

# **Bond Case Briefs**

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## **Prisons Built With Junk-Bonds Get Their Ratings Yanked by S&P.**

- **Marshals Service, Bureau of Prisons haven't responded: S&P**
- **Regular contact with federal agencies is important, S&P said**

In 2015, a riot broke out at the detention center in Willacy County, Texas, as inmates protested flooding toilets, rodents and overcrowding in the facility overseen by Management & Training Corp. That prompted the Federal Bureau of Prisons to pull out its inmates and the prison closed, shutting off some of the revenue needed to repay its debts.

The closure shows the level of volatility that investors owning prison bonds can encounter. In fact, Wall Street analysts still aren't sure how to gauge the risk of a default on \$13 million of outstanding debt tied to another Willacy County lockup for an entirely different reason.

Those bonds and debt issued for three other Texas jails had their already-junk credit ratings pulled by S&P Global Ratings, an unusual step that reflects the spotty financial disclosures in a corner of the \$3.8 trillion market that once boomed as local governments sought to profit by holding federal inmates. That uncertainty has been amplified under President Donald Trump, whose policy shifts have left it unclear whether federal contracts will be renewed or jeopardized by deals cut in Congress.

S&P said in a statement that it withdrew the ratings after repeated, unsuccessful efforts to speak with the Bureau of Prisons and the U.S. Marshals Service, leaving its analysts doubtful that "meaningful dialogue will be forthcoming or be maintained on a regular basis." In December, the company said such regular contact with federal agencies has become increasingly important.

In addition to Willacy County's jail, S&P also withdrew the rating on debt sold for detention centers in Fannin County, Hudspeth County and Garza County.

"As an investor, you have to assume that no news is bad news for a credit," said Matt Fabian, a partner at Municipal Market Analytics. "S&P is totally on solid ground pulling those ratings."

### **Ripple Effect**

Financial disclosures made to investors in the municipal-bond market are less closely regulated than those made by corporations that sell stocks and bonds, whose filings are monitored by the U.S. Securities and Exchange Commission. Some government's audited financial statements can take a year or more to be reported.

But the ripple effects cast by the federal government is unusual. S&P said information from agencies in Washington has become key amid debates like the one in February over the budget, when Democrats sought to slash the amount of money being provided to U.S. Immigration and Customs Enforcement to detain immigrants swept up by Trump's crackdown on those who enter the country illegally. It also said it had "little insight" into issues like contract renewals.

Garza County Judge Lee Norman said he thinks part of the issue is that the detention center, which is run by MTC, hasn't been able to secure a long-term contract with the Bureau of Prisons. Its troubles began when then-President Barack Obama's administration moved to end the Bureau of Prisons' use of privately-run prisons. But even under the Trump administration, which reversed that order, Garza County's detention facility has had a tough time securing a 10-year contract with the agency.

"It's been hard to get back on track, honestly," Norman said. He added that he thinks it comes down to bureaucratic issues at the Bureau of Prisons rather than issues with the detention center.

## **More Arrests**

Representatives at the Marshals Service and the Bureau of Prisons did not respond to requests for comment. Issa Arnita, a spokesman for MTC, didn't respond to requests for comment.

The outlook for jail financings has improved under Trump, Fabian said. Former Attorney General Jeff Sessions in April 2018 announced a "zero-tolerance policy" toward illegal entry into the U.S. and said law enforcement would prioritize prosecuting criminal immigration offenses.

That's helped translate into more arrests by ICE, which is good financial news for the state and local detention facilities that house detainees on behalf of ICE and receive payment for doing so. ICE's Enforcement and Removal Operations reported an 11 percent increase in arrests of people in the country illegally in fiscal 2018.

Lack of information over what was happening in Willacy County's corrections facility was an issue prior to the 2015 riots. The county sued MTC in 2016, saying the company failed to alert the county to issues at the prison. MTC "turned a blind eye to the enormous problems that plagued the prison from its inception," according to the complaint. After the Bureau of Prisons ended its contract, investors that owned bonds sold for that portion of the prison complex took losses on the debt as part of a distressed exchange, according to S&P.

The county, which is in a remote area of the Rio Grande Valley, struggled after the prison closed, given many people in the area worked for MTC. Ultimately, officials last year decided to reopen the privately-run corrections center, something that was met with protests, according to local news reports.

The withdrawn ratings could suggest something "systemic" with the risks surrounding jail projects, Fabian said. "Lack of disclosure is typically more telling than what's being disclosed," he said.

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