



Legislative Post Audit Performance Audit Report Highlights

Department of Corrections: Comparing the Merits of Lease and Bond Options for Replacing Lansing Correctional Facility

July 2017 • R-17-011

QUESTION 1: How do the Costs, Benefits, and Risks of Bonding Versus Leasing Compare as a Way to Pay for the Improvements to the Lansing Correctional Facility?

Background Information

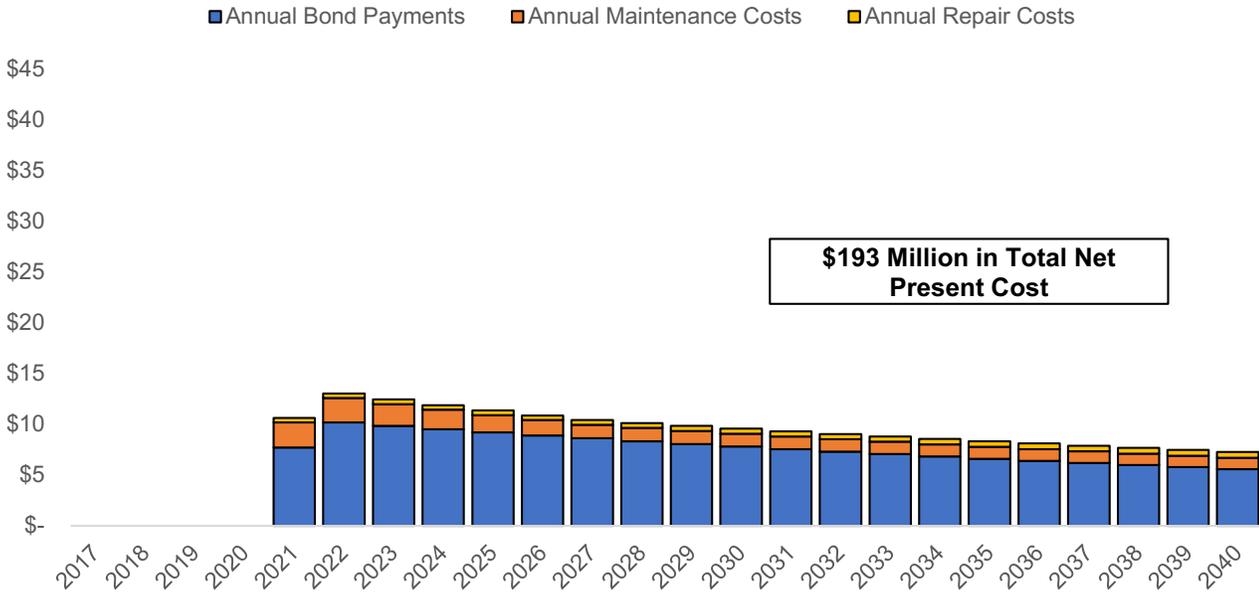
With its original facility completed in 1867, Lansing Correctional Facility (Lansing) is the oldest and largest correctional facility in the state. As of June 2017, Lansing had a population of more than 2,300 inmates. For fiscal year 2017, it employed almost 600 staff and had an operating budget of more than \$40 million. The original part of the prison is still in use, and houses maximum security inmates.

The Kansas Department of Corrections (KDOC) currently plans to rebuild Lansing's medium security unit so it can hold medium and maximum security inmates. A request for proposals for this project was issued in April 2017. KDOC officials are not considering renovating the existing facilities due to their age and outdated design. To make the project budget neutral, the prison design must be updated so fewer correctional officers are required.

