



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2006

Commission file number: 1-14260

**The GEO Group, Inc.**

(Exact name of registrant as specified in its charter)

**Florida**

(State or other jurisdiction of  
incorporation or organization)

**One Park Place, Suite 700,  
621 Northwest 53rd Street  
Boca Raton, Florida**

(Address of principal executive offices)

**65-0043078**

(I.R.S. Employer  
Identification No.)

**33487-8242**

(Zip Code)

**Registrant's telephone number (including area code):**  
**(561) 893-0101**

**Securities registered pursuant to Section 12(b) of the Act:**

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, \$0.01 Par Value	New York Stock Exchange

Indicate by a check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by a check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by a check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by a check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and larger accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the 8,159,812 shares of common stock held by non-affiliates of the registrant as of June 30, 2006 (based on the last reported sales price of such stock on the New York Stock Exchange on such date of \$35.05 per share) was approximately \$286,001,411.

As of February 23, 2007 the registrant had 19,753,084 shares of common stock outstanding.

Certain portions of the registrant's annual report to security holders for fiscal year ended December 31, 2006 are incorporated by reference into Part III of this report. Certain portions of the registrant's definitive proxy statement pursuant to Regulation 14A of the Securities Exchange Act of 1934 for its 2007 annual meeting of shareholders are incorporated by reference into Part III of this report.

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**PART I**

**Item 1. Business**

*As used in this report, the terms “we,” “us,” “our,” “GEO” and the “Company” refer to The GEO Group, Inc., its consolidated subsidiaries and its unconsolidated affiliates, unless otherwise expressly stated or the context otherwise requires.*

**General**

We are a leading provider of government-outsourced services specializing in the management of correctional, detention and mental health and residential treatment facilities in the United States, Australia, South Africa, the United Kingdom and Canada. We operate a broad range of correctional and detention facilities including maximum, medium and minimum security prisons, immigration detention centers, minimum security detention centers and mental health and residential treatment facilities. Our correctional and detention management services involve the provision of security, administrative, rehabilitation, education, health and food services, primarily at adult male correctional and detention facilities. Our mental health and residential treatment services involve the delivery of quality care, innovative programming and active patient treatment, primarily at privatized state mental health. We also develop new facilities based on contract awards, using our project development expertise and experience to design, construct and finance what we believe are state-of-the-art facilities that maximize security and efficiency.

Our business was founded in 1984 as a division of The Wackenhut Corporation, or TWC, a multinational provider of global security services. We were incorporated in 1988 as a wholly-owned subsidiary of TWC. In July 1994, we became a publicly-traded company. In 2002, TWC was acquired by Group 4 Falck A/S, which became our new parent company. In July 2003, we purchased all of our common stock owned by Group 4 Falck A/S and became an independent company. In November 2003, we changed our corporate name to “The GEO Group, Inc.” We currently trade on the New York Stock Exchange under the ticker symbol “GEO.”

As of December 31, 2006, we operated a total of 62 correctional, detention and mental health and residential treatment facilities and had over 54,000 beds under management or for which we had been awarded contracts. We maintained an average facility occupancy rate of 96.1% for the fiscal year ended December 31, 2006. For the fiscal year ended December 31, 2006, we had consolidated revenues of \$860.9 million and consolidated operating income of \$64.2 million.

We offer services that go beyond simply housing offenders in a safe and secure manner for our correctional and detention facilities. We offer a wide array of in-facility rehabilitative and educational programs. Inmates at most of our facilities can also receive basic education through academic programs designed to improve inmates’ literacy levels and enhance the opportunity to acquire General Education Development certificates. Most of our managed facilities also offer vocational training for in-demand occupations to inmates who lack marketable job skills. In addition, most of our managed facilities offer life skills/transition planning programs that provide inmates job search training and employment skills, anger management skills, health education, financial responsibility training, parenting skills and other skills associated with becoming productive citizens. We also offer counseling, education and/or treatment to inmates with alcohol and drug abuse problems at most of the domestic facilities we manage.

Our mental health facilities and residential treatment services primarily involve the provision of acute mental health and related administrative services to mentally ill patients that have been placed under public sector supervision and care. At these mental health facilities, we employ psychiatrists, physicians, nurses, counselors, social workers and other trained personnel to deliver active psychiatric treatment designed to diagnose, treat and rehabilitate patients for community reintegration.

**Business Segments**

We conduct our business through three reportable business segments: our U.S. corrections segment; our international services segment; and our GEO Care segment. We have identified these three reportable segments

to reflect our current view that we operate three distinct business lines, each of which constitutes a material part of our overall business. This treatment also reflects how we have discussed our business with investors and analysts. The U.S. corrections segment primarily encompasses our U.S.-based privatized corrections and detention business. The International services segment primarily consists of our privatized corrections and detention operations in South Africa, Australia and the United Kingdom. This segment also operates our recently acquired United Kingdom-based prisoner transportation business and reviews opportunities to further diversify into related foreign-based governmental-outsourced services on an ongoing basis. Our GEO Care segment, which is operated by our wholly-owned subsidiary GEO Care, Inc., comprises our privatized mental health and residential treatment services business, all of which is currently conducted in the U.S. Financial information about these segments for fiscal years 2004, 2005 and 2006 is contained in "Note 16- Business Segments and Geographic Information" of the "Notes to Consolidated Financial Statements" included in this Form 10-K and is incorporated herein by this reference.

#### **Recent Developments**

On June 12, 2006, we sold in a follow-on public offering 3,000,000 shares of our common stock at a price of \$35.46 per share (4,500,000 shares of its common stock at a price of \$23.64 reflecting the 3 for 2 stock split). All shares were issued from treasury. The aggregate net proceeds (after deducting underwriter's discounts and expenses) was approximately \$100 million. On June 13, 2006, we utilized approximately \$74.6 million of the proceeds to repay all outstanding debt under the term loan portion of our Senior Credit Facility. In addition, on August 11, 2006, we used \$4.0 million of the proceeds of the offering to purchase from certain directors, executive officers and employees stock options that were currently outstanding and exercisable, and which were due to expire within the next three years. The balance of the net proceeds was used for general corporate purposes including working capital, capital expenditures and the acquisition of CPT.

On August 10, 2006, our board of directors declared a 3-for-2 stock split of our common stock. The stock split took effect on October 2, 2006 with respect to shareholders of record on September 15, 2006. Following the stock split, the shares outstanding increased from 13.0 million to 19.5 million. All relevant share and per share data has been adjusted to reflect the stock split.

On September 20, 2006, we entered into an Agreement and Plan of Merger by and among us and CentraCore Properties Trust, which we refer to as CPT. On January 24, 2007, we completed the acquisition of CPT pursuant to an Agreement and Plan of Merger, dated as of September 19, 2006, referred to as the Merger Agreement, by and among us, GEO Acquisition II, Inc., a direct wholly-owned subsidiary of GEO, and CPT. Under the terms of the Merger Agreement, CPT merged with and into GEO Acquisition II, Inc., referred to as the Merger, with GEO Acquisition II, Inc., being the surviving corporation of the Merger.

As a result of the Merger, each share of common stock of CPT was converted into the right to receive \$32.5826 in cash, inclusive of a pro-rated dividend for all quarters or partial quarters for which CPT's dividend had not yet been paid as of the closing date. In addition, each outstanding option to purchase CPT common stock having an exercise price less than \$32.00 per share was converted into the right to receive the difference between \$32.00 per share and the exercise price per share of the option, multiplied by the total number of shares of CPT common stock subject to the option. We paid an aggregate purchase price of approximately \$427.6 million for the acquisition of CPT, inclusive of the payment of approximately \$367.6 million in exchange for the common stock and the options, the repayment of approximately \$40.0 million in CPT debt and the payment of approximately \$20.0 million in transaction related fees and expenses. We financed the acquisition through the use of \$365.0 million in new borrowings under a new Term Loan B and approximately \$62.6 million in cash on hand.

On October 13, 2006, we acquired United Kingdom based Recruitment Solutions International (RSI) for approximately \$2.3 million plus transaction related expenses. RSI is a privately-held provider of transportation services to The Home Office Nationality and Immigration Directorate. The acquisition of RSI did not materially impact our 2006 result of operations.

Additional information regarding significant events affecting us during the fiscal year ended December 31, 2006 is set forth in Item 7 below under Management's Discussion and Analysis of Financial Condition and Results of Operations.

#### **Quality of Operations**

We operate each facility in accordance with our company-wide policies and procedures and with the standards and guidelines required under the relevant management contract. For many facilities, the standards and guidelines include those established by the American Correctional Association, or ACA. The ACA is an independent organization of corrections professionals, which establishes correctional facility standards and guidelines that are generally acknowledged as a benchmark by governmental agencies responsible for correctional facilities. Many of our contracts in the United States require us to seek and maintain ACA accreditation of the facility. We have sought and received ACA accreditation and re-accreditation for all such facilities. We achieved a median re-accreditation score of 97.9% in fiscal year 2006. Approximately 66% of our 2006 U.S. corrections revenue was derived from ACA accredited facilities. We have also achieved and maintained certification by the Joint Commission on Accreditation for Healthcare Organizations, or JCAHO, for our mental health facilities and two of our correctional facilities. We have been successful in achieving and maintaining accreditation under the National Commission on Correctional Health Care, or NCCHC, in a majority of the facilities that we currently operate. The NCCHC accreditation is a voluntary process which we have used to establish comprehensive health care policies and procedures to meet and adhere to the ACA standards. The NCCHC standards, in most cases, exceed ACA Health Care Standards.

#### **Marketing and Business Proposals**

Our primary potential customers are governmental agencies responsible for local, state and federal correctional facilities in the United States and governmental agencies responsible for correctional facilities in Australia, South Africa and the United Kingdom. Other primary customers include state agencies in the U.S. responsible for mental health facilities, and other foreign governmental agencies.

Governmental agencies responsible for correctional and detention facilities generally procure goods and services through requests for proposals. A typical request for proposal requires bidders to provide detailed information, including, but not limited to, descriptions of the following: the services to be provided by the bidder, its experience and qualifications, and the price at which the bidder is willing to provide the services, which services may include the renovation, improvement or expansion of an existing facility, or the planning, design and construction of a new facility.

If the project meets our profile for new projects, we then will submit a written response to the request for proposal. We estimate that we typically spend between \$100,000 and \$200,000 when responding to a request for proposal. We have engaged and intend in the future to engage independent consultants to assist us in developing privatization opportunities and in responding to requests for proposals, monitoring the legislative and business climate, and maintaining relationships with existing customers.

Our state and local experience has been that a period of approximately 60 to 90 days is generally required from the issuance of a request for proposal to the submission of our response to the request for proposals; that between one and four months elapse between the submission of our response and the agency's award for a contract; and that between one and four months elapse between the award of a contract and the commencement of construction of the facility, in the case of a new facility, or the management of the facility, in the case of an existing facility. If the facility for which an award has been made must be constructed, our experience is that construction usually takes between nine and 24 months, depending on the size and complexity of the project; therefore, management of a newly constructed facility typically commences between 10 and 28 months after the governmental agency's award.

Our federal experience has been that a period of approximately 60 to 90 days is generally required from the issuance of a request for proposal to the submission of our response to the request for proposal; that between 12 and 18 months elapse between the submission of our response and the agency's award for a contract; and that between four and 18 weeks elapse between the award of a contract and the commencement

of construction of the facility, in the case of a new facility, or the management of the facility in the case of an existing facility. If the facility for which an award has been made must be constructed, our experience is that construction usually takes between nine and 24 months, depending on the size and complexity of the project; therefore, management of a newly constructed facility typically commences between 10 and 28 months after the governmental agency's award.

### **Facility Design, Construction and Finance**

We offer governmental agencies consultation and management services relating to the design and construction of new correctional and detention facilities and the redesign and renovation of older facilities. As of December 31, 2006, we had provided services for the design and construction of forty-three facilities and for the redesign and renovation of thirteen facilities.

Contracts to design and construct or to redesign and renovate facilities may be financed in a variety of ways. Governmental agencies may finance the construction of such facilities through the following:

- a one time general revenue appropriation by the governmental agency for the cost of the new facility;
- general obligation bonds that are secured by either a limited or unlimited tax levy by the issuing governmental entity; or
- revenue bonds or certificates of participation secured by an annual lease payment that is subject to annual or bi-annual legislative appropriations.

We may also act as a source of financing or as a facilitator with respect to the financing of the construction of a facility. In these cases, the construction of such facilities may be financed through various methods including the following:

- funds from equity offerings of our stock;
- cash flows from operations;
- borrowings from banks or other institutions (which may or may not be subject to government guarantees in the event of contract termination); or
- lease arrangements with third parties.

If the project is financed using direct governmental appropriations, with proceeds of the sale of bonds or other obligations issued prior to the award of the project or by us directly, then financing is in place when the contract relating to the construction or renovation project is executed. If the project is financed using project-specific tax-exempt bonds or other obligations, the construction contract is generally subject to the sale of such bonds or obligations. Generally, substantial expenditures for construction will not be made on such a project until the tax-exempt bonds or other obligations are sold; and, if such bonds or obligations are not sold, construction and therefore, management of the facility, may either be delayed until alternative financing is procured or the development of the project will be suspended or entirely cancelled. If the project is self-financed by us, then financing is generally in place prior to the commencement of construction.

Under our construction and design management contracts, we generally agree to be responsible for overall project development and completion. We typically act as the primary developer on construction contracts for facilities and subcontract with national general contractors. Where possible, we subcontract with construction companies that we have worked with previously. We make use of an in-house staff of architects and operational experts from various correctional disciplines (e.g. security, medical service, food service, inmate programs and facility maintenance) as part of the team that participates from conceptual design through final construction of the project. This staff coordinates all aspects of the development with subcontractors and provides site-specific services.

When designing a facility, our architects use, with appropriate modifications, prototype designs we have used in developing prior projects. We believe that the use of these designs allows us to reduce cost overruns and construction delays and to reduce the number of correctional officers required to provide security at a

facility, thus controlling costs both to construct and to manage the facility. Our facility designs also maintain security because they increase the area under direct surveillance by correctional officers and make use of additional electronic surveillance.

## **Competitive Strengths**

### ***Regional Operating Structure***

We operate three regional U.S. offices and three international offices that provide administrative oversight and support to our correctional and detention facilities and allow us to maintain close relationships with our customers and suppliers. Each of our three regional U.S. offices is responsible for the facilities located within a defined geographic area. The regional offices perform regular internal audits of the facilities in order to ensure continued compliance with the underlying contracts, applicable accreditation standards, governmental regulations and our internal policies and procedures.

### ***Long-Term Relationships with High-Quality Government Customers***

We have developed long-term relationships with our government customers and have been successful at retaining our facility management contracts. We have provided correctional and detention management services to the United States Federal Government for 19 years, the State of California for 18 years, the State of Texas for 18 years, various Australian state government entities for 14 years and the State of Florida for 12 years. These customers accounted for approximately 54.9% of our consolidated revenues for the fiscal year ended December 31, 2006. Our strong operating track record has enabled us to achieve a high renewal rate for contracts. Our government customers typically satisfy their payment obligations to us through budgetary appropriations.

### ***Full-Service Facility Developer***

We have developed comprehensive expertise in the design, construction and financing of high quality correctional, detention and mental health facilities. In addition, we have extensive experience in overall facility operations, including staff recruitment, administration, facility maintenance, food service, healthcare, security, supervision, treatment and education of inmates. We believe that the breadth of our service offerings gives us the flexibility and resources to respond to customers' needs as they develop. We believe that the relationships we foster when offering these additional services also help us win new contracts and renew existing contracts.

### ***Experienced, Proven Senior Management Team***

Our top three senior executives have over 57 years of combined industry experience, have worked together at our company for more than 15 years and have established a track record of growth and profitability. Under their leadership, our annual consolidated revenues have grown from \$40.0 million in 1991 to \$860.9 million in 2006. Our Chief Executive Officer, George C. Zoley, is one of the pioneers of the industry, having developed and opened what we believe was one of the first privatized detention facilities in the U.S. in 1986. In addition to senior management, our operational and facility level management has significant operational experience and expertise.

## **Business Strategies**

### ***Provide High Quality, Essential Services at Lower Costs***

Our objective is to provide federal, state and local governmental agencies with high quality, essential services at a lower cost than they themselves could achieve.

### ***Maintain Disciplined Operating Approach***

We manage our business on a contract by contract basis in order to maximize our operating margins. We typically refrain from pursuing contracts that we do not believe will yield attractive profit margins in relation to the associated operational risks. Generally, we do not engage in speculative development and do not build



facilities without having a corresponding management contract award in place, although we may opt to do so in select situations when we believe attractive business development opportunities may become available. In addition, we have elected not to enter certain international markets with a history of economic and political instability. We believe that our strategy of emphasizing lower risk, higher profit opportunities helps us to consistently deliver strong operational performance, lower our costs and increase our overall profitability.

**Expand Into Complementary Government-Outsourced Services**

We intend to capitalize on our long-term relationships with governmental agencies to continue to grow our correctional, detention and mental health facilities management services and to become a preferred provider of complementary government-outsourced services. These opportunities may include services which leverage our existing competencies and expertise, including the design, construction and management of large facilities, the training and management of a large workforce and our ability to service the needs and meet the requirements of government clients. We believe that government outsourcing of currently internalized functions will increase largely as a result of the public sector's desire to maintain quality service levels amid governmental budgetary constraints. We believe that our successful expansion into the mental health and residential treatment services sector is an example of our ability to deliver higher quality services at lower costs in new areas of privatization.

**Pursue International Growth Opportunities**

As a global international provider of privatized correctional services, we are able to capitalize on opportunities to operate existing or new facilities on behalf of foreign governments. We currently have operations in Australia, the United Kingdom, South Africa and Canada. We intend to further penetrate the current markets we operate in and to expand into new international markets which we deem attractive. For example, during the fourth quarter of 2004, we opened an office in the United Kingdom to vigorously pursue new business opportunities in England, Wales and Scotland. In March 2006, we entered into a contract to manage the operations of the 198-bed Campsfield House in Kidlington, United Kingdom. We began operations under this contract in the second quarter of 2006.

**Selectively Pursue Acquisition Opportunities**

We consider acquisitions that are strategic in nature and enhance our geographic platform on an ongoing basis. On November 4, 2005, we acquired Correctional Services Corporation or CSC, bringing over 8,000 additional adult correctional and detention beds under our management. We will continue to review acquisition opportunities that may become available in the future, both in the privatized corrections, detention, mental health and residential treatment services sectors, and in complementary government outsourced services areas.

**Facilities**

The following table summarizes certain information with respect to facilities that GEO (or a subsidiary or joint venture of GEO) operated under a management contract or had an award to manage as of December 31, 2006:

<b>Facility Name &amp; Location(1)</b>	<b>Design Capacity</b>	<b>Customer</b>	<b>Facility Type</b>	<b>Security Level</b>	<b>Commencement of Current Term</b>	<b>Duration</b>	<b>Renewal Option</b>	<b>Type of Ownership</b>
<i>Domestic Contracts:</i> Allen Correctional Center Kinder, LA	1,538	LA DPS&C	State Correctional Facility	Medium/Maximum	October 2003	3 years	One, Two-year	Manage only
Arizona State Prison Florence West Florence, AZ	750	ADC	State DUI/RTC Correctional Facility	Minimum/Medium	October 2002	10 years	Two, Five-year	Lease

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<b>Facility Name &amp; Location(1)</b>	<b>Design Capacity</b>	<b>Customer</b>	<b>Facility Type</b>	<b>Security Level</b>	<b>Commencement of Current Term</b>	<b>Duration</b>	<b>Renewal Option</b>	<b>Type of Ownership</b>
Central Arizona Correctional Facility Florence, AZ	1,000	ADC	State Sex Offender Correctional Facility	Minimum/ Medium	December 2006	10 years	Two, Five-year	Lease
Arizona State Prison Phoenix West Phoenix, AZ	450	ADC	State DWI Correctional Facility	Minimum/ Medium	July 2002	10 years	Two, Five-year	Lease
Aurora ICE Processing Center Aurora, CO	400	ICE	Federal Detention Facility	Minimum/ Medium	October 2006	8 months	Four, One-year	Own(7)
Bill Clayton Detention Center Littlefield, TX	310	Littlefield, TX/ IDOC	Local/State Correctional/ Detention Facility	Minimum/ Medium	January 2004 July 2006	10 years 2 years	Two, Five-year Unlimited One-year	Manage Only
Bridgeport Correctional Center Bridgeport, TX	520	TDCJ	State Correctional Facility	Minimum/ Medium	September 2005	3 year	Two, One-year	Manage Only
Bronx Community Re-entry Center Bronx, NY	130	BOP	Federal Halfway House	Minimum	April 2002	2 years	Three, One-year	Lease
Brooklyn Community Corrections Center Brooklyn, NY	174	BOP	Federal Halfway House	Minimum	February 2005	2 years	Three, One-year	Lease
Broward Transition Center Deerfield Beach, FL	600	ICE	Federal Detention Facility	Minimum	October 2003	1 year	Four, One-year	Own(7)
Central Texas Detention Facility San Antonio, TX(2)	688	Bexar County/ICE & USMS	Local & Federal Detention Facility	All Levels	January 2002	3 years	One, Two-year	Lease- County
Central Valley MCCF McFarland, CA	625	CDCR	State Correctional Facility	Medium	December 1997	10 years	N/A	Own(7)
Cleveland Correctional Center Cleveland, TX	520	TDCJ	State Correctional Facility	Minimum/ Medium	January 2004	3 year	Two, One-year	Manage Only
Coke County JJC Bronte, TX	200	TYC	State Juvenile Correctional Facility	Medium/ Maximum	September 2004	2 year	One, Two-year	Lease
Colorado Medium Custody Prison(6) TBD	1,504		State Correctional Facility					
Desert View MCCF Adelanto, CA	643	CDCR	State Correctional Facility	Medium	December 1997	10 years	N/A	Own(7)

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Facility Name & Location(1)	Design Capacity	Customer	Facility Type	Security Level	Commencement of Current Term	Duration	Renewal Option	Type of Ownership
Dickens County Correctional Center Spur, TX	489	Dickens County/ IDOC/ ICE/Other Counties	Local/State Federal Correctional Facility	All Levels	August 2001 (IDOC) July 2006	15 years 2 years	N/A Unlimited One-year	Manage Only
East Mississippi Correctional Facility Meridian, MS	1,000	MDOC	State Correctional Facility	Mental Health All Levels	August 2006	2 years	Two, One-year	Manage only
Fort Worth Community Corrections Facility Fort Worth, TX	225	TDCJ	State Halfway House	Minimum	September 2003	2 years	Two, Two-year	Leased
Frio County Detention Center Pearsall, TX	391	Frio County/ Other Counties	Local Detention Facility	All Levels	December 1997	12 years	One, Five-year	Part Leased/ Part Owned
George W. Hill Correctional Facility Thornton, PA	1,883	Delaware County	Local Detention Facility	All Levels	June 2006	19 months	Successive, Two-year	Manage Only
Golden State MCCF McFarland, CA	625	CDCR	State Correctional Facility	Medium	December 1997	10 years	N/A	Own(7)
Graceville Correctional Facility Graceville, FL	1,500	DMS	State Correctional Facility	Medium/ Close	N/A	3 years	Successive, Two-year	N/A
Guadalupe County Correctional Facility Santa Rosa, NM(3)	600	Guadalupe County/ NMCD	Local/State Correctional Facility	Medium	September 1998	3 years (revised term)	Five, one-year extensions beginning 2004	Own
Jefferson County Downtown Jail Beaumont, TX	500	Jefferson County/ TDCJ/ ICE/USMS	Local/State Federal Detention Facility	All Levels	September 1998	Month to Month	Unlimited, One-month	Manage Only
Karnes Correctional Center Karnes City, TX(2)	679	Karnes County/ ICE & USMS	Local & Federal Detention Facility	All Levels	January 1998	30 years	N/A	Own(7)
Lawrenceville Correctional Center Lawrenceville, VA	1,536	VDOC	State Correctional Facility	Medium	March 2003	5 years	Ten, One-year	Manage Only
Lawton Correctional Facility Lawton, OK	2,518	ODOC	State Correctional Facility	Medium	July 2003	1 year	Four, One-year	Own(7)
Lea County Correctional Facility Hobbs, NM(3)	1,200	Lea County/ NMCD	Local/State Correctional Facility	All Levels	September 1998	3 years	Five, One-year beginning 2003	Own(7)

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<b>Facility Name &amp; Location(1)</b>	<b>Design Capacity</b>	<b>Customer</b>	<b>Facility Type</b>	<b>Security Level</b>	<b>Commencement of Current Term</b>	<b>Duration</b>	<b>Renewal Option</b>	<b>Type of Ownership</b>
Lockhart Secure Work Program Facilities Lockhart, TX	1,000	TDCJ	State Correctional Facility	Minimum	January 2004	3 years	Two, One-year	Manage Only
Marshall County Correctional Holly Springs, MS	1,000	MDOC	State Correctional Facility	Medium	September 2006	2 years	Two, One-year	Manage Only
McFarland CCF McFarland, CA	224	CDCR	State Correctional Facility	Minimum	January 2006	5 years	Two, Five-year	Own(7)
Migrant Operations Center Guantanamo Bay NAS, Cuba	130	ICE	Federal Migrant Center	Minimum	November 2006	11 Months	Four, One-year	Manage Only
Moore Haven Correctional Facility Moore Haven, FL	750 + 235 exp.	DMS	State Correctional Facility	Medium	January 2000	2 years	Unlimited, Two-year	Manage Only
New Castle Correctional Facility New Castle, IN	2,416	IDOC	State Correctional Facility	Medium	January 2006	4 years	Three, Two-year	Manage Only
Newton County Correctional Center Newton, TX	872	Newton County/ TDCJ	Local/State Correctional Facility	All Levels	February 2002	5 years	Two, Five-year	Manage Only
Northeast New Mexico Detention Facility Clayton, NM	625	Clayton/ NMCD	Local/State Correctional Facility	Medium	open	5 years	Five, One-year	open
North Texas ISF Fort Worth, TX	400	TDCJ	State Intermediate Sanction Facility	Minimum	March 2004	3 years	Four, One-year	Lease
Northwest Detention Center Tacoma, WA	1,000	ICE	Federal Detention Facility	Minimum/ Medium	April 2004	1 year	Four, One-year	Own
Queens Detention Facility Jamaica, NY	229	OFDT/USMS	Federal Detention Facility	Minimum/ Medium	April 2002	1 year	Four, One-year	Own(7)
Reeves County Detention Complex R1/R2 Pecos, TX(2)	2,200	Reeves County/ BOP	Federal Correctional Facility	Low	April 2005	9 years	Unlimited, Ten-year	Manage Only
Reeves County Detention Complex R3 Pecos, TX(2)	1,356	Reeves County/BOP	Federal Correctional Facility	Low	April 2005	9 years	Unlimited, Ten-year	Manage Only
Rivers Correctional Institution Winton, NC	1,200	BOP	Federal Correctional Facility	Low	March 2001	3 years	Seven, One-year	Own

