 85007

Dear Mr. MacFarlane:

At the request of the Arizona Department of Corrections (ADC), MAXIMUS, Inc. has completed a review of schedules prepared by ADC that provide a state versus private cost comparison of Level 2 male inmate beds. The cost comparison is based on actual costs and inmate data incurred during the State fiscal year ended June 30, 2003 (FY 2003). Only costs appropriated to ADC are included in the comparison. The schedules that were reviewed are provided as Exhibit A.

In our opinion the State Versus Private Cost Comparison of Level 2 Male Inmate Beds (Exhibit A) reasonably presents a comparison of the FY 2003 costs incurred by ADC to maintain a male inmate in a level 2 bed in ADC operated prisons and private contract prisons. Our opinion is based on a review of ADC's FY 2003 Operating Per Capita Cost Report, organization charts, organizational duties and responsibilities, and methods for identifying and allocating costs. Cost information included in the cost comparison reconciles to the FY 2003 Per Capita Cost Report and to ADC's actual financial information as recorded on the Arizona Uniform Statewide Accounting System. Average daily population (ADP) is in accordance with ADC's "Institutional Capacity and Committed Population" report.

All ADC appropriated direct and indirect costs that are applicable to Level 2 prison facilities have been identified and utilized in developing the cost comparison. Direct costs are costs directly incurred by and/or for the benefit of an ADC prison unit and payments to private contractors. Indirect costs are costs of ADC administration and support units, and program operational support units that benefit multiple ADC prison units and/or private contract prison units. Indirect costs benefiting only ADC operated prison units have been allocated only to ADC operated prison units based either on ADP or number of assigned full-time equivalent positions. Indirect costs benefiting both ADC operated prison units and private contract prison units have been allocated based on ADP.

As previously noted, the cost comparison only includes FY 2003 costs appropriated to ADC. Costs of central support services provided by other Arizona state agencies in support of ADC operations and asset depreciation on ADC facilities and equipment have not been included. Also, inmate intake and transportation costs have been incorrectly included in ADC's costs

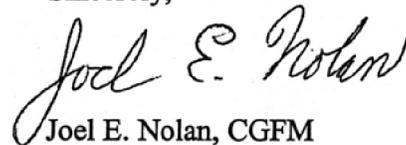
Mr. MacFarlane

- 2 -

because ADC does not currently track inmate intake or transportation costs as separated cost centers. Based on our cursory review, the inclusion of central support and asset depreciation costs and the exclusion of inmate intake and transportation costs attributable to level 2 male inmate beds would increase ADC's average daily costs by less than \$2, an increase of less than 5%.

If you have any questions concerning our review or opinion, please contact us. MAXIMUS appreciated this opportunity to be of service to the Arizona Department of Corrections.

Sincerely,

A handwritten signature in cursive script that reads "Joel E. Nolan".

Joel E. Nolan, CGFM
Vice President

JEN\ksm

MAXIMUS

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2003 DATA

	STATE BEDS			AVERAGE - PRIVATE BEDS		
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,687	\$101,707,322	\$41.67	1,250	\$20,776,165	\$45.54
High Cost Health	6,687	(4,159,504)	(1.70)			0.00
Work Incentive Pay Plan	6,687	(1,661,541)	(0.68)			0.00
Sub-Total Direct Cost		95,886,276	39.29		20,776,165	45.54
Private Prison Monitoring			0.00	1,250	789,722	1.73
Total Direct Costs		95,886,276	39.29		21,565,887	47.27
INDIRECT COSTS						
Office of the Director						
Emp Relations / Equal Opportunity	6,687	146,445	0.06			
Other Director Services	6,687	488,151	0.20	1,250	91,250	0.20
Pris Ops - Central Office	6,687	414,928	0.17	1,250	77,563	0.17
Programs	6,687	439,336	0.18	1,250	82,125	0.18
Security	6,687	366,113	0.15	1,250	68,438	0.15
Offender Svcs	6,687	732,227	0.30	1,250	136,875	0.30
Health Svcs - Central Office	6,687	585,781	0.24	1,250	109,500	0.24
OHU	6,687	122,038	0.05			
Inspect & Invest Bureau	6,687	878,672	0.36	1,250	164,250	0.36
Administrative Services						
Information Tech Svcs	6,687	1,025,117	0.42			
Fleet and Facility Maint.	6,687	244,076	0.10			
Rent/Risk Mgt	6,687	2,172,272	0.89			
Other Admin. Services	6,687	1,000,710	0.41	1,250	187,063	0.41
Human Res / Dev	6,687	805,449	0.33			
Total Indirect Costs		9,421,314	3.86		917,063	2.01
TOTAL COSTS		\$105,307,591	\$43.15		\$22,482,950	\$49.28

