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A C Wharton, Jr., Mayor

MEMORANDUM

TO: **Commissioner Steve Mulroy**

FROM: **LISA KELLY, Assistant County Attorney**

DATE: **Thursday, September 04, 2008 (Confidential Draft and Work Product)**

RE: **Corrections Corporation of America – Land Purchase Option for 3335 Old Getwell Road, Memphis, TN**

ISSUES

This Memorandum serves as a response to your inquiry into the following questions presented in relation to the potential sale of the above mentioned property under the Lease and Management Agreements regarding same. The issues presented for discussion are as follows:

1. Does the County have the option to buy the property?
2. Who else or what other entity has the option to purchase the property under the terms of the Contract?
3. What are the County's options to keep the land?
4. What would happen if the Commission does not approve the sale of the property?

FACTS AND HISTORY

The set of contracts at issue involve a Lease Agreement, a Management Agreement, and a Construction Agreement (hereinafter collectively referred to as "Contract" or 'Contracts"). All of the Agreements are intertwined and are not severable. The Agreements were entered into in 1985 to address the issue of the lack of a local facility to house juveniles who had been adjudicated delinquent and who were unable to be placed in with the other juvenile detainees. This was an alternative to sending a certain class of juveniles to a state facility in Nashville, far away from their families.

Shelby County agreed to lease the land to Corrections Corporation of America for a nominal fee and in return, Corrections Corporation of America agreed to construct and manage a facility to meet the need of a local facility. The facility Corrections

Corporation of America built had a pre-estimated construction cost of $6.5 million which was contained in the original set of Contracts.

Under the plan, Corrections Corporation of America would house the detainees and provide programs which met the standards as provided by State law. Juvenile Court would send the detainees and be responsible for funding the cost of care to the extent provided by the State funding. The Contract provided that at the end of the thirty (30) year term, the land and all of the improvements would belong to the County. The thirty (30) year term, if completed, would be up in 2015.

In the event the thirty (30) year term was not completed, the Contracts provided for remedies. The remedies are all partial towards Corrections Corporation of America due to the fact the Corporation had made a hefty investment in the facility and needed to recoup the expense in the event the County was unable or unwilling to perform under the Contract or the State ended the funding of the Contract.

The contracts with Tennessee Department of Children's Services (DCS) were annually renewable for state fiscal years beginning on July 1 and ending on June 30 from 1985 through 2015. Since July, 2001, the Contract amount of $7,010,452.00 has not increased. Under the statue, the allowance is to be no less than seventy-five (75%) percent of the current average cost ($243.27) to maintain a child in a state juvenile correctional institution. Seventy-five percent of the current cost would be $182.45. Under the contract, the per diem rate allocated to Shebly Training Center ("STC") is $99.58. For FY 07-08, DCS approved a Juvenile Court proposed rate adjustment for STC of $110.33, based upon a reduction of the number of beds authorized at STC from 175 to 150. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

Juvenile Court sought an increase in the contract for FY 08-09 in early 2007 from DCS. In correspondence, telephone conferences, and in two fully staffed meetings, in Memphis on October 19, 2007, and in Nashville on December 19, 2007, DCS held firm to its position that projected state revenue shortfall prevented the administration from increasing the contract amount for FY 08-09. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

At the December 19 meeting, DCS Deputy Commissioner Steve Hornsby signaled the department's desire to start moving toward a more therapeutic model, which would require the three local facilities to operate more like the state's regional youth development centers, such as the Wilder YDC at Somerville. DCS also wanted broader powers to monitor pursuant to T.C.A. § 37-5-126, which became be effective June 28, 2007. The evidence-based model was to be phased in over a four year period, beginning with state FY 09-10. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

DCS has been trying to cope with some 60 additional best practice policy standards imposed on the department by a Chancery Court ruling in Nashville. Known as the "Doe" standards, they arise from a specific case and are stricter than American

Corrections Association (ACA) standards. STC has been fully accredited by ACA, and operates an educational program licensed by the state Department of Education. The federal class action lawsuits of John B and Brian A are continuing to affect the development of policy standards and are creating additional liability concerns for DCS. According to Commissioner Hornsby, Juvenile Court would be expected to perform the anticipated additional requirements with "no new money." *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

The current funding level will not permit STC or the other local facilities to operate like state youth development centers, with the more comprehensive social services now expected by DCS. While Shelby County youth should receive the same level of services as youth in state correctional custody, without a funding increase YSB will be unable to meet the increasingly stringent requirements mandated by federal and state courts. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