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<b>Facility Name &amp; Location(1)</b>	<b>Design Capacity</b>	<b>Customer</b>	<b>Facility Type</b>	<b>Security Level</b>	<b>Commencement of Current Term</b>	<b>Duration</b>	<b>Renewal Option</b>	<b>Type of Ownership</b>
Sanders Estes Unit Venus, TX	1,000	TDCJ	State Correctional Facility	Minimum/ Medium	January 2004	3 years	Two, One-year	Manage Only
South Bay Correctional Facility South Bay, FL	1,862	DMS	State Correctional Facility	Medium/ Close	July 2006	3 years	Unlimited, Two-year	Manage Only
South Texas Detention Complex Pearsall, TX	1,904	ICE	Federal Detention Facility	Minimum/ Medium	June 2005	1 year	Four, One-year	Lease
South Texas ISF Houston, TX	450	TDCJ	State Intermediate Sanction Facility	Minimum	March 2004	3 years	Two, One-year	Manage Only
Taft Correctional Institution Taft, CA	2,048	BOP	Federal Correctional Facility	Low/ Minimum	December 1997	3 years	Seven, One-year	Manage Only
Tri-County Justice & Detention Center Ullin, IL	226	Pulaski County/ ICE	Local & Federal Detention Facility	All Levels	July 2004	6 years	Two, Five-year	Manage Only
Val Verde Correctional Facility Del Rio, TX(2)	784 + 576 exp	Val Verde County/ USMS/ ICE	Local & Federal Detention Facility	All Levels	January 2001	20 years	Unlimited, Five-year	Own
Western Region Detention Facility at San Diego San Diego, CA	700	USMS	Federal Detention Facility	Maximum	January 2006	5 years	One, Five-year	Lease
<b>International Contracts:</b>								
Arthur Gorrie Correctional Centre Wacol, Australia	710 + 180 exp	QLD DCS	Reception & Remand Centre	High/ Maximum	December 2002	5 years	One, Five-year	Manage Only
Fulham Correctional Centre Victoria, Australia	717	VIC MOC	State Prison	Minimum/ Medium	September 2005	3 years	Four, Three-year	Manage Only
Junee Correctional Centre Junee, Australia	790	NSW	State Prison	Minimum/ Medium	April 2001	5 years	One, Three-year	Manage Only
Kutama-Sinthumule Correctional Centre Northern Province, Republic of South Africa	3,024	RSA DCS	National Prison	Maximum	July 1999	25 years	None	Manage Only
Melbourne Custody Centre Melbourne, Australia	67	VIC CC	State Jail	All Levels	March 2005	3 years	Two, One-year	Manage Only
New Brunswick Youth Centre Mirimachi, Canada(4)	N/A	PNB	Provincial Juvenile Facility	All Levels	October 1997	25 years	One, Ten-year	Manage Only

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<b>Facility Name &amp; Location(1)</b>	<b>Design Capacity</b>	<b>Customer</b>	<b>Facility Type</b>	<b>Security Level</b>	<b>Commencement of Current Term</b>	<b>Duration</b>	<b>Renewal Option</b>	<b>Type of Ownership</b>
Pacific Shores Healthcare Victoria, Australia(5)	N/A	VIC CV	Health Care Services	N/A	December 2003	3 years	Four, Six-months	Manage Only
Campsfield House Immigration Removal Centre Kidlington, England	198	UK Home Office of Immigration	Detention Centre	Minimum	May 2006	3 years	One, Two-year	Manage Only
<b>GEO Care Services:</b> Florida Civil Commitment Center Arcadia, FL	680/40	FL — DCF	State Civil Commitment	All Levels	July 2006	5 years	Three, Five-year	Manage Only
Palm Beach County Jail Palm Beach, FL	N/A	PBC as Subcontractor To Healthcare Armor	Mental Health Services to County Jail	All Levels	May 2006	5 years	N/A	Manage Only
South Florida State Hospital Pembroke Pines, FL	335	FL- DCF	State Psychiatric Hospital	Mental Health	July 2003	5 years	Two, Five-year	Manage Only
Fort Bayard Medical Center Ft. Bayard, NM	230	State of NM, Department of Health	Special Needs Long-Term Care Facility	Special Needs & Long-Term Care	November 2005	3 years	Four, Five-year	Manage Only
South Florida Evaluation and Treatment Center Miami, FL	213	FL — DCF	State Forensic Hospital	Mental Health	July 2005	5 years	Two, Five-year	Manage Only
South Florida Evaluation and Treatment Center — Annex Miami, FL	100	FL — DCF	State Forensic Hospital	Mental Health	March 2007	5 years	One, Four-year	Manage Only

**Customer Legend:**

<u>Abbreviation</u>	<u>Customer</u>
LA DPS&C	Louisiana Department of Public Safety & Corrections
ADOC	Arizona Department of Corrections
ICE	U.S. Immigration & Customs Enforcement
WDOC	Wyoming Department of Corrections
TDCJ	Texas Department of Criminal Justice
CDCR	California Department of Corrections
CDOC	Colorado Department of Corrections
TYC	Texas Youth Commission
MDOC	Mississippi Department of Corrections (East Mississippi & Marshall County)
NMCD	New Mexico Corrections Department
VDOC	Virginia Department of Corrections
ODOC	Oklahoma Department of Corrections
DMS	Florida Department of Management Services
BOP	Federal Bureau of Prisons
USMS	United States Marshals Service
IDOC	Indiana Department of Corrections

<u>Abbreviation</u>	<u>Customer</u>
QLD DCS	Department of Corrective Services of the State of Queensland
OFDT	Office of Federal Detention Trustees
VIC MOC	Minister of Corrections of the State of Victoria
NSW	Commissioner of Corrective Services for New South Wales
RSA DCS	Republic of South Africa Department of Correctional Services
VIC CC	The Chief Commissioner of the Victoria Police
PNB	Province of New Brunswick
VIC CV	The State of Victoria represented by Corrections Victoria
DCF	Florida Department of Children & Families

- (1) GEO also owns facilities in Jena, LA and Baldwin, MI that were not in use during fiscal year 2006. Both of these facilities remain inactive. See Note 12 of the Financial Statements.
- (2) GEO provides services at this facility through various Inter-Governmental Agreements, or IGAs, for the county, USMS, ICE, BOP, and other state jurisdictions.
- (3) GEO has a five-year contract with four one-year options to operate this facility on behalf of the county. The county, in turn, has a one-year contract, subject to annual renewal, with the state to house state prisoners at the facility.
- (4) The contract for this facility only requires GEO to provide maintenance services.
- (5) GEO provides comprehensive healthcare services to 9 government-operated prisons under this contract.
- (6) GEO provided notice of award from CDOC for medium security prison. No contracts have been signed as of this date.
- (7) GEO acquired these facilities from CPT on January 24, 2007. Prior to this date these facilities were leased by GEO from CPT.

**Government Contracts — Rebids**

The following table sets forth the number of contracts that are subject to renewal or re-bid in each of the next five years:

<u>Year</u>	<u>Re-bid(1)</u>	<u>Total Number of Beds up for Renewal</u>
2007	9	6,260
2008	7	6,744
2009	12	8,381
2010	5	3,665
2011	7	6,979
Thereafter	21	17,117
	<u>61</u>	<u>49,146</u>

- (1) Many of our contracts with our government customers have an initial fixed term and are thereafter subject to periodic renewals at the unilateral option of the customer. This table assumes that all of our government customers will exercise their unilateral renewal options under each existing facility management contract and, accordingly, that each contract will not be up for renewal or re-bid, as the case may be, until the full stated term of the contract, including the exercise of all applicable renewal options, has run. Although our historical contract renewal rate exceeds 90%, we cannot assure you that our customers will in fact exercise all of their unilateral renewal options under existing contracts. In addition, our government contracts can generally be terminated by our government customers at any time without cause. See “Risk Factors — We are subject to the termination or non-renewal of our government contracts, which could adversely affect our results of operations and liquidity, and our ability to secure new facility management contracts from other government customers.”

We undertake substantial efforts to renew our contracts upon their expiration but we can provide no assurance that we will in fact be able to do so. Previously, in connection with our contract renewals, either we or the contracting government agency have typically requested changes or adjustments to contractual terms. As a result, contract renewals may be made on terms that are more or less favorable to us than in prior contractual terms.

Our contracts typically allow a contracting governmental agency to terminate a contract with or without cause by giving us written notice ranging from 30 to 180 days. If government agencies were to use these provisions to terminate, or renegotiate the terms of their agreements with us, our financial condition and results of operations could be materially adversely affected.

In addition, in connection with our management of such facilities, we are required to comply with all applicable local, state and federal laws and related rules and regulations. Our contracts typically require us to maintain certain levels of coverage for general liability, workers' compensation, vehicle liability, and property loss or damage. If we do not maintain the required categories and levels of coverage, the contracting governmental agency may be permitted to terminate the contract. In addition, we are required under our contracts to indemnify the contracting governmental agency for all claims and costs arising out of our management of facilities and, in some instances, we are required to maintain performance bonds relating to the construction, development and operation of facilities.

#### **Competition**

We compete primarily on the basis of the quality and range of services we offer; our experience domestically and internationally in the design, construction, and management of privatized correctional and detention facilities; our reputation; and our pricing. We compete directly with the public sector, where governmental agencies that are responsible for the operation of correctional, detention and mental health and residential treatment facilities are often seeking to retain projects that might otherwise be privatized. In the private sector, our U.S. corrections and international services business segments compete with a number of companies, including, but not limited to: Corrections Corporation of America; Cornell Companies, Inc.; Management and Training Corporation; Group 4 Securicor, Global Solutions, and Serco. Our GEO Care business segment competes with a number of different small-to-medium sized companies, reflecting the highly fragmented nature of the mental health and residential treatment services industry. Some of our competitors are larger and have more resources than we do. We also compete in some markets with small local companies that may have a better knowledge of the local conditions and may be better able to gain political and public acceptance.

#### **Employees and Employee Training**

At December 31, 2006, we had 10,253 full-time employees. Of such full-time employees, 195 were employed at our headquarters and regional offices and 10,058 were employed at facilities and international offices. We employ management, administrative and clerical, security, educational services, health services and general maintenance personnel at our various locations. Approximately 535 and 916 employees are covered by collective bargaining agreements in the United States and at international offices, respectively. We believe that our relations with our employees are satisfactory.

Under the laws applicable to most of our operations, and internal company policies, our correctional officers are required to complete a minimum amount of training. We generally require at least 160 hours of pre-service training before an employee is allowed to work in a position that will bring the employee in contact with inmates in our domestic facilities, consistent with ACA standards and/or applicable state laws. In addition to a minimum of 160 hours of pre-service training, most states require 40 or 80 hours of on-the-job training. Florida law requires that correctional officers receive 520 hours of training. We believe that our training programs meet or exceed all applicable requirements.

Our training program for domestic facilities begins with approximately 40 hours of instruction regarding our policies, operational procedures and management philosophy. Training continues with an additional 120 hours of instruction covering legal issues, rights of inmates, techniques of communication and supervision,



interpersonal skills and job training relating to the particular position to be held. Each of our employees, who has contact with inmates receives a minimum of 40 hours of additional training each year, and each manager receives at least 24 hours of training each year.

At least 240 and 160 hours of training are required for our employees in Australia and South Africa, respectively, before such employees are allowed to work in positions that will bring them into contact with inmates. Our employees in Australia and South Africa receive a minimum of 40 hours of additional training each year.

#### **Business Regulations and Legal Considerations**

Many governmental agencies are required to enter into a competitive bidding procedure before awarding contracts for products or services. The laws of certain jurisdictions may also require us to award subcontracts on a competitive basis or to subcontract or partner with businesses owned by women or members of minority groups.

Certain states, such as Florida, deem correctional officers to be peace officers and require our personnel to be licensed and subject to background investigation. State law also typically requires correctional officers to meet certain training standards.

The failure to comply with any applicable laws, rules or regulations or the loss of any required license could have a material adverse effect on our business, financial condition and results of operations. Furthermore, our current and future operations may be subject to additional regulations as a result of, among other factors, new statutes and regulations and changes in the manner in which existing statutes and regulations are or may be interpreted or applied. Any such additional regulations could have a material adverse effect on our business, financial condition and results of operations.

#### **Insurance**

The nature of our business exposes us to various types of third-party legal claims, including, but not limited to, civil rights claims relating to conditions of confinement and/or mistreatment, sexual misconduct claims brought by prisoners or detainees, medical malpractice claims, claims relating to employment matters (including, but not limited to, employment discrimination claims, union grievances and wage and hour claims), property loss claims, environmental claims, automobile liability claims, contractual claims and claims for personal injury or other damages resulting from contact with our facilities, programs, personnel or prisoners, including damages arising from a prisoner's escape or from a disturbance or riot at a facility. In addition, our management contracts generally require us to indemnify the governmental agency against any damages to which the governmental agency may be subject in connection with such claims or litigation. We maintain insurance coverage for these general types of claims, except for claims relating to employment matters, for which we carry no insurance.

Claims for which we are insured arising from our U.S. operations that have an occurrence date of October 1, 2002 or earlier are handled by TWC and are commercially insured up to an aggregate limit of between \$25.0 million and \$50.0 million, depending on the nature of the claim and the applicable policy terms and conditions. With respect to claims for which we are insured arising after October 1, 2002, we maintain a general liability policy for all U.S. corrections operations with \$52.0 million per occurrence and in the aggregate. On October 1, 2004, we increased our deductible on this general liability policy from \$1.0 million to \$3.0 million for each claim which occurs after October 1, 2004. GEO Care, Inc. is separately insured for general and professional liability. Coverage is maintained with limits of \$10.0 million per occurrence and in the aggregate subject to a \$3.0 million self-insured retention. We also maintain various levels of insurance to cover property and casualty risks, workers' compensation, medical malpractice, environmental liability and automobile liability. Our Australian subsidiary is required to carry tail insurance on a general liability policy providing an extended reporting period through 2011 related to a discontinued contract. We also carry various types of insurance with respect to our operations in South Africa, Australia and the United Kingdom. There can be no assurance that our insurance coverage will be adequate to cover all claims to which we may be exposed.

### International Operations

Our international operations for fiscal years 2006 and 2005 consisted of the operations of our wholly-owned Australian subsidiaries, and of our consolidated joint venture in South Africa (South African Custodial Management Pty. Limited, or SACM). Through our wholly-owned subsidiary, GEO Group Australia Pty. Limited, we currently manage five facilities in Australia. We operate one facility in South Africa through SACM. During the fourth quarter of 2004, we opened an office in the United Kingdom to pursue new business opportunities throughout Europe. On March 6, 2006, we were awarded a contract to manage the operations of the 198 bed Campsfield House in Kidlington, United Kingdom. We began operations under this contract in the second quarter of 2006. See Item 7 for more information on SACM. Financial information about our operations in different geographic regions appears in "Item 8. Financial Statements — Note 16 Business Segment and Geographic Information."

### Business Concentration

Except for the major customers noted in the following table, no single customer provided more than 10% of our consolidated revenues during fiscal years 2006, 2005 or 2004:

<u>Customer</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Various agencies of the U.S. Federal Government	30%	27%	27%
Various agencies of the State of Florida	5%	7%	12%

Concentration of credit risk related to accounts receivable is reflective of the related revenues.

### Available Information

Additional information about us can be found at [www.thegeogroupinc.com](http://www.thegeogroupinc.com). We make available on our website, free of charge, access to our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, our annual proxy statement on Schedule 14A and amendments to those materials filed or furnished pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act of 1934 as soon as reasonably practicable after we electronically submit such materials to the Securities and Exchange Commission, or the SEC. In addition, the SEC makes available on its website, free of charge, reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including GEO. The SEC's website is located at <http://www.sec.gov>. Information provided on our website or on the SEC's website is not part of this Annual Report on Form 10-K.

### Item 1A. Risk Factors

The following are certain of the risks to which our business operations are subject. Any of these risks could materially adversely affect our business, financial condition, or results of operations. These risks could also cause our actual results to differ materially from those indicated in the forward-looking statements contained herein and elsewhere. The risks described below are not the only risks facing us. Additional risks not currently known to us or those we currently deem to be immaterial may also materially and adversely affect our business operations.

#### Risks Related to Our High Level of Indebtedness

*Our significant level of indebtedness could adversely affect our financial condition and prevent us from fulfilling our debt service obligations.*

We have a significant amount of indebtedness. Our total consolidated long-term indebtedness as of December 31, 2006 was \$145.0 million, excluding non recourse debt of \$131.7 million and capital lease liability balances of \$16.6 million. In addition, as of December 31, 2006, we had \$54.5 million outstanding in letters of credit under the revolving loan portion of our senior secured credit facility. As a result, as of that date, we would have had the ability to borrow an additional approximately \$45.5 million under the revolving loan portion of our Senior Credit Facility, subject to our satisfying the relevant borrowing conditions under the Senior Credit Facility with respect to the incurrence of additional indebtedness.

Additionally, on January 24, 2007, we completed the refinancing of our senior secured credit facility, referred to as the Senior Credit Facility through the execution of a Third Amended and Restated Credit Agreement, referred to as the Amended Senior Credit Facility. The Amended Senior Credit Facility consists of a \$365 million 7-year term loan referred to as the Term Loan B and a \$150 million 5-year revolver, expiring September 14, 2010, referred to as the Revolver. The initial interest rate for the Term Loan B is LIBOR plus 1.5% and the Revolver would bear interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, we used the \$365 million in borrowings under the Term Loan B to finance our acquisition of CPT. After giving effect to these borrowings, we currently have approximately \$515 million in total consolidated long-term indebtedness, excluding non recourse debt of \$131.7 million and capital lease liability balances of \$16.6 million. Based on our debt covenants and the amount of indebtedness we have outstanding, we currently have the ability to borrow an additional approximately \$55 million under our Amended Senior Credit Facility.

Our substantial indebtedness could have important consequences. For example, it could:

- require us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, and other general corporate purposes;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- increase our vulnerability to adverse economic and industry conditions;
- place us at a competitive disadvantage compared to competitors that may be less leveraged; and
- limit our ability to borrow additional funds or refinance existing indebtedness on favorable terms.

If we are unable to meet our debt service obligations, we may need to reduce capital expenditures, restructure or refinance our indebtedness, obtain additional equity financing or sell assets. We may be unable to restructure or refinance our indebtedness, obtain additional equity financing or sell assets on satisfactory terms or at all. In addition, our ability to incur additional indebtedness will be restricted by the terms of our Amended Senior Credit Facility and the indenture governing our outstanding 8<sup>3</sup>/<sub>4</sub> % Senior Unsecured Notes, referred to as the Notes.

***Despite current indebtedness levels, we may still incur more indebtedness, which could further exacerbate the risks described above. Future indebtedness issued pursuant to our universal shelf registration statement could have rights superior to those of our existing or future indebtedness.***

The terms of the indenture governing the Notes and our Amended Senior Credit Facility restrict our ability to incur but do not prohibit us from incurring significant additional indebtedness in the future. In addition, we may refinance all or a portion of our indebtedness, including borrowings under our Amended Senior Credit Facility, and incur more indebtedness as a result. If new indebtedness is added to our and our subsidiaries' current debt levels, the related risks that we and they now face could intensify. Additionally, on January 28, 2004, our universal shelf registration statement on Form S-3 was declared effective by the SEC. The universal shelf registration statement provides for the offer and sale by us, from time to time, on a delayed basis of up to \$200.0 million aggregate amount of certain of our securities, including our debt securities. On June 12, 2006 we completed a public offering of 4.5 million shares of our common stock (reflecting our recent 3-for-2 stock split) for approximately \$110 million under the universal shelf registration statement. As a result, we have approximately \$90 million remaining for the offer and sale by us of certain of our securities including our debt securities. Such debt securities could have rights superior to those of our existing indebtedness.

***The covenants in the indenture governing the Notes and our Amended Senior Credit Facility impose significant operating and financial restrictions which may adversely affect our ability to operate our business.***

The indenture governing the Notes and our Amended Senior Credit Facility impose significant operating and financial restrictions on us and certain of our subsidiaries, which we refer to as restricted subsidiaries. These restrictions limit our ability to, among other things:

- incur additional indebtedness;
- pay dividends and or distributions on our capital stock, repurchase, redeem or retire our capital stock, prepay subordinated indebtedness, make investments;
- issue preferred stock of subsidiaries;
- make certain types of investments;
- guarantee other indebtedness;
- create liens on our assets;
- transfer and sell assets;
- create or permit restrictions on the ability of our restricted subsidiaries to make dividends or make other distributions to us;
- enter into sale/leaseback transactions;
- enter into transactions with affiliates; and
- merge or consolidate with another company or sell all or substantially all of our assets.

These restrictions could limit our ability to finance our future operations or capital needs, make acquisitions or pursue available business opportunities. In addition, our Amended Senior Credit Facility requires us to maintain specified financial ratios and satisfy certain financial covenants, including maintaining maximum senior and total leverage ratios, a minimum fixed charge coverage ratio, a minimum net worth and a limit on the amount of our annual capital expenditures. Some of these financial ratios become more restrictive over the life of the Amended Senior Credit Facility. We may be required to take action to reduce our indebtedness or to act in a manner contrary to our business objectives to meet these ratios and satisfy these covenants. Our failure to comply with any of the covenants under our Amended Senior Credit Facility and the indenture governing the Notes could cause an event of default under such documents and result in an acceleration of all of our outstanding indebtedness. If all of our outstanding indebtedness were to be accelerated, we likely would not be able to simultaneously satisfy all of our obligations under such indebtedness, which would materially adversely affect our financial condition and results of operations.

***Servicing our indebtedness will require a significant amount of cash. Our ability to generate cash depends on many factors beyond our control.***

Our ability to make payments on our indebtedness and to fund planned capital expenditures will depend on our ability to generate cash in the future. This, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control.

Our business may not be able to generate sufficient cash flow from operations or future borrowings may not be available to us under our Amended Senior Credit Facility or otherwise in an amount sufficient to enable us to pay our indebtedness or new debt securities, or to fund our other liquidity needs. We may need to refinance all or a portion of our indebtedness on or before maturity. However, we may not be able to complete such refinancing on commercially reasonable terms or at all.

***Because portions of our indebtedness have floating interest rates, a general increase in interest rates will adversely affect cash flows.***

Our Amended Senior Credit Facility bears interest at a variable rate. To the extent our exposure to increases in interest rates is not eliminated through interest rate protection agreements, such increases will adversely affect our cash flows. We do not currently have any interest rate protection agreements in place to protect against interest rate fluctuations related to our Amended Senior Credit Facility. Our estimated total annual interest expense based on borrowings outstanding as of January 24, 2007 reflecting the acquisition of CPT is approximately \$25.1 million. Based on estimated borrowings of \$365 million outstanding under the Amended Senior Credit Facility, a one percent increase in the interest rate applicable to the Senior Credit Facility, will increase interest expense by \$3.7 million.

In addition, effective September 18, 2003, we entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. The agreements, which have payment and expiration dates that coincide with the payment and expiration terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, we receive a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while we make a variable interest rate payment to the same counterparties equal to the six-month London Interbank Offered Rate plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. As a result, for every one percent increase in the interest rate applicable to the swap agreements, our total annual interest expense will increase by \$0.5 million.

***We depend on distributions from our subsidiaries to make payments on our indebtedness. These distributions may not be made.***

We generate a substantial portion of our revenues from distributions on the equity interests we hold in our subsidiaries. Therefore, our ability to meet our payment obligations on our indebtedness is substantially dependent on the earnings of our subsidiaries and the payment of funds to us by our subsidiaries as dividends, loans, advances or other payments. Our subsidiaries are separate and distinct legal entities and are not obligated to make funds available for payment of our other indebtedness in the form of loans, distributions or otherwise. Our subsidiaries' ability to make any such loans, distributions or other payments to us will depend on their earnings, business results, the terms of their existing and any future indebtedness, tax considerations and legal or contractual restrictions to which they may be subject. If our subsidiaries do not make such payments to us, our ability to repay our indebtedness may be materially adversely affected. For the fiscal year ended December 31, 2006, our subsidiaries accounted for 28.8% of our consolidated revenues, and, as of December 31, 2006 our subsidiaries accounted for 20.3% of our consolidated total assets.

#### **Risks Related to Our Business and Industry**

***We are subject to the termination or non-renewal of our government contracts, which could adversely affect our results of operations and liquidity, including our ability to secure new facility management contracts from other government customers.***

Governmental agencies may terminate a facility contract at any time without cause or use the possibility of termination to negotiate a lower fee for per diem rates. They also generally have the right to renew facility contracts at their option. Notwithstanding any contractual renewal option, as of December 31, 2006, nine of our facility management contracts are scheduled to expire on or before December 31, 2007. These contracts represented 14.5% of our consolidated revenues for the fiscal year ended December 31, 2006. Some or all of these contracts may not be renewed by the corresponding governmental agency. See "Business — Government Contracts — Rebids." In addition, governmental agencies may determine not to exercise renewal options with respect to any of our contracts in the future. In the event any of our management contracts are terminated or are not renewed on favorable terms or otherwise, we may not be able to obtain additional replacement contracts. The non-renewal or termination of any of our contracts with governmental agencies could materially adversely affect our financial condition, results of operations and liquidity, including our ability to secure new facility management contracts from other government customers.

***Our growth depends on our ability to secure contracts to develop and manage new correctional and detention facilities, the demand for which is outside our control.***

Our growth is generally dependent upon our ability to obtain new contracts to develop and manage new correctional and detention facilities, because contracts to manage existing public facilities have not to date typically been offered to private operators. Public sector demand for new facilities may decrease and our potential for growth will depend on a number of factors we cannot control, including overall economic conditions, crime rates and sentencing patterns in jurisdictions in which we operate, governmental and public acceptance of the concept of privatization, and the number of facilities available for privatization.

The demand for our facilities and services could be adversely affected by the relaxation of criminal enforcement efforts, leniency in conviction and sentencing practices, or through the decriminalization of certain activities that are currently proscribed by criminal laws. For instance, any changes with respect to the decriminalization of drugs and controlled substances or a loosening of immigration laws could affect the number of persons arrested, convicted, sentenced and incarcerated, thereby potentially reducing demand for correctional facilities to house them. Similarly, reductions in crime rates could lead to reductions in arrests, convictions and sentences requiring incarceration at correctional facilities.

***We may not be able to secure financing and land for new facilities, which could adversely affect our results of operations and future growth.***

In certain cases, the development and construction of facilities by us is subject to obtaining construction financing. Such financing may be obtained through a variety of means, including without limitation, the sale of tax-exempt or taxable bonds or other obligations or direct governmental appropriations. The sale of tax-exempt or taxable bonds or other obligations may be adversely affected by changes in applicable tax laws or adverse changes in the market for tax-exempt or taxable bonds or other obligations.

Moreover, certain jurisdictions, including California, where we have a significant amount of operations, have in the past required successful bidders to make a significant capital investment in connection with the financing of a particular project. If this trend were to continue in the future, we may not be able to obtain sufficient capital resources when needed to compete effectively for facility management contracts. Additionally, our success in obtaining new awards and contracts may depend, in part, upon our ability to locate land that can be leased or acquired under favorable terms. Otherwise desirable locations may be in or near populated areas and, therefore, may generate legal action or other forms of opposition from residents in areas surrounding a proposed site. Our inability to secure financing and desirable locations for new facilities could adversely affect our results of operations and future growth.

***We depend on a limited number of governmental customers for a significant portion of our revenues. The loss of, or a significant decrease in business from, these customers could seriously harm our financial condition and results of operations.***

We currently derive, and expect to continue to derive, a significant portion of our revenues from a limited number of governmental agencies. Of our 32 governmental clients, six customers accounted for over 50% of our consolidated revenues for the fiscal year ended December 31, 2006. In addition, the three federal governmental agencies with correctional and detention responsibilities, the Bureau of Prisons, the Bureau of Immigration and Customs Enforcement, which we refer to as ICE, and the Marshals Service, accounted for approximately 29.5% of our total consolidated revenues for the fiscal year ended December 31, 2006, with the Bureau of Prisons accounting for approximately 9.8% of our total consolidated revenues for such period, the Marshals Service accounting for approximately 9.6% of our total consolidated revenues for such period, and ICE accounting for approximately 10.1% of our total consolidated revenues for such period. The loss of, or a significant decrease in, business from the Bureau of Prisons, ICE, or the U.S. Marshals Service or any other significant customers could seriously harm our financial condition and results of operations. We expect to continue to depend upon these federal agencies and a relatively small group of other governmental customers for a significant percentage of our revenues.