¹ Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
² Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
³ Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2003 DATA

	STATE BEDS			MARANA - PRIVATE BEDS		
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,687	\$101,707,322	\$41.67	450	\$7,151,445	\$43.54
High Cost Health	6,687	(4,159,504)	(1.70)			0.00
Work Incentive Pay Plan	6,687	(1,961,541)	(0.68)			0.00
Sub-Total Direct Cost		95,886,276	39.29		7,151,445	43.54
Private Prison Monitoring			0.00	450	284,300	1.73
Total Direct Costs		95,886,276	39.29		7,435,745	45.27
INDIRECT COSTS						
Office of the Director						
Emp Relations / Equal Opportunity	6,687	146,445	0.06			
Other Director Services	6,687	488,151	0.20	450	32,850	0.20
Pris Ops - Central Office	6,687	414,928	0.17	450	27,923	0.17
Programs	6,687	439,336	0.18	450	29,565	0.18
Security	6,687	366,113	0.15	450	24,638	0.15
Offender Svcs	6,687	732,227	0.30	450	49,275	0.30
Health Svcs - Central Office	6,687	585,781	0.24	450	39,420	0.24
OHU	6,687	122,038	0.05			
Inspect & Invest Bureau	6,687	878,672	0.36	450	59,130	0.36
Administrative Services						
Information Tech Svcs	6,687	1,025,117	0.42			
Fleet and Facility Maint.	6,687	244,076	0.10			
Rent/Risk Mgt	6,687	2,172,272	0.89			
Other Admin. Services	6,687	1,000,710	0.41	450	67,343	0.41
Human Res / Dev	6,687	805,449	0.33			
Total Indirect Costs		9,421,314	3.86		330,143	2.01
TOTAL COSTS		\$105,307,591	\$43.15		\$7,765,888	\$47.28

* Comparison does not include Rast (Level 4 cell environment) and Level 2 Female Inmates.
 * Costs based on Department appropriations only.
 * Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 * Inmate transportation costs are included in ADC's costs.
 * Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2003 DATA

	STATE BEDS		FLORENCE WEST DWI - PRIVATE BEDS			
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,687	\$101,707,322	\$41.67	400	\$7,234,300	\$49.55
High Cost Health	6,687	(4,159,504)	(1.70)			0.00
Work Incentive Pay Plan	6,687	(1,661,541)	(0.68)			0.00
Sub-Total Direct Cost		95,886,276	39.29		7,234,300	49.55
Private Prison Monitoring			0.00	400	252,711	1.73
Total Direct Costs		95,886,276	39.29		7,487,011	51.28
INDIRECT COSTS						
Office of the Director						
Emp Relations / Equal Opportunity	6,687	146,445	0.06			
Other Director Services	6,687	488,151	0.20	400	29,200	0.20
Pris Ops - Central Office	6,687	414,928	0.17	400	24,820	0.17
Programs	6,687	439,336	0.18	400	26,280	0.18
Security	6,687	366,113	0.15	400	21,900	0.15
Offender Svcs	6,687	732,227	0.30	400	43,800	0.30
Health Svcs - Central Office	6,687	585,781	0.24	400	35,040	0.24
OHU	6,687	122,038	0.05			
Inspect & Invest Bureau	6,687	878,672	0.36	400	52,560	0.36
Administrative Services						
Information Tech Svcs	6,687	1,025,117	0.42			
Fleet and Facility Maint.	6,687	244,076	0.10			
Rent/Risk Mgt	6,687	2,172,272	0.89			
Other Admin. Services	6,687	1,000,710	0.41	400	59,860	0.41
Human Res / Dev	6,687	805,449	0.33			
Total Indirect Costs		9,421,314	3.86		293,460	2.01
TOTAL COSTS		\$105,307,591	\$43.15		\$7,780,471	\$53.29