On March 5, 2008, Juvenile Court and DCS reached an agreement to wind down the Contract and transition from local residential services providers to DCS corrective placement. The final Contract period was extended until July 31, 2008, to permit the orderly release of youthful offenders form the local facilities. Some 200 youthful offenders, almost all having completed their required periods of confinement, were released from STC, Reconation Academy, and YHS by July 31. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

Juvenile Court is still waiting for final payment by DCS, from which any amounts due and owing the subcontractor providers will be paid. According to DCS staff, the final DCS payment should be forthcoming by September 15, 2008. *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

Due to the fact State funding is directly tied to the juveniles in the facility, the decision to move the juveniles from the facility ended the State's funding of the Contract which terminated the agreement and triggered the remedies as outlined in the Contract and are presented below for your review.

QUESTION 1. DOES THE COUNTY HAVE THE OPTION TO PURCHASE THE PROPERTY?

No. The Contract provides for the following in the event of a default or early termination of the supporting collective Contracts:

1) If the lease is terminated by the County without cause, then Lessee may purchase the property for $150,000.00.
2) If the State fails to fund the contract, then the Lessee may purchase the property for $150,000.00.

3) If the Lessee breaches the contract, then the Lessee may purchase the property for its fair market value, as agreed to by the Lessor and the Lessee. Lessor shall convey said property in fee simple to Lessee.
4) If the lease is terminated by the Lessee, without cause, the Lessee shall purchase the property for its fair market value, as agreed to by Lessee and Lessor.
5) Should the Lessor breach the contract, then the Lessee may purchase the property for $150,000.00

Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America. March 14, 1985. Pages 7, 8, Paragraph 12.

Under the terms of the Contract, the Lessee, Corrections Corporation of America, has the option to purchase the property under all given scenarios.

QUESTION 2. WHO ELSE OR WHAT OTHER ENTITY HAS THE OPTION TO PURCHASE THE PROPERTY UNDER THE TERMS OF THE CONTRACT?

As reflected in Question 1 above, only Corrections Corporation of America has the option to purchase the Property under the terms of the Contract. The option to purchase provision of the Contract is the same as the default or early termination remedy provision and provides the following:

1) If the lease is terminated by the County without cause, then Lessee may purchase the property for $150,000.00.
2) If the State fails to fund the contract, then the Lessee may purchase the property for $150,000.00.
3) If the Lessee breaches the contract, then the Lessee may purchase the property for its fair market value, as agreed to by the Lessor and the Lessee. Lessor shall convey said property in fee simple to Lessee.
4) If the lease is terminated by the Lessee, without cause, the Lessee shall purchase the property for its fair market value, as agreed to by Lessee and Lessor.
5) Should the Lessor breach the contract, then the Lessee may purchase the property for $150,000.00

Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America. March 14, 1985. Pages 7, 8, Paragraph 12.

Under the terms of the Contract, the Lessee, Corrections Corporation of America, is the only person or entity with the option to purchase the property under all given scenarios. The collective Contracts make no mention of any option which would allow for the sale of the property to any other person or entity.

QUESTION 3. WHAT ARE THE COUNTY'S OPTIONS TO KEEP THE LAND?

The only option given under the terms of the Contract for the County to keep the land is to complete the term of the Lease Agreement which ends in 2015.

As reflected in Questions 1 and 2 above, only Corrections Corporation of America has the option to purchase the Property under the terms of the Contract. The option to purchase provision of the Contract is the same as the default or early termination remedy provision and provides the following:

1) If the lease is terminated by the County without cause, then Lessee may purchase the property for $150,000.00.
2) If the State fails to fund the contract, then the Lessee may purchase the property for $150,000.00.
3) If the Lessee breaches the contract, then the Lessee may purchase the property for its fair market value, as agreed to by the Lessor and the Lessee. Lessor shall convey said property in fee simple to Lessee.
4) If the lease is terminated by the Lessee, without cause, the Lessee shall purchase the property for its fair market value, as agreed to by Lessee and Lessor.
5) Should the Lessor breach the contract, then the Lessee may purchase the property for $150,000.00

Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America. March 14, 1985. Pages 7, 8, Paragraph 12.

