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# Left at the Altar

## Cornell's History of Broken Promises

### Background on Cornell Companies, of Houston, Texas

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*Truth is in things, and not in words.*  
—Herman Melville

## **Background**

On November 17, 2003 Cornell Companies, Inc. submitted a document entitled “Plan, Site and Promote a 500-750 Bed Private Correctional Facility in Lamar, Colorado.” The document was a response to a request for qualifications (RFQ) issued by an ad-hoc committee comprised of several local government officials and business owners.

This document provides additional information—vital to the ability of Prowers County residents to make an informed decision about the proposed prison—that Cornell conveniently omitted from their proposal. While Cornell can write inspiring descriptions of their commitment to help people and communities, their track record of actions is far more telling.

Our document is organized to mirror the format of Cornell’s response to the RFQ. Each section consists of three elements: the text of the question from the original RFQ, Cornell’s response (or an excerpt thereof), and evidence from newspapers and other sources.

Cornell’s complete response can be viewed at Lamar City Administrator Jeff Anderson’s office in the Lamar Municipal Complex (336-4376).

**RFQ:** [Discuss the] general background of the Company to include its legal domicile, headquarters, name and resume of CEO, CFO, Governmental Affairs Director and Board of Directors

**Cornell’s Response:** Cornell responded by discussing its five “core values,” each of which is discussed in more detail below.

### Core Value #1: Quality Services

*Cornell believes that through caring, comprehensive programs that provide dignity, hope, safety and accountability, people can change. We ensure the quality of our facilities and programs by voluntarily submitting to rigorous accreditation processes, adhering to our programming foundations and serving local communities. (page 3)*

△ Cornell was recently forced to close its New Morgan Academy youth facility in Morgantown, PA when it lost its state license to operate a juvenile facility. A state investigator remarked “this is unheard of to have that many allegations [of abuse]...in any program.” Cornell spokesman Paul Doucette told reporters that “we have had a series of people who not only failed to abide by (company) policy, but failed to abide by state law and common decency,” adding that the New Morgan Academy “did not work and we were not able to get the job done.”<sup>1</sup>

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<sup>1</sup> Associated Press, “Juvenile detention center to close following abuse cases,” September 28, 2002; Steve Twedt, “Facilities scarcer for special delinquents” *Pittsburgh Post-Gazette* November 3, 2002, B-1.

- ⚠ An audit of Cornell's prison in Folkston, Georgia found that staff was conducting inaccurate inmate head counts and did not have certified employees patrolling the perimeter.<sup>2</sup>

### Core Value #2: Employee Value

*Our business bears an immense responsibility in caring for human lives. Our employees must understand and embrace both the privilege and burden that accompanies the care of an adult or adolescent. Employee training is a priority because it helps to ensure that our residents receive the highest quality care possible offering delivery of the innovative, appropriate and effective treatment. (page 4)*

- ⚠ Pennsylvania state investigators announced 31 separate substantiated reports of abuse against teenage residents of Cornell's New Morgan Academy (Morgantown, PA) occurring over the course of two years. Sixteen cases involved sexual abuse, including sexual intercourse between staff and residents. Twenty staff members were fired as a result of an investigation.<sup>3</sup>
- ⚠ In 1999 Cornell hired four people with felony records to work as corrections officers at the Santa Fe County Juvenile Detention Center. One of the men was fired after a 15 year-old female inmate accused him of raping her. Even though Cornell's contract required background checks for all new employees, Cornell claimed they were not aware of that provision.<sup>4</sup>

### Core Value #3: Leadership

*We focus on establishing industry standards that become the benchmarks of quality care and ethical behavior. Committing to and carrying out our desire to make a positive difference in the lives of individuals, families and communities accomplish this ambitious goal. (page 4)*

- ⚠ Cornell hired Lawrence Barreras as the warden of the Santa Fe County Detention Center, without disclosing to county officials that Mr. Barreras had been fired as the head of a state prison two years previously for "conspiring to misappropriate public funds for private gains, as well as other unspecified felonies and misdemeanors."<sup>5</sup>

### Core Value #4: Partnership

*Dedicated to creating synergistic partnerships, Cornell works closely with representatives of contracting agencies, family members of our residents and offenders, and community members in which a facility is located. Regular, responsive communication is essential to meeting the needs of the individuals entrusted to our care and the company's success. (page 4)*

- ⚠ The town of Delta Junction, Alaska agreed to award a non-competitive contract to Cornell's subsidiary Allvest, Inc. to operate a prison at the decommissioned Fort Greely Army Post. When the city clerk certified a voter petition to put the issue on the ballot, Allvest/Cornell sued the city, asking for more than \$1 million in damages if the vote did not go in Cornell's favor. City Council voted to cancel the contract in order to avoid the

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<sup>2</sup> James Pilcher, "Private prison working on problems in critical state audits," *Associated Press* December 30, 1998.