^y Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
^z Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
^x Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2003 DATA

	STATE BEDS			PHOENIX WEST DWI - PRIVATE BEDS		
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,687	\$101,707,322	\$41.67	400	\$6,390,420	\$43.77
High Cost Health	6,687	(4,159,504)	(1.70)			0.00
Work Incentive Pay Plan	6,687	(1,661,541)	(0.68)			0.00
Sub-Total Direct Cost		95,886,276	39.29		6,390,420	43.77
Private Prison Monitoring			0.00	400	252,711	1.73
Total Direct Costs		95,886,276	39.29		6,643,131	45.50
INDIRECT COSTS						
Office of the Director						
Emp Relations / Equal Opportunity	6,687	146,445	0.06			
Other Director Services	6,687	488,151	0.20	400	29,200	0.20
Pris Ops - Central Office	6,687	414,928	0.17	400	24,820	0.17
Programs	6,687	439,336	0.18	400	26,280	0.18
Security	6,687	366,113	0.15	400	21,900	0.15
Offender Svcs	6,687	732,227	0.30	400	43,800	0.30
Health Svcs - Central Office	6,687	585,781	0.24	400	35,040	0.24
OHU	6,687	122,038	0.05			
Inspect & Invest Bureau	6,687	878,672	0.36	400	52,560	0.36
Administrative Services						
Information Tech Svcs	6,687	1,025,117	0.42			
Fleet and Facility Maint.	6,687	244,076	0.10			
Rent/Risk Mgt	6,687	2,172,272	0.89			
Other Admin. Services	6,687	1,000,710	0.41	400	59,860	0.41
Human Res / Dev	6,687	805,449	0.33			
Total Indirect Costs		9,421,314	3.86		293,460	2.01
TOTAL COSTS		\$105,307,591	\$43.15		\$6,936,591	\$47.51

^y Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
^z Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
^x Comparison does not include Return to Custody Beds.

MAXIMUS®

HELPING GOVERNMENT SERVE THE PEOPLE®

February 7, 2006

Mr. Doug MacFarlane
Division Director, Support Services
Arizona Department of Corrections
1601 West Jefferson, MC 328
Phoenix, Arizona 85007

Dear Mr. MacFarlane:

At the request of the Arizona Department of Corrections (ADC), MAXIMUS, Inc. has completed a review of schedules prepared by ADC that provide a state versus private cost comparison of Level 2 male inmate beds. The cost comparison is based on actual costs and inmate data incurred during the State fiscal year ended June 30, 2004 (FY 2004). Only costs appropriated to ADC are included in the comparison. The schedules that were reviewed are provided as Exhibit A.

In our opinion the State Versus Private Cost Comparison of Level 2 Male Inmate Beds (Exhibit A) reasonably presents a comparison of the FY 2004 costs incurred by ADC to maintain a male inmate in a level 2 bed in ADC operated prisons and private contract prisons. Our opinion is based on a review of ADC's FY 2004 Operating Per Capita Cost Report, organization charts, organizational duties and responsibilities, and methods for identifying and allocating costs. Cost information included in the cost comparison reconciles to the FY 2004 Per Capita Cost Report and to ADC's actual financial information as recorded on the Arizona Uniform Statewide Accounting System (USAS). Average daily population (ADP) is in accordance with ADC's "Institutional Capacity and Committed Population" report.

All ADC appropriated direct and indirect costs that are applicable to Level 2 prison facilities have been identified and utilized in developing the cost comparison. Direct costs are costs directly incurred by and/or for the benefit of an ADC prison unit and payments to private contractors. Indirect costs are costs of ADC administration and support units, and program operational support units that benefit multiple ADC prison units and/or private contract prison units. Indirect costs benefiting only ADC operated prison units have been allocated only to ADC operated prison units based either on ADP or number of assigned full-time equivalent positions. Indirect costs benefiting both ADC operated prison units and private contract prison units have been allocated based on ADP.

