

STATE OF WASHINGTON

Department of Corrections



REPORT FOR DEPOSITING INMATE SAVINGS ACCOUNT FUNDS INTO AN INTEREST BEARING ACCOUNT

Report to the Legislature
December 1, 1999

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Introduction:

Chapter 325 Laws of 1999 directs "the secretary of corrections shall prepare a plan for depositing inmate savings account funds into an interest bearing account. The plan shall assume that the funds shall be deposited into a commingled account for all inmates and that the interest shall be paid in a manner pro rata to the inmate's share of the total deposits. The secretary shall present the plan to the governor and the legislature not later than December 1, 1999. The plan shall minimize the cost of administering the account and the inmates shall receive interest at a rate not less than the passbook savings rate."¹ The Department worked with the Office of the State Treasurer, the Trust Accounting System vendor, and potential banking partners to develop scenarios and cost analyses.

The report consists of the statutory authority for deduction from monies for savings accounts; background for the current process; taxation issues; public funds, bank accounts and interest earnings; banking fees; scenarios for placing offenders' savings in interest bearing accounts; a scenario pro and con matrix; and a cost analysis.

Statutory Authority for Deduction from Monies for Savings Accounts:

The Department of Corrections derives statutory authority for the management of the Department from chapter 72.09 RCW.

Revised Code of Washington 72.09.111 requires the secretary to deduct 10 percent from the gross wages or gratuities of each offender working in Correctional Industries Class I and Class II work programs and to put such deduction in a savings account. The savings account, together with any accrued interest, shall only be available to an offender at the time of his or her release from confinement, unless the secretary determines that an emergency exists for the offender, at which time the funds can be made available in an amount determined by the secretary. Offenders serving Life without Parole are exempt from this statute.

Revised Code of Washington 72.09.480 requires when an offender receives funds in addition to his or her wages or gratuities, the additional funds shall be subject to the deductions in RCW 72.09.111 (1) (a) (including the 10 percent to offender savings account), subject to certain exceptions in RCW 72.09.480 (4).

Background for the Current Process:

The Department holds the offenders' funds in trust. Monies held in trust for offenders are deposited in a non-interest bearing account. Banking fees are not charged on these accounts. Currently, there is one bank account for each institution.

¹ This report only addresses interest on offender funds deposited into the offender's savings account. The term "passbook savings rate" is no longer used in the banking industry.

The Department currently keeps track of such funds in an in-house computer application known as the Trust Accounting System. This system accounts for offenders' money on an individual basis. In this computer system, each offender has an account, which includes a spendable balance (similar to a checking account), a regular savings account, and a Work Release savings account, if appropriate.

Deposits to the regular savings account come from deductions from Correctional Industries Class I and Class II wages and gratuities as defined in RCW 72.09.111 and from other deposits as defined in RCW 72.09.480. Offenders cannot access their savings accounts while incarcerated, except when approved by the secretary, in the case of an emergency. Offenders are not allowed to make voluntary deposits into their savings accounts to pay for the products and services used in prison (such as personal hygiene products and medical co-pay).

Deposits to the Work Release savings are governed by Department of Corrections Policy 200.000, Offender Trust Accounts. Earnings while at Work Release are subject to a 12 percent deduction for savings. Withdrawals are limited to disbursement, upon release from the jurisdiction of the Department, and for collection of debt if an offender is returned to prison or to pre-release.

Scenarios:

For purposes of this report, the Department is comparing the following three scenarios:

1. The Department develops a system to calculate and allocate the interest and fees;
2. The interest and fee calculations are performed by a bank; and
3. Interest and fees would not be applied to offender savings accounts.