<sup>3</sup> Steve Twedt, "Facilities scarcer for special delinquents" *Pittsburgh Post-Gazette* November 3, 2002, B-1.

<sup>4</sup> S.U. Mahesh, "Officials: Firm hiring guards with criminal records" *Albuquerque Journal* April 29, 1999, 6.

<sup>5</sup> Steve Terrell, "Jail warden was fired from state prisons position" *Santa Fe New Mexican* June 2, 1999, A-4.

election, prompting Allvest/Cornell to file another lawsuit against the city. City Councilwoman Mary Leith Dowling told the press that “every time we turned around we got hit with a nasty letter from them about something. They did not attempt to work with us as business partners.” The city ended up signing a settlement with Allvest/Cornell for \$1.1 million.<sup>6</sup>

⚠️ Cornell worked with the city of Central Falls, Rhode Island to build a detention center for short-term federal detainees. Shortly after the facility opened, Cornell broke their original promise not to hold sentenced prisoners and signed a contract with North Carolina to house 190 state prisoners in the Central Falls prison. Left without any other options, the city sued Cornell in 1994.<sup>7</sup>

⚠️ In 1999 Cornell responded to a request for proposals issued by the state of Utah. Cornell was selected as the best bidder, *but no contract was ever signed*. When the state finally announced its plans to not award a contract due to a decline in the prison population, Cornell threatened to sue, finally settling a \$1.57 million payment from the taxpayers of Utah.<sup>8</sup>

#### Core Value #5: Reinvestment and Company Growth

*We reinvest Company profits back into our operations to continually grow our programs and staff, thereby increasing Company value. By expanding our Company’s national presence, we are able to provide more comprehensive, responsive and enhanced services. We deliver the most appropriate services and programs by a well-trained work force in a cost-effective environment. (page 5)*

⚠️ Cornell compensates its corporate executives with salaries and bonuses that far surpass the salaries paid to the management of the Colorado Department of Corrections (DOC). Since the state would only pay Cornell an amount roughly equal to the per-inmate cost of a medium security inmate in the state prison system, that means Cornell’s lavish compensation plans would come at the expense of local staff. Some examples include:

⚠️ In September 2002, Cornell’s president Steven W. Logan resigned after the company’s accounting scandal had become public. Cornell paid Logan \$1.5 million in severance anyway.<sup>9</sup> Moreover, in 2002 (the last full year of Logan’s employment), Mr. Logan received total compensation of nearly three million dollars, in the following manner: \$425,000 base salary, \$205,000 bonus, \$6,128 in fringe benefits, and an estimated \$2.28 million in stock options (based on the value at year end 2001).<sup>10</sup>

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<sup>6</sup> Associated Press, “Allvest files breach-of-contract lawsuit against Delta Junction” September 15, 1999; Associated Press, “Delta Junction unsure how to fill \$1 million hole” July 5, 2002.

<sup>7</sup> Marion Davis, “Prison gets crowded as lawsuit nears on who should stay” *Providence Journal-Bulletin* December 30, 1996, 1C; Associated Press, “Central Falls detention center plans \$25039 million expansion” December 2, 2001.

<sup>8</sup> Greg Burton, “Prison that wasn’t may cost state” *Salt Lake Tribune* March 31, 2001 B1; Dennis Romboy, “Utah pays \$12 million to settle a few disputes” *Deseret News* June 21, 2001, A-01.

<sup>9</sup> Cornell Companies, Inc., Fiscal Year 2003 Form 10-K, SEC Accession Number 0001104659-04-007464 (March 15, 2004), 40.

<sup>10</sup> Cornell Companies, Inc., SEC Form DEF 14A, SEC Accession Number 0000912057-02-020130 (May 14, 2002), 11-12.