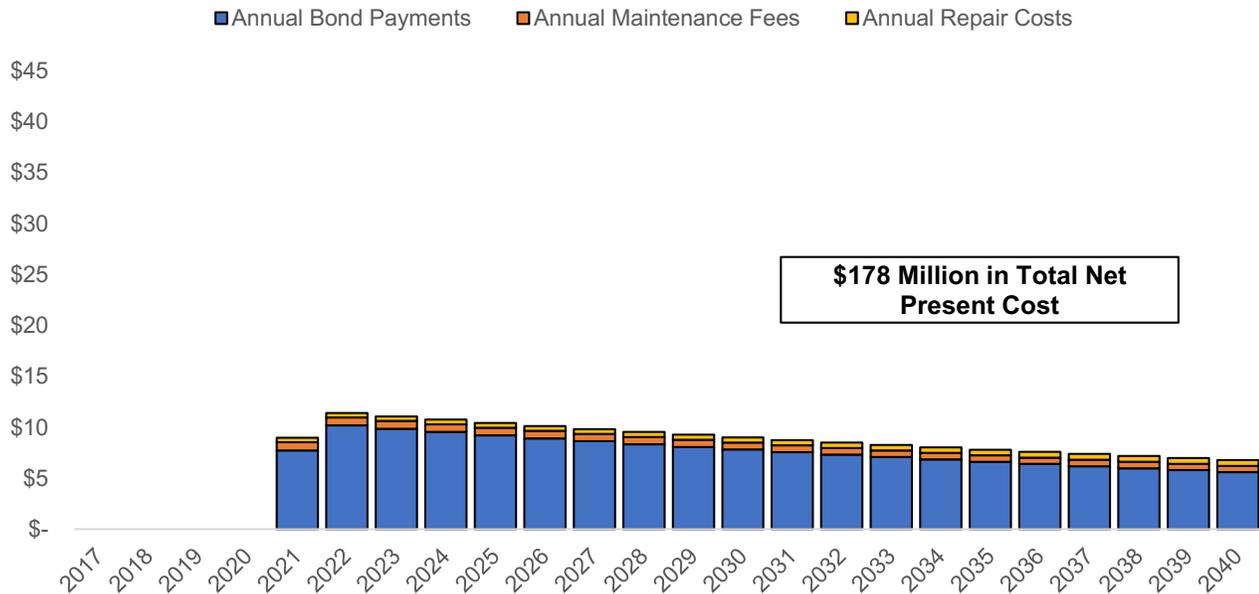
- KDOC is considering both state financing (bonding) and contractor financing (leasing) for Lansing. Regardless of which option is chosen, the state will continue to operate the facility. (p. 7)
 - *With bond financing, the state would issue bonds to pay for construction of the new facility and would own it from the beginning.*
 - *With lease-purchase financing, a private firm would build and own the new facility, then lease it to the state for a period of time before eventually selling it to the state.*
- We used a life-cycle cost model to estimate which option would be most cost effective. (p. 9)
 - *A life-cycle cost model is commonly used to estimate the costs associated with different project options to identify which is least expensive over time.*
 - *We considered the following costs: design and construction costs, ongoing maintenance costs, rehabilitation and repair costs, annual bond debt service payments, annual lease payments, and the final purchase price.*
 - *Finally, we discounted the cash flows to current dollars to calculate the net present cost of each option.*
- Our analysis found bond financing with contracted maintenance would likely be the most cost effective option, with an estimated net present cost of \$178 million over 20 years. (p. 13)
 - *Bond financing with state maintenance had an estimated net present cost of \$193 million over 20 years.*
 - *A 20-year lease-purchase agreement with either a final purchase payment or the purchase price built into the lease payments had an estimated net present cost of \$206 million over 20 years.*
- These results differ from KDOC's preliminary estimates, which were missing key variables and used inconsistent assumptions that tended to favor a lease-purchase option (p. 16)
- The state's two options for rebuilding Lansing create some additional risks and benefits for the state. (p. 17)
 - *If KDOC chooses a lease-purchase option, there are some additional contract risks that will require legal counsel with skills specific to lease financing for large scale construction projects.*
 - *A lease-purchase contract lowers the state's risks related to construction costs, property damage, and ongoing repairs.*
 - *Regardless of whether lease or bond financing is used, relying on contracted maintenance increases the risk that necessary maintenance will be deferred.*