***A decrease in occupancy levels could cause a decrease in revenues and profitability.***

While a substantial portion of our cost structure is generally fixed, a significant portion of our revenues are generated under facility management contracts which provide for per diem payments based upon daily occupancy. We are dependent upon the governmental agencies with which we have contracts to provide inmates for our managed facilities. We cannot control occupancy levels at our managed facilities. Under a per diem rate structure, a decrease in our occupancy rates could cause a decrease in revenues and profitability. When combined with relatively fixed costs for operating each facility, regardless of the occupancy level, a decrease in occupancy levels could have a material adverse effect on our profitability.

***Competition for inmates may adversely affect the profitability of our business.***

We compete with government entities and other private operators on the basis of cost, quality and range of services offered, experience in managing facilities, and reputation of management and personnel. Barriers to entering the market for the management of correctional and detention facilities may not be sufficient to limit additional competition in our industry. In addition, our government customers may assume the management of a facility currently managed by us upon the termination of the corresponding management contract or, if such customers have capacity at the facilities which they operate, they may take inmates currently housed in our facilities and transfer them to government operated facilities. Since we are paid on a per diem basis with no minimum guaranteed occupancy under most of our contracts, the loss of such inmates and resulting decrease in occupancy would cause a decrease in both our revenues and our profitability.

***We are dependent on government appropriations, which may not be made on a timely basis or at all.***

Our cash flow is subject to the receipt of sufficient funding of and timely payment by contracting governmental entities. If the contracting governmental agency does not receive sufficient appropriations to cover its contractual obligations, it may terminate our contract or delay or reduce payment to us. Any delays in payment, or the termination of a contract, could have a material adverse effect on our cash flow and financial condition, which may make it difficult to satisfy our payment obligations on our indebtedness, including the Notes and the Senior Credit Facility, in a timely manner. The Governor of the State of Michigan's veto in October 2005 of appropriations for our Michigan Correctional Facility in October 2005 is an example of this risk. See Item 3. Legal Proceedings. In addition, as a result of, among other things, recent economic developments, federal, state and local governments have encountered, and may continue to encounter, unusual budgetary constraints. As a result, a number of state and local governments are under pressure to control additional spending or reduce current levels of spending. Accordingly, we may be requested in the future to reduce our existing per diem contract rates or forego prospective increases to those rates. In addition, it may become more difficult to renew our existing contracts on favorable terms or at all.

***Public resistance to privatization of correctional and detention facilities could result in our inability to obtain new contracts or the loss of existing contracts, which could have a material adverse effect on our business, financial condition and results of operations.***

The management and operation of correctional and detention facilities by private entities has not achieved complete acceptance by either governments or the public. Some governmental agencies have limitations on their ability to delegate their traditional management responsibilities for correctional and detention facilities to private companies and additional legislative changes or prohibitions could occur that further increase these limitations. In addition, the movement toward privatization of correctional and detention facilities has encountered resistance from groups, such as labor unions, that believe that correctional and detention facilities should only be operated by governmental agencies. Changes in dominant political parties could also result in significant changes to previously established views of privatization. Increased public resistance to the privatization of correctional and detention facilities in any of the markets in which we operate, as a result of these or other factors, could have a material adverse effect on our business, financial condition and results of operations.

***Adverse publicity may negatively impact our ability to retain existing contracts and obtain new contracts. Our business is subject to public scrutiny.***

Any negative publicity about an escape, riot or other disturbance or perceived poor conditions at a privately managed facility may result in publicity adverse to us and the private corrections industry in general. Any of these occurrences or continued trends may make it more difficult for us to renew existing contracts or to obtain new contracts or could result in the termination of an existing contract or the closure of one of our facilities, which could have a material adverse effect on our business.

***We may incur significant start-up and operating costs on new contracts before receiving related revenues, which may impact our cash flows and not be recouped.***

When we are awarded a contract to manage a facility, we may incur significant start-up and operating expenses, including the cost of constructing the facility, purchasing equipment and staffing the facility, before we receive any payments under the contract. These expenditures could result in a significant reduction in our cash reserves and may make it more difficult for us to meet other cash obligations, including our payment obligations on the Notes and the Amended Senior Credit Facility. In addition, a contract may be terminated prior to its scheduled expiration and as a result we may not recover these expenditures or realize any return on our investment.

***Failure to comply with extensive government regulation and applicable contractual requirements could have a material adverse effect on our business, financial condition or results of operations.***

The industry in which we operate is subject to extensive federal, state and local regulations, including educational, environmental, health care and safety regulations, which are administered by many regulatory authorities. Some of the regulations are unique to the corrections industry, and the combination of regulations affects all areas of our operations. Facility management contracts typically include reporting requirements, supervision and on-site monitoring by representatives of the contracting governmental agencies. Corrections officers and juvenile care workers are customarily required to meet certain training standards and, in some instances, facility personnel are required to be licensed and are subject to background investigations. Certain jurisdictions also require us to award subcontracts on a competitive basis or to subcontract with businesses owned by members of minority groups. We may not always successfully comply with these and other regulations to which we are subject and failure to comply can result in material penalties or the non-renewal or termination of facility management contracts. In addition, changes in existing regulations could require us to substantially modify the manner in which we conduct our business and, therefore, could have a material adverse effect on us.

In addition, private prison managers are increasingly subject to government legislation and regulation attempting to restrict the ability of private prison managers to house certain types of inmates, such as inmates from other jurisdictions or inmates at medium or higher security levels. Legislation has been enacted in several states, and has previously been proposed in the United States House of Representatives, containing such restrictions. Although we do not believe that existing legislation will have a material adverse effect on us, future legislation may have such an effect on us.

Governmental agencies may investigate and audit our contracts and, if any improprieties are found, we may be required to refund amounts we have received, to forego anticipated revenues and we may be subject to penalties and sanctions, including prohibitions on our bidding in response to Requests for Proposals, or RFPs, from governmental agencies to manage correctional facilities. Governmental agencies we contract with have the authority to audit and investigate our contracts with them. As part of that process, governmental agencies may review our performance of the contract, our pricing practices, our cost structure and our compliance with applicable laws, regulations and standards. For contracts that actually or effectively provide for certain reimbursement of expenses, if an agency determines that we have improperly allocated costs to a specific contract, we may not be reimbursed for those costs, and we could be required to refund the amount of any such costs that have been reimbursed. If a government audit asserts improper or illegal activities by us, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts,



forfeitures of profits, suspension of payments, fines and suspension or disqualification from doing business with certain governmental entities. Any adverse determination could adversely impact our ability to bid in response to RFPs in one or more jurisdictions.

***We may face community opposition to facility location, which may adversely affect our ability to obtain new contracts.***

Our success in obtaining new awards and contracts sometimes depends, in part, upon our ability to locate land that can be leased or acquired, on economically favorable terms, by us or other entities working with us in conjunction with our proposal to construct and/or manage a facility. Some locations may be in or near populous areas and, therefore, may generate legal action or other forms of opposition from residents in areas surrounding a proposed site. When we select the intended project site, we attempt to conduct business in communities where local leaders and residents generally support the establishment of a privatized correctional or detention facility. Future efforts to find suitable host communities may not be successful. In many cases, the site selection is made by the contracting governmental entity. In such cases, site selection may be made for reasons related to political and/or economic development interests and may lead to the selection of sites that have less favorable environments.

***Our business operations expose us to various liabilities for which we may not have adequate insurance.***

The nature of our business exposes us to various types of third-party legal claims, including, but not limited to, civil rights claims relating to conditions of confinement and/or mistreatment, sexual misconduct claims brought by prisoners or detainees, medical malpractice claims, claims relating to employment matters (including, but not limited to, employment discrimination claims, union grievances and wage and hour claims), property loss claims, environmental claims, automobile liability claims, contractual claims and claims for personal injury or other damages resulting from contact with our facilities, programs, personnel or prisoners, including damages arising from a prisoner's escape or from a disturbance or riot at a facility. In addition, our management contracts generally require us to indemnify the governmental agency against any damages to which the governmental agency may be subject in connection with such claims or litigation. We maintain insurance coverage for these general types of claims, except for claims relating to employment matters, for which we carry no insurance. However, the insurance we maintain to cover the various liabilities to which we are exposed may not be adequate. Any losses relating to matters for which we are either uninsured or for which we do not have adequate insurance could have a material adverse effect on our business, financial condition or results of operations. In addition, any losses relating to employment matters could have a material adverse effect on our business, financial condition or results of operations.

Claims for which we are insured arising from our U.S. operations that have an occurrence date of October 1, 2002 or earlier are handled by TWC and are commercially insured up to an aggregate limit of between \$25.0 million and \$50.0 million, depending on the nature of the claim and the applicable policy terms and conditions. With respect to claims for which we are insured arising after October 1, 2002, we maintain a general liability policy for all U.S. corrections operations with \$52.0 million per occurrence and in the aggregate. On October 1, 2004, we increased our deductible on this general liability policy from \$1.0 million to \$3.0 million for each claim which occurs after October 1, 2004. We also maintain insurance to cover property and casualty risks, workers' compensation, medical malpractice, environmental liability and automobile liability. Our Australian subsidiary is required to carry tail insurance on a general liability policy providing an extended reporting period through 2011 related to a discontinued contract. We also carry various types of insurance with respect to our operations in South Africa, the United Kingdom and Australia. There can be no assurance that our insurance coverage will be adequate to cover all claims to which we may be exposed.

Since our insurance policies generally have high deductible amounts (including a \$3.0 million per claim deductible under our general liability and auto liability policies and a \$2.0 million per claim deductible under our workers' compensation policy), losses are recorded as reported and a provision is made to cover losses incurred but not reported. Loss reserves are undiscounted and are computed based on independent actuarial studies. Our management uses judgments in assessing loss estimates based on actuarial studies, which include actual claim amounts and loss development based on both GEO's own historical experience and industry

experience. If actual losses related to insurance claims significantly differ from our estimates, our financial condition and results of operations could be materially impacted.

Certain GEO facilities located in Florida and determined by insurers to be in high-risk hurricane areas carry substantial windstorm deductibles of up to \$3.0 million. Since hurricanes are considered unpredictable future events, no reserves have been established to pre-fund for potential windstorm damage. Limited commercial availability of certain types of insurance relating to windstorm exposure in coastal areas and earthquake exposure mainly in California may prevent us from insuring our facilities to full replacement value.

***We may not be able to obtain or maintain the insurance levels required by our government contracts.***

Our government contracts require us to obtain and maintain specified insurance levels. The occurrence of any events specific to our company or to our industry, or a general rise in insurance rates, could substantially increase our costs of obtaining or maintaining the levels of insurance required under our government contracts, or prevent us from obtaining or maintaining such insurance altogether. If we are unable to obtain or maintain the required insurance levels, our ability to win new government contracts, renew government contracts that have expired and retain existing government contracts could be significantly impaired, which could have a material adverse effect on our business, financial condition and results of operations.

***Our international operations expose us to risks which could materially adversely affect our financial condition and results of operations.***

For the fiscal year ended December 31, 2006, our international operations accounted for approximately 12% of our consolidated revenues. We face risks associated with our operations outside the U.S. These risks include, among others, political and economic instability, exchange rate fluctuations, taxes, duties and the laws or regulations in those foreign jurisdictions in which we operate. In the event that we experience any difficulties arising from our operations in foreign markets, our business, financial condition and results of operations may be materially adversely affected.

***We conduct certain of our operations through joint ventures, which may lead to disagreements with our joint venture partners and adversely affect our interest in the joint ventures.***

We conduct substantially all of our operations in South Africa through joint ventures with third parties and may enter into additional joint ventures in the future. Our joint venture agreements generally provide that the joint venture partners will equally share voting control on all significant matters to come before the joint venture. Our joint venture partners may have interests that are different from ours which may result in conflicting views as to the conduct of the business of the joint venture. In the event that we have a disagreement with a joint venture partner as to the resolution of a particular issue to come before the joint venture, or as to the management or conduct of the business of the joint venture in general, we may not be able to resolve such disagreement in our favor and such disagreement could have a material adverse effect on our interest in the joint venture or the business of the joint venture in general.

***We are dependent upon our senior management and our ability to attract and retain sufficient qualified personnel.***

We are dependent upon the continued service of each member of our senior management team, including George C. Zoley, our Chairman and Chief Executive Officer, Wayne H. Calabrese, our Vice Chairman and President, and John G. O'Rourke, our Chief Financial Officer. Under the terms of their retirement agreements, each of these executives is currently eligible to retire at any time from GEO and receive significant lump sum retirement payments. The unexpected loss of any of these individuals could materially adversely affect our business, financial condition or results of operations. We do not maintain key-man life insurance to protect against the loss of any of these individuals.

In addition, the services we provide are labor-intensive. When we are awarded a facility management contract or open a new facility, we must hire operating management, correctional officers and other personnel. The success of our business requires that we attract, develop and retain these personnel. Our inability to hire

sufficient qualified personnel on a timely basis or the loss of significant numbers of personnel at existing facilities could have a material effect on our business, financial condition or results of operations.

***Our profitability may be materially adversely affected by inflation.***

Many of our facility management contracts provide for fixed management fees or fees that increase by only small amounts during their terms. While a substantial portion of our cost structure is generally fixed, if, due to inflation or other causes, our operating expenses, such as costs relating to personnel, utilities, insurance, medical and food, increase at rates faster than increases, if any, in our facility management fees, then our profitability could be materially adversely affected.

***Various risks associated with the ownership of real estate may increase costs, expose us to uninsured losses and adversely affect our financial condition and results of operations.***

Our ownership of correctional and detention facilities subjects us to risks typically associated with investments in real estate. Investments in real estate, and in particular, correctional and detention facilities, are relatively illiquid and, therefore, our ability to divest ourselves of one or more of our facilities promptly in response to changed conditions is limited. Investments in correctional and detention facilities, in particular, subject us to risks involving potential exposure to environmental liability and uninsured loss. Our operating costs may be affected by the obligation to pay for the cost of complying with existing environmental laws, ordinances and regulations, as well as the cost of complying with future legislation. In addition, although we maintain insurance for many types of losses, there are certain types of losses, such as losses from earthquakes, riots and acts of terrorism, which may be either uninsurable or for which it may not be economically feasible to obtain insurance coverage, in light of the substantial costs associated with such insurance. As a result, we could lose both our capital invested in, and anticipated profits from, one or more of the facilities we own. Further, even if we have insurance for a particular loss, we may experience losses that may exceed the limits of our coverage.

***Risks related to facility construction and development activities may increase our costs related to such activities.***

When we are engaged to perform construction and design services for a facility, we typically act as the primary contractor and subcontract with other companies who act as the general contractors. As primary contractor, we are subject to the various risks associated with construction (including, without limitation, shortages of labor and materials, work stoppages, labor disputes and weather interference) which could cause construction delays. In addition, we are subject to the risk that the general contractor will be unable to complete construction at the budgeted costs or be unable to fund any excess construction costs, even though we typically require general contractors to post construction bonds and insurance. Under such contracts, we are ultimately liable for all late delivery penalties and cost overruns.

***The rising cost and increasing difficulty of obtaining adequate levels of surety credit on favorable terms could adversely affect our operating results.***

We are often required to post performance bonds issued by a surety company as a condition to bidding on or being awarded a facility development contract. Availability and pricing of these surety commitments is subject to general market and industry conditions, among other factors. Recent events in the economy have caused the surety market to become unsettled, causing many reinsurers and sureties to reevaluate their commitment levels and required returns. As a result, surety bond premiums generally are increasing. If we are unable to effectively pass along the higher surety costs to our customers, any increase in surety costs could adversely affect our operating results. In addition, we may not continue to have access to surety credit or be able to secure bonds economically, without additional collateral, or at the levels required for any potential facility development or contract bids. If we are unable to obtain adequate levels of surety credit on favorable terms, we would have to rely upon letters of credit under our Senior Credit Facility, which would entail higher costs even if such borrowing capacity was available when desired, and our ability to bid for or obtain new contracts could be impaired.

***We may not be able to successfully identify, consummate or integrate acquisitions.***

We have an active acquisition program, the objective of which is to identify suitable acquisition targets that will enhance our growth. The pursuit of acquisitions may pose certain risks to us. We may not be able to identify acquisition candidates that fit our criteria for growth and profitability. Even if we are able to identify such candidates, we may not be able to acquire them on terms satisfactory to us. We will incur expenses and dedicate attention and resources associated with the review of acquisition opportunities, whether or not we consummate such acquisitions. Additionally, even if we are able to acquire suitable targets on agreeable terms, we may not be able to successfully integrate their operations with ours. We may also assume liabilities in connection with acquisitions that we would otherwise not be exposed to.

**Risks Related to our Common Stock**

***Fluctuations in the stock market as well as general economic, market and industry conditions may harm the market price of our common stock.***

The market price of our common stock has been subject to significant fluctuation. The market price of our common stock may continue to be subject to significant fluctuations in response to operating results and other factors, including:

- actual or anticipated quarterly fluctuations in our financial results, particularly if they differ from investors' expectations;
- changes in financial estimates and recommendations by securities analysts;
- general economic, market and political conditions, including war or acts of terrorism, not related to our business;
- actions of our competitors and changes in the market valuations, strategy and capability of our competitors;
- our ability to successfully integrate acquisitions and consolidations; and
- changes in the prospects of the privatized corrections and detention industry.

In addition, the stock market in recent years has experienced price and volume fluctuations that often have been unrelated or disproportionate to the operating performance of companies. These fluctuations, may harm the market price of our common stock, regardless of our operating results.

***Future sales of our common stock in the public market could adversely affect the trading price of our common stock that we may issue and our ability to raise funds in new securities offerings.***

Future sales of substantial amounts of our common stock in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and could impair our ability to raise capital through future offerings of equity or equity-related securities. We cannot predict the effect, if any, that future sales of shares of common stock or the availability of shares of common stock for future sale will have on the trading price of our common stock.

***Various anti-takeover protections applicable to us may make an acquisition of us more difficult and reduce the market value of our common stock.***

We are a Florida corporation and the anti-takeover provisions of Florida law impose various impediments to the ability of a third party to acquire control of our company, even if a change of control would be beneficial to our shareholders. In addition, provisions of our articles of incorporation may make an acquisition of us more difficult. Our articles of incorporation authorize the issuance by our board of directors of "blank check" preferred stock without shareholder approval. Such shares of preferred stock could be given voting rights, dividend rights, liquidation rights or other similar rights superior to those of our common stock, making a takeover of us more difficult and expensive. We also have adopted a shareholder rights plan, commonly known as a "poison pill," which could result in the significant dilution of the proportionate ownership of any

person that engages in an unsolicited attempt to take over our company and, accordingly, could discourage potential acquirors. In addition to discouraging takeovers, the anti-takeover provisions of Florida law and our articles of incorporation, as well as our shareholder rights plan, may have the impact of reducing the market value of our common stock.

***Failure to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 could have an adverse effect on our business and the trading price of our common stock.***

If we fail to maintain the adequacy of our internal controls, in accordance with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002. Failure to achieve and maintain effective internal controls could have an adverse effect on the price of our common stock.

***We may issue additional debt securities that could limit our operating flexibility and negatively affect the value of our common stock.***

In the future, we may issue additional debt securities which may be governed by an indenture or other instrument containing covenants that could place restrictions on the operation of our business and the execution of our business strategy in addition to the restrictions on our business already contained in the agreements governing our existing debt. In addition, we may choose to issue debt that is convertible or exchangeable for other securities, including our common stock, or that has rights, preferences and privileges senior to our common stock. Because any decision to issue debt securities will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of any future debt financings and we may be required to accept unfavorable terms for any such financings. Accordingly, any future issuance of debt could dilute the interest of holders of our common stock and reduce the value of our common stock.

***Because we do not intend to pay dividends, shareholders will benefit from an investment in our common stock only if it appreciates in value.***

We currently intend to retain our future earnings, if any, to finance the further expansion and continued growth of our business and do not expect to pay any cash dividends in the foreseeable future. As a result, the success of an investment in our common stock will depend upon any future appreciation in its value. There is no guarantee that our common stock will appreciate in value or even maintain the price at which shareholders purchase their shares.

**Item 1B. *Unresolved Staff Comments***

None.

**Item 2. *Properties***

Our corporate offices are located in Boca Raton, Florida, under a 10-year lease expiring 2013. In addition, we lease office space for our eastern regional office in Palm Beach Gardens, Florida; our central regional office in New Braunfels, Texas; and our western regional office in Carlsbad, California. We also lease office space in Sydney, Australia, through our overseas affiliates, in Sandton, South Africa, and in Theale, England to support our Australian, South African, and UK operations, respectively.

See "Facilities" listing under Item 1 for a list of the correctional, detention and mental health properties we own or lease in connection with our operations.

**Item 3. Legal Proceedings**

On May 19, 2006, we, along with Corrections Corporation of America, referred to as CCA, were sued by an individual plaintiff in the Circuit Court of the Second Judicial Circuit for Leon County, Florida (Case No. 2005CA001884). The complaint alleges that, during the period from 1995 to 2004, we and CCA overbilled the State of Florida by an amount of at least \$12.7 million by submitting to the State false claims for various items relating to (i) repairs, maintenance and improvements to certain facilities which we operate in Florida, (ii) our staffing patterns in filling vacant security positions at those facilities, and (iii) our alleged failure to meet the conditions of certain waivers granted to us by the State of Florida from the payment of liquidated damages penalties relating to our staffing patterns at those facilities. The portion of the complaint relating to us arises out of our operations at our South Bay and Moore Haven, Florida correctional facilities. The complaint appears to be based largely on the same set of issues raised by a Florida Inspector General's Evaluation Report released in late June 2005, referred to as the IG Report, which alleged that us and CCA overbilled the State of Florida by over \$12 million.

Subsequently, the Florida Department of Management Services, referred to as the DMS, which is responsible for administering our correctional contracts with the State of Florida, conducted a detailed analysis of the allegations raised by the IG Report which included a comprehensive written response to the IG Report which we had prepared and delivered to the DMS. In September 2005, the DMS provided a letter to us stating that, although its review had not yet been fully completed, it did not find any indication of any improper conduct by us. On October 17, 2006, DMS provided a letter to us stating that its review had been completed. We and DMS then agreed to settle this matter for \$0.3 million. Although this determination is not dispositive of the recently initiated litigation, we believe it supports our position that we have valid defenses in this matter. We will continue to investigate this matter and intend to defend our rights vigorously. However, given the amounts claimed by the plaintiff and the fact that the nature of the allegations could cause adverse publicity to us, we believe that this matter, if settled unfavorably to us, could have a material adverse effect on our financial condition and results of operations.

On September 15, 2006, a jury in an inmate wrongful death lawsuit in a Texas state court awarded a \$47.5 million verdict against us. Recently, the verdict was entered as a judgment against us in the amount of \$51.7 million. On December 9, 2006, the trial court denied our post trial motions and we filed a notice of appeal on December 18, 2006. The lawsuit is being administered under an insurance program established by The Wackenhut Corporation, our former parent company, in which we participated until October 2002. Policies secured by us under that program provide \$55 million in aggregate annual coverage. As a result, we believe we are fully insured for all damages, costs and expenses associated with the lawsuit and as such we have not taken any reserves in connection with the matter. The lawsuit stems from an inmate death which occurred at our former Willacy County State Jail in Raymondville, Texas, in April 2001, when two inmates at the facility attacked another inmate. Separate investigations conducted internally by us, The Texas Rangers and the Texas Office of the Inspector General, exonerated us and our employees of any culpability with respect to the incident. We believe that the verdict in the lawsuit is contrary to law and unsubstantiated by the evidence. Our insurance carrier has posted a superseded bond in the amount of approximately \$60.0 million to cover the judgment.

We own the 480-bed Michigan Correctional Facility in Baldwin, Michigan, referred to as the Michigan Facility. We operated the Michigan Facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. Separately, we leased the Michigan Facility, as lessor, to the State, as lessee, under a lease with an initial term of 20 years followed by two five-year options. In September 2005, the Governor of the State of Michigan closed the Michigan Facility and terminated the our management contract with the MDOC. In October 2005, the State of Michigan also sought to terminate its lease for the Michigan Facility. We believe that the State did not have the right to unilaterally terminate the Michigan Facility lease. As a result, in November 2005, we filed a lawsuit against the State to enforce our rights under the lease. On February 24, 2006, the Ingham County Circuit Court, the trial court with jurisdiction over the case, granted summary judgment in favor of the State and against us and granted us leave to amend the complaint. We filed an amended complaint and on September 13, 2006, the trial court granted summary judgment on the amended complaint in favor of the State and against us. We have filed a notice of appeal and

are proceeding with the appeal. We reviewed the Michigan Facility for impairment in accordance with FAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", and recorded an impairment charge in the fourth quarter of 2005 for \$20.9 million based on an independent appraisal of fair market value.

In June 2004, we received notice of a third-party claim for property damage incurred during 2002 and 2001 at several detention facilities that our Australian subsidiary formerly operated pursuant to its discontinued operation. The claim relates to property damage caused by detainees at the detention facilities. The notice was given by the Australian government's insurance provider and did not specify the amount of damages being sought. In May 2005, we received additional correspondence indicating that the insurance provider still intends to pursue the claim against our Australian subsidiary. Although the claim is in the initial stages and we are still in the process of fully evaluating its merits, we believe that we have defenses to the allegations underlying the claim and intend to vigorously defend our rights with respect to this matter. While the insurance provider has not quantified its damage claim and the outcome of this matter discussed above cannot be predicted with certainty, based on information known to date, and management's preliminary review of the claim, we believe that, if settled unfavorably, this matter could have a material adverse effect on our financial condition, results of operations and cash flows. We are uninsured for any damages or costs that it may incur as a result of this claim, including the expenses of defending the claim. We have accrued a reserve related to this claim based on our estimate of the most probable costs that may be incurred based on the facts and circumstances known to date, and the advice of our legal counsel.

The nature of the our business exposes us to various types of claims or litigation, including, but not limited to, civil rights claims relating to conditions of confinement and/or mistreatment, sexual misconduct claims brought by prisoners or detainees, medical malpractice claims, claims relating to employment matters (including, but not limited to, employment discrimination claims, union grievances and wage and hour claims), property loss claims, environmental claims, automobile liability claims, indemnification claims by our customers and other third parties, contractual claims and claims for personal injury or other damages resulting from contact with the our facilities, programs, personnel or prisoners, including damages arising from a prisoner's escape or from a disturbance or riot at a facility. Except as otherwise disclosed above, we do not expect the outcome of any pending claims or legal proceedings to have a material adverse effect on our financial condition, results of operations or cash flows.

**Item 4.      *Submission of Matters to a Vote of Security Holders***

No matters were submitted to a vote of our shareholders during the thirteen weeks ended December 31, 2006.

PART II

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Securities**

Our common stock trades on the New York Stock Exchange under the symbol "GEO." The following table shows the high and low prices for our common stock, as reported by the New York Stock Exchange, for each of the four quarters of fiscal years 2006 and 2005 and reflects the effect of the October 2, 2006 stock split. The prices shown have been rounded to the nearest \$1/100. The approximate number of shareholders of record as of February 23, 2007, was 130 which includes shares held in street name.