- ⚠ In 2003, company founder David M. Cornell—who is no longer an employee of the corporation—received over three-quarters of a million dollars in the following manner: \$255,000 consulting contract, \$75,000 consulting contract *bonus*, \$100,000 cash bonus in lieu of exercising stock options, \$120,000 from non-compete agreement (payment terms of \$10,000 per month for *seven years*), and \$223,000 in premium payments to a personal life insurance policy.<sup>11</sup> This is seven times the FY 2003 salary of the Executive Director of the Colorado DOC.<sup>12</sup>
- ⚠ Cornell has spent a lot of money to compensate for financial mistakes and litigation. All of these expenditures represent money that isn't put into communities where Cornell's facilities are located. For example:
  - ⚠ In 2002, Cornell paid \$1.9 million in legal fees to sort out accounting irregularities (which resulted in an SEC investigation which is still ongoing, see next section).<sup>13</sup>
  - ⚠ In 2003, Cornell lost track of \$12.9 million budgeted for the purchase of a new juvenile correctional facility in Cañon City, Colorado. Cornell deposited the money into the wrong bank account and by the time they located the funds (at a different bank), \$7.9 million was missing.<sup>14</sup>
  - ⚠ During 2001, Cornell spent \$200,000 to defend itself against class action lawsuits by shareholders who were upset by the company's accounting practices.<sup>15</sup> More recent figures are not available, but litigation against Cornell is still pending.<sup>16</sup>

**RFQ:** [provide] Financial Statements for the last three fiscal years and at least one bank reference.

*Cornell is a financially strong company. Company revenues in 2002 were \$275.1 million, representing a 3.7% increase from 2001.*

- ⚠ As the fallout from Cornell's accounting restatements has continued, revenue and profits have dropped. Cornell's total revenues for 2003 represented a 1.3% decrease from prior year's revenues, while 2003 profits declined 37.6% from 2002 levels.<sup>17</sup> Decreased profits have continued, with Cornell's first quarter 2004 profits down 63.9% from the same quarter in 2003.<sup>18</sup>
- ⚠ In 2002, Cornell withdrew from two real estate partnerships which raised concerns due to the financial structures used. Cornell had employed a sale/leaseback transaction and a synthetic lease transaction to reduce the amount of debt that appeared on the corporate balance sheet. These transactions resulted in Cornell restating financial statements for

<sup>11</sup> Cornell Companies, Inc., SEC Form DEF 14A, SEC Accession Number 0001047469-04-014371 (April 29, 2004), 9-10.

<sup>12</sup> Colorado Department of Corrections, *FY 2004-05 Budget Request*, 301.

<sup>13</sup> Cornell FY 2003 Form 10-K, 43.

<sup>14</sup> Cornell FY 2003 Form 10-K, 16.

<sup>15</sup> Cornell FY 2003 Form 10-K, 43.

<sup>16</sup> See *Williams v. Cornell Companies*, No. H-02-0866 (S.D. Tex.).

<sup>17</sup> Cornell FY 2003 Form 10-K, 63.

<sup>18</sup> Cornell Companies, Inc., SEC Form 10-Q, SEC Accession Number 0001104659-04-013617 (May 10, 2004), 3.

two fiscal years, which led to a 63% drop in stock prices.<sup>19</sup> Investors were particularly upset due to the similarities between Cornell's accounting methods and the Enron scandal. Cornell's auditor at the time of the suspect transactions was Arthur Anderson (also the auditor for Enron).<sup>20</sup>

⚠ On June 4, 2004, Moody's Investors Service assigned Cornell a credit rating of B3 for senior unsecured notes.<sup>21</sup> Ratings in the B category are "considered speculative and are subject to high credit risk." The 3 is a sub-category assigned on a scale of 1 (high end of the main category) to 3 (low end of the main category).<sup>22</sup> Cornell's main competitors (Corrections Corporation of America and the GEO Group) both have slightly higher ratings of B1 for senior unsecured notes. To illustrate the risk of a B-rated security, Moody's reports that from 1970-97, the average five-year cumulative default rate for B-rated securities was 30.8%—nearly three times higher than the average default rate of 11.5% for Ba-rated securities (the next highest rating category).<sup>23</sup>

**RFQ:** Address your company's corporate philosophy on maximizing economic benefits to the community where you are located.

*One of the most basic methods for maintaining our reputation for quality and effectiveness is constantly improving the performance and productivity of our projects. Cornell accomplishes this by working to improve the quality of our people through our proven hiring system. (page 16)*

⚠ In 2002, Cornell's Alexander Youth Services Center in Arkansas was the subject of an investigation by the U.S. Department of Justice. Investigators focused on recent suicides by residents and found that "direct care staff had failed to conduct required checks on the [suicide victim], had falsified records, and failed to ensure his safety and security." In their report, Justice Department investigators noted "many of the counselors we interviewed during our visit stated that they did not believe they had the knowledge or experience to provide individual mental health treatment to residents."<sup>24</sup>

*Cornell has gained a reputation of being able to build positive relationships with a variety of local educational providers to meet the needs of residents. Our team recognizes the value of educational and training services for the residents in our care and will begin working with the Lamar Community College upon award of a contract. (page 18)*

⚠ The 2002 Justice Department investigation of Cornell's Arkansas youth facility (see previous section) found that employees were not adequately trained and that "the general

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<sup>19</sup> L.M. Sixel, "Houston-Based Prison Management Firm Corrects Its Accounts" *Houston Chronicle* March 7, 2002; and "Law Firm of Scott & Scott, LLC Announces Class Action Lawsuit Against Cornell Companies," *PR Newswire* April 26, 2002.