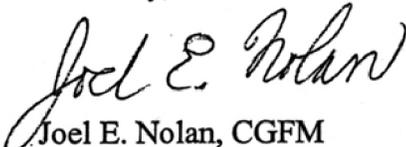
As previously noted, the cost comparison only includes FY 2004 costs appropriated to ADC. Costs of central support services provided by other Arizona state agencies in support of ADC operations and asset depreciation on ADC facilities and equipment have not been included. Also, inmate intake and transportation costs have been incorrectly included in ADC's costs

because ADC does not track inmate intake or transportation costs as separated cost centers. Based on our cursory review, the inclusion of central support and asset depreciation costs and the exclusion of inmate intake and transportation costs attributable to level 2 male inmate beds would increase ADC's average daily costs by less than \$2, an increase of less than 5%.

This is the second year MAXIMUS has reviewed the level 2 male inmate beds comparison. ADC continues to demonstrate an ability to utilize the appropriate methodologies and procedures required to develop an accurate, reasonable comparison of the cost to maintain a male inmate in a State versus private prison. The reconciliation of all expenditure data to the annual per capita cost report and to USAS financial information, and the use of ADP information from published reports ensure the validity of the financial and ADP information on which the comparison is based. The allocation of indirect costs only to State and private prisons benefiting from each services and using allocation bases that reasonably represent benefit received ensure that only appropriate indirect costs are allocated to private prisons. Continuation of current methodologies and procedures should enable ADC to develop accurate cost comparisons in future years.

If you have any questions concerning our review or opinion, please contact us. MAXIMUS appreciated this opportunity to be of service to the Arizona Department of Corrections.

Sincerely,


Joel E. Nolan, CGFM
Vice President

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STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2004 DATA

	STATE BEDS			AVERAGE - PRIVATE BEDS		
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,750 ¹	\$105,022,997 ²	\$42.51	1,250 ²	\$20,833,086	\$45.54
High Cost Health	6,750	(4,634,615)	(1.88)			0.00
Work Incentive Pay Plan	6,750	(2,696,065)	(1.09)			0.00
Sub-Total Direct Cost		97,692,317	39.54		20,833,086	45.54
Private Prison Monitoring			0.00	1,250	821,985	1.80
Total Direct Costs		97,692,317	39.54		21,655,071	47.33
INDIRECT COSTS						
Office of the Director						
Emp Relations / Equal Opportunit	6,750	74,115	0.03			
Other Director Services	6,750	568,215	0.23	1,250	106,221	0.23
Pris Ops - Central Office	6,750	469,395	0.19	1,250	88,451	0.19
Programs	6,750	444,690	0.18	1,250	82,538	0.18
Security	6,750	123,525	0.05	1,250	24,682	0.05
Offender Svcs	6,750	691,740	0.28	1,250	129,217	0.28
Health Svcs - Central Office	6,750	765,855	0.31	1,250	141,410	0.31
OHU	6,750	123,525	0.05			
Inspect & Invest Bureau	6,750	765,855	0.31	1,250	142,320	0.31
Administrative Services						
Information Tech Svcs	6,750	1,087,020	0.44			
Fleet and Facility Maint.	6,750	148,230	0.06			
Rent/Risk Mgt	6,750	3,063,420	1.24			
Other Admin. Services	6,750	617,625	0.25	1,250	115,176	0.25
Human Res / Dev	6,750	988,200	0.40			
Total Indirect Costs		9,931,410	4.02		830,014	1.81
TOTAL COSTS		\$107,623,727	\$43.56		\$22,485,085	\$49.15

¹ Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
² Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
³ Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2004 DATA