Quarter	2006		2005	
	High	Low	High	Low
First	\$ 22.23	\$ 14.74	\$ 21.47	\$ 17.07
Second	26.44	21.53	19.15	15.35
Third	30.68	21.92	19.30	16.77
Fourth	40.00	28.21	17.07	13.81

We did not pay any cash dividends on our common stock for fiscal years 2006 and 2005. We intend to retain our earnings to finance the growth and development of our business and do not anticipate paying cash dividends on our capital stock in the foreseeable future. Future dividends, if any, will depend, on our future earnings, our capital requirements, our financial condition and on such other factors as our Board of Directors may consider relevant. In addition, the indenture governing our \$150.0 million 8<sup>1</sup>/<sub>4</sub>% senior notes due in 2013, and our \$175.0 million senior credit facility also place material restrictions on our ability to pay dividends. See "Item 7. Management's Discussion and Analysis, Cash Flow and Liquidity" and "Item 8. Financial Statements — Note 10-Debt" for further description of these restrictions.

We did not buy back any of our common stock during 2006 and 2005. On August 10, 2006, our Board of Directors declared a 3-for-2 stock split of our common stock. The stock split took effect on October 2, 2006 with respect to stockholders of record on September 15, 2006. Following the stock split, our shares outstanding increased from 13.0 million to 19.5 million. All per share amounts have been retro-actively restated to reflect the 3-for-2 stock split.

**Equity Compensation Plan Information**

The following table sets forth information about our common stock that may be issued upon the exercise of options, warrants and rights under all of our equity compensation plans as of December 31, 2006, including our 1994 Second Stock Option Plan, our 1999 Stock Option Plan, our 2006 Stock Incentive Plan and our 1995 Non-Employee Director Stock Option Plan. Our shareholders have approved all of these plans.

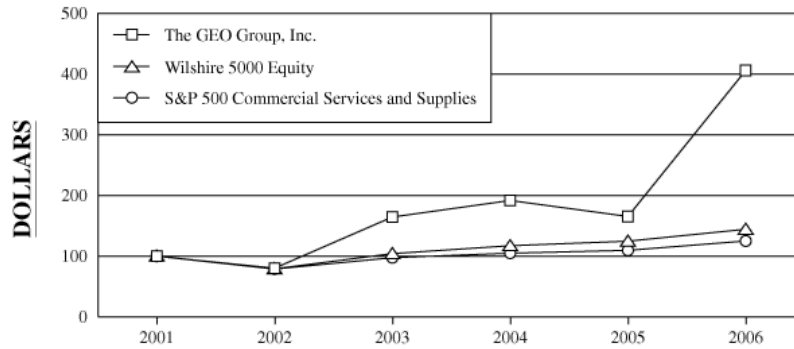
Plan Category	(a)	(b)	(c)
	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Equity compensation plans approved by security holders	1,538,819	\$ 9.22	225,300
Equity compensation plans not approved by security holders	—	—	—
<b>Total</b>	<b>1,538,819</b>	<b>\$ 9.22</b>	<b>225,300</b>



**Performance Graph**

The following performance graph compares the performance of our common stock to the New York Stock Exchange Composite Index and to an index of peer companies we selected, and is provided in accordance with Item 201(e) of Regulation S-K.

**Comparison of Five-Year Cumulative Total Return\*  
The GEO Group, Inc., Wilshire 500 Equity, and  
S&P 500 Commercial Services and Supplies Indexes  
(Performance through December 31, 2006)**



Date	The GEO Group, Inc.	Wilshire 500 Equity	S&P 500 Commercial Services and Supplies
December 31, 2001	\$100.00	\$100.00	\$100.00
December 31, 2002	\$ 80.16	\$ 79.14	\$ 78.81
December 31, 2003	\$164.50	\$104.19	\$ 97.45
December 31, 2004	\$191.77	\$117.20	\$104.95
December 31, 2005	\$165.44	\$124.69	\$109.59
December 31, 2006	\$406.06	\$144.36	\$125.04

Assumes \$100 invested on December 31, 2001 in The GEO Group, Inc. common stock and the Index companies.

\* Total return assumes reinvestment of dividends.

**Item 6. Selected Financial Data**

The selected consolidated financial data should be read in conjunction with our consolidated financial statements and the notes to the consolidated financial statements (in thousands, except per share data).

Fiscal Year Ended:(1)	2006		2005		2004		2003		2002	
<b>Results of Continuing Operations:</b>										
Revenues	\$ 860,882	100.0%	\$ 612,900	100.0%	\$ 593,994	100.0%	\$ 549,238	100.0%	\$ 501,982	100.0%
Operating income from continuing operations	64,201	7.5%	7,938	1.3%	38,991	6.6%	29,500	5.4%	23,195	4.6%
Income from continuing operations	<u>\$ 30,308</u>	<u>3.5%</u>	<u>\$ 5,879</u>	<u>1.0%</u>	<u>\$ 17,163</u>	<u>2.9%</u>	<u>\$ 36,375</u>	<u>6.6%</u>	<u>\$ 17,617</u>	<u>3.5%</u>
Income from continuing operations per common share:										
<b>Basic:</b>	<u>\$ 1.76</u>		<u>\$ 0.41</u>		<u>\$ 1.22</u>		<u>\$ 1.55</u>		<u>\$ 0.56</u>	
<b>Diluted:</b>	<u>\$ 1.70</u>		<u>\$ 0.39</u>		<u>\$ 1.17</u>		<u>\$ 1.53</u>		<u>\$ 0.55</u>	
<b>Weighted Average Shares Outstanding:</b>										
Basic	17,221		14,370		14,076		23,427		31,722	
Diluted	17,872		15,015		14,607		23,744		32,046	
<b>Financial Condition:</b>										
Current assets	\$ 322,754		\$ 229,292		\$ 222,766		\$ 191,811		\$ 142,839	
Current liabilities	173,703		136,519		117,478		118,704		79,360	
Total assets	743,453		639,511		480,326		505,341		405,378	
Long-term debt, including current portion (excluding non-recourse debt and capital leases)	154,259		220,004		198,204		245,086		125,000	
Shareholders' equity	<u>\$ 248,610</u>		<u>\$ 108,594</u>		<u>\$ 99,739</u>		<u>\$ 77,325</u>		<u>\$ 150,215</u>	
<b>Operational Data:</b>										
Contracts/awards	73		59		47		43		50	
Facilities in operation	62		56		41		38		50	
Design capacity of contracts	54,548		48,370		34,813		38,287		40,757	
Compensated resident days(2)	15,788,208		12,607,525		12,458,102		11,389,821		10,591,019	

- (1) Our fiscal year ends on the Sunday closest to the calendar year end. The fiscal year ended January 2, 2005 contained 53 weeks. Discontinued Operations have not been included with Selected Financial Data. Information related to Discontinued Operations is listed in "Item 8. Financial Statements — Note 3 Discontinued Operations."
- (2) Compensated resident days are calculated as follows: (a) for per diem rate facilities — the number of beds occupied by residents on a daily basis during the fiscal year; and (b) for fixed rate facilities — the design capacity of the facility multiplied by the number of days the facility was in operation during the fiscal year. Amounts exclude compensated resident days for United Kingdom for fiscal years 2002 to 2005.

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

**Introduction**

The following discussion and analysis provides information which management believes is relevant to an assessment and understanding of our consolidated results of operations and financial condition. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of numerous factors including, but not limited to, those described below under "Item 1A. Risk Factors," and Forward-Looking Statements. The discussion should be read in conjunction with the consolidated financial statements and notes thereto.

We are a leading provider of government-outsourced services specializing in the management of correctional, detention and mental health and residential treatment facilities in the United States, Australia, South Africa, the United Kingdom and Canada. We operate a broad range of correctional and detention facilities including maximum, medium and minimum security prisons, immigration detention centers, minimum security detention centers and mental health and residential treatment facilities. Our correctional and detention management services involve the provision of security, administrative, rehabilitation, education, health and food services, primarily at adult male correctional and detention facilities. Our mental health and residential treatment services involve the delivery of quality care, innovative programming and active patient treatment, primarily at privatized state mental health. We also develop new facilities based on contract awards, using our project development expertise and experience to design, construct and finance what we believe are state-of-the-art facilities that maximize security and efficiency.

Our business was founded in 1984 as a division of The Wackenhut Corporation, or TWC, a multinational provider of global security services. We were incorporated in 1988 as a wholly-owned subsidiary of TWC. In July 1994, we became a publicly-traded company. In 2002, TWC was acquired by Group 4 Falck A/S, which became our new parent company. In July 2003, we purchased all of our common stock owned by Group 4 Falck A/S and became an independent company. In November 2003, we changed our corporate name to "The GEO Group, Inc." We currently trade on the New York Stock Exchange under the ticker symbol "GEO."

As of December 31, 2006, we operated a total of 62 correctional, detention and mental health and residential treatment facilities and had over 54,000 beds under management or for which we had been awarded contracts. We maintained an average facility occupancy rate of 96.1% for the fiscal year ended December 31, 2006. For the fiscal year ended December 31, 2006, we had consolidated revenues of \$860.9 million and consolidated operating income of \$64.2 million.

#### **Recent Developments**

On September 20, 2006, we entered into an Agreement and Plan of Merger by and among us and CentraCore Properties Trust, which we refer to as CPT. On January 24, 2007, we completed the acquisition of CPT pursuant to the Agreement and Plan of Merger, dated as of September 19, 2006, referred to as the Merger Agreement, by and among us, GEO Acquisition II, Inc., a direct wholly-owned subsidiary of GEO, and CPT. Under the terms of the Merger Agreement, CPT merged with and into GEO Acquisition II, Inc., referred to as the Merger, with GEO Acquisition II, Inc., being the surviving corporation of the Merger.

As a result of the Merger, each share of common stock of CPT was converted into the right to receive \$32.5826 in cash, inclusive of a pro-rated dividend for all quarters or partial quarters for which CPT's dividend had not yet been paid as of the closing date. In addition, each outstanding option to purchase CPT common stock having an exercise price less than \$32.00 per share was converted into the right to receive the difference between \$32.00 per share and the exercise price per share of the option, multiplied by the total number of shares of CPT common stock subject to the option. We paid an aggregate purchase price of approximately \$427.6 million for the acquisition of CPT, inclusive of the payment of approximately \$367.6 million in exchange for the common stock and the options, the repayment of approximately \$40.0 million in CPT debt and the payment of approximately \$20.0 million in transaction related fees and expenses. We financed the acquisition through the use of \$365.0 million in new borrowings under a new Term Loan B and approximately \$62.6 million in cash on hand. As a result of the acquisition we will no longer have ongoing lease expense related to the properties we previously leased from CPT. However, we will have increased depreciation expense reflecting our ownership of the properties and higher interest expense as a result of borrowings used to fund the acquisition.

#### **RSI Acquisition**

On October 13, 2006, we acquired United Kingdom based Recruitment Solutions International (RSI) for approximately \$2.3 million plus transaction related expenses. RSI is a privately-held provider of transportation services to The Home Office Nationality and Immigration Directorate. The acquisition of RSI did not materially impact 2006 results of operations.

### **CSC Acquisition**

On November 4, 2005, we completed the acquisition of Correctional Services Corporation, or CSC, a Florida-based provider of privatized corrections/detention, community corrections and alternative sentencing services. The acquisition was completed through the merger of CSC into GEO Acquisition, Inc., a wholly owned subsidiary of GEO, referred to as the Merger. Under the terms of the Merger, we acquired 100% of the 10.2 million outstanding shares of CSC common stock for \$6.00 per share, or approximately \$62.1 million in cash. As a result of the Merger, we became responsible for supervising the operation of the 16 adult correctional/detention facilities, totaling 8,037 beds, formerly run by CSC. Immediately following the purchase of CSC, we sold Youth Services International, Inc., (YSI) the former juvenile services division of CSC, for \$3.75 million, \$1.75 million of which was paid in cash and the remaining \$2.0 million of which will be paid in the form of a promissory note accruing interest at a rate of 6% per annum. During 2006, in connection with the CSC acquisition and related sale of YSI, we received approximately \$2.0 million in additional sales proceeds, \$1.5 million in cash and \$0.5 million as additional promissory note, based on an unresolved matter relating to the closing balance sheet of YSI. This reduced goodwill by \$2.0 million. The financial information included in the discussion below for fiscal year 2005 reflects the operations of CSC from November 4, 2005 through January 1, 2006.

### **Recent Financings**

On January 24, 2007, we completed the refinancing of our Senior Credit Facility through the execution of the Amended Senior Credit Facility. The Amended Senior Credit Facility consists of a \$365 million 7-year term loan referred to as the Term Loan B and a \$150 million 5-year revolver, referred to as the Revolver. The initial interest rate for the Term Loan B is LIBOR plus 1.50% and the Revolver would bear interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, GEO used the \$365 million in borrowings under the Term Loan B to finance GEO's acquisition of CPT. See Item 7 Management's Discussion and Analysis, Financial Condition — Cash and Liquidity for further discussion of the Amended Senior Credit facility.

On June 12, 2006, we sold in a follow-on public offering 3,000,000 shares of our common stock at a price of \$35.46 per share (4,500,000 shares of its common stock at a price of \$23.64 reflecting the 3 for 2 stock split). All shares were issued from treasury. The aggregate net proceeds (after deducting underwriter's discounts and expenses) was approximately \$100 million. On June 13, 2006, we utilized approximately \$74.6 million of the proceeds to repay all outstanding debt under the term loan portion of our Senior Credit Facility. In addition, on August 11, 2006, we used \$4.0 million of the proceeds of the offering to purchase from certain directors, executive officers and employees stock options that were currently outstanding and exercisable, and which were due to expire within the next three years. The balance of the net proceeds was used for general corporate purposes including working capital, capital expenditures and the acquisition of CPT.

### **Stock Split**

On August 10, 2006, our board of directors declared a 3-for-2 stock split of our common stock. The stock split took effect on October 2, 2006 with respect to shareholders of record on September 15, 2006. Following the stock split, our shares outstanding increased from 13.0 million to 19.5 million.

### **Discontinued Operations**

Through our Australian subsidiary, we previously had a contract with the Department of Immigration, Multicultural and Indigenous Affairs, or DIMIA, for the management and operation of Australia's immigration centers. In 2003, the contract was not renewed, and effective February 29, 2004, we completed the transition of the contract and exited the management and operation of the DIMIA centers.

In early 2005, the New Zealand Parliament repealed the law that permitted private prison operation resulting in the termination of our contract for the management and operation of the Auckland Central Remand Prison or Auckland. We have operated this facility since July 2000. We ceased operating the facility upon the expiration of the contract on July 13, 2005.

On January 1, 2006, the last day of our 2005 fiscal year, we completed the sale of Atlantic Shores Hospital, a 72 bed private mental health hospital which we owned and operated since 1997 for approximately \$11.5 million. We recognized a gain on the sale of this transaction of approximately \$1.6 million or \$1.0 million net of tax.

The accompanying consolidated financial statements and notes reflect the operations of DIMIA, Auckland and Atlantic Shores Hospital as discontinued operations.

#### **Variable Interest Entities**

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities," which addressed consolidation by a business of variable interest entities in which it is the primary beneficiary. In December 2003, the FASB issued FIN No. 46R which replaced FIN No. 46. Our 50% owned South African joint venture in South African Custodial Services Pty. Limited, which we refer to as SACS, is a variable interest entity. We determined that we are not the primary beneficiary of SACS and as a result are not required to consolidate SACS under FIN 46R. We account for SACS as an equity affiliate. SACS was established in 2001, to design, finance and build the Kutama Sinthumule Correctional Center. Subsequently, SACS was awarded a 25 year contract to design, construct, manage and finance a facility in Louis Trichardt, South Africa. SACS, based on the terms of the contract with government, was able to obtain long term financing to build the prison. The financing is fully guaranteed by the government, except in the event of default, for which it provides an 80% guarantee. "See Item 7. Financial Condition — Guarantees" for a discussion of our guarantees related to SACS. Separately, SACS entered into a long term operating contract with South African Custodial Management (Pty) Limited, which we refer to as SACM, to provide security and other management services and with SACS's joint venture partner to provide purchasing, programs and maintenance services upon completion of the construction phase, which concluded in February 2002. Our maximum exposure for loss under this contract is \$15.6 million, which represents our initial investment and the guarantees discussed in Item 7. Management's Discussion and Analysis of Financial Condition.

In February 2004, CSC was awarded a contract by the Department of Homeland Security, Immigration and Customs Enforcement, or ICE, to develop and operate a 1,020 bed detention complex in Frio County, Texas. South Texas Local Development Corporation, referred to as STLDC, a non profit corporation, was created and issued \$49.5 million in taxable revenue bonds to finance the construction of the detention complex. Additionally, CSC provided a \$5 million subordinated note to STLDC for initial development costs. We determined that we are the primary beneficiary of STLDC and consolidate the entity as a result. STLDC is the owner of the complex and entered into a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require that the revenue from CSC's contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums, are distributed to CSC to cover CSC's operating expenses and management fee. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities resulting from its ownership. The bonds have a ten year term and are non-recourse to CSC and STLDC. The bonds are fully insured and the sole source of payment for the bonds is the operating revenues of the center.

#### **Shelf Registration Statement**

On January 28, 2004, our universal shelf registration statement on Form S-3 was declared effective by the Securities and Exchange Commission, which we refer to as the SEC. The universal shelf registration statement provides for the offer and sale by us, from time to time, on a delayed basis, of up to \$200.0 million aggregate amount of our common stock, preferred stock, debt securities, warrants, and/or depository shares. These securities, which may be offered in one or more offerings and in any combination, will in each case be offered pursuant to a separate prospectus supplement issued at the time of the particular offering that will describe the specific types, amounts, prices and terms of the offered securities. Unless otherwise described in the applicable prospectus supplement relating to the offered securities, we anticipate using the net proceeds of each offering

for general corporate purposes, including debt repayment, capital expenditures, acquisitions, business expansion, investments in subsidiaries or affiliates, and/or working capital.

On June 12, 2006 we completed a public offering of 4.5 million shares of our common stock for approximately \$110 million under the universal shelf registration statement. As a result, we have approximately \$90 million remaining for the offer and sale by us of certain of our securities including our debt securities.

#### **Rights Agreement**

On October 9, 2003, we entered into a rights agreement with EquiServe Trust Company, N.A., as rights agent. Under the terms of the rights agreement, each share of our common stock carries with it one preferred share purchase right. If the rights become exercisable pursuant to the rights agreement, each right entitles the registered holder to purchase from us one one-thousandth of a share of Series A Junior Participating Preferred Stock at a fixed price, subject to adjustment. Until a right is exercised, the holder of the right has no right to vote or receive dividends or any other rights as a shareholder as a result of holding the right. The rights trade automatically with shares of our common stock, and may only be exercised in connection with certain attempts to acquire our company. The rights are designed to protect the interests of our company and our shareholders against coercive acquisition tactics and encourage potential acquirers to negotiate with our board of directors before attempting an acquisition. The rights may, but are not intended to, deter acquisition proposals that may be in the interests of our shareholders.

#### **Critical Accounting Policies**

We believe that the accounting policies described below are critical to understanding our business, results of operations and financial condition because they involve the more significant judgments and estimates used in the preparation of our consolidated financial statements. We have discussed the development, selection and application of our critical accounting policies with the audit committee of our board of directors, and our audit committee has reviewed our disclosure relating to our critical accounting policies in this "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We routinely evaluate our estimates based on historical experience and on various other assumptions that our management believes are reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. If actual results significantly differ from our estimates, our financial condition and results of operations could be materially impacted.

Other significant accounting policies, primarily those with lower levels of uncertainty than those discussed below, are also critical to understanding our consolidated financial statements. The notes to our consolidated financial statements contain additional information related to our accounting policies and should be read in conjunction with this discussion.

#### ***Revenue Recognition***

We recognize revenue in accordance with Staff Accounting Bulletin, or SAB, No. 101, "Revenue Recognition in Financial Statements", as amended by SAB No. 104, "Revenue Recognition", and related interpretations. Facility management revenues are recognized as services are provided under facility management contracts with approved government appropriations based on a net rate per day per inmate or on a fixed monthly rate.

Project development and design revenues are recognized as earned on a percentage of completion basis measured by the percentage of costs incurred to date as compared to estimated total cost for each contract.

This method is used because we consider costs incurred to date to be the best available measure of progress on these contracts. Provisions for estimated losses on uncompleted contracts and changes to cost estimates are made in the period in which we determine that such losses and changes are probable. Typically, we enter into fixed price contracts and do not perform additional work unless approved change orders are in place. Costs attributable to unapproved change orders are expensed in the period in which the costs are incurred if we believe that it is not probable that the costs will be recovered through a change in the contract price. If we believe that it is probable that the costs will be recovered through a change in the contract price, costs related to unapproved change orders are expensed in the period in which they are incurred, and contract revenue is recognized to the extent of the cost incurred. Revenue in excess of the costs attributable to unapproved change orders is not recognized until the change order is approved. Contract costs include all direct material and labor costs and those indirect costs related to contract performance. Changes in job performance, job conditions, and estimated profitability, including those arising from contract penalty provisions, and final contract settlements, may result in revisions to estimated costs and income, and are recognized in the period in which the revisions are determined.

We extend credit to the governmental agencies we contract with and other parties in the normal course of business as a result of billing and receiving payment for services thirty to sixty days in arrears. Further, we regularly review outstanding receivables, and provide estimated losses through an allowance for doubtful accounts. In evaluating the level of established loss reserves, we make judgments regarding our customers' ability to make required payments, economic events and other factors. As the financial condition of these parties change, circumstances develop or additional information becomes available, adjustments to the allowance for doubtful accounts may be required. We also perform ongoing credit evaluations of our customers' financial condition and generally do not require collateral. We maintain reserves for potential credit losses, and such losses traditionally have been within our expectations.

#### **Reserves for Insurance Losses**

Claims for which we are insured arising from our U.S. operations that have an occurrence date of October 1, 2002 or earlier are handled by TWC and are commercially insured up to an aggregate limit of between \$25.0 million and \$50.0 million, depending on the nature of the claim and the applicable policy terms and conditions. With respect to claims for which we are insured arising after October 1, 2002, we maintain a general liability policy for all U.S. corrections operations with \$52.0 million per occurrence and in the aggregate. On October 1, 2004, we increased our deductible on this general liability policy from \$1.0 million to \$3.0 million for each claim which occurs after October 1, 2004. GEO Care, Inc. is separately insured for general and professional liability. Coverage is maintained with limits of \$10.0 million per occurrence and in the aggregate subject to a \$3.0 million self-insured retention. We also maintain insurance to cover property and casualty risks, workers' compensation, medical malpractice, environmental liability and automobile liability. Our Australian subsidiary is required to carry tail insurance on a general liability policy providing an extended reporting period through 2011 related to a discontinued contract. We also carry various types of insurance with respect to our operations in South Africa, the United Kingdom and Australia. There can be no assurance that our insurance coverage will be adequate to cover all claims to which we may be exposed.

Since our insurance policies generally have high deductible amounts (including a \$3.0 million per claim deductible under our general liability and auto liability policies and a \$2.0 million per claim deductible under our workers' compensation policy), losses are recorded as reported and a provision is made to cover losses incurred but not reported. Loss reserves are undiscounted and are computed based on independent actuarial studies. Our management uses judgments in assessing loss estimates based on actuarial studies, which include actual claim amounts and loss development based on both GEO's own historical experience and industry experience. If actual losses related to insurance claims significantly differ from our estimates, our financial condition and results of operations could be materially impacted.

Certain GEO facilities located in Florida and determined by insurers to be in high-risk hurricane areas carry substantial windstorm deductibles of up to \$3.0 million. Since hurricanes are considered unpredictable future events, no reserves have been established to pre-fund for potential windstorm damage. Limited

commercial availability of certain types of insurance relating to windstorm exposure in coastal areas and earthquake exposure mainly in California may prevent us from insuring our facilities to full replacement value.

***Income Taxes***

We account for income taxes in accordance with Financial Accounting Standards, or FAS, No. 109, "Accounting for Income Taxes." Under this method, deferred income taxes are determined based on the estimated future tax effects of differences between the financial statement and tax bases of assets and liabilities given the provisions of enacted tax laws. Deferred income tax provisions and benefits are based on changes to the assets or liabilities from year to year. Valuation allowances are recorded related to deferred tax assets based on the "more likely than not" criteria of FAS No. 109.

In providing for deferred taxes, we consider tax regulations of the jurisdictions in which we operate, and estimates of future taxable income and available tax planning strategies. If tax regulations, operating results or the ability to implement tax-planning strategies vary, adjustments to the carrying value of deferred tax assets and liabilities may be required.

***Property and Equipment***

As of December 31, 2006, we had approximately \$287.4 million in long-lived property and equipment. Property and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 2 to 40 years. Equipment and furniture and fixtures are depreciated over 3 to 10 years. Accelerated methods of depreciation are generally used for income tax purposes. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvement or the term of the lease. We perform ongoing evaluations of the estimated useful lives of our property and equipment for depreciation purposes. The estimated useful lives are determined and continually evaluated based on the period over which services are expected to be rendered by the asset. Maintenance and repairs are expensed as incurred.

We review long-lived assets to be held and used for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable in accordance with FAS No. 144 "Accounting for the Impairment of Disposal of Long-Lived Assets". Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell. Management has reviewed our long-lived assets and determined that there are no events requiring impairment loss recognition for the period ended December 31, 2006. Events that would trigger an impairment assessment include deterioration of profits for a business segment that has long-lived assets, or when other changes occur which might impair recovery of long-lived assets.

***Stock-Based Compensation Expense***

We account for stock-based compensation in accordance with the provisions of SFAS 123R. Under the fair value recognition provisions of FAS 123R, stock-based compensation cost is estimated at the grant date based on the fair value of the award and is recognized as expense ratably over the requisite service period of the award. Determining the appropriate fair value model and calculating the fair value of the stock-based awards, which includes estimates of stock price volatility, forfeiture rates and expected lives, requires judgment that could materially impact our operating results.

***Recent Accounting Pronouncements***

See Note 1 of the Consolidated Financial Statements for a description of certain other recent accounting pronouncements including the expected dates of adoption and effects on our results of operations and financial condition.



**Results of Operations**

The following discussion should be read in conjunction with our consolidated financial statements and the notes to the consolidated financial statements accompanying this report. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those described under "Item 1A. Risk Factors" and those included in other portions of this report.

As further discussed above, the discussion of our results of operations below excludes the results of our discontinued operations resulting from the termination of our management contract with DIMIA, Auckland, and Atlantic Shores Hospital for all periods presented.

For the purposes of the discussion below, "2006" means the 52 week fiscal year ended December 31, 2006, "2005" means the 52 week fiscal year ended January 1, 2006, and "2004" means the 53 week fiscal year ended January 2, 2005.

**Overview**

2006 versus 2005

**Revenues and Operating Expenses**

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
	(Dollars in thousands)					
<b>Revenue</b>						
<b>U.S. Corrections</b>	\$ 612,810	71.2%	\$ 473,280	77.3%	\$ 139,530	29.5%
<b>International Services</b>	\$ 103,553	12.0%	\$ 98,829	16.1%	\$ 4,724	4.8%
<b>GEO Care</b>	\$ 70,379	8.2%	\$ 32,616	5.3%	\$ 37,763	115.8%
<b>Other</b>	\$ 74,140	8.6%	\$ 8,175	1.3%	\$ 65,965	806.9%
<b>Total</b>	\$ 860,882	100.0%	\$ 612,900	100.0%	\$ 247,982	40.5%

**U.S. Corrections Services**

The increase in revenues for U.S. corrections facilities in 2006 compared to 2005 is primarily attributable to five items: (i) revenues increased \$104.5 million as a result of the acquisition of Correctional Services Corporation, referred to as CSC, in November 2005; (ii) revenues increased \$12.1 million in 2006 as a result of the New Castle Correctional Facility in New Castle, Indiana, which we began managing in January 2006; (iii) revenues increased approximately \$12.6 million in 2006 as a result of improved contractual terms at the San Diego facility; (iv) revenues decreased approximately \$13.8 million in 2006 as a result of the Michigan Correctional Facility contract termination in October 2005; and (v) revenues increased due to contractual adjustments for inflation, and improved terms negotiated into a number of contracts.