Under the terms of the Contract, the Lessee, Corrections Corporation of America, is the only entity with the option to purchase the property under all given scenarios. The collective Contracts make no mention of any option which would allow for the sale of the property to any other person or entity. The only option under the terms of the Contract for the County to keep the land is the completion and fulfillment of the obligations and responsibilities of the thirty (30) year Contract, at which point the property including the improvements would become the sole property of the County of Shelby. "At the conclusion of this thirty (30) year Lease Agreement, the above-described facility and any and all structures, improvements, and buildings will become the sole property of the County of Shelby, such will occur at the end of the lease term or any subsequent renewal time at no cost to the Lessor." (*Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America.* March 14, 1985. Page 5, Paragraph 7.)

QUESTION 4. WOULD HAPPEN IF THE COMMISSION DOES NOT APPROVE THE SALE OF THE PROPERTY?

If the Commission does not approve the sale of the Property, Corrections Corporation of America would likely seek remedies through legal action. Since the

Contract does not provide for arbitration, this would likely be in the form of a lawsuit filed in a Court of proper jurisdiction.

LAW AND ANALYSIS

In an action for real property based on the seller's refusal to perform under the terms of the Contract, the buyer traditionally has three (3) remedies:

(1) An action for damages,
(2) An equitable action for specific performance,
(3) An action for rescission of the contract and restitution of any money paid.

Tennessee case law suggests the remedy of specific performance is the prevailing remedy in actions involving real property. "If a contract has all the essentials of validity, and is certain in its terms, is based on an adequate and valuable consideration, is fair and just in all its provisions, is free from any fraud, misrepresentation, illegality, or mistake, is capable of being enforced without hardship to either party, and if compensation in damages for its breach is impracticable, or would be inadequate, a complaint will be maintained for its specific performance." *Lane v. Associated Housing Developers*, 767 S.W.2d 640, 642 (Tenn.App.,1988). *See also Morrow v. Jones*, 165 S.W.3d 254 (Tenn.Ct.App.,2004) (To support specific performance, the contract must be clear, complete and definite in all its essential terms; the Court will not make a contract for the parties and the agreement sought to be enforced specifically must show beyond doubt that the minds of the parties actually met and that they themselves made the agreement.) "The remedy of specific performance of a contract is a discretionary one. By this is not meant that the judges can exercise arbitrary discretion in refusing the relief or granting it. It is a legal discretion, and is firmly established in our jurisprudence. It is necessary, when parties refuse to perform and when adequate remedy at law does not exist, to the fulfillment and completion of the Contract of the parties. It is given as a substitute for the legal remedy of compensation whenever the legal remedy is inadequate or impracticable." *Lane v. Associated Housing Developers*, 767 S.W.2d 640, 643 (Tenn.App.,1988).

Establishing a prima facie case in an action by a buyer against a seller for damages for breech of a contract to sell real property requires proof that:

(1) The plaintiff had a valid and enforceable contract with the defendant for the sale and purchase of the property in question;
(2) The plaintiff performed all conditions precedent to the defendant's performance and
(3) The defendant breached the contract by failing or refusing to convey the property in accordance with the terms of the contract.

"Purchaser and vendor may assert action for specific performance of contract for sale of real estate, though remedy is not available to either party as matter of right, but rests in sound discretion of court under facts of each particular case. Chancery court has

discretion to adjust equities of party in order to do complete justice between them." *Id.* at 643.

The remedy of specific performance is deemed to be mutual as between seller and buyer. However, prevailing case law tends to suggest equity compels specific performance in favor of the seller, not on the ground of mutuality of remedy, but on the ground that compensation in damages, measured by the difference in price, as ascertained by the market value and by the contract, is not regarded as adequate indemnity for the nonfulfillment of the contract. Other sources suggest, where parties make a mutual executory contract for the sale of real estate, equity regards the buyer as the beneficial owner of the premises, even though he has not paid the purchase price, and holds that the seller has the right to enforce payment of the purchase money by a suit in equity against the buyer's equitable estate in the land, instead of by an ordinary action at law to recover the debt. See 71 Am.Jur.2d *Specific Performance*, § 115 (1973)."To deny the right to specific performance and remit the plaintiff to an action at law for damages is to accord the choice of proceedings to the one who is in default, an option which fairly belongs to the other." *Lane v. Associated Housing Developers*, 767 S.W.2d 640, 643 (Tenn.App.,1988).