	STATE BEDS			MARANA - PRIVATE BEDS		
	ADP	TOTAL COST	DAILY AVG	ADP	TOTAL COST	DAILY AVG
DIRECT COSTS:						
Direct Costs / Contract Costs	6,750 ^y	\$105,022,997 ^z	\$42.51	450	\$7,171,038	\$43.54
High Cost Health	6,750	(4,634,615)	(1.88)			0.00
Work Incentive Pay Plan	6,750	(2,696,065)	(1.09)			0.00
Sub-Total Direct Cost		97,692,317	39.54		7,171,038	43.54
Private Prison Monitoring			0.00	450	295,915	1.80
Total Direct Costs		97,692,317	39.54		7,466,953	45.34
INDIRECT COSTS						
Office of the Director	6,750	74,115	0.03			
Emp Relations / Equal Opportunit	6,750	588,215	0.23	450	38,240	0.23
Other Director Services						
Pris Ops - Central Office	6,750	469,395	0.19	450	31,842	0.19
Programs	6,750	444,690	0.18	450	29,714	0.18
Security	6,750	123,525	0.05	450	8,886	0.05
Offender Svcs	6,750	691,740	0.28	450	46,518	0.28
Health Svcs - Central Office	6,750	765,855	0.31	450	50,908	0.31
OHU	6,750	123,525	0.05			
Inspect & Invest Bureau	6,750	765,855	0.31	450	51,235	0.31
Administrative Services						
Information Tech Svcs	6,750	1,087,020	0.44			
Fleet and Facility Maint.	6,750	148,230	0.06			
Rent/Risk Mgt	6,750	3,063,420	1.24			
Other Admin. Services	6,750	617,625	0.25	450	41,463	0.25
Human Res / Dev	6,750	988,200	0.40			
Total Indirect Costs		9,931,410	4.02		298,805	1.81
TOTAL COSTS		\$107,623,727	\$43.56		\$7,765,758	\$47.15

^y Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.

^z Costs based on Department appropriations only.

Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.

Inmate transportation costs are included in ADC's costs.

^x Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2004 DATA

	STATE BEDS		FLORENCE WEST DWI - PRIVATE BEDS	
	ADP	TOTAL COST	ADP	TOTAL COST
DIRECT COSTS:				
Direct Costs / Contract Costs	6,750 ¹	\$105,022,997 ²	400	\$7,254,120
High Cost Health	6,750	(4,634,615)		\$49.55
Work Incentive Pay Plan	6,750	(2,696,065)		0.00
				0.00
Sub-Total Direct Cost		97,692,317		49.55
Private Prison Monitoring			400	263,035
				1.80
Total Direct Costs		97,692,317		51.35
INDIRECT COSTS				
Office of the Director				
Emp Relations / Equal Opportunit	6,750	74,115		0.03
Other Director Services	6,750	568,215	400	33,991
				0.23
Pris Ops - Central Office	6,750	469,395	400	28,304
Programs	6,750	444,690	400	26,412
Security	6,750	123,525	400	7,898
Offender Svcs	6,750	691,740	400	41,349
Health Svcs - Central Office	6,750	765,855	400	45,251
OHU	6,750	123,525	400	0.31
Inspect & Invest Bureau	6,750	765,855	400	45,542
Administrative Services				0.31
Information Tech Svcs	6,750	1,087,020		0.44
Fleet and Facility Maint.	6,750	148,230		0.06
Rent/Risk Mgt	6,750	3,063,420		1.24
Other Admin. Services	6,750	617,625	400	36,856
Human Res / Dev	6,750	988,200		0.25
				0.40
Total Indirect Costs		9,931,410		4.02
TOTAL COSTS		\$107,623,727		\$43.56
				\$7,782,760
				1.81
				\$53.16

¹ Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
² Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
³ Comparison does not include Return to Custody Beds.