The number of compensated resident days in U.S. corrections facilities increased to 13.4 million in 2006 from 10.7 million in 2005 due to the additional capacity of the acquired CSC facilities of 2.0 million. We look at the average occupancy in our facilities to determine how we are managing our available beds. The average occupancy is calculated by taking compensated mandays as a percentage of capacity. The average occupancy in our U.S. corrections facilities was 96.0% of capacity in 2006 compared to 95.7% in 2005, excluding our vacant Michigan and Jena facilities.

**International Services**

Revenues for international services facilities remained consistent in 2006 compared to 2005. Revenues increased by \$4.7 million as a result of the June 2006 commencement of the Campsfield House contract in the United Kingdom. However, this increase was offset by the weakening of the Australian dollar and South African Rand, which resulted in a decrease of \$1.0 million and \$0.8 million, respectively, while lower

occupancy rates in Australia and South Africa accounted for a decrease in \$0.2 million and \$0.5 million, respectively for 2006.

The number of compensated resident days in international services facilities remained consistent at 2.0 million during 2006 and 2005. We look at the average occupancy in our facilities to determine how we are managing our available beds. The average occupancy is calculated by taking compensated mandays as a percentage of capacity. The average occupancy in our international service facilities was 98.1% of capacity in 2006 compared to 99.6% in 2005.

**GEO Care**

The increase in revenues for GEO Care in 2006 compared to 2005 is primarily attributable to four new contracts which commenced operation in 2006. In January 2006, the South Florida Evaluation & Treatment Center in Miami, Florida and the Fort Bayard Medical Center in Fort Bayard, New Mexico commenced operations increasing revenues by \$23.9 million and \$3.3 million, respectively. The Palm Beach County Jail in Palm Beach County, Florida commenced operations in May 2006 and increased revenues \$1.7 million. Annual revenues are expected to be approximately \$2.7 million. In July 2006, we commenced operations of the Florida Civil Commitment Center in Arcadia, Florida, which contributed revenues of \$8.3 million. Annual revenues are expected to be approximately \$20 million.

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
	(Dollars in thousands)					
<b>Operating Expenses</b>						
<b>U.S. Corrections</b>	\$ 485,583	56.4%	\$ 415,978	67.9%	\$ 69,605	16.7%
<b>International Services</b>	\$ 94,068	10.9%	\$ 85,634	14.0%	\$ 8,434	9.8%
<b>GEO Care</b>	\$ 63,799	7.4%	\$ 30,203	4.9%	\$ 33,596	111.2%
<b>Other</b>	\$ 74,728	8.7%	\$ 8,313	1.4%	\$ 66,415	798.9%
<b>Total</b>	\$ 718,178	83.4%	\$ 540,128	88.2%	\$ 178,050	33.0%

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health and GEO Care facilities. Expenses also include construction costs which are included in "Other".

**U.S. Corrections**

The increase in U.S. corrections operating expenses primarily reflects the acquisition of CSC (which increased operating expenses by \$71.1 million in fiscal 2006), the New Castle Correctional Facility, opened in January 2006, as well as general increases in labor costs and utilities. Operating expenses as a percentage of revenues decreased in 2006 compared to 2005 primarily as a result of \$20.9 million impairment charge related to the Michigan facility and a \$4.3 million charge related to the Jena lease.

Operating expenses in 2006 were favorably impacted by a \$4.0 million reduction in our reserves for general liability, auto liability, and workers compensation insurance. The \$4.0 million reduction in insurance reserves related to general liability, auto and workers compensation was the result of revised actuarial projections related to loss estimates for the initial four years of our insurance program which was established on October 2, 2002. Prior to October 2, 2002, our insurance coverage was provided through an insurance program established by TWC, our former parent company. We experienced significant adverse claims development in general liability and workers' compensation in the late 1990's. Beginning in approximately 1999, we made significant operational changes and began to aggressively manage our risk in a proactive manner. These changes have resulted in improved claims experience and loss development, which we are realizing in our actuarial projections. As a result of improving loss trends, our independent actuary reduced its expected losses for claims arising since October 2, 2002. We have adjusted our reserve at October 1, 2006 and October 2, 2005 to reflect the actuary's expected loss. Similarly, 2005 operating expenses were favorably impacted by a \$3.4 million reduction in our reserves for general liability, auto liability, and workers' compensation insurance. Fiscal year 2005 operating expense reflect an additional operating charge on the Jena

lease of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010. Fiscal year 2005 operating expenses were also effected by higher than anticipated employee health insurance costs of approximately \$1.7 million as well as start-up expenses of approximately \$0.8 million associated with transitioning customers at our Queens, New York Facility.

#### **International Services**

Operating expenses for international services facilities increased in 2006 compared to 2005 largely as a result of the June 2006 commencement of the Campsfield House contract in the United Kingdom. Australian operating expenses decreased slightly during 2006 due to a 2005 insurance reserve adjustment which increased expenses by approximately \$0.4 million in 2005. South African operating expenses remained consistent overall for 2006 and 2005.

International services segment operating expenses were impacted by reductions in the reserves related to the contract with DIMIA that was discontinued in February 2004. The company has exposure to general liability claims under the previous contract for seven years following the discontinuation of the contract. The Company reduced its reserves for this exposure \$0.5 million and \$0.9 million in the second quarter 2006 and second quarter 2005, respectively. The remaining reserve balance at December 31, 2006 is approximately \$1.2 million and approximately 4 years remain until the tail period expires.

#### **GEO Care**

Operating expenses for GEO Care increased approximately \$33.6 million during 2006 from 2005 primarily due to the activation of the new contracts discussed above.

#### **Other Revenue and Operating Expense**

"Other" primarily consists of revenues and related operating expenses associated with our construction business. There was an increase in revenue in our construction business of approximately \$66.0 million in 2006 as compared to 2005. The construction revenue is related to our expansion of the Moore Haven Facility, which we currently manage, and the new construction of the Graceville Facility, which we will manage upon completion in the third quarter of 2007. Furthermore, operating expenses relating to the construction of both the Graceville Facility and Moore Haven Facility were approximately \$50.4 and \$11.9 million, respectively. Offsetting this increase was the completion of the expansion of South Bay at the end of the third quarter of 2005, which represented \$7.1 million of construction revenue in 2005.

#### **Other Unallocated Operating Expenses**

##### **General and Administrative Expenses**

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
	(Dollars in thousands)					
<b>General and Administrative Expenses</b>	\$ 56,268	6.5%	\$ 48,958	8.0%	\$ 7,310	14.9%

General and administrative expenses consist primarily of corporate management salaries and benefits, professional fees and other administrative expenses. General and administrative expenses increased by \$7.3 million in 2006 compared to 2005, however decreased slightly as a percentage of revenues due to the overall increase in revenue during 2006. The increase in general and administrative costs is mainly due to increases in direct labor costs and related taxes of approximately \$4.8 million as a result of increased headcount of administrative staff and higher estimated annual bonus payments under the Company's incentive compensation plans due to an increase in earnings. Amortization of deferred compensation and expense related to stock options increased general and administrative expenses \$1.4 million. Administrative costs as well as general increases in travel expense increased approximately \$1.7 million.

**Non Operating Expenses**

**Interest Income and Interest Expense**

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>Interest Income</b>	\$ 10,687	1.2%	\$ 9,154	1.5%	\$ 1,533	16.8%
<b>Interest Expense</b>	\$ 28,231	3.3%	\$ 23,016	3.8%	\$ 5,215	22.7%

The increase in interest income is primarily due to higher average invested cash balances.

The increase in interest expense is primarily attributable to the increase in our debt as a result of the CSC acquisition, as well as the increase in LIBOR rates.

**Provision for Income Taxes**

	<u>2006</u>	<u>Effective Rate</u>	<u>2005</u>	<u>Effective Rate</u>
		(Dollars in thousands)		
<b>Income Taxes</b>	\$ 16,505	36.4%	\$ (11,826)	N/A

Income taxes for 2006 include certain one time items of \$0.7 million resulting in an effective tax rate of 36.4%. Without such items the rate would have been approximately 38%.

Income taxes for 2005 reflect a benefit as a result of the loss before income taxes which primarily resulted from the \$20.9 million impairment charge for the Michigan Facility and the \$4.3 million charge to record the remaining lease obligation for the Jena lease with CPT. The income tax benefit for 2005 reflects a benefit of \$6.5 million in the fourth quarter 2005 related to a step up in tax basis for an asset in Australia which resulted in a decreased deferred tax liability. The income tax benefit for 2005 also reflects a benefit of \$1.7 million in the second quarter 2005 related to the American Jobs Creation Act of 2004, or the AJCA. A key provision of the AJCA creates a temporary incentive for U.S. corporations to repatriate undistributed income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations.

**Minority Interest**

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>Minority Interest</b>	\$ (125)	(0.0)%	\$ (742)	(0.1)%	\$ 617	(83.2)%

Decrease in minority interest reflects reduced performance during 2006 as a result of lower revenues during the first and second quarter of 2006 related to facility modifications which resulted in reduced capacity and related billings.

**Equity in Earnings of Affiliate**

	<u>2006</u>	<u>% of Revenue</u>	<u>2005</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>Equity in Earnings of Affiliate</b>	\$ 1,576	0.2%	\$ 2,079	0.3%	\$ (503)	(24.2)%

Equity in earnings of affiliates in 2006 reflects the normal operations of South African Custodial Services Pty. Limited ("SACS").

Equity in earnings of affiliate in 2005 reflects a one time tax benefit of \$2.1 million related to a change in South African tax law.

In 2005, our equity affiliate, SACS, recognized a one time tax benefit of \$2.1 million related to a change in South African Tax law applicable to companies in a qualified Public Private Partnership ("PPP") with the South African Government. The tax law change has the effect that beginning in 2005 government revenues earned under the PPP are exempt from South African taxation. The one time tax benefit in part related to

deferred tax liabilities that were eliminated during 2005 as a result of the change in the tax law. In February 2007 the South African legislature passed legislation that has the effect of removing the exemption from taxation on government revenue. The law change will impact the equity in earnings of affiliate beginning in 2007. The Company is in the process of fully assessing the impact of the new legislation. However, as a result of the new legislation, deferred tax liabilities will have to be established at the applicable tax rate of 29%. This is estimated to result in a one time tax charge of up to \$2.3 million in the first quarter of 2007.

**2005 versus 2004**

*Revenues and Operating Expenses*

	<u>2005</u>	<u>% of Revenue</u>	<u>2004</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
	(Dollars in thousands)					
<b>Revenue</b>						
<b>U.S. Corrections</b>	\$ 473,280	77.3%	\$ 455,947	76.8%	\$ 17,333	3.8%
<b>International Services</b>	\$ 98,829	16.1%	\$ 91,005	15.3%	\$ 7,824	8.6%
<b>GEO Care</b>	\$ 32,616	5.3%	\$ 31,704	5.3%	\$ 912	2.9%
<b>Other</b>	\$ 8,175	1.3%	\$ 15,338	2.6%	\$ (7,163)	(46.7)%
<b>Total</b>	\$ 612,900	100.0%	\$ 593,994	100.0%	\$ 18,906	3.2%

*U.S. Corrections*

The increase in revenues for U.S. corrections facilities in 2005 compared to 2004 is primarily attributable to four items: (i) the acquisition of CSC in November 2005 increased revenues \$17.3 million; (ii) the McFarland facility was idle for all of 2004 and was re-opened in January 2005 resulting in an increase in revenues of approximately \$3.1 million; (iii) domestic revenues also increased due to contractual adjustments for inflation, slightly higher occupancy rates and improved terms negotiated into a number of contracts. These increases offset a decrease in revenues due to the transition of the Queens contract from ICE to USMS, the closure of the Michigan Correctional Facility on October 14, 2005, the expiration of our operating contract for the Kyle Facility on August 31, 2005, and lower populations in our Val Verde, and San Diego Facilities; and revenues decreased in 2005 because it contained 52 weeks compared to 2004, which contained 53 weeks.

The number of compensated resident days in U.S. corrections facilities increased to 10.7 million in 2005 from 10.5 million in 2004. We look at the average occupancy in our facilities to determine how we are managing our available beds. The average occupancy is calculated by taking compensated mandays as a percentage of capacity. The average occupancy in our U.S. corrections facilities was 97.5% of capacity in 2005 compared to 99.3% in 2004. The decrease in the average occupancy is due to an increase in the number of beds made available to us under our contracts and lower populations in our Val Verde and San Diego facilities.

*International Services*

Revenues for international services facilities in 2005 compared to 2004 increased approximately \$7.8 million, \$2.6 million and \$0.2 million of which was due to the strengthening of the Australian dollar and South African Rand, respectively, and \$5.0 million of which was due to higher occupancy rates and contractual adjustments for inflation.

The number of compensated resident days in international services facilities remained consistent at 2.0 million during 2005 and 2004. We look at the average occupancy in our facilities to determine how we are managing our available beds. The average occupancy is calculated by taking compensated mandays as a percentage of capacity. The average occupancy in our international services facilities was 99.6% of capacity in 2005 compared to 100.0% in 2004, excluding the Auckland facility.

*GEO Care*

The revenues for GEO Care in 2005 compared to 2004 remained consistent at \$30 million. The revenues in 2005 and 2004 primarily reflect the operations of a single facility.

	<u>2005</u>	<u>% of Revenue</u>	<u>2004</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
	(Dollars in thousands)					
<b>Operating Expenses</b>						
<b>U.S. Corrections</b>	\$ 415,978	67.9%	\$ 375,590	63.2%	\$ 40,388	10.8%
<b>International Services</b>	\$ 85,634	14.0%	\$ 75,043	12.6%	\$ 10,591	14.1%
<b>GEO Care</b>	\$ 30,203	4.9%	\$ 29,567	5.0%	\$ 636	2.2%
<b>Other</b>	\$ 8,313	1.4%	\$ 15,026	2.5%	\$ (6,713)	(44.7)%
<b>Total</b>	\$ 540,128	88.2%	\$ 495,226	83.3%	\$ 44,902	9.1%

*U.S. Corrections*

U.S. corrections operating expenses for fiscal year 2005 reflect an impairment charge of \$20.9 million for the Michigan Correctional Facility. We own the 480-bed Michigan Correctional Facility and operated the facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. On September 30, 2005, the Governor of the State of Michigan announced her decision to close the facility and as a result our management contract with the MDOC was terminated. Additionally, 2005 operating expenses reflect an operating charge on the Jena lease of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010.

Operating expenses in 2005 were favorably impacted by a \$3.4 million reduction in our reserves for general liability, auto liability, and workers' compensation insurance. This favorable reduction was largely offset by higher than anticipated U.S. employee health insurance costs of approximately \$1.7 million, transition expenses of approximately \$0.8 million associated with our Queens, New York Facility, and start-up expenses at certain domestic facilities of approximately \$0.6 million.

The \$3.4 million reduction in insurance reserves was the result of revised actuarial projections related to loss estimates for the initial three years of our insurance program which was established on October 2, 2002. Prior to October 2, 2002, our insurance coverage was provided through an insurance program established by TWC, our former parent company. We experienced significant adverse claims development in general liability and workers' compensation in the late 1990's. Beginning in approximately 1999, we made significant operational changes and began to aggressively manage our risk in a proactive manner. These changes have resulted in improved claims experience and loss development, which we are realizing in our actuarial projections. As a result of improving loss trends, our independent actuary reduced its expected losses for claims arising since October 2, 2002. We adjusted our reserves in the third quarter of 2005 to reflect the actuary's improved expected loss projections. There can be no assurance that our improved claims experience and loss developments will continue. Similarly, 2004 operating expenses reflect a \$4.2 million reduction in insurance reserves also attributable to improved actuarial loss projections.

During 2005, we experienced an adverse development in our employee health program. Since we are self-insured for employee healthcare, this adverse development resulted in additional claims expense and increased reserve requirements. During the third quarter of 2005, we completed a review of our employee health program and made adjustments to the plan to reduce future costs. The revised plan was effective November 1, 2005. There can be no assurance that these modifications will improve our claims experience.

Operating expenses in 2004 reflect an additional provision for operating losses of approximately \$3.0 million related to our inactive facility in Jena, Louisiana.

The remaining increase in operating expenses is consistent with and proportional to the increase in revenues discussed above as a result of the CSC acquisition, the start-up of new facilities and the expansion of existing facilities.

*International Services*

Operating expenses for international services facilities increased in 2005 compared to 2004 as a result of the strengthening of the Australian dollar and South African Rand. Australian operating expenses increased slightly during 2005 due to a 2005 insurance reserve adjustment which increased expenses by approximately \$0.4 million in 2005. South African operating expenses remained consistent overall for 2005 and 2004.

International services segment operating expenses were impacted by reductions in the reserves related to the contract with DIMIA discontinued in February 2004. The company has exposure to general liability claims under the previous contract for seven years following the discontinuation of the contract. The Company reduced its reserves for this exposure \$0.9 million and \$0.9 million in the second quarter 2005 and second quarter 2004, respectively.

*GEO Care*

The operating expenses for GEO Care in 2005 compared to 2004 remained consistent and primarily reflect the operations of a single facility.

**Other Revenue and Operating Expense**

“Other” primarily consists of revenues and related operating expenses associated with our construction business. The decrease in 2005 primarily relates to approximately \$7.2 million less construction revenue as compared to 2004. The construction revenue is related to our expansion of the South Bay Facility, one of the facilities that we manage. The expansion was completed at the end of the second quarter of 2005.

**Other Unallocated Operating Expenses**

*General and Administrative Expenses*

	<u>2005</u>	<u>% of Revenue</u>	<u>2004</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>General and Administrative Expenses</b>	\$ 48,958	8.0%	\$ 45,879	7.7%	\$ 3,079	6.7%

General and administrative expenses consist primarily of corporate management salaries and benefits, professional fees and other administrative expenses. The increase in expense reflects increased personnel and business development costs associated with the expansion of our mental health business. The increase also reflects costs associated with compliance with Sarbanes-Oxley requirements for management’s assessment over internal controls, which resulted in an increase in professional fees in 2005 of \$0.9 million. The remaining increase in general and administrative costs relates to other increases in professional fees, travel, expenses associated with our acquisition program and rent expense for our corporate offices.

**Non Operating Expenses**

*Interest Income and Interest Expense*

	<u>2005</u>	<u>% of Revenue</u>	<u>2004</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>Interest Income</b>	\$ 9,154	1.5%	\$ 9,568	1.6%	\$ (414)	(4.3)%
<b>Interest Expense</b>	\$ 23,016	3.8%	\$ 22,138	3.7%	\$ 878	4.0%

The decrease in interest income is primarily due to lower average invested cash balances. Interest income for 2005 and 2004 reflects income from interest rate swap agreements entered into September 2003 for our domestic operations, which increased interest income. The interest rate swap agreements in the aggregate notional amounts of \$50.0 million are hedges against the change in the fair value of a designated portion of the Notes due to changes in the underlying interest rates. The interest rate swap agreements have payment and expiration dates and call provisions that coincide with the terms of the Notes.

The increase in interest expense is primarily attributable to the refinancing of the term loan portion of our Senior Credit Facility.

**Costs Associated with Debt Refinancing**

Deferred financing fees of \$1.4 million were written off in 2005 in connection with the refinancing of the term loan portion of the Senior Credit Facility. In 2004, \$0.3 million was written off in connection with the \$43.0 million payment related to the term loan portion of the Senior Credit Facility.

**Provision for Income Taxes**

	<u>2005</u>	<u>Effective Rate</u>	<u>2004</u>	<u>Effective Rate</u>
		(Dollars in thousands)		
<b>Income Taxes</b>	\$ (11,826)	N/A	\$ 8,231	31.5%

Income taxes for 2005 reflect a benefit as a result of the loss before income taxes which primarily resulted from the \$20.9 million impairment charge for the Michigan Facility and the \$4.3 million charge to record the remaining lease obligation for the Jena lease with CPT.

The income tax benefit for 2005 reflects a benefit of \$6.5 million in the fourth quarter 2005 related to a step up in tax basis for an asset in Australia which resulted in a decreased deferred tax liability.

The income tax benefit for 2005 also reflects a benefit of \$1.7 million in the second quarter 2005 related to the American Jobs Creation Act of 2004, or the AJCA. A key provision of the AJCA creates a temporary incentive for U.S. corporations to repatriate undistributed income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations.

**Equity in Earnings of Affiliate**

	<u>2005</u>	<u>% of Revenue</u>	<u>2004</u>	<u>% of Revenue</u>	<u>\$ Change</u>	<u>% Change</u>
			(Dollars in thousands)			
<b>Equity in Earnings of Affiliate</b>	\$ 2,079	0.3%	\$ —	0.0%	\$ 2,079	100.0%

Equity in earnings of affiliate in 2005 reflects a one time tax benefit of \$2.1 million related to a change in South African tax law.

**Financial Condition**

*Liquidity and Capital Resources*

On January 24, 2007, we completed the refinancing of our Senior Credit Facility through the execution of the Amended Senior Credit Facility, by and among GEO, as Borrower, BNP Paribas, as Administrative Agent, BNP Paribas Securities Corp, as Lead Arranger and Syndication Agent, and the lenders who are, or may from time to time become, a party thereto. The Amended Senior Credit Facility consists of a \$365 million 7-year term loan referred to as the Term Loan B and a \$150 million 5-year revolver, expiring September 14, 2010, referred to as the Revolver. The initial interest rate for the Term Loan B is LIBOR plus 1.50%. The Revolver would bear interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, GEO used the \$365 million in borrowings under the Term Loan B to finance GEO's acquisition of CPT.

Current cash requirements consist of amounts needed for working capital, debt service, capital expenditures, supply purchases and investments in joint ventures. Our primary source of liquidity to meet these requirements is cash flow from operations and, after January 24, 2007, borrowings from the \$150 million Revolver under our Amended Senior Credit Facility. As of December 31, 2006, we had \$45.5 million available for borrowing under the revolving portion of the Senior Credit Facility.

We incurred substantial indebtedness in connection with the acquisition CPT on January 24, 2007, CSC on November 4, 2005 and the share purchase in 2003. As of December 31, 2006, we had \$150.0 million of consolidated debt outstanding, excluding \$147.3 million of non-recourse debt. As of December 31, 2006, we also had outstanding seven letters of guarantee totaling approximately \$6.1 million under separate international



credit facilities. As a result of the refinancing of our Senior Credit Facility we have \$515 million consolidated debt outstanding, excluding non-recourse debt. After giving effect to these borrowings, we currently have approximately \$515 million in total consolidated long-term indebtedness, excluding non recourse debt of \$131.7 million and capital lease liability balances of \$16.6 million. Based on our debt covenants and the amount of indebtedness we have outstanding, we currently have the ability to borrow an additional approximately \$55 million under our Amended Senior Credit Facility. Our significant debt service obligations could have material consequences. See "Risk Factors — Risks Related to Our High Level of Indebtedness." However, our management believes that cash on hand, cash flows from operations and our Senior Credit Facility will be adequate to support currently planned business expansion and various obligations incurred in the operation of our business, both on a near and long-term basis.

In the future, our access to capital and ability to compete for future capital-intensive projects will be dependent upon, among other things, our ability to meet certain financial covenants in the indenture governing the Notes and in our Senior Credit Facility. A substantial decline in our financial performance could limit our access to capital and have a material adverse effect on our liquidity and capital resources and, as a result, on our financial condition and results of operations.

Our business requires us to make various capital expenditures from time to time, including expenditures related to the development of new correctional, detention and/or mental health facilities. In addition, some of our management contracts require us to make substantial initial expenditures of cash in connection with opening or renovating a facility. Generally, these initial expenditures are subsequently fully or partially recoverable as pass-through costs or are billable as a component of the per diem rates or monthly fixed fees to the contracting agency over the original term of the contract. However, we cannot assure you that any of these expenditures will, if made, be recovered. Based on current estimates of our capital needs, we anticipate that our capital expenditures will range from \$50 million to \$150 million during the next 12 months. We are in the process of a 576 bed expansion of Val Verde Correctional Facility in Del Rio, Texas for approximately \$20 million. The expansion is expected to be completed in the third quarter of 2007. Additionally, as a result of the acquisition of CPT, we will fund an expansion of Delaney Hall, a facility which we do not operate, for approximately \$10 million, with expected completion in the first quarter 2008. Capital expenditures related to other facility expansions and normal operating activities are expected to range between \$20 million and \$40 million. Our range of \$50 million to \$150 million for capital needs includes potential capital expenditures related to expansion of existing facilities if we receive new contracts or contract modifications. We plan to fund these capital expenditures from cash from operations, borrowings under the Amended Senior Credit Facility or other financings.

We have entered into individual executive retirement agreements with our CEO and Chairman, President and Vice Chairman, and Chief Financial Officer. These agreements provide each executive with a lump sum payment upon retirement. Under the agreements, each executive may retire at any time after reaching the age of 55. Each of the executives reached the eligible retirement age of 55 in 2005. None of the executives have indicated their intent to retire as of this time. However, under the retirement agreements, retirement may be taken at any time at the individual executive's discretion. In the event that all three executives were to retire in the same year, we believe we will have funds available to pay the retirement obligations from various sources, including cash on hand, operating cash flows or borrowings under our revolving credit facility. Based on our current capitalization, we do not believe that making these payments in any one period, whether in separate installments or in the aggregate, would materially adversely impact our liquidity.

We are exposed to various commitments and contingencies which may have a material adverse effect on our financial condition and results of operations. See Item 3. Legal Proceedings.

#### ***The Amended Senior Credit Facility***

On January 24, 2007, we completed the Amended Senior Credit Facility and used the \$365 million in borrowings under the Term Loan B to finance the acquisition of CPT. GEO has no current borrowings under the Revolver and intends to use future borrowings thereunder for the purposes permitted under the Amended senior Credit Facility, including to fund general corporate purposes.

All of the obligations under the Amended Senior Credit Facility are unconditionally guaranteed by each of GEO's existing material domestic subsidiaries. The Amended Senior Credit Facility and the related guarantees are secured by substantially all of GEO's present and future tangible and intangible assets and all present and future tangible and intangible assets of each guarantor, including but not limited to (i) a first-priority pledge of all of the outstanding capital stock owned by GEO and each guarantor, and (ii) perfected first-priority security interests in all of GEO's present and future tangible and intangible assets and the present and future tangible and intangible assets of each guarantor.

Indebtedness under the Revolver bears interest in each of the instances below at the stated rate:

	<b>Interest Rate under the Revolver</b>
Borrowings	LIBOR plus 2.25% or base rate plus 1.25%.
Letters of Credit	1.50% to 2.50%.
Available Borrowings	0.38% to 0.5%.