**Figure 1-3
Payments Made During Bond Repayment Period
(Discounted to Net Present Cost)**

Design-Build with Reduced State Maintenance Cost (In Millions) (a)



Design-Build-Maintain with Contracted Maintenance (In Millions) (b)

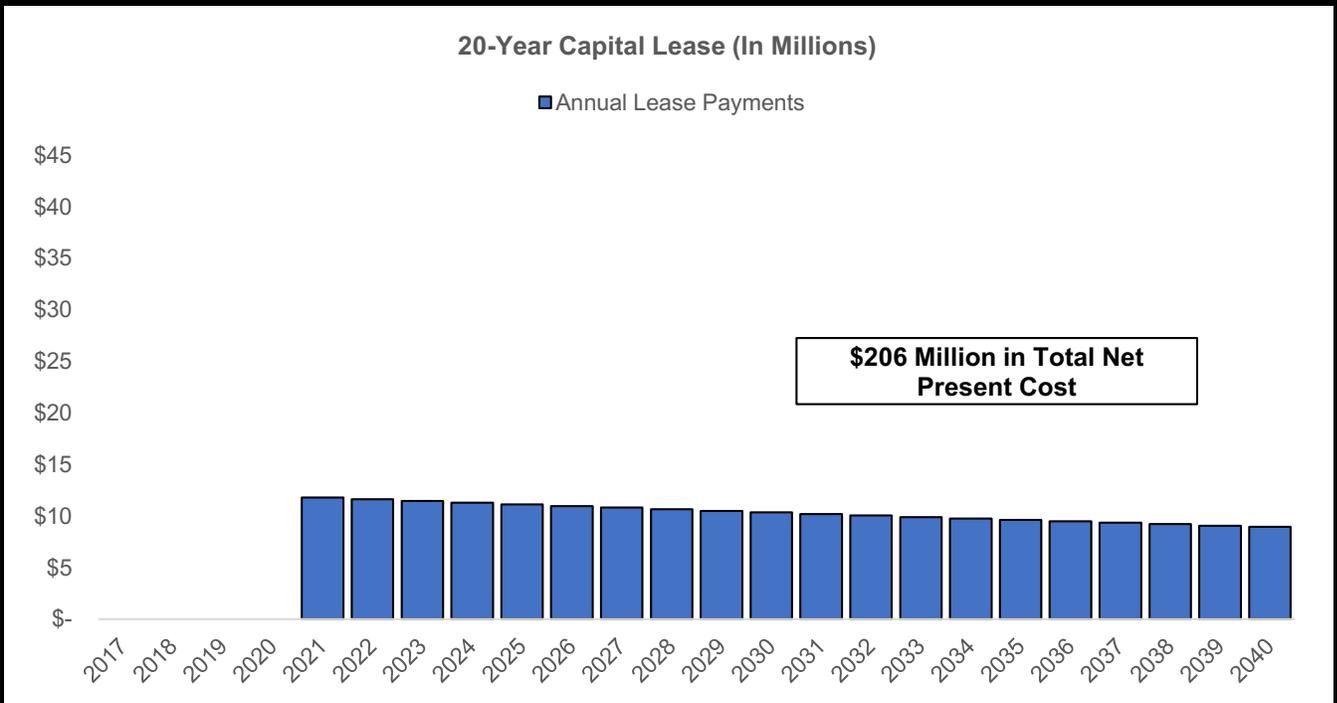
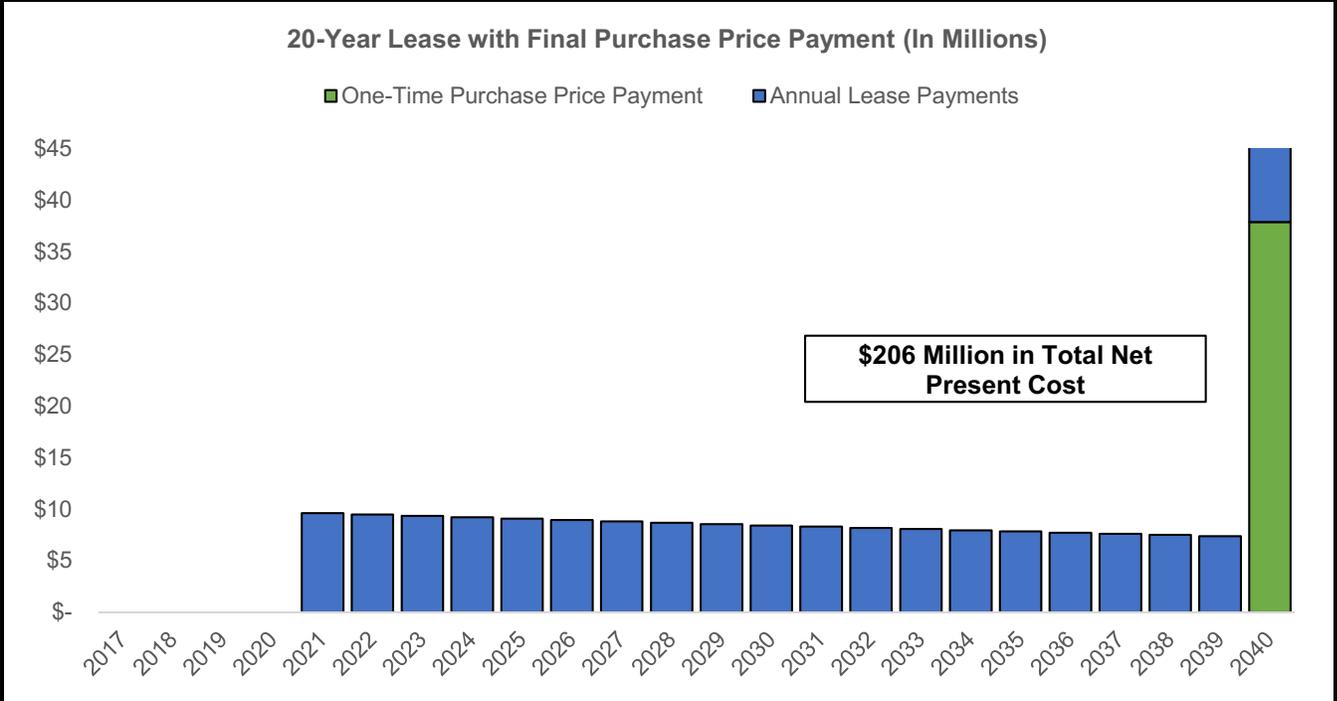