Under our facts, Corrections Corporation of America has built a facility on the premises for the facilitation of the Contract. While Corrections Corporation of America has likely profited from this venture, they have also given notice to the County via letter dated July 9, 2008 of their intention to purchase the property under the terms of the Contract. Due to the investment into the construction of the building, anticipated profits from running the facility under a new model, other intangible factors, and the fact that equity allows for specific performance in cases involving the sale of real property, it would likely be difficult for a court to assess monetary damages and find reason to invoke the equitable remedy of specific performance and force the County to sell the property.

Although Tennessee case law suggests the remedy of specific performance is the prevailing remedy in actions involving real property, the sale price in the contract is typically a defined term. However under the facts presented, it is not clear which provision of the Contract should be applied in calculating the sale price for the subject property. The Contract provides for five possible scenarios in which the County must sell the property to Corrections Corporation of America.

1) If the lease is terminated by the County without cause, then Lessee may purchase the property for $150,000.00.
2) If the State fails to fund the contract, then the Lessee may purchase the property for $150,000.00.
3) If the Lessee breaches the contract, then the Lessee may purchase the property for its fair market value, as agreed to by the Lessor and the Lessee. Lessor shall convey said property in fee simple to Lessee.
4) If the lease is terminated by the Lessee, without cause, the Lessee shall purchase the property for its fair market value, as agreed to by Lessee and Lessor.

5) Should the Lessor breach the contract, then the Lessee may purchase the property for $150,000.00

Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America. March 14, 1985. Pages 7, 8, Paragraph 12.

In the facts presented in the Memorandum provided by Juvenile Court, it suggests Corrections Corporation of America was unable to provide services to the detainees at the level required by Tennessee State Law.[1] According to the terms of the Contract[2], Corrections Corporation of America was obligated to provide "residential services for post adjudicatory care and treatment of delinquent juveniles, which shall at all times meet such standards as provided by law." *Contract between The County of Shelby, Tennessee for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America dated January 1984.*

Due to the aforementioned inability to provide these services on a continuing basis within the budget allotted by State funding, there is a plausible argument that Juvenile Court moved the juvenile detainees which in turn canceled the State funding in an effort to mitigate the damages being caused by Corrections Corporation of America's breach of the Contract based on inability to perform. Under this argument, the County remains obligated to transfer the property to Corrections Corporation of America but under provision 3 which reads, "If the Lessee breaches the contract, then the Lessee may purchase the property for its fair market value, as agreed to by the Lessor and the Lessee. Lessor shall convey said property in fee simple to Lessee." *Lease Agreement between The County of Shelby for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America.* March 14, 1985. Pages 7, 8, Paragraph 12.

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[1] "The current funding level will not permit STC or the other local facilities to operate like state youth development centers, with the more comprehensive social services now expected by DCS. While Shelby County youth should receive the same level of services as youth in state correctional custody, without a funding increase YSB will be unable to meet the increasingly stringent requirements mandated by federal and state courts." *Memorandum from Larry Scroggs to Lisa Kelly dated August 28, 2008.*

[2] Lease Agreement between the County of Shelby, Tennessee for the Juvenile Court of Memphis and Shelby County and Corrections Corporation of America dated March 14, 1885. Paragraph 6. "Upon completion of the new construction, the Lessee shall be prepared at all times to deliver appropriate residential and programmatic services for as many as 150 adjudicated delinquent juveniles…"

Contract between The County of Shelby, Tennessee for The Juvenile Court of Memphis and Shelby County and Corrections Corporation of America dated January 1984. Section A. The Contractor agrees to the following:

> 1. To provide residential services for post adjudicatory care and treatment of delinquent juveniles, which shall at all times meet such standards as provided by law….
> 3. The Contractor shall be prepared at all times to deliver appropriate residential and programmatic services, for as many as 35 adjudicated delinquent males.

In conclusion, although it is likely Shelby County will be required to transfer the property in question to Corrections Corporation of America, it is arguable the transfer is properly done under the terms as stated in provision 3 of the Contract which provides for fair market value instead of provision 2 which provides for $150,000.00.

Cc: Honorable Mayor A. C. Wharton, Jr.
Chairman Deidre Malone
Chariman Pro Tempore Joyce Avery
Commissioner Mike Ritz
Commissioner George S. Flinn, Jr
Commissioner Mike Carpenter
Commissioner J. W. Gibson, II
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Tom Moss, Administrator, Land Bank
Dottie Jones, Director of Division of Community Services