The following three issues significantly affect any plan to pay interest to offenders:

- **Taxation Issues:**

Federal taxation regulations significantly affect this plan. The Internal Revenue Service requires that information returns (Internal Revenue Service Form 1099-INT) be provided to all recipients of interest in excess of \$10 in a calendar year, as well as filed with the Internal Revenue Service. Interest earned is reported by Taxpayer Identification Number, in this case the individual's social security number. Offenders self-report their social security numbers. In the offender population, there are individuals who have reported a correct social security number, an incorrect social security number, multiple social security numbers, and no social security number. Additionally, there are offenders who are not entitled to a social security number. This is an important issue because there is an Internal Revenue Service penalty for failing to file a correct information return (\$15 per 1099-INT). Currently, the Department does not require a social security number until an offender transfers to Work Release. At that time, the social security number is validated with the Social Security Administration. Currently, there are approximately 9,500 offenders in prison and pre-release who do not have a

validated social security number. It is not possible to estimate how many offenders have a valid social security number.

For the purposes of this report, it is assumed that offenders must have a social security number validated by the Social Security Administration before earning any interest. Should an offender be unable to provide or acquire a valid social security number, his/her savings funds would be maintained in a non-interest bearing account. Validating the social security numbers results in a significant workload. There would be a start-up cost to validate social security numbers for all offenders in prison and pre-release, as well as on-going annual costs to validate social security numbers for offenders entering the prison system (see page 8, *Cost Analysis*).

- **Public Funds, Bank Accounts, and Estimated Interest Earnings:**

To determine the type of bank account where offender savings can be deposited and then estimate the interest earnings, we consulted with the Office of the State Treasurer and reviewed the statutes. Revised Code of Washington 39.58.010 defines public funds as "moneys under the control of a treasurer or custodian belonging to, or hold for the benefit of, the state or any of its political subdivisions, public corporations, municipal corporations, agencies, courts, boards, commissions or committees, including moneys held as a trustee or bailee". For purposes of this report, it is assumed that offender savings accounts are public funds because they are held in trust.

The assumption that offender savings are public funds is key in determining the type of bank account that is available for this purpose. Chapter 39.58 RCW details the requirement for public funds. These include, in part, the use of a public depository, maintenance of collateral by the bank for public funds, and limitations on the amount of public funds that a bank can hold. These statutory restrictions safeguard public funds, but they also limit the types of accounts that banks can provide to the Department. Further, these funds may not qualify to be placed in a savings account at a bank. This is due to bank restrictions on the number of withdrawals per month. Nearly all of the withdrawal activity on the offenders' savings account will be due to offenders being released from the custody of the Department. Approximately 550 offenders are released each month, which results in daily withdrawals from the bank account. Based upon informal discussions with the bank² that currently holds these funds, the account that offers the highest interest would be a commercial checking account. The rate on this account is currently 2.71 percent. Offender savings accounts balances total \$2,435,888. Using a formula provided by the Office of the State Treasurer to compound interest, the earnings on offender savings are estimated to be \$67,200. The estimated interest earnings are somewhat overstated in this analysis because it is not possible to estimate the amount of offender savings balances that would not qualify to be placed in an interest bearing account. This would include savings for offenders who are illegal aliens and other offenders that would not be able to provide or obtain a valid social security number.

² To pay interest to offenders, the Department would work with the Office of State Treasurer to competitively procure banking services.

- **Banking Fees:**

To the extent possible, the Department attempts to mirror the values and norms of the community by stressing personal responsibility and accountability by the offender. The Department would expect that if offenders were earning interest on their savings account they would also pay the banking fees associated with the process. Payment of banking fees would have to be considered in light of the passage of Initiative 695.

Each of the three issues listed above significantly affects the complexity, staff required, and the estimated cost of the scenarios discussed below. Each scenario includes a cost analysis as well as advantages and disadvantages.

Scenario 1: The Department develops the system to calculate and allocate the interest and fees³.