<sup>20</sup> Michael Davis, "Houston-Based Prison Operator Sees Share Price Fall Due to Accounting Review" *Houston Chronicle* February 7, 2002.

<sup>21</sup> Reuters, "Moody's assigns Cornell Cos Inc. ratings," press release (June 4, 2004).

<sup>22</sup> Moody's Investors Service, "Rating Definitions," available at [www.moodys.com](http://www.moodys.com).

<sup>23</sup> Moody's Investors Service, *Rating Policy: Understanding Moody's Corporate Bond Ratings And Rating Process* (May 2002), 10.

<sup>24</sup> Letter from U.S. Assistant Attorney General Ralph F. Boyd to Arkansas Governor Mike Huckabee, November 8, 2002.

education program at Alexander is inadequate. This deficiency is caused by the failure to provide all students with adequate instruction; the absence of vocational training; the failure to employ a school counselor; inadequate access to reading materials; and the failure to assign homework.”<sup>25</sup> Staff training, lack of educational services, and poor mental health care were all part of a federal lawsuit filed by the Department of Justice against the Arkansas Division of Youth Services (the entity responsible for contracting with Cornell).<sup>26</sup>

- △ A Santa Fe County (New Mexico) grand jury toured Cornell’s Santa Fe County Detention Center in 2000 and noted that despite reports of a vocational and educational programs with the local community college, they found no evidence of such programs being offered.<sup>27</sup>

*Cornell is committed to working with the local community whenever possible for the betterment not only of residents but also the community in which we operate. (page 18)*

- △ In 1998, the city of Oxnard, California allowed Cornell to build a 40-bed halfway house within a block of a downtown elementary school. When the city’s planning commission later revoked Cornell’s special-use permit, Cornell threatened to sue the city if they did not get \$1 million in taxpayer dollars as a settlement. The city agreed, paying the \$1 million to get Cornell to leave.<sup>28</sup>
- △ Cornell proposed in 2001 to expand their detention center in Central Falls, Rhode Island (a plan that is now on hold), despite the objections of Mayor Lee Matthews who said the expansion “would have no long-term benefit to the city.”<sup>29</sup>

*Cornell will contract with a local medical provider to ensure service delivery is organized and that everyone needing care gets the appropriate care—promptly and professionally. (page 18)*

- △ In March 2000, the Oklahoma Department of Corrections fined Cornell \$168,750 for failing to provide adequate medical service to inmates in the Great Plains Correctional Facility. At the time, the fine was the largest ever levied by the Oklahoma DOC against a private prison company. DOC auditors found faulty or missing healthcare records and inadequate care for chronically ill inmates.<sup>30</sup>
- △ The New Mexico grand jury that investigated Cornell’s Santa Fe County jail, noted in their report “all medical/dental areas the grand jury was shown failed even the most minimum sanitary requirements. No protective gear (i.e., rubber gloves, etc.) was produced even when requested by jurors.”<sup>31</sup>

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<sup>25</sup> Ibid.

<sup>26</sup> U.S. v. State of Arkansas (E.D. Arkansas), complaint and settlement available at [www.usdoj.gov](http://www.usdoj.gov).

<sup>27</sup> Santa Fe Grand Jury Report on the Santa Fe County Detention Center, November 30, 2000.

<sup>28</sup> Raul Hernandez, “City, Cornell strike \$1 million deal” *Ventura County Star* February 10, 1999, B-01.

<sup>29</sup> Tatiana Pina, “Mayor opposes proposal to expand jail” *Providence Journal-Bulletin* April 12, 2002, B-01.

<sup>30</sup> Associated Press, “State fines private prison \$168,750” March 10, 2000.

<sup>31</sup> Santa Fe Grand Jury Report on the Santa Fe County Detention Center, November 30, 2000.

*Cornell recognizes that to provide a quality dental care system, accurate and timely communication is required between the Company and a local provider. We will work with the local dental provider to coordinate community based dental services to meet the needs of all residents in our care. (page 18)*

⚠ A 1998 inspection of Cornell's D. Ray James prison in Georgia cited the company for "not having an operating dental clinic."<sup>32</sup>

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<sup>32</sup>James Pilcher, "Private prison working on problems in critical state audits" *Associated Press* December 30, 1998.