The Amended Senior Credit Facility contains financial covenants which require us to maintain the following ratios, as computed at the end of each fiscal quarter for the immediately preceding four quarter-period:

<b>Period</b>	<b>Leverage Ratio</b>
Through December 30, 2008	Total leverage ratio £ 5.50 to 1.00
From December 31, 2008 through December 31, 2011	Reduces from 4.75 to 1.00, to 3.00 to 1.00
Through December 30, 2008	Senior secured leverage ratio £ 4.00 to 1.00
From December 31, 2008 through December 31, 2011	Reduces from 3.25 to 1.00, to 2.00 to 1.00
Four quarters ending June 29, 2008, to December 30, 2009	Fixed charge coverage ratio of 1.00, thereafter increases to 1.10 to 1.00

In addition, the Amended Senior Credit Facility prohibits us from making capital expenditures greater than \$55.0 million in the aggregate during fiscal year 2007 and \$25.0 million during each of the fiscal years thereafter, provided that to the extent that our capital expenditures during any fiscal year are less than the limit, such amount will be added to the maximum amount of capital expenditures that we can make in the following year. In addition, certain capital expenditures, including those made with the proceeds of any future equity offerings, are not subject to numerical limitations.

The Amended Senior Credit Facility contains certain customary representations and warranties, and certain customary covenants that restrict GEO's ability to, among other things (i) create, incur or assume any indebtedness, (ii) incur liens, (iii) make loans and investments, (iv) engage in mergers, acquisitions and asset sales, (v) sell its assets, (vi) make certain restricted payments, including declaring any cash dividends or redeem or repurchase capital stock, except as otherwise permitted, (vii) issue, sell or otherwise dispose of capital stock, (viii) transact with affiliates, (ix) make changes in accounting treatment, (x) amend or modify the terms of any subordinated indebtedness, (xi) enter into debt agreements that contain negative pledges on its assets or covenants more restrictive than contained in the Amended Senior Credit Facility, (xii) alter the business GEO conducts, and (xiii) materially impair GEO's lenders' security interests in the collateral for its loans.

Events of default under the Amended Senior Credit Facility include, but are not limited to, (i) GEO's failure to pay principal or interest when due, (ii) GEO's material breach of any representations or warranty, (iii) covenant defaults, (iv) bankruptcy, (v) cross default to certain other indebtedness, (vi) unsatisfied final judgments over a specified threshold, (vii) material environmental claims which are asserted against GEO, and (viii) a change of control.

The covenants governing our Amended Senior Credit Facility, including the covenants described above, impose significant operating and financial restrictions which may substantially restrict, and materially adversely affect, our ability to operate our business.

See “Risk Factors — Risks Related to Our High Level of Indebtedness — The covenants in the indenture governing the Notes and our Senior Credit Facility impose significant operating and financial restrictions which may adversely affect our ability to operate our business.”

**Senior 8<sup>1</sup>/<sub>4</sub>% Notes**

To facilitate the completion of the purchase of the 12 million shares from Group 4 Falck, we issued \$150.0 million aggregate principal amount, ten-year, 8<sup>1</sup>/<sub>4</sub>% senior unsecured notes, which we refer to as the Notes. The Notes are general, unsecured, senior obligations of ours. Interest is payable semi-annually on January 15 and July 15 at 8<sup>1</sup>/<sub>4</sub>%. The Notes are governed by the terms of an Indenture, dated July 9, 2003, between us and the Bank of New York, as trustee, referred to as the Indenture. Additionally, after July 15, 2008, we may redeem, at our option, all or a portion of the Notes plus accrued and unpaid interest at various redemption prices ranging from 104.125% to 100.000% of the principal amount to be redeemed, depending on when the redemption occurs. The Indenture contains certain covenants that limit our ability to incur additional indebtedness, pay dividends or distributions on our common stock, repurchase our common stock, and prepay subordinated indebtedness. The Indenture also limits our ability to issue preferred stock, make certain types of investments, merge or consolidate with another company, guarantee other indebtedness, create liens and transfer and sell assets.

The covenants governing the Notes impose significant operating and financial restrictions which may substantially restrict and adversely affect our ability to operate our business. See “Risk Factors — Risks Related to Our High Level of Indebtedness — The covenants in the indenture governing the Notes and our Senior Credit Facility impose significant operating and financial restrictions which may adversely affect our ability to operate our business.” We are in compliance with all of the covenants of the Indenture governing the Notes as of December 31, 2006.

**Non-Recourse Debt**

**South Texas Detention Complex:**

In February 2004, CSC was awarded a contract by ICE to develop and operate a 1,020 bed detention complex in Frio County Texas. STLDC was created and issued \$49.5 million in taxable revenue bonds to finance the construction of the detention center. Additionally, CSC provided a \$5 million subordinated note to STLDC for initial development. We determined that we are the primary beneficiary of STLDC and consolidate the entity as a result. STLDC is the owner of the complex and entered into a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require the revenue from CSC’s contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums are distributed to CSC to cover CSC’s operating expenses and management fee. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities for the operation of the facility resulting from its ownership. The bonds have a ten year term and are non-recourse to CSC and STLDC. The bonds are fully insured and the sole source of payment for the bonds is the operating revenues of the center.

Included in current and non-current restricted cash is \$18.6 million as of December 31, 2006 as funds held in trust with respect to the STLDC for debt service and other reserves.

**Northwest Detention Center**

On June 30, 2003 CSC arranged financing for the construction of the Northwest Detention Center in Tacoma, Washington (the “Northwest Detention Center”), which CSC completed and opened for operation in April 2004. In connection with this financing, CSC of Tacoma LLC, a wholly owned subsidiary of CSC, issued a \$57 million note payable to the Washington Economic Development Finance Authority (“WEDFA”), an instrumentality of the State of Washington, which issued revenue bonds and subsequently loaned the

proceeds of the bond issuance to CSC of Tacoma LLC for the purposes of constructing the Northwest Detention Center. The bonds are non-recourse to CSC and the loan from WEDFA to CSC of Tacoma, LLC is non-recourse to CSC. The proceeds of the loan were disbursed into escrow accounts held in trust to be used to pay the issuance costs for the revenue bonds, to construct the Northwest Detention Center and to establish debt service and other reserves.

Included in current and non-current restricted cash is \$11.1 million as of December 31, 2006 as funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.

#### ***Australia***

In connection with the financing and management of one Australian facility, our wholly owned Australian subsidiary financed the facility's development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to us. As a condition of the loan, we are required to maintain a restricted cash balance of AUD 5.0 million, which, at December 31, 2006, was approximately \$3.9 million. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria.

#### ***Guarantees***

In connection with the creation of SACS, we entered into certain guarantees related to the financing, construction and operation of the prison. We guaranteed certain obligations of SACS under its debt agreements up to a maximum amount of 60.0 million South African Rand, or approximately \$8.6 million, to SACS' senior lenders through the issuance of letters of credit. Additionally, SACS is required to fund a restricted account for the payment of certain costs in the event of contract termination. We have guaranteed the payment of 50% of amounts which may be payable by SACS into the restricted account and provided a standby letter of credit of 7.0 million South African Rand, or approximately \$1.0 million, as security for our guarantee. Our obligations under this guarantee expire upon the release from SACS of its obligations in respect of the restricted account under its debt agreements. No amounts have been drawn against these letters of credit, which are included in our outstanding letters of credit under the revolving loan portion of our Senior Credit Facility.

We have agreed to provide a loan, if necessary, of up to 20.0 million South African Rand, or approximately \$2.9 million, referred to as the Standby Facility, to SACS for the purpose of financing the obligations under the contract between SACS and the South African government. No amounts have been funded under the Standby Facility, and we do not currently anticipate that such funding will be required by SACS in the future. Our obligations under the Standby Facility expire upon the earlier of full funding or release from SACS of its obligations under its debt agreements. The lenders' ability to draw on the Standby Facility is limited to certain circumstances, including termination of the contract.

We have also guaranteed certain obligations of SACS to the security trustee for SACS lenders. We have secured our guarantee to the security trustee by ceding our rights to claims against SACS in respect of any loans or other finance agreements, and by pledging our shares in SACS. Our liability under the guarantee is limited to the cession and pledge of shares. The guarantee expires upon expiration of the cession and pledge agreements.

In connection with a design, build, finance and maintenance contract for a facility in Canada, we guaranteed certain potential tax obligations of a not-for-profit entity. The potential estimated exposure of these obligations is CAD 2.5 million, or approximately \$2.2 million commencing in 2017. We have a liability of \$0.7 million and \$0.6 million related to this exposure as of December 31, 2006 and January 1, 2006, respectively. To secure this guarantee, we purchased Canadian dollar denominated securities with maturities matched to the estimated tax obligations in 2017 to 2021. We have recorded an asset and a liability equal to the current fair market value of those securities on our balance sheet. We do not currently operate or manage this facility

At December 31, 2006, we also had outstanding seven letters of guarantee totaling approximately \$6.1 million under separate international facilities. We do not have any off balance sheet arrangements.

**Derivatives**

Effective September 18, 2003, we entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. We have designated the swaps as hedges against changes in the fair value of a designated portion of the Notes due to changes in underlying interest rates. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the Notes. The agreements, which have payment and expiration dates and call provisions that coincide with the terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, we receive a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while we make a variable interest rate payment to the same counterparties equal to the six-month LIBOR plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. As of December 31, 2006 and January 1, 2006, the fair value of the swaps totaled approximately \$(1.7) million and \$(1.1) million, respectively, and is included in other non-current liabilities in the accompanying consolidated balance sheets. There was no material ineffectiveness of our interest rate swaps for the years ended December 31, 2006 or January 1, 2006.

Our Australian subsidiary is a party to an interest rate swap agreement to fix the interest rate on the variable rate non-recourse debt to 9.7%. We have determined the swap to be an effective cash flow hedge. Accordingly, we record the value of the interest rate swap in accumulated other comprehensive income, net of applicable income taxes. The total value of the swap as of December 31, 2006 and January 1, 2006 was approximately \$3.2 million and (\$0.4) million, respectively, and is recorded as a component of other non-current assets and of other non-current liabilities in the accompanying consolidated financial statements. There was no material ineffectiveness of the interest rate swaps for the fiscal years presented. We do not expect to enter into any transactions during the next twelve months which will result in the reclassification into earnings of gains or losses associated with this swap that are currently reported in accumulated other comprehensive loss.

**Cash Flow**

Cash and cash equivalents as of December 31, 2006 were \$111.5 million, an increase of \$54.4 million from January 1, 2006.

Cash provided by operating activities of continuing operations in 2006, 2005 and 2004 was \$45.8 million, \$31.4 million, and \$31.5 million, respectively. Cash provided by operating activities of continuing operations in 2006 was positively impacted by \$22.2 million of depreciation and amortization expense as well as an increase in accounts payable and accrued expenses. Cash provided by operating activities of continuing operations in 2005 was positively impacted by impairment charges of \$20.9 million for our Michigan Correctional Facility and \$4.3 million related to our Jena facility. Cash provided by operating activities of continuing operations in 2004 was positively impacted by an increase in accrued payroll and related taxes and other liabilities as well as a \$3.0 million charge related to our Jena facility.

Cash provided by operating activities of continuing operations in 2006 was negatively impacted by an increase in accounts receivable. The increase in accounts receivable is attributable to the increase in value of our Australian subsidiary's accounts receivable due to an increase in foreign exchange rates, the addition of CSC for the entire year, new contracts at New Castle, the South Florida Evaluation and Treatment Center, Fort Bayard Medical Center and Campsfield House as well as slightly higher billings reflecting a general increase in facility occupancy levels.

Cash used in investing activities of continuing operations in 2006 was \$16.9 million. Cash used by investing activities in 2005 was \$104.5 million and cash provided by investing activities in 2004 was \$42.1 million, respectively. Cash used in investing activities in 2006 relate to capital expenditures partially offset by purchase price adjustments related to the sale of YSI. Cash used in investing activities in 2005 reflect the acquisition of CSC. In 2004, there was a decrease in the restricted cash balance of \$52.0 million due to the

payment of \$43.0 million of the term loan portion of the Senior Credit Facility with the net proceeds of the sale of PCG. This payment satisfied the restriction on cash imposed by the terms of the Senior Credit Facility and the remainder was reclassified to cash.

Cash provided by financing activities in 2006 was \$21.7 million and reflects proceeds received from the equity offering of \$99.9 million and proceeds received from the exercise of stock options of \$5.4 million offset by payments of debt of \$82.6 million. Cash provided by financing activities in 2005 was \$24.6 million. Cash used in financing activities in 2004 was \$47.1 million. Cash provided by financing activities in 2005 reflects the payoff of \$53.4 million and the refinancing of \$75.0 million of the term loan portion of the Senior Credit Facility. Cash used in financing activities in 2004 reflects payments of \$10.0 million on borrowings under the Revolving Credit Facility, \$4.0 million in scheduled payments on the Term Loan Facility, and a one-time \$43.0 million payment on the Term Loan Facility from the net proceeds from the sale of our interest in PCG.

**Contractual Obligations and Off Balance Sheet Arrangements**

The following is a table of certain of our contractual obligations, as of December 31, 2006, which requires us to make payments over the periods presented.

Contractual Obligations	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years (In thousands)	3-5 Years	More Than 5 Years
Long-term debt obligations	\$ 150,111	\$ 28	\$ 56	\$ 27	\$ 150,000
Capital lease obligations (includes imputed interest)	30,757	2,195	4,123	3,864	20,575
Operating lease obligations	42,908	10,112	17,130	7,629	8,037
Non-recourse debt	147,260	11,873	25,930	29,049	80,408
Estimated interest payments on debt (a)	133,213	20,116	38,721	36,183	38,193
Estimated payments on interest rate swaps (a)	(2,054)	(316)	(632)	(632)	(474)
Other long-term liabilities	14,297	11,947	220	301	1,829
Total	\$ 516,492	\$ 55,955	\$ 85,548	\$ 76,421	\$ 298,568

(a) Due to the uncertainties of future LIBOR rates, the variable interest payments on our credit facility and swap agreements were calculated using LIBOR rates of 5.30% and 5.38% based on our bank rates as of February 15, 2007 and January 12, 2007, respectively.

We do not have any additional off balance sheet arrangements which would subject us to additional liabilities.

**Inflation**

We believe that inflation, in general, did not have a material effect on our results of operations during 2006, 2005 and 2004. While some of our contracts include provisions for inflationary indexing, inflation could have a substantial adverse effect on our results of operations in the future to the extent that wages and salaries, which represent our largest expense, increase at a faster rate than the per diem or fixed rates received by us for our management services.

**Outlook**

The following discussion of our future performance contains statements that are not historical statements and, therefore, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Our forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those stated or implied in the forward-looking statement. Please refer to "Item 1A. Risk Factors" in this Annual Report on Form 10-K, the "Forward-Looking Statements — Safe

Harbor,” as well as the other disclosures contained in this Annual Report on Form 10-K, for further discussion on forward-looking statements and the risks and other factors that could prevent us from achieving our goals and cause the assumptions underlying the forward-looking statements and the actual results to differ materially from those expressed in or implied by those forward-looking statements.

The private corrections industry has played an increasingly important role in addressing U.S. detention and correctional needs over the past five years. Since year-end 2000, the number of federal inmates held at private correctional and detention facilities has increased over 50 percent. At midyear 2005, the private sector housed approximately 14.4% of federal inmates. Approximately 57% of the estimated 2.2 million individuals incarcerated in the United States at year-end 2004 were held in state prisons. At midyear 2005, the private sector housed approximately 5.6% of all state inmates. In addition to our strong position in the U.S. market, we are the only publicly traded U.S. correctional company with international operations. We believe that our existing international presence positions us to capitalize on growth opportunities within the private corrections and detention industry in new and established international markets.

We intend to pursue a diversified growth strategy by winning new clients and contracts, expanding our government services portfolio and pursuing selective acquisition opportunities. We achieve organic growth through competitive bidding that begins with the issuance by a government agency of a request for proposal, or RFP. We primarily rely on the RFP process for organic growth in our U.S. and international corrections operations as well as in our mental health and residential treatment services. We believe that our long operating history and reputation have earned us credibility with both existing and prospective clients when bidding on new facility management contracts or when renewing existing contracts. Our success in the RFP process has resulted in a pipeline of new projects with significant revenue potential. In 2006, we announced 10 new projects representing 4,934 beds. In addition to pursuing organic growth through the RFP process, we will from time to time selectively consider the financing and construction of new facilities or expansions to existing facilities on a speculative basis without having a signed contract with a known client. We also plan to leverage our experience to expand the range of government-outsourced services that we provide. We will continue to pursue selected acquisition opportunities in our core services and other government services areas that meet our criteria for growth and profitability.

#### **Revenue**

Domestically, we continue to be encouraged by the number of opportunities that have recently developed in the privatized corrections and detention industry. The need for additional bed space at the federal, state or local levels has been as strong as it has been at any time during the last decade, and we currently expect that trend to continue for the foreseeable future. Overcrowding at corrections facilities in various states, most recently California and Arizona, and increased demand for bed space at federal prisons and detention facilities primarily resulting from government initiatives to improve immigration security are two of the factors that have contributed to the greater number of opportunities for privatization. We plan to actively bid on any new projects that fit our target profile for profitability and operational risk. Although we are pleased with the overall industry outlook, positive trends in the industry may be offset by several factors, including budgetary constraints, unanticipated contract terminations and contract non-renewals. In Michigan, the State cancelled our Baldwin Correctional Facility management contract in 2005 based upon the Governor’s veto of funding for the project. Although we do not expect this termination to represent a trend, any future unexpected terminations of our existing management contracts could have a material adverse impact on our revenues. Additionally, several of our management contracts are up for renewal and/or re-bid in 2007. Although we have historically had a relative high contract renewal rate, there can be no assurance that we will be able to renew our management contracts scheduled to expire in 2007 on favorable terms, or at all.

Internationally, in the United Kingdom, we recently won our first contract since re-establishing operations. We believe that additional opportunities will become available in that market and plan to actively bid on any opportunities that fit our target profile for profitability and operational risk. In South Africa, we anticipate that the government will seek to outsource the development and operation of one or more correctional facilities in the near future. We expect to bid on any suitable opportunities.

With respect to our mental health residential treatment services business conducted through our wholly-owned subsidiary, GEO Care, Inc., we are currently pursuing a number of business development opportunities. In addition, we continue to expend resources on informing state and local governments about the benefits of privatization and we anticipate that there will be new opportunities in the future as those efforts begin to yield results. We believe we are well positioned to capitalize on any suitable opportunities that become available in this area.

#### ***Operating Expenses***

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health facilities. In 2006, operating expenses totaled approximately 83.4% of our consolidated revenues. Our operating expenses as a percentage of revenue in 2007 will be impacted by several factors. We could experience continued savings under our general liability, auto liability and workers' compensation insurance program, although the amount of these potential savings cannot be predicted. These savings, which totaled \$4.0 million in fiscal year 2006 and are now reflected in our current actuarial projections are a result of improved claims experience and loss development as compared to our results under our prior insurance program. In addition, as a result of our CPT acquisition, we will no longer incur lease expense relating to the eleven facilities that we purchased in that transaction which we formerly leased from CPT. As a result, our operating expenses will decrease by the aggregate amount of that lease expense, which totaled \$23.0 million in fiscal year 2006. These potential reductions in operating expenses may be offset by increased start-up expenses relating to a number of new projects which we are developing, including our new Graceville prison and Moore Haven expansion project in Florida, our Clayton facility in New Mexico, our Lawton, Oklahoma prison expansion and our Florence West expansion project in Arizona. Overall, excluding start-up expenses and the elimination of lease expense as a result of the CPT acquisition, we anticipate that operating expenses as a percentage of our revenue will remain relatively flat, consistent with our historical performance.

#### ***General and Administrative Expenses***

General and administrative expenses consist primarily of corporate management salaries and benefits, professional fees and other administrative expenses. We have recently incurred increasing general and administrative costs including increased costs associated with increases in business development costs, professional fees and travel costs, primarily relating to our mental health residential treatment services business. We expect this trend to continue as we pursue additional business development opportunities in all of our business lines and build the corporate infrastructure necessary to support our mental health residential treatment services business. We also plan to continue expending resources on the evaluation of potential acquisition targets.

#### **Forward-Looking Statements — Safe Harbor**

This report and the documents incorporated by reference herein contain "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. "Forward-looking" statements are any statements that are not based on historical information. Statements other than statements of historical facts included in this report, including, without limitation, statements regarding our future financial position, business strategy, budgets, projected costs and plans and objectives of management for future operations, are "forward-looking" statements. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may," "will," "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate" or "continue" or the negative of such words or variations of such words and similar expressions. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements and we can give no assurance that such forward-looking statements will



prove to be correct. Important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, or “cautionary statements,” include, but are not limited to:

- our ability to timely build and/or open facilities as planned, profitably manage such facilities and successfully integrate such facilities into our operations without substantial additional costs;
- the instability of foreign exchange rates, exposing us to currency risks in Australia, the United Kingdom, and South Africa, or other countries in which we may choose to conduct our business;
- our ability to reactivate the Michigan Correctional Facility;
- an increase in unreimbursed labor rates;
- our ability to expand, diversify and grow our correctional and residential treatment services;
- our ability to win management contracts for which we have submitted proposals and to retain existing management contracts;
- our ability to raise new project development capital given the often short-term nature of the customers’ commitment to use newly developed facilities;
- our ability to estimate the government’s level of dependency on privatized correctional services;
- our ability to grow our mental health and residential treatment services;
- our ability to accurately project the size and growth of the U.S. and international privatized corrections industry;
- our ability to develop long-term earnings visibility;
- our ability to obtain future financing at competitive rates;
- our exposure to rising general insurance costs;
- our exposure to claims for which we are uninsured;
- our exposure to rising employee and inmate medical costs;
- our ability to maintain occupancy rates at our facilities;
- our ability to manage costs and expenses relating to ongoing litigation arising from our operations;
- our ability to accurately estimate on an annual basis, loss reserves related to general liability, workers compensation and automobile liability claims;
- our ability to identify suitable acquisitions, and to successfully complete and integrate such acquisitions on satisfactory terms;
- the ability of our government customers to secure budgetary appropriations to fund their payment obligations to us; and
- other factors contained in our filings with the Securities and Exchange Commission, or the SEC, including, but not limited to, those detailed in this annual report on Form 10-K, our Form 10-Qs and our Form 8-Ks filed with the SEC.

We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. All subsequent written and oral forward-looking statements attributable to us, or persons acting on our behalf, are expressly qualified in their entirety by the cautionary statements included in this report.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

**Interest Rate Risk**

We are exposed to market risks related to changes in interest rates with respect to our Senior Credit Facility. Payments under the Senior Credit Facility are indexed to a variable interest rate. Based on borrowings outstanding under the Term Loan B of our Amended Senior Credit Facility of \$365.0 million as of January 24, 2007, immediately following the acquisition of CPT, for every one percent increase in the interest rate applicable to the Amended Senior Credit Facility, our total annual interest expense would increase by \$3.7 million.

Effective September 18, 2003, we entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. We have designated the swaps as hedges against changes in the fair value of a designated portion of the Notes due to changes in underlying interest rates. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the Notes. The agreements, which have payment and expiration dates and call provisions that coincide with the terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, we receive a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while we make a variable interest rate payment to the same counterparties equal to the six-month LIBOR plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. For every one percent increase in the interest rate applicable to the \$50.0 million swap agreements on the Notes described above, our total annual interest expense would increase by \$0.5 million.

We have entered into certain interest rate swap arrangements for hedging purposes, fixing the interest rate on our Australian non-recourse debt to 9.7%. The difference between the floating rate and the swap rate on these instruments is recognized in interest expense within the respective entity. Because the interest rates with respect to these instruments are fixed, a hypothetical 100 basis point change in the current interest rate would not have a material impact on our financial condition or results of operations.

Additionally, we invest our cash in a variety of short-term financial instruments to provide a return. These instruments generally consist of highly liquid investments with original maturities at the date of purchase of three months or less. While these instruments are subject to interest rate risk, a hypothetical 100 basis point increase or decrease in market interest rates would not have a material impact on our financial condition or results of operations.

**Foreign Currency Exchange Rate Risk**

We are exposed to market risks related to fluctuations in foreign currency exchange rates between the U.S. dollar and the Australian dollar and the South African Rand and the U.K. pound currency exchange rates. Based upon our foreign currency exchange rate exposure as of December 31, 2006 with respect to our international operations, every 10 percent change in historical currency rates would have approximately a \$3.3 million effect on our financial position and approximately a \$1.1 million impact on our results of operations over the next fiscal year.

**Item 8. Financial Statements and Supplementary Data**

**MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS**

To the Shareholders of  
The GEO Group, Inc.:

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States. They include amounts based on judgments and estimates.

Representation in the consolidated financial statements and the fairness and integrity of such statements are the responsibility of management. In order to meet management's responsibility, the Company maintains a system of internal controls and procedures and a program of internal audits designed to provide reasonable assurance that our assets are controlled and safeguarded, that transactions are executed in accordance with management's authorization and properly recorded, and that accounting records may be relied upon in the preparation of financial statements.

The consolidated financial statements have been audited by Grant Thornton LLP, independent registered public accountants, whose appointment by our Audit Committee was ratified by our shareholders. Their report expresses a professional opinion as to whether management's consolidated financial statements considered in their entirety present fairly, in conformity with accounting principles generally accepted in the United States, the Company's financial position and results of operations. Their audit was conducted in accordance with the standards of the Public Company Accounting Oversight Board. As part of this audit, Grant Thornton LLP considered the Company's system of internal controls to the degree they deemed necessary to determine the nature, timing, and extent of their audit tests which support their opinion on the consolidated financial statements.

The Audit Committee of the Board of Directors meets periodically with representatives of management, the independent registered public accountants and our internal auditors to review matters relating to financial reporting, internal accounting controls and auditing. Both the internal auditors and the independent registered certified public accountants have unrestricted access to the Audit Committee to discuss the results of their reviews.

George C. Zoley  
*Chairman and Chief Executive Officer*

Wayne H. Calabrese  
*Vice Chairman, President  
and Chief Operating Officer*

John G. O'Rourke  
*Senior Vice President of Finance  
and Chief Financial Officer*

**MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL  
OVER FINANCIAL REPORTING**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. The Company's internal control over financial reporting is a process designed under the supervision of the Company's Chief Executive Officer and Chief Financial Officer that: (i) pertains to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the Company's assets; (ii) provides reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements for external reporting in accordance with accounting principles generally accepted in the United States, and that receipts and expenditures are being made only in accordance with authorization of the Company's management and directors; and (iii) provides reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedure may deteriorate. Management has assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2006. In making its assessment of internal control over financial reporting, management used the criteria set forth by the Committee of Sponsoring Organizations ("COSO") of the Treadway Commission in *Internal Control — Integrated Framework*.

The Company evaluated, with the participation of its Chief Executive Officer and Chief Financial Officer, its internal control over financial reporting as of December 31, 2006, based on the COSO *Internal Control — Integrated Framework*. Based on this evaluation, the Company's management concluded that as of December 31, 2006, its internal control over financial reporting is effective in providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in their report which appears on page 61.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and  
Shareholders of The GEO Group, Inc.

We have audited the accompanying consolidated balance sheet of The GEO Group, Inc. (a Florida corporation) and Subsidiaries (the "Company") as of December 31, 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for the year ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The GEO Group, Inc. and subsidiaries as of December 31, 2006, and the consolidated results of their operations and their consolidated cash flows for the year ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. Schedule II is presented for purposes of additional analysis and is not a required part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

As described in Note 1 to the consolidated financial statements, effective January 2, 2006, the Company changed its method of accounting for share-based compensation to adopt Statement of Financial Accounting Standards No. 123R, Share-Based Payment. As described in Notes 1 and 16, to the consolidated financial statements, the Company recognized the funded status of its benefit plans in accordance with the provisions of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106, and 132R, as of December 31, 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of The GEO Group, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 27, 2007 expressed an unqualified opinion thereon.