STATE OF ARIZONA
DEPARTMENT OF CORRECTIONS
STATE VERSUS PRIVATE
COMPARISON OF LEVEL 2 MALE INMATE BEDS
BASED ON FY 2004 DATA

	STATE BEDS		PHOENIX WEST DWI - PRIVATE BEDS	
	ADP	TOTAL COST	ADP	TOTAL COST
DIRECT COSTS:				
Direct Costs / Contract Costs	6,750 ¹	\$105,022,997 ²	400	\$6,407,928
High Cost Health	6,750	(4,934,615)		
Work Incentive Pay Plan	6,750	(2,696,065)		
				\$43.77
				0.00
				0.00
Sub-Total Direct Cost		97,692,317		6,407,928
Private Prison Monitoring			400	263,035
				1.80
Total Direct Costs		97,692,317		6,670,963
				45.57
INDIRECT COSTS				
Office of the Director				
Emp Relations / Equal Opportunit	6,750	74,115		0.03
Other Director Services	6,750	568,215	400	33,991
				0.23
Pris Ops - Central Office	6,750	469,395	400	28,304
Programs	6,750	444,690	400	26,412
Security	6,750	123,525	400	7,898
Offender Svcs	6,750	691,740	400	41,349
Health Svcs - Central Office	6,750	765,855	400	45,251
OHU	6,750	123,525	400	45,251
Inspect & Invest Bureau	6,750	765,855	400	45,542
Administrative Services				0.31
Information Tech Svcs	6,750	1,087,020		0.44
Fleet and Facility Maint.	6,750	148,230		0.06
Rent/Risk Mgt	6,750	3,063,420		1.24
Other Admin. Services	6,750	617,625	400	36,856
Human Res / Dev	6,750	988,200		0.25
				0.40
Total Indirect Costs		9,931,410		265,605
				1.81
TOTAL COSTS		\$107,623,727		\$6,936,568
				\$47.38

¹ Comparison does not include Rast (Level 4 cell environment) and Level 2 Female inmates.
² Costs based on Department appropriations only.
 Costs of support services provided by other state agencies in support of ADC operations and asset depreciation are not included.
 Inmate transportation costs are included in ADC's costs.
³ Comparison does not include Return to Custody Beds.

Arizona Department of Corrections



JANET NAPOLITANO
GOVERNOR

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DORA B. SCHIRO
DIRECTOR

February 8, 2006

Joel E. Nolan
Vice President, Cost Services Division
MAXIMUS, Inc.
2226 W. Northern Avenue, Suite C 207
Phoenix, Arizona 85021

RE: ADC response to "Report on the Evaluation of Arizona Department of Corrections Operating Per Capita Cost Report and Private Prison Cost Model"

Dear Mr. Nolan:

The Arizona Department of Corrections (ADC) issued a request for proposals and selected Maximus, Inc. to evaluate the methodologies by which the ADC compares the costs of various prison operating structures and review its financial data for FY 2003 and FY 2004. The ADC received your report this month and has reviewed the document in its entirety.

The report recommends that the ADC improves the Per Capita Cost Report and limits its usage, strengthens the Private Prison Cost Model to meet the requirements of ARS 41-1609.01 (G), and adopts specific cost comparisons of the operation of state and private prison beds to respond to ARS 41-1609.01 (L). The ADC agrees with all of the recommendations concerning each of the three reports and has determined that most of them can be implemented immediately. In several instances however, additional financial reports must be developed to capture detailed data effective FY 2007. In all instances, recommendations will be implemented in full in time to produce FY 2007 reports. Information about the implementation of each recommendation follows.

Recommendations for Improvement: Operating Per Capita Cost Report

Section II, Page 12, Report Format - Additional Narrative: It is recommended that narratives be added stating the objectives of the Cost Report, clarifying the methodologies, and describing the purpose of and the information presented on each exhibit.

Response: ADC agrees to implement immediately. The narrative was included in the FY 2004 Per Capita Cost Report.

Section II, Page 12, Report Format - New and Reordering Exhibits: Exhibits should be developed and presented in an order that supports the objectives of the cost report.

Response: ADC agrees to implement immediately. Exhibits will be presented in a manner that supports the objectives of the cost report beginning with the FY 2005 Operating Per Capita Cost Report.

Section II, Page 13, Report Format - Redesign Exhibits: Exhibits should be either redesigned or new exhibits added that present direct costs by major cost component.