In this option, the Department would establish one interest bearing account with a bank. Offenders who have a validated social security number would have their savings placed in this account. As they receive money from outside the institution or earn wages or gratuities, the savings portion of these funds would be deposited in the account. The individual accounting of each offender balance would be done in the Trust Accounting System. Additionally, this system would allocate interest and fees to the individual accounts each month. This effort requires a considerable amount of additional data in the Trust Accounting System, as well as supporting a substantial number of additional calculations and allocations.

The main advantage of this option is that offenders receive interest on their savings accounts. Based upon current interest rates and savings balances, it is estimated that the account would earn approximately \$67,200. An additional advantage is that, similarly, offenders would pay the bank fees. However, since this would be a new fee, it must be considered in light of Initiative 695.

This option adds considerable complexity and cost to the responsibility of holding offender funds in trust. In the first fiscal year, the cost of providing interest on savings accounts is estimated to be \$328,450. This includes start-up costs of \$223,000, as well as on-going annual costs of \$105,450. The costs exceed the estimated interest earnings by a considerable amount. The Department would need to develop the technology to allocate both interest earnings and fees. This would involve planning a significant computer programming effort and acquiring equipment. Another substantial cost is validating the offender social security number to comply with federal taxation requirements. Annually, the Department would produce a Form 1099-INT for every offender who earned greater than \$10 in interest. In addition to distributing these forms in the institution, the Department would have to mail the form to offenders who were released during the year (approximately 6,600). Business staff would be added to handle the additional workload of transferring money to and from the savings account, reconciling the account, calculating the interest to be allocated, monitoring the processes associated with interest and fee allocation, working with Information Technology staff, producing and distributing Form 1099-INT, planning and

³ See Attachment 1, p. 9, for detailed explanation of this scenario.

start-up activities for the program, and responding to offender grievances. It is estimated that this option is likely to produce the greatest number of offender grievances regarding the methodology and calculation of both interest and fees.

In conclusion, Scenario 1 estimates that offenders' interest earnings would be \$67,200 annually. If offenders pay only the annual banking fees of \$2,100, then taxpayers would pay the remaining \$326,350 for the first fiscal year. If the intent is for offenders to pay the full costs of \$328,450, the costs far exceed the estimated interest earnings.

Scenario 2: The interest and fee calculations are performed by a bank⁴.

Similar to Scenario 1, the Department would establish one interest bearing account with a bank. Offenders who have a validated social security number would have their savings placed in this account. The bank would establish a sub-account for each offender. The Department would transfer account transactions on a daily basis. The bank would allocate both interest and fees to the individual sub-accounts. The Department would record the interest and fees in the Trust Accounting System to provide offender statements. Additionally, the bank would produce and mail the Form 1099-INT.

Advantages of this option include offenders earning interest and paying fees. Banks have existing technology and expertise in this process, and the risk of offender grievances regarding methodology and calculations is reduced. The estimated interest earnings are \$67,200. While it is assumed in this report that offenders will pay a bank fee, this would be a new fee and would need to be considered in light of the passage of Initiative 695. A significant advantage of this scenario is the existing technology and expertise by banks in allocating interest and fees, as well as the production of Form 1099-INT. This results in lower start-up and annual costs. By using technology and processes that currently exist and are already very well tested, offender grievances will be minimized.

The primary disadvantage is cost. Although this scenario takes advantage of existing resources, it is still complex and the costs exceed potential interest earnings. Total costs in the first year are estimated to be \$198,200. This includes \$97,600 of start-up costs and \$100,600 of on-going annual costs. Additional staffing is required to handle the workload of transferring money in and out of the savings bank account, reconciling accounts, notifying the bank to close an offenders sub-account, coordinating with the bank and Information Technology staff, monitoring the processes associated with interest and fee allocation, planning and start-up activities, and responding to offender grievances. Computer programming would be required to provide daily information to the bank, receive interest and fee allocation data from the bank, and update offender records and provide information to the bank for the production of Form 1099-INT. Bank fees would be considerably higher, but that would be expected where the service is much greater.