/s/ Grant Thornton LLP

Miami, FL  
February 27, 2007

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and  
Shareholders of The GEO Group, Inc.

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting, that The GEO Group, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The GEO Group, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that The GEO Group, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the COSO criteria. Also in our opinion, The GEO Group, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of The GEO Group, Inc. and subsidiaries as of December 31, 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for the year ended December 31, 2006 and our report dated February 27, 2007 expressed an unqualified opinion on those financial statements.

/s/ Grant Thornton LLP

Miami, FL  
February 27, 2007

**REPORT OF INDEPENDENT REGISTERED CERTIFIED PUBLIC ACCOUNTANTS**

The Board of Directors and Shareholders of The GEO Group, Inc.

We have audited the accompanying consolidated balance sheet of The GEO Group, Inc. as of January 1, 2006, and the related consolidated statements of income, shareholders' equity and comprehensive income, and cash flows for each of the two years in the period ended January 1, 2006. Our audits also included the financial statement schedule for each of the two years in the period ended January 1, 2006 listed in the index at item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The GEO Group, Inc. at January 1, 2006 and the consolidated results of its operations and its cash flows for each of the two years in the period ended January 1, 2006, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein for each of the two years in the period ended January 1, 2006.

/s/ Ernst & Young LLP

West Palm Beach, Florida  
March 14, 2006

THE GEO GROUP, INC.  
 CONSOLIDATED STATEMENTS OF INCOME  
 Fiscal Years Ended December 31, 2006, January 1, 2006, and January 2, 2005

	2006	2005	2004
	(In thousands, except per share data)		
<b>Revenues</b>	\$ 860,882	\$ 612,900	\$ 593,994
<b>Operating Expenses</b>	718,178	540,128	495,226
<b>Depreciation and Amortization</b>	22,235	15,876	13,898
<b>General and Administrative Expenses</b>	56,268	48,958	45,879
<b>Operating Income</b>	64,201	7,938	38,991
<b>Interest Income</b>	10,687	9,154	9,568
<b>Interest Expense</b>	(28,231)	(23,016)	(22,138)
<b>Write-off of Deferred Financing Fees from Extinguishment of Debt</b>	(1,295)	(1,360)	(317)
<b>Income (loss) Before Income Taxes, Minority Interest, Equity in Earnings of Affiliates, and Discontinued Operations</b>	45,362	(7,284)	26,104
<b>Provision (benefit) for Income Taxes</b>	16,505	(11,826)	8,231
<b>Minority Interest</b>	(125)	(742)	(710)
<b>Equity in Earnings of Affiliates, (net of income tax provision (benefit) of \$56, \$(2,016), and \$0)</b>	1,576	2,079	—
<b>Income from Continuing Operations</b>	30,308	5,879	17,163
<b>Income (loss) from discontinued operations, (net of tax (benefit) provision of \$(151), \$895, and \$(181))</b>	(277)	1,127	(348)
<b>Net Income</b>	<u>\$ 30,031</u>	<u>\$ 7,006</u>	<u>\$ 16,815</u>
<b>Weighted Average Common Shares Outstanding:</b>			
Basic	17,221	14,370	14,076
Diluted	17,872	15,015	14,607
<b>Earnings (loss) per Common Share:</b>			
<b>Basic:</b>			
Income from continuing operations	\$ 1.76	\$ 0.41	\$ 1.22
Income (loss) from discontinued operations	(0.02)	0.08	(0.03)
<b>Net income per share — basic</b>	<u>\$ 1.74</u>	<u>\$ 0.49</u>	<u>\$ 1.19</u>
<b>Diluted:</b>			
Income from continuing operations	\$ 1.70	\$ 0.39	\$ 1.17
Income (loss) from discontinued operations	(0.02)	0.08	(0.02)
<b>Net income per share — diluted</b>	<u>\$ 1.68</u>	<u>\$ 0.47</u>	<u>\$ 1.15</u>

The accompanying notes are an integral part of these consolidated financial statements.



**THE GEO GROUP, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
**December 31, 2006 and January 1, 2006**

	2006	2005
	(In thousands, except share data)	
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 111,520	\$ 57,094
Restricted cash	13,953	8,882
Accounts receivable, less allowance for doubtful accounts of \$926 and \$224	162,867	127,612
Deferred income tax asset	19,492	19,755
Other current assets	14,922	15,826
Current assets of discontinued operations	—	123
Total current assets	<u>322,754</u>	<u>229,292</u>
Restricted Cash	19,698	17,484
Property and Equipment, Net	287,374	282,236
Assets Held for Sale	1,610	5,000
Direct Finance Lease Receivable	39,271	38,492
Deferred Income Tax Assets	4,941	—
Goodwill and Other Intangible Assets, Net	41,554	52,127
Other Non Current Assets	26,251	14,880
	<u>\$ 743,453</u>	<u>\$ 639,511</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 48,890	\$ 27,762
Accrued payroll and related taxes	31,320	26,985
Accrued expenses	77,675	70,177
Current portion of deferred revenue	1,830	1,894
Current portion of capital lease obligations, long-term debt and non-recourse debt	12,685	8,441
Current liabilities of discontinued operations	1,303	1,260
Total current liabilities	<u>173,703</u>	<u>136,519</u>
Deferred Revenue	1,755	3,267
Deferred Tax Liability	—	2,085
Minority Interest	1,297	1,840
Other Non Current Liabilities	24,816	19,601
Capital Lease Obligations	16,621	17,072
Long-Term Debt	144,971	219,254
Non-Recourse Debt	131,680	131,279
Commitments and Contingencies		
<b>Shareholders' Equity</b>		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, none issued or outstanding	—	—
Common stock, \$0.01 par value, 45,000,000 shares authorized, 33,248,584 and 32,536,715 issued and 19,748,584 and 14,536,715 outstanding	197	145
Additional paid-in capital	143,233	70,736
Retained earnings	201,697	171,666
Accumulated other comprehensive income (loss)	2,393	(2,073)
Treasury stock 13,500,000 and 18,000,000 shares	(98,910)	(131,880)
Total shareholders' equity	<u>248,610</u>	<u>108,594</u>
	<u>\$ 743,453</u>	<u>\$ 639,511</u>

The accompanying notes are an integral part of these consolidated financial statements.

**THE GEO GROUP, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**Fiscal Years Ended December 31, 2006, January 1, 2006, and January 2, 2005**

	2006	2005	2004
	(In thousands)		
<b>Cash Flow from Operating Activities:</b>			
Income from continuing operations	\$ 30,308	\$ 5,879	\$ 17,163
Adjustments to reconcile income from continuing operations to net cash provided by operating activities			
Impairment charge	—	20,859	—
Idle facility charge	—	4,255	3,000
Amortization of unearned compensation	966	—	—
Stock-based compensation expense	374	—	—
Depreciation and amortization expenses	22,235	15,876	13,898
Amortization of debt issuance costs	1,089	449	303
Deferred tax liability (benefit)	(5,080)	(10,614)	3,433
Provision for doubtful accounts	762	—	229
Major maintenance reserve	193	290	465
Equity in earnings (losses) of affiliates, net of tax	(1,576)	(2,079)	—
Minority interests in earnings (losses) of consolidated entity	125	742	710
Dividend to minority interest	(757)	—	—
Other non-cash charges	—	—	141
Income tax benefit of equity compensation	(2,793)	731	773
Write-off of deferred financing fees from extinguishment of debt	1,295	1,360	317
Changes in assets and liabilities, net of acquisition			
Accounts receivable	(35,733)	(7,238)	(6,688)
Other current assets	36	(3,235)	(1,283)
Other assets	(366)	(564)	1,442
Accounts payable and accrued expenses	30,688	4,918	(12,558)
Accrued payroll and related taxes	3,797	(996)	6,699
Deferred revenue	(1,576)	(1,003)	(1,844)
Other liabilities	1,799	1,763	5,282
Net cash provided by operating activities of continuing operations	45,786	31,393	31,482
Net cash provided by operating activities of discontinued operations	166	3,420	14,024
Net cash provided by operating activities	45,952	34,813	45,506
<b>Cash Flow from Investing Activities:</b>			
Acquisitions, net of cash acquired	(2,578)	(79,290)	—
YSL purchase price adjustment	15,080	—	—
Proceeds from sale of assets	20,246	707	315
Proceeds from sales of short-term investments	—	39,000	56,835
Purchases of short-term investments	—	(29,000)	(56,835)
Change in restricted cash	(7,285)	(4,406)	—
Insurance proceeds related to hurricane damage	781	—	52,000
Capital expenditures	(43,165)	(31,465)	(10,235)
Net cash provided by (used in) investing activities of continuing operations	(16,921)	(104,454)	42,080
Net cash provided by investing activities of discontinued operations	—	11,500	—
Net cash provided by (used in) investing activities	(16,921)	(92,954)	42,080
<b>Cash Flow from Financing Activities:</b>			
Proceeds from equity offering, net	99,936	—	—
Proceeds from long-term debt	111	75,000	10,000
Income tax benefit of equity compensation	2,793	—	—
Repurchase of stock options from employees and directors	(3,955)	—	—
Payments on long-term debt	(82,627)	(53,398)	(58,704)
Proceeds from the exercise of stock options	5,405	2,999	1,589
Net cash provided by (used in) financing activities	21,663	24,601	(47,115)
<b>Effect of Exchange Rate Changes on Cash and Cash Equivalents</b>	3,732	(1,371)	1,575
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	54,426	(34,911)	42,046
<b>Cash and Cash Equivalents, beginning of period</b>	57,094	92,005	49,959
<b>Cash and Cash Equivalents, end of period</b>	\$ 111,520	\$ 57,094	\$ 92,005
<b>Supplemental Disclosures:</b>			
<b>Cash paid (received) during the year for:</b>			
Income taxes	\$ (853)	\$ (636)	\$ 8,906
Interest	\$ 25,740	\$ 21,181	\$ 20,158
<b>Non-cash investing and financing activities:</b>			
Fair value of assets acquired, net of cash acquired	\$ 2,578	\$ 223,934	\$ —
Total liabilities assumed	\$ —	\$ 144,644	\$ —
	\$ —	\$ 79,290	\$ —
Sale of assets in exchange for note receivable	\$ —	\$ 2,000	\$ —

The accompanying notes are an integral part of these consolidated financial statements.

## THE GEO GROUP, INC.

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
AND COMPREHENSIVE INCOME**  
Fiscal Years Ended December 31, 2006, January 1, 2006, and January 2, 2005

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock		Total Shareholders' Equity
	Number of Shares	Amount				Number of Shares	Amount	
	(In thousands)							
<b>Balance, December 28, 2003</b>	14,000	\$ 140	\$ 64,558	\$ 147,845	\$ (3,338)	(18,000)	\$ (131,880)	\$ 77,325
Proceeds from stock options exercised	261	3	1,588	—	—	—	—	1,591
Tax benefit related to employee stock options	—	—	773	—	—	—	—	773
Acceleration of vesting on employee stock options	—	—	38	—	—	—	—	38
Comprehensive income:								
Net income	—	—	—	16,815	—	—	—	—
Change in foreign currency translation, net of income tax expense of \$384	—	—	—	—	600	—	—	—
Minimum pension liability adjustment, net of income tax expense of \$480	—	—	—	—	661	—	—	—
Unrealized gain on derivative instruments, net of income tax expense of \$815	—	—	—	—	1,936	—	—	—
Total comprehensive income	—	—	—	—	—	—	—	20,012
<b>Balance, January 2, 2005</b>	14,261	143	66,957	164,660	(141)	(18,000)	(131,880)	99,739
Proceeds from stock options exercised	276	2	2,997	—	—	—	—	2,999
Tax benefit related to employee stock options	—	—	731	—	—	—	—	731
Acceleration of vesting on employee stock options	—	—	51	—	—	—	—	51
Comprehensive income:								
Net income	—	—	—	7,006	—	—	—	—
Change in foreign currency translation, net of income tax benefit of \$2,158	—	—	—	—	(3,375)	—	—	—
Minimum pension liability adjustment, net of income tax expense of \$8	—	—	—	—	12	—	—	—
Unrealized gain on derivative instruments, net of income tax expense of \$625	—	—	—	—	1,431	—	—	—
Total comprehensive income	—	—	—	—	—	—	—	5,074
<b>Balance, January 1, 2006</b>	14,537	145	70,736	171,666	(2,073)	(18,000)	(131,880)	108,594
Proceeds from stock options exercised	487	5	5,400	—	—	—	—	5,405
Tax benefit related to employee stock options	—	—	2,793	—	—	—	—	2,793
Stock based compensation expense	—	—	374	—	—	—	—	374
Restricted stock granted	225	2	(2)	—	—	—	—	—
Amortization of restricted stock	—	—	966	—	—	—	—	966
Issuance of treasury stock in conjunction with offering	4,500	45	66,921	—	—	4,500	32,970	99,936
Buyout of stock options	—	—	(3,955)	—	—	—	—	(3,955)
Comprehensive income:								
Net income	—	—	—	30,031	—	—	—	—
Change in foreign currency translation, net of income tax expense of \$2,356	—	—	—	—	3,846	—	—	—
Minimum pension liability adjustment, net of income tax benefit of \$1,259	—	—	—	—	(1,933)	—	—	—
Unrealized gain on derivative instruments, net of income tax expense of \$1,121	—	—	—	—	2,553	—	—	—
Total comprehensive income	—	—	—	—	—	—	—	34,497
<b>Balance, December 31, 2006</b>	<u>19,749</u>	<u>\$ 197</u>	<u>\$ 143,233</u>	<u>\$ 201,697</u>	<u>\$ 2,393</u>	<u>(13,500)</u>	<u>\$ (98,910)</u>	<u>\$ 248,610</u>

The accompanying notes are an integral part of these consolidated financial statements.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the Fiscal Years Ended December 31, 2006, January 1, 2006, and January 2, 2005

**1. Summary of Business Operations and Significant Accounting Policies**

The GEO Group, Inc., a Florida corporation, and subsidiaries (the "Company") is a leading developer and manager of privatized correctional, detention and mental health residential treatment services facilities located in the United States, Australia, South Africa, the United Kingdom and Canada. Until July 9, 2003, the Company was a majority owned subsidiary of The Wackenhut Corporation, ("TWC"). TWC previously owned 12 million shares of the Company's common stock.

On January 24, 2007, the Company completed its previously announced acquisition of CentraCore Properties Trust ("CPT"), a Maryland real estate investment trust, pursuant to an Agreement and Plan of Merger, dated as of September 19, 2006 (the "Merger Agreement"), by and among the Company, GEO Acquisition II, Inc., a direct wholly-owned subsidiary of the Company ("Merger Sub") and CPT. Under the terms of the Merger Agreement, CPT merged with and into Merger Sub (the "Merger"), with Merger Sub being the surviving corporation of the Merger.

As a result of the Merger, each share of common stock of CPT (collectively, the "Shares") was converted into the right to receive \$32.5826 in cash, inclusive of a pro-rated dividend for all quarters or partial quarters for which CPT's dividend had not yet been paid as of the closing date. In addition, each outstanding option to purchase CPT common stock (collectively, the "Options") having an exercise price less than \$32.00 per share was converted into the right to receive the difference between \$32.00 per share and the exercise price per share of the option, multiplied by the total number of shares of CPT common stock subject to the option. The Company paid an aggregate purchase price of approximately \$427.6 million for the acquisition of CPT, inclusive of the payment of approximately \$367.6 million in exchange for the Shares and the Options, the repayment of approximately \$40.0 million in CPT debt and the payment of approximately \$20.0 million in transaction related fees and expenses. The Company financed the acquisition through the use of \$365.0 million in new borrowings under a new Term Loan B and approximately \$62.6 million in cash on hand. As a result of the Acquisition, the Company will no longer have ongoing lease expense related to the properties the Company previously leased from CPT. However, the Company will have increased depreciation expense reflecting its ownership of the properties and higher interest expense as a result of borrowings used to fund the acquisition.

On June 12, 2006, the Company sold in a follow-on public offering 3,000,000 shares of its common stock at a price of \$35.46 per share (4,500,000 shares of its common stock at a price of \$23.64 reflecting the 3 for 2 stock split). All shares were issued from treasury. The aggregate net proceeds (after deducting underwriter's discounts and expenses) was approximately \$100 million. On June 13, 2006, the Company utilized approximately \$74.6 million of the proceeds to repay all outstanding debt under the term loan portion of the Company's Senior Credit Facility. In addition, on August 11, 2006, the Company used \$4.0 million of the proceeds of the offering to purchase from certain directors, executive officers and employees stock options that were currently outstanding and exercisable, and which were due to expire within the next three years. The balance of the net proceeds was used for general corporate purposes including working capital, capital expenditures and the acquisition of CPT.

On August 10, 2006, the Board of Directors declared a 3-for-2 stock split of the Company's common stock. The stock split took effect on October 2, 2006 with respect to stockholders of record on September 15, 2006. Following the stock split, the shares outstanding increased from 13.0 million to 19.5 million. All share and per share data has been adjusted to reflect the stock split.

On November 4, 2005, the Company completed the acquisition of Correctional Services Corporation (CSC), a Florida-based provider of privatized jail, community corrections and alternative sentencing services. Under the terms of the merger, the Company acquired for cash, 100% of the 10.2 million outstanding shares of CSC common stock for \$6.00 per share or approximately \$62.1 million. As a result of the merger, the

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Company became responsible for supervising the operation of the sixteen adult correctional and detention facilities, totaling 8,037 beds, formerly run by CSC. Immediately following the purchase of CSC, the Company sold Youth Services International, Inc., the former juvenile services division of CSC, for \$3.75 million, \$1.75 million of which was paid in cash and the remaining \$2.0 million of which was paid in the form of a promissory note accruing interest at a rate of 6% per annum. Principal and interest are due quarterly. The annual maturities are \$0.7 million in 2007, and \$0.7 million in 2008.

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States. The significant accounting policies of the Company are described below.

***Fiscal Year***

The Company's fiscal year ends on the Sunday closest to the calendar year end. Fiscal years 2006 and 2005 each included 52 weeks. Fiscal year 2004 included 53 weeks. The Company reports the results of its South African equity affiliate, South African Custodial Services Pty. Limited, ("SACS"), and its consolidated South African entity, South African Custodial Management Pty. Limited ("SACM") on a calendar year end, due to the availability of information.

***Basis of Presentation***

The consolidated financial statements include the accounts of the Company and all controlled subsidiaries. Investments in 50% owned affiliates, which the Company does not control, are accounted for under the equity method of accounting. Intercompany transactions have been eliminated.

***Use of Estimates***

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company's significant estimates include reserves for self-insured retention related to general liability insurance, workers' compensation insurance, auto liability insurance, employer group health insurance, percentage of completion and estimated cost to complete, allowance for doubtful accounts and accrued vacation. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. While the Company believes that such estimates are fair when considered in conjunction with the consolidated financial statements taken as a whole, the actual amounts of such estimates, when known, will vary from these estimates. If actual results significantly differ from the Company's estimates, the Company's financial condition and results of operations could be materially impacted.

***Fair Value of Financial Instruments***

The carrying value of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses approximate their fair value due to the short maturity of these items. The carrying value of the Company's long-term debt related to its Senior Credit Facility (See Note 10) and non-recourse debt approximates fair value based on the variable interest rates on the debt. For the Company's 8<sup>1</sup>/<sub>4</sub>% Senior Unsecured Notes, the stated value and fair value based on quoted market rates was \$150.0 million and \$153.8 million, respectively, at December 31, 2006. For the Company's non-recourse debt related to the South Texas Detention Complex and Northwest Detention Center, the stated value and fair value based on quoted market rates was \$97.3 million and \$93.2 million, respectively, at December 31, 2006.

**THE GEO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)*****Cash and Cash Equivalents***

Cash and cash equivalents include all interest-bearing deposits or investments with original maturities of three months or less.

***Accounts Receivable***

The Company extends credit to the governmental agencies it contracts with and other parties in the normal course of business as a result of billing and receiving payment for services thirty to sixty days in arrears. Further, the Company regularly reviews outstanding receivables, and provides estimated losses through an allowance for doubtful accounts. In evaluating the level of established loss reserves, the Company makes judgments regarding its customers' ability to make required payments, economic events and other factors. As the financial condition of these parties change, circumstances develop or additional information becomes available, adjustments to the allowance for doubtful accounts may be required. The Company also performs ongoing credit evaluations of customers' financial condition and generally does not require collateral. The Company maintains reserves for potential credit losses, and such losses traditionally have been within its expectations.

***Inventories***

Food and supplies inventories are carried at the lower of cost or market, on a first-in first-out basis and are included in "other current assets" in the accompanying consolidated balance sheets. Uniform inventories are carried at amortized cost and are amortized over a period of eighteen months. The current portion of unamortized uniforms is included in "other current assets" and the long-term portion is included in "other non current assets" in the accompanying consolidated balance sheets.

***Restricted Cash***

The Company had \$14.0 million in current restricted cash and cash equivalents and \$19.7 million in long-term restricted cash equivalents at December 31, 2006. The balances in those accounts are attributable primarily to amounts held in escrow or in trust in connection with the 1,020-bed South Texas Detention Complex in Frio County, Texas and the 890-bed Northwest Detention Center in Tacoma, Washington.

Additionally, the Company's wholly owned Australian subsidiary financed a facility's development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to the Company. As a condition of the loan, the Company is required to maintain a restricted cash balance of AUD 5.0 million, approximately \$3.9 million at December 31, 2006. The term of the non-recourse debt is through 2017.

***Costs of Acquisition Opportunities***

Internal costs associated with a business combination are expensed as incurred. Direct and incremental costs related to successful negotiations where the Company is the acquiring company are capitalized as part of the cost of the acquisition. As of December 31, 2006 the Company had \$1.1 million of capitalized costs. Costs associated with unsuccessful negotiations are expensed when it is probable that the acquisition will not occur. During 2004, the Company wrote off approximately \$1.3 million of costs.

***Property and Equipment***

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 2 to 40 years. Equipment and furniture and fixtures are depreciated over 3 to 10 years. Accelerated methods of depreciation are generally used for income tax purposes. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvement or the term of the

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

lease. The Company performs ongoing evaluations of the estimated useful lives of the property and equipment for depreciation purposes. The estimated useful lives are determined and continually evaluated based on the period over which services are expected to be rendered by the asset. Maintenance and repairs are expensed as incurred. Interest is capitalized in connection with the construction of correctional and detention facilities. Capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life. Approximately \$0.2 million of interest cost was capitalized in 2006 related to the expansion of an existing facility. No interest cost was capitalized in 2005 and 2004.

**Assets Held Under Capital Leases**

Assets held under capital leases are recorded at the lower of the net present value of the minimum lease payments or the fair value of the leased asset at the inception of the lease. Amortization expense is recognized using the straight-line method over the shorter of the estimated useful life of the asset or the term of the related lease and is included in depreciation expense.

**Long-Lived Assets**

The Company reviews long-lived assets to be held and used for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell. Management has reviewed the Company's long-lived assets and determined that there are no events requiring impairment loss recognition. In 2005, the Company recorded a charge of \$20.9 million related to the Michigan Facility. See Note 12. Events that would trigger an impairment assessment include deterioration of profits for a business segment that has long-lived assets, or when other changes occur which might impair recovery of long-lived assets. The book value of the Michigan Facility at December 31, 2006 is \$12.6 million.

**Goodwill and Other Intangible Assets**

The Company's goodwill at December 31, 2006 consisted of \$24.0 million related to the November 4, 2005 acquisition of CSC (See Note 2: Acquisition), \$2.5 million related to the October 12, 2006 acquisition of RSI and \$0.6 million related to its Australian subsidiary and at January 1, 2006 consisted of \$35.3 million related to the November 4, 2005 acquisition of CSC and \$0.6 million associated with its Australian subsidiary. Goodwill related to CSC is included in the U.S. corrections segment and goodwill related to RSI and Australia is included in the International Services segment. With the adoption of Financial Accounting Standard ("FAS") No. 142, the Company's goodwill is no longer amortized, but is subject to an annual impairment test. There was no impairment of goodwill as a result of the annual impairment test completed during the fourth quarter of 2006 and 2005 related to goodwill associated with CSC or the Company's Australian subsidiary. The annual impairment test for the goodwill related to the acquisition of RSI will be on the first day of the fourth quarter of 2007.

Acquired intangible assets are separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, rented or exchanged, regardless of the Company's intent to do so. The Company's intangible assets were recorded in connection with the acquisition of CSC and have finite lives ranging from 4-17 years and are amortized using a straight-line method. The Company reviews finite-lived intangible assets for impairment whenever an event occurs or circumstances change which indicate that the carrying amount of such assets may not be fully recoverable. See Note 8.

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**Variable Interest Entities**

In January 2003, the Financial Accounting Standards Board (“FASB”) issued Financial Interpretation FIN No. 46, “Consolidation of Variable Interest Entities,” which addressed consolidation by a business of variable interest entities in which it is the primary beneficiary. In December 2003, the FASB issued FIN No. 46R which replaced FIN No. 46. The Company’s 50% owned South African joint venture in South African Custodial Services Pty. Limited, which the Company refers to as SACS, is a variable interest entity. The Company determined that it is not the primary beneficiary of SACS and as a result it is not required to consolidate SACS under FIN 46R. The Company accounts for SACS as an equity affiliate. SACS was established in 2001, to design, finance and build the Kutama Sinthumule Correctional Center. Subsequently, SACS was awarded a 25 year contract to design, construct, manage and finance a facility in Louis Trichardt, South Africa. SACS, based on the terms of the contract with the government, was able to obtain long-term financing to build the prison. The financing is fully guaranteed by the government, except in the event of default, for which it provides an 80% guarantee. Separately, SACS entered into a long-term operating contract with South African Custodial Management (Pty) Limited (“SACM”) to provide security and other management services and with SACS’ joint venture partner to provide purchasing, programs and maintenance services upon completion of the construction phase, which concluded in February 2002. The Company’s maximum exposure for loss under this contract is \$15.6 million, which represents the Company’s initial investment and the guarantees discussed in Note 10.

In February 2004, CSC was awarded a contract by the Department of Homeland Security, Bureau of Immigration and Customs Enforcement (“ICE”) to develop and operate a 1,020 bed detention center in Frio County Texas. South Texas Local Development Corporation (“STLDC”) was created and issued \$49.5 million in taxable revenue bonds to finance the construction of the detention complex. Additionally, CSC provided a \$5 million subordinated note to STLDC for initial development. The Company determined that it is the primary beneficiary of STLDC and consolidates the entity as a result. STLDC is the owner of the complex and entered into a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require the revenue from CSC’s contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums are distributed to CSC to cover CSC’s operating expenses and management fee. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities resulting from its ownership. The bonds have a ten year term and are non-recourse to CSC and STLDC. The bonds are fully insured and the sole source of payment for the bonds is the operating revenues of the complex.

**Deferred Revenue**

Deferred revenue primarily represents the unamortized net gain on the development of properties and on the sale and leaseback of properties by the Company. The Company leases these properties back from CPT under operating leases. Deferred revenue is being amortized over the lives of the leases and is recognized in income as a reduction of rental expenses.

**Revenue Recognition**

In accordance with Staff Accounting Bulletin (“SAB”) No. 101, “Revenue Recognition in Financial Statements”, as amended by SAB No. 104, “Revenue Recognition”, and related interpretations, facility management revenues are recognized as services are provided under facility management contracts with approved government appropriations based on a net rate per day per inmate or on a fixed monthly rate.