Response: ADC agrees to implement the accounting structure will be modified and added to capture costs beginning in FY 2007.

Section II, Page 14, Methodology Improvements - Classifying Costs: Currently, costs associated with inmate intake and transportation are classified as direct costs of the ADC prison unit or complex incurring the expenses. These costs should not be direct costs utilized in the development of a unit's operating per capita cost. These costs benefit both ADC and private prisons, and should be tracked and identified as a separate cost category in the cost report.

Response: ADC agrees to implement. The accounting structure will be modified to capture these costs appropriately beginning FY 2007.

Section II, Page 14, Methodology Improvements - Indirect Cost Allocations: Certain indirect costs (labor relations, information technology, and administrative services) should be reallocated.

Response: ADC agrees to implement immediately. The identified indirect costs were reallocated in the FY 2004 Per Capita Cost Report.

Section II, Page 15, Documentation of Procedures: Develop a comprehensive manual including written detailed regarding methodologies, assumptions, procedures, time lines, and sources of data presented in the Per Capita Cost Report.

Response: ADC agrees to implement immediately. The manual will be completed and included with the FY 2005 Per Capita Cost Report.

Recommendations for Improvement: State Versus Private Prison Cost Comparison

Section III, Page 19, Narratives: Narratives should be developed stating the objectives of the comparison report, clarifying the methodologies, and describing the purpose of and the information on each exhibit.

Response: ADC agrees and will include appropriate narratives in cost comparison reports beginning in FY 2006.

Section III, Page 19, Exhibits: Exhibits should be developed presenting direct and indirect costs by major cost component or service.

Response: ADC agrees and will present direct and indirect costs by major component beginning in FY 2006.

Section III, Page 20, Cost Identification - Costs to be Included: The comprehensive costs of each custody level should be comprised of three principal components: ADC direct and indirect operating costs, asset depreciation, and costs of central support services provided by other Arizona State agencies in support of ADC operations.

Response: ADC agrees and will include these components in cost comparison reports beginning in FY 2006.

Section III, Page 21 Cost Identification - Costs to be Excluded: The Cost Report only includes costs of inmate intake, transportation, high cost health and the work incentive pay plan in the average daily cost of the ADC operated prisons. These costs should be excluded in developing a cost comparison.

Response: ADC agrees and excluded High Cost Health and WIPP in the FY 2003 and FY 2004 cost comparison reports. Inmate intake and transportation will be excluded beginning FY 2007 after accounting structure is modified.

Section III, Page 22, Documentation of Procedures: MAXIMUS recommends the development of a comprehensive manual that includes written details regarding methodologies, assumptions, procedures, time lines, and sources of the data presented in the Comparison Report.

Response: ADC agrees and will include a comprehensive manual beginning with reports generated for FY 2006.

Recommendations for Improvement: Private Prison Cost Model

Section III, Page 27, Discontinue the Usage of the Historical Cost Model: Only the projected Cost Model should be utilized for developing comparative analysis.

Response: ADC agrees that only the revised projected cost model will be employed in all future cost comparisons and that the historical cost model will be discontinued.

Section III, Page 27, Costs to be Included: ADC should only include additional costs incurred as the result of operating a new facility.

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 27, Projected Construction Costs: Construction cost estimates should be specific to the size of the facility and its site.

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 27, Start-Up Costs: Start-up costs should be estimated and included in ADC's costs.

Joel E. Nolan
February 8, 2006
Page 4

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 27, Operating Costs: A budget should be developed for the size of and the site of the facility being analyzed.

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 28, Central Administrative Support: Only the personal services costs of additional staff and other operating costs should be developed.

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 28, Contractor Support: ADC should only add actual additional costs to contract.

Response: ADC agrees and will employ in all future cost comparisons.

Section III, Page 28, Comprehensive Manual: Develop a comprehensive manual including written detailed regarding methodologies, assumptions, procedures, time lines, and sources of data presented in the Private Prison Cost Report.

Response: ADC agrees and will employ in all future cost comparisons.

Sincerely,



Douglas E. Macfarlane
Division Director
Support Services

DEM/cp