In conclusion, Scenario 2 estimates that offenders interest earnings would be \$67,200 annually. If offenders pay only the annual banking fees of \$14,600, then taxpayers would pay the remaining \$183,600 for the first fiscal year. If the intent is for offenders to pay the full costs of \$198,200, the costs far exceed the estimated interest earnings.

⁴ See Attachment 1, p. 10, for detailed explanation of this scenario.

Scenario 3: Interest and fees would not be applied to offender savings accounts.

In this option, offenders do not earn interest on their savings accounts and no additional fee is charged to the offender.

The primary advantage of this option is cost savings. It does not require additional staff and the Department would not incur the cost of validating additional social security numbers and no annual information return (Form 1099-INT) would be required. Additionally, the risk of offender grievances due to the methodology and calculation of interest is eliminated. Since this scenario does not add any costs, offenders would not have new fees to pay and costs to the taxpayer are minimized.

The disadvantage is that offenders do not receive interest on their savings account.

Scenario Analysis Pro and Con Matrix

Department Option - Scenario 1		Outsourcing Option - Scenario 2		No Interest Option - Scenario 3	
Pro	Con	Pro	Con	Pro	Con
Offenders with a valid social security number receive interest on their savings account. Annual interest earnings are estimated at \$67,200		Offenders with a valid social security number receive interest on their savings account. Annual interest earnings are estimated at \$67,200.			Offenders do not receive interest on their savings account.
	Total costs for the first fiscal year are \$328,450, which include \$223,000 for start-up and \$105,450 for on-going annual costs.		Total costs for the first fiscal year are \$198,200, which include \$97,600 for start-up and \$100,600 for on-going annual costs.	Does not cost taxpayers money.	
Offenders pay banking fees.	Banking fees would need to be considered in light of the passage of Initiative 695.	Offenders pay banking fees.	Banking fees would need to be considered in light of the passage of Initiative 695.		
	Both the Department and the Trust Accounting System computer program vendor must develop expertise and technology for the interest allocation and reporting.	Banks have existing expertise and technology.			
	The Department must add staff to manage the savings account, interest allocation, and related accounting and systems.		The Department must add staff to manage the savings account, interest allocation, and related accounting and systems.	Does not increase staff.	
	Validation of offender social security numbers is expensive.		Validation of offender social security numbers is expensive.	Department only validates social security numbers for offenders going to Work Release.	
	Annual information returns (Form 1099-INT) must be produced and mailed or distributed by the Department.	Bank produces and mails the required annual information returns (Form 1099-INT).	Annual information returns (Form 1099-INT) must be distributed to offenders still in prison.	No annual information returns (Form 1099-INT) required.	
	Greatest risk of offender grievances regarding methodology and calculation of interest.	Lesser risk of offender grievances regarding methodology and calculation of interest.		No risk of offender grievances regarding methodology and calculation of interest.	

Scenario 1 - Department develops the system to calculate and allocate interest and fees.

Resource required

Business staffing
 Information technology staffing
 Staff costs for validation of offender social security numbers
 Equipment costs
 Equipment installation and integration
 Computer programming services and maintenance
 IRS 1099-INT printing, forms, mail and distribution costs
 Banking fees
Total estimated costs

Start-up costs

\$ 12,500.00
 \$ 8,700.00
 \$ 37,000.00
 \$ 81,600.00
 \$ 12,000.00
 \$ 71,200.00
\$ 223,000.00

Annual costs

\$ 57,250.00
 \$ 11,100.00
 \$ 25,000.00

 \$ 5,000.00
 \$ 5,000.00
 \$ 2,100.00
\$ 105,450.00

**Total estimated costs
 for the first fiscal year**

\$ 328,450.00

Scenario 2 - The interest and fee calculations are performed by a bank.