(a) Reflects a 40% maintenance cost reduction compared to the existing facility because the new facility is newer and less labor intensive, with these savings phased in gradually during the first seven years of operation.

(b) Includes 20 years of contracted maintenance followed by state maintenance provision at the reduced rates described in footnote (a).

Source: LPA research and LPA analysis of information from Kansas Department of Corrections and Kansas Development Finance Authority (audited).

**Figure 1-4
Payments Made During Lease Term
(Discounted to Net Present Cost)**



Source: LPA research and LPA analysis of information from Kansas Department of Corrections and Kansas Development Finance Authority (audited).

SUMMARY OF RECOMMENDATIONS

Recommendations for the Kansas Department of Corrections (p. 19)

KDOC should evaluate the proposals it receives using a life-cycle cost model that takes all relevant factors into account and ensure any cost comparisons use consistent assumptions.

If KDOC chooses a lease-purchase contract, it should consult with independent outside counsel and ensure the final contract includes a final purchase price.

KDOC should conduct a review of Lansing's maintenance needs and develop a plan to scale down its maintenance staff.

AGENCY RESPONSE

Department officials agreed with the findings and indicated they would implement the recommendations. (p. 22)

HOW DO I REQUEST AN AUDIT?

By law, individual legislators, legislative committees, or the Governor may request an audit, but any audit work conducted by the division must be directed by the Legislative Post Audit Committee. Any legislator who would like to request an audit should contact the division directly at (785) 296-3792.

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