Resource required

Business staffing
 Information technology staffing
 Staff costs for validation of offender social security numbers
 Equipment costs
 Computer programming services
 Banking fees
Total estimated costs

Start-up costs

\$ 12,500.00
 \$ 8,700.00
 \$ 37,000.00
 \$ 1,600.00
 \$ 35,800.00
 \$ 2,000.00
\$ 97,600.00

Annual costs

\$ 51,000.00
 \$ 10,000.00
 \$ 25,000.00
 \$ -
 \$ 14,600.00
\$ 100,600.00

**Total estimated costs
 for the first fiscal year**

\$ 198,200.00

**Attachment 1 - Detail Explanation of the Proposal
Scenario 1 – The Department develops the system to calculate the
interest and fees.**

In this scenario:

- The Department would set up one consolidated interest bearing account. Offenders who have a validated social security number would have their funds placed in this account. All other funds would remain in the checking account, which is non-interest bearing.
- The Trust Accounting System would be programmed to calculate and store the average daily balance of the offender. This program is essentially a banking program, which is typically handled by a bank. In addition, a method to allocate the interest, less bank fees, must be developed.
- All deposits for offender receipts would be made to the checking accounts at the local institutions.
- Business staff would electronically transfer funds daily from the checking accounts to the consolidated savings account for the saving portion of the deposits. Staff would also be responsible to reconcile the accounts on a monthly basis, answer grievances associated with this process, calculate the interest to be allocated, run the process that allocates the interest to each offenders account, work with Information Technology staff, and monitor the accuracy of the interest calculations.
- On a monthly basis, the fees would be subtracted from the interest and the net interest would be allocated to each offender based on his/her share of the average daily balance of the consolidated account.
- When offenders are released, the savings account would be electronically transferred to the checking account. This will facilitate giving the offender one check upon release. There are approximately 550 offenders released each month.
- It is unclear at this time how mid-month interest allocation could occur. It is possible to get the interest on the consolidated account at any time in the month, but it is unclear if or how the fees could be allocated mid-month. For this report, it is assumed that interest would not be paid to an offender in the month he/she is released from the custody of the Department.
- The Department would be responsible to complete the programming to store and print the Internal Revenue Service 1099-INT. The Department would be responsible to distribute and mail the Internal Revenue Service 1099-INT.

Attachment 1 - Detail Explanation of the Proposal

Scenario 2 – The interest and fee calculations are performed by a bank.

In this scenario:

- The Department would set up one consolidated interest bearing account. Offenders who have a validated social security number would have their funds placed in this account. All other funds would remain in the checking account, which is non-interest bearing. The bank would set up a sub-account for each offender. This account number would be based on the Department of Corrections' number and a suffix for the type of savings account (regular or Work Release).
- The Trust Accounting System would be programmed to generate a daily file of all savings transactions that occur for each offender. This will enable the bank/banking service provider to allocate the one-lump deposit to each offender's account. The bank then calculates the average daily balance for each offender. This file would include the first deposit that would open up a sub-account and closure codes indicating which sub-accounts were closed daily. The file and the transfer records would be reconciled daily.
- All deposits for offender receipts would be made to the checking accounts at the local institutions.
- Business staff would electronically transfer funds daily between the consolidated savings account and the checking accounts for the saving portion of the deposits. Staff would also be responsible to reconcile the accounts on a monthly basis, answer grievances associated with this process, liaison with the bank/banking service provider and Information Technology staff on the process associated with the allocation of interest.
- When offenders are released, the savings account funds would be electronically transferred from the savings account to the checking account. This would facilitate giving the offender upon release one check for all funds.
- On a monthly basis, the bank/banking service provider would provide an electronic file of the interest and fee allocations to each offender's savings account. There are several ways that banking fees can be allocated. One option is to allocate fees in the same manner as the interest, based on the average daily balance of the offender's account. Alternatively, a monthly fee schedule can be developed and the banking service provider will charge each offender a set fee per month.
- The bank/banking service provider would be responsible to print and mail the Internal Revenue Service 1099-INT.