**THE GEO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

Project development and design revenues are recognized as earned on a percentage of completion basis measured by the percentage of costs incurred to date as compared to estimated total cost for each contract. This method is used because the Company considers costs incurred to date to be the best available measure of progress on these contracts. Provisions for estimated losses on uncompleted contracts and changes to cost estimates are made in the period in which the Company determines that such losses and changes are probable. Typically, the Company enters into fixed price contracts and does not perform additional work unless approved change orders are in place. Costs attributable to unapproved change orders are expensed in the period in which the costs are incurred if the Company believes that it is not probable that the costs will be recovered through a change in the contract price. If the Company believes that it is probable that the costs will be recovered through a change in contract price, costs related to unapproved change orders are expensed in the period in which they are incurred, and contract revenue is recognized to the extent of the costs incurred. Revenue in excess of the costs attributable to unapproved change orders is not recognized until the change order is approved. Contract costs include all direct material and labor costs and those indirect costs related to contract performance. Changes in job performance, job conditions, and estimated profitability, including those arising from contract penalty provisions, and final contract settlements, may result in revisions to estimated costs and income, and are recognized in the period in which the revisions are determined.

***Income Taxes***

The Company accounts for income taxes in accordance with FAS No. 109, "Accounting for Income Taxes." ("FAS 109") Under this method, deferred income taxes are determined based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities given the provisions of enacted tax laws. Deferred income tax provisions and benefits are based on changes to the assets or liabilities from year to year. Valuation allowances are recorded related to deferred tax assets based on the "more likely than not" criteria of FAS 109.

***Earnings Per Share***

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding. On October 1, 2006 the Company initiated a 3-for-2 stock split. All earnings per share amounts and common shares amounts have been restated to reflect the stock split. The calculation of diluted earnings per share is similar to that of basic earnings per share, except that the denominator includes dilutive common share equivalents such as share options and restricted shares.

***Direct Finance Leases***

The Company accounts for the portion of its contracts with certain governmental agencies that represent capitalized lease payments on buildings and equipment as investments in direct finance leases. Accordingly, the minimum lease payments to be received over the term of the leases less unearned income are capitalized as the Company's investments in the leases. Unearned income is recognized as income over the term of the leases using the interest method.

***Reserves for Insurance Losses***

Claims for which the Company is insured arising from its U.S. operations that have an occurrence date of October 1, 2002 or earlier are handled by TWC and are commercially insured up to an aggregate limit of between \$25.0 million and \$50.0 million, depending on the nature of the claim and the applicable policy terms and conditions. With respect to claims for which the Company is insured arising after October 1, 2002, the Company maintains a general liability policy for all U.S. corrections operations with \$52.0 million per occurrence and in the aggregate. On October 1, 2004, the Company increased its deductible on this general liability policy from \$1.0 million to \$3.0 million for each claim that occurs after October 1, 2004. GEO Care,

**THE GEO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

Inc. is separately insured for general and professional liability. Coverage is maintained with limits of \$10.0 million per occurrence and in the aggregate subject to a \$3.0 million self-insured retention. The Company also maintains insurance to cover property and casualty risks, workers' compensation, medical malpractice, environmental liability and automobile liability. The Company's Australian subsidiary is required to carry tail insurance on a general liability policy providing an extended reporting period through 2011 related to a discontinued contract. The Company also carries various types of insurance with respect to its operations in South Africa, the United Kingdom and Australia. There can be no assurance that the Company's insurance coverage will be adequate to cover all claims to which the Company may be exposed.

Since the Company's insurance policies generally have high deductible amounts (including a \$3.0 million per claim deductible under the general liability and auto liability policies and a \$2.0 million per claim deductible under the workers' compensation policy), losses are recorded as reported and a provision is made to cover losses incurred but not reported. Loss reserves are undiscounted and are computed based on independent actuarial studies. The Company's management uses judgments in assessing loss estimates based on actuarial studies, which include actual claim amounts and loss development based on both the Company's own historical experience and industry experience. If actual losses related to insurance claims significantly differ from the estimates, the Company's financial condition and results of operations could be materially impacted.

Certain of the Company's facilities located in Florida and determined by insurers to be in high-risk hurricane areas carry substantial windstorm deductibles of up to \$3.0 million. Since hurricanes are considered unpredictable future events, no reserves have been established to pre-fund for potential windstorm damage. Limited commercial availability of certain types of insurance relating to windstorm exposure in coastal areas and earthquake exposure mainly in California may prevent the Company from insuring all facilities to full replacement value.

***Debt Issuance Costs***

Debt issuance costs totaling \$4.8 million and \$7.0 million at December 31, 2006, and January 1, 2006, respectively, are included in other non current assets in the consolidated balance sheets and are amortized to interest expense using the effective interest method, over the term of the related debt.

***Comprehensive Income***

The Company's comprehensive income is comprised of net income, foreign currency translation adjustments, unrealized gain (loss) on derivative instruments, and minimum pension liability adjustments in the Consolidated Statements of Shareholders' Equity and Comprehensive Income.

***Concentration of Credit Risk***

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, trade accounts receivable, short-term investments, direct finance lease receivable, long-term debt and financial instruments used in hedging activities. The Company's cash management and investment policies restrict investments to low-risk, highly liquid securities, and the Company performs periodic evaluations of the credit standing of the financial institutions with which it deals. As of December 31, 2006, and January 1, 2006, the Company had no significant concentrations of credit risk except as disclosed in Note 16.

***Foreign Currency Translation***

The Company's foreign operations use their local currencies as their functional currencies. Assets and liabilities of the operations are translated at the exchange rates in effect on the balance sheet date and

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

shareholders' equity is translated at historical rates. Income statement items are translated at the average exchange rates for the year. The impact of foreign currency fluctuation is included in shareholders' equity as a component of accumulated other comprehensive income (loss) and totaled \$2.2 million at December 31, 2006 and \$(0.9) million as of January 1, 2006.

**Financial Instruments**

In accordance with FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its related interpretations and amendments, the Company records derivatives as either assets or liabilities on the balance sheet and measures those instruments at fair value. For derivatives that are designed as and qualify as effective cash flow hedges, the portion of gain or loss on the derivative instrument effective at offsetting changes in the hedged item is reported as a component of accumulated other comprehensive income (loss) and reclassified into earnings when the hedged transaction affects earnings. Total accumulated other comprehensive income (loss) related to these cash flow hedges was \$2.2 million and \$(0.3) million as of December 31, 2006 and January 1, 2006, respectively. For derivative instruments that are designated as and qualify as effective fair value hedges, the gain or loss on the derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk is recognized in current earnings as interest income (expense) during the period of the change in fair values.

The Company formally documents all relationships between hedging instruments and hedge items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes attributing all derivatives that are designated as cash flow hedges to floating rate liabilities and attributing all derivatives that are designated as fair value hedges to fixed rate liabilities. The Company also assesses whether each derivative is highly effective in offsetting changes in the cash flows of the hedged item. Fluctuations in the value of the derivative instruments are generally offset by changes in the hedged item; however, if it is determined that a derivative is not highly effective as a hedge or if a derivative ceases to be a highly effective hedge, the Company will discontinue hedge accounting prospectively for the affected derivative.

**Stock-Based Compensation Expense**

On January 2, 2006, the Company adopted FAS No. 123R, "Share-Based Payment" (FAS 123R), which revises FAS 123, "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB25). FAS 123R requires companies to recognize the cost of employee services received in exchange for awards of equity instruments based upon the grant date fair value of those awards. The Company adopted FAS 123R using the modified prospective method. Under this method the Company recognizes compensation cost for all share-based payments granted after January 2, 2006, plus any awards granted to employees prior to January 1, 2006 that remain unvested at that time. Under this method of adoption, no restatement of prior periods is made. The Company uses a Black-Scholes option valuation model to estimate the fair value of each option awarded. The impact of forfeitures that may occur prior to vesting is also estimated and considered in the amount recognized.

The impact of the adoption of FAS 123R on the Company's Consolidated Statement of Income for fiscal year 2006 is as follows (in thousands, except per share data):

	<u>2006</u>
Stock-based compensation expense included in general and administrative expenses	\$ 374
Tax benefit	(148)
Stock-based compensation expense related to employee stock options, net of tax	<u>\$ 226</u>
Effect of FAS 123R on basic earnings per share	\$ (0.01)
Effect of FAS 123R on diluted earnings per share	\$ (0.01)

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Prior to January 2, 2006, the Company recognized the cost of employee services received in exchange for equity instruments under the intrinsic value method in accordance with APB 25 and its related interpretations, which measured compensation cost as the excess, if any, of the quoted market price of the stock over the amount the employee must pay for the stock. Compensation expense for all of the Company's equity-based awards was measured on the date the shares were granted. Accordingly, in accordance with APB 25 compensation expense for stock option awards was not recognized in the Consolidated Statements of Income for fiscal years 2005 and 2004.

The following table reflects pro forma net income and earnings per share for the fiscal years ended January 1, 2006 and January 2, 2005, had the Company elected to recognize the cost of employee services received in exchange for equity instruments based on the grant date fair value of those instruments in accordance with FAS 123 (in thousands, except per share data).

	2005	2004
Net income — as reported	\$ 7,006	\$ 16,815
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(397)	(765)
Net income — pro forma	<u>\$ 6,609</u>	<u>\$ 16,050</u>
Basic earnings per share:		
As reported	\$ 0.49	\$ 1.19
Pro forma	<u>\$ 0.46</u>	<u>\$ 1.14</u>
Diluted earnings per share:		
As reported	\$ 0.47	\$ 1.15
Pro forma	<u>\$ 0.44</u>	<u>\$ 1.10</u>

The fair value of stock-based awards was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions for fiscal years ending 2006, 2005 and 2004, respectively:

	2006	2005	2004
Risk free interest rates	4.65%	3.96%	3.25%
Expected lives	3-4 years	3-7 years	3-7 years
Expected volatility	41%	39%	40%
Expected dividend	—	—	—

Expected volatilities are based on the historical and implied volatility of the Company's common stock. The Company uses historical data to estimate award exercises and employee terminations within the valuation model. The expected lives of the awards represents the period of time that awards granted are expected to be outstanding and is based on historical data and expected holding periods. The risk-free rate for the periods within the contractual life of the award is based on the rate for ten year U.S. Treasury Bonds. See Note 14.

**Recent Accounting Pronouncements**

In September 2006, the Financial Accounting Standards Board (FASB) issued FAS No. 157 (FAS 157), "Fair Value Measurements", which establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. FAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. FAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently

**THE GEO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

evaluating the impact this standard will have on its financial condition, results of operations, cash flows or disclosures.

In September 2006, the FASB issued FAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88 106, and 132(R)" (FAS 158). FAS 158 requires that the funded status of defined benefit postretirement plans be recognized on the Company's balance sheet, and changes in the funded status be reflected in comprehensive income, effective for fiscal years ending after December 15, 2006. The funded status is measured as the difference between plan assets at fair value and the benefit obligation (the projected benefit obligation for pension plans or the accumulated benefit obligation for other post-retirement benefit plans). The Company was required to recognize the funded status of its defined benefit post-retirement benefit plans in its financial statements for its fiscal year ended December 31, 2006. The adoption of this standard reduced comprehensive income by \$1.9 million as of December 31, 2006. FAS 158 also requires an entity to measure a defined benefit postretirement plan's assets and obligations that determine its funded status as of the end of the employer's fiscal year, and recognize changes in the funded status of a defined benefit postretirement plan in comprehensive income in the year in which the changes occur. Since the Company currently has a measurement date of December 31 for all plans, this provision will not have a material impact in the year of adoption.

In June, 2006 the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 clarifies, among other things, the accounting for uncertain income tax positions by prescribing a minimum probability threshold that a tax position must meet before a financial statement income tax benefit is recognized. The minimum threshold is defined as a tax position that based solely on its technical merits is more likely than not to be sustained upon examination by the relevant taxing authority. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. FIN 48 must be applied to all existing tax positions upon adoption. The cumulative effect of applying FIN 48 at adoption is required to be reported separately as an adjustment to the opening balance of retained earnings in the year of adoption. FIN 48 is required to be implemented at the beginning of a fiscal year and is effective for the Company for fiscal 2007. The Company is finalizing, but has not yet determined, the impact of adopting FIN 48 on the financial statements for fiscal 2007.

In September 2006, the SEC Office of the Chief Accountant and Divisions of Corporation Finance and Investment Management released Staff Accounting Bulletin Number 108 (SAB 108), "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements", which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. The transition provisions of SAB 108 permit a registrant to adjust retained earnings for the cumulative effect of immaterial errors relating to prior years. The Company was required to adopt SAB 108 in its current fiscal year and there was no impact to its financial statements as a result of adoption.

**2. Acquisition**

On November 4, 2005, the Company completed the acquisition of CSC, a Florida-based provider of privatized corrections/detention, community corrections and alternative sentencing services. The allocation of the purchase price for this transaction at January 1, 2006 was preliminary. During 2006, the Company received information from its independent valuation specialists and finalized the purchase price allocation related to property and equipment, other assets and capital lease obligations. This information resulted in an increase in goodwill of \$3.8 million net of tax. Additionally during 2006 the Company completed certain tax elections and finalized the purchase price allocation related to taxes for these elections. The Company is continuing to

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

review additional tax matters related to the acquisition that, when finalized, may result in additional purchase price adjustments.

In addition, during 2006, in connection with the CSC acquisition and related sale of Youth Services International (“YSI”), the Company received approximately \$2.0 million in additional sales proceeds, consisting of approximately \$1.5 million in cash and a \$0.5 million increase in the promissory note related to the final purchase price of YSI. This reduced goodwill by \$2.0 million. Finally, in 2006, the completion of certain tax elections related to the CSC acquisition decreased goodwill \$13.2 million. The Company expects to finalize additional tax elections related to a CSC subsidiary during first quarter 2007 which may result in additional adjustments to goodwill.

On October 13, 2006, the Company acquired United Kingdom based Recruitment Solutions International (RSI) for approximately \$2.3 million plus transaction related expenses. RSI is a privately-held provider of transportation services to The Home Office Nationality and Immigration Directorate. The acquisition of RSI did not materially impact 2006 results of operations.

As discussed in Note 1 above, the Company completed the acquisition of CPT on January 24, 2007. In connection with the acquisition, the Company acquired all of CPT’s assets and liabilities. Total assets at December 31, 2006 for CPT were approximately \$252.1 million consisting primarily of net property and equipment with a net book value of \$240.8 million. Total liabilities acquired were approximately \$42.4 million at December 31, 2006.

**3. Discontinued Operations**

The Company formerly had, through its Australian subsidiary, a contract with the Department of Immigration, Multicultural and Indigenous Affairs (“DIMIA”) for the management and operation of Australia’s immigration centers. In 2003, the contract was not renewed, and effective February 29, 2004, the Company completed the transition of the contract and exited the management and operation of the DIMIA centers. In accordance with the provisions related to discontinued operations specified within FAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets”, the accompanying consolidated financial statements and notes reflect the operations of DIMIA as a discontinued operation in all periods presented.

In New Zealand, the New Zealand Parliament in early 2005 repealed the law that permitted private prison operation resulting in the termination of the Company’s contract for the management and operation of the Auckland Central Remand Prison (“Auckland”). The Company has operated this facility since July 2000. The Company ceased operating the facility upon the expiration of the contract on July 13, 2005. The accompanying consolidated financial statements and notes reflect the operations of Auckland as a discontinued operation.

On January 1, 2006, the Company completed the sale of Atlantic Shores Hospital, a 72 bed private mental health hospital which the Company owned and operated since 1997 for approximately \$11.5 million. The Company recognized a gain on the sale of this transaction of approximately \$1.6 million or \$1.0 million net of tax. Pre-tax profit related to the 72 bed private mental health hospital was \$0.1 million, and \$(0.2) million in 2005 and 2004, respectively. The accompanying consolidated financial statements and notes reflect the operations of the hospital and the related sale as a discontinued operation.

The Company does not expect material future impacts related to these discontinued operations.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following are the revenues related to DIMIA, Auckland and Atlantic Shores Hospital for the periods presented (in thousands):

	<u>2006</u>	<u>2005</u> (In thousands)	<u>2004</u>
Revenues — DIMIA	\$ —	\$ 20	\$ 6,040
Revenues — Auckland	—	7,256	12,940
Revenues — Atlantic Shores	—	8,602	7,614

**4. Property and Equipment**

Property and equipment consist of the following at fiscal year end:

	<u>Useful Life (Years)</u>	<u>2006</u> (In thousands)	<u>2005</u> (In thousands)
Land	—	\$ 12,911	\$ 6,195
Buildings and improvements	2 to 40	249,079	258,008
Leasehold improvements	1 to 15	54,000	45,356
Equipment	3 to 10	42,243	32,541
Furniture and fixtures	3 to 7	7,326	9,309
		<u>\$ 365,559</u>	<u>\$ 351,409</u>
Less accumulated depreciation and amortization		<u>(78,185)</u>	<u>(69,173)</u>
		<u>\$ 287,374</u>	<u>\$ 282,236</u>

At December 31, 2006, the Company had \$18.2 million of assets recorded under capital leases including \$17.5 million related to buildings and improvements, \$0.6 million related to equipment and \$0.1 million related to leasehold improvements with accumulated amortization of \$1.3 million. At January 1, 2006, the Company had \$17.3 million of assets recorded under capital leases including \$16.6 million related to buildings and improvements, \$0.6 million related to equipment and \$0.1 million related to leasehold improvements with accumulated amortization of \$0.1 million.

**5. Assets Held for Sale**

In conjunction with the acquisition of CSC, the Company acquired a building and assets associated with a program that had been discontinued by CSC in October 2003. The Company also owns land in Australia that it intends to sell. These assets meet the criteria to be classified as held for sale per the guidance of FAS No. 144 and have been recorded at their net realizable value of approximately \$1.6 million at December 31, 2006. No depreciation has been recorded related to these assets in accordance with FAS No. 144.

**6. Investment in Direct Finance Leases**

The Company's investment in direct finance leases relates to the financing and management of one Australian facility. The Company's wholly-owned Australian subsidiary financed the facility's development with long-term debt obligations, which are non-recourse to the Company.

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The future minimum rentals to be received are as follows:

Fiscal Year	Annual Repayment (In thousands)
2007	\$ 6,093
2008	6,142
2009	6,184
2010	6,235
2011	6,300
Thereafter	36,150
Total minimum obligation	\$ 67,104
Less unearned interest income	(25,667)
Less current portion of direct finance lease	(2,166)
Investment in direct finance lease	\$ 39,271

#### 7. Derivative Financial Instruments

Effective September 18, 2003, the Company entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. The Company has designated the swaps as hedges against changes in the fair value of a designated portion of the Notes due to changes in underlying interest rates. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the Notes. The agreements, which have payment and expiration dates and call provisions that coincide with the terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, the Company receives a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while the Company makes a variable interest rate payment to the same counterparties equal to the six-month London Interbank Offered Rate, ("LIBOR") plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. As of December 31, 2006 and January 1, 2006 the fair value of the swaps totaled approximately \$(1.7) million and \$(1.1) million and is included in other non-current assets or liabilities and as an adjustment to the carrying value of the Notes in the accompanying consolidated balance sheets. There was no material ineffectiveness of the Company's interest rate swaps for the fiscal year ended December 31, 2006.

The Company's Australian subsidiary is a party to an interest rate swap agreement to fix the interest rate on the variable rate non-recourse debt to 9.7%. The Company has determined the swap to be an effective cash flow hedge. Accordingly, the Company records the value of the interest rate swap in accumulated other comprehensive income (loss), net of applicable income taxes. The total value of the swap liability as of December 31, 2006 and January 1, 2006 was approximately \$3.2 million and \$(0.4) million, respectively, and is recorded as a component of other non-current assets and other non-current liabilities in the accompanying consolidated financial statements. There was no material ineffectiveness of the Company's interest rate swaps for the fiscal years presented. The Company does not expect to enter into any transactions during the next twelve months which would result in the reclassification into earnings or losses associated with this swap currently reported in accumulated other comprehensive income (loss).

#### 8. Goodwill and Other Intangible Assets, Net

As of December 31, 2006 and January 1, 2006, the Company had \$27.1 million and \$35.9 million of goodwill, respectively.



THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Changes in the Company's goodwill balances for 2006 were as follows (in thousands):

	Balance as of January 1, 2006	Goodwill resulting from Business Combinations	Foreign Currency Translation	Balance as of December 31, 2006
U.S. corrections	\$ 35,350	\$ (11,351)	\$ —	\$ 23,999
International services	546	2,487	42	3,075
<b>Total Segments</b>	<b>\$ 35,896</b>	<b>\$ (8,864)</b>	<b>\$ 42</b>	<b>\$ 27,074</b>

The U.S. corrections' goodwill decreased \$11.4 million during 2006 as a result of (i) a \$3.8 million increase in goodwill as a result of the finalization of purchase price allocation related to property and equipment, other assets and capital lease obligations of the CSC acquisition during the first quarter of 2006; (ii) \$2.0 million decrease in goodwill relating to additional cash proceeds and an increase in the promissory note related to the sale of YSI; (iii) a \$13.2 million decrease in goodwill due to the completion of certain tax elections related to the CSC acquisition and related sale of YSI.

International services goodwill increased \$2.5 million as a result of the completion of the RSI acquisition in October 2006. The Company has not finalized its purchase price allocation related to the RSI acquisition related to intangible assets, other assets, accrued liabilities and income taxes.

Intangible assets consisted of the following (in thousands):

	Useful Life in Years	2006	2005
Facility Management Contracts	7-17	\$ 15,050	\$ 15,050
Covenants not to compete	4	1,470	1,470
		<b>\$ 16,520</b>	<b>\$ 16,520</b>
Less Accumulated Amortization		(2,040)	(289)
		<b>\$ 14,480</b>	<b>\$ 16,231</b>

Amortization expense was \$1.8 million for the fiscal year ended 2006. Amortization is recognized on a straight-line basis over the estimated useful life of the intangible assets. Estimated amortization expense for fiscal 2007 through fiscal 2011 and thereafter are as follows:

Fiscal Year	Expense Amortization (In thousands)
2007	\$ 1,754
2008	1,754
2009	1,693
2010	1,387
2011	1,387
Thereafter	6,505
	<b>\$ 14,480</b>

**THE GEO GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

**9. Accrued Expenses**

Accrued expenses consisted of the following (dollars in thousands):

	<u>2006</u>	<u>2005</u>
Accrued interest	\$ 7,224	\$ 7,193
Accrued bonus	8,504	4,369
Accrued insurance	24,430	25,923
Accrued income taxes	7,792	882
Jena idle facility lease reserve	6,971	8,257
Other	22,754	23,553
<b>Total</b>	<b>\$ 77,675</b>	<b>\$ 70,177</b>

**10. Debt**

Debt consisted of the following (dollars in thousands):

	<u>2006</u>	<u>2005</u>
<b>Capital Lease Obligations</b>	<b>\$ 17,405</b>	<b>\$ 17,755</b>
<b>Senior Credit Facility:</b>		
Term loan	\$ —	\$ 74,813
<b>Senior 8<sup>1</sup>/<sub>4</sub>% Notes:</b>		
Notes Due in 2013	\$ 150,000	\$ 150,000
Discount on Notes	(3,376)	(3,735)
Swap on Notes	(1,736)	(1,074)
Total Senior 8 <sup>1</sup> / <sub>4</sub> % Notes	\$ 144,888	\$ 145,191
<b>Non Recourse Debt:</b>		
Non recourse debt	\$ 147,260	\$ 142,479
Discount on bonds	(3,707)	(4,493)
Total non recourse debt	143,553	137,986
Other debt	111	301
Total debt	\$ 305,957	\$ 376,046
Current portion of capital lease obligations, long-term debt and non-recourse debt	(12,685)	(8,441)
Capital lease obligations	(16,621)	(17,072)
Non recourse debt	(131,680)	(131,279)
Long term debt	<u>\$ 144,971</u>	<u>\$ 219,254</u>

***The Amended Senior Credit Facility***

On January 24, 2007, the Company completed the refinancing of its senior secured credit facility through the execution of a Third Amended and Restated Credit Agreement (the "Amended Senior Credit Facility"), by and among the Company, as Borrower, BNP Paribas, as Administrative Agent, BNP Paribas Securities Corp. as Lead Arranger and Syndication Agent, and the lenders who are, or may from time to time become, a party thereto. Previously, on September 14, 2005, the Company amended its senior secured credit facility to consist of a \$75 million, six-year term-loan bearing interest at LIBOR plus 2.00%, and a \$100 million, five-year

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

revolving credit facility bearing interest at LIBOR plus 2.00%. The Company used the borrowings under the Senior Credit Facility to fund general corporate purposes and to finance the acquisition of CSC for approximately \$62 million plus transaction-related costs. The acquisition of CSC closed in the fourth quarter of 2005. As of December 31, 2006, the Company had no borrowings outstanding under the term loan portion of the Senior Credit Facility, no amounts outstanding under the revolving portion of the Senior Credit Facility, and \$54.5 million outstanding in letters of credit under the revolving portion of the Senior Credit Facility. As of December 31, 2006 the Company had \$45.5 million available for borrowings under the revolving portion of the Senior Credit Facility.

The Amended Senior Credit Facility consists of a \$365 million 7-year term loan (the "Term Loan B") and a \$150 million 5-year revolver (the "Revolver"). The initial interest rate for the Term Loan B is LIBOR plus 1.5% and the Revolver bears interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, the Company used the \$365 million in borrowings under the Term Loan B to finance its acquisition of CPT, as further discussed below. The Company has no current borrowings under the Revolver and intends to use future borrowings thereunder for the purposes permitted under the Amended Senior Credit Facility, including to fund general corporate purposes.

Indebtedness under the Revolver bears interest in each of the instances below at the stated rate:

	<u>Interest Rate under the Revolver</u>
Borrowings	LIBOR plus 2.25% or base rate plus 1.25%.
Letters of Credit	1.50% to 2.50%.
Available Borrowings	0.38% to 0.5%.

The Amended Senior Credit Facility contains financial covenants which require us to maintain the following ratios, as computed at the end of each fiscal quarter for the immediately preceding four quarter-period:

<u>Period</u>	<u>Leverage Ratio</u>
Through December 30, 2008	Total leverage ratio £ 5.50 to 1.00
From December 31, 2008 through December 31, 2011	Reduces from 4.75 to 1.00, to 3.00 to 1.00
Through December 30, 2008	Senior secured leverage ratio £ 4.00 to 1.00
From December 31, 2008 through December 31, 2011	Reduces from 3.25 to 1.00, to 2.00 to 1.00
Four quarters ending June 29, 2008, to December 30, 2009	Fixed charge coverage ratio of 1.00, thereafter 1.10 to 1.00

All of the obligations under the Amended Senior Credit Facility are unconditionally guaranteed by each of the Company's existing material domestic subsidiaries. The Amended Senior Credit Facility and the related guarantees are secured by substantially all of the Company's present and future tangible and intangible assets and all present and future tangible and intangible assets of each guarantor, including but not limited to (i) a first-priority pledge of all of the outstanding capital stock owned by the Company and each guarantor, and (ii) perfected first-priority security interests in all of the Company's present and future tangible and intangible assets and the present and future tangible and intangible assets of each guarantor.

The Amended Senior Credit Facility contains certain customary representations and warranties, and certain customary covenants that restrict the Company's ability to, among other things (i) create, incur or assume any indebtedness, (ii) incur liens, (iii) make loans and investments, (iv) engage in mergers, acquisitions and asset sales, (v) sell its assets, (vi) make certain restricted payments, including declaring any cash dividends or redeem or repurchase capital stock, except as otherwise permitted, (vii) issue, sell or otherwise dispose of capital stock, (viii) transact with affiliates, (ix) make changes in accounting treatment, (x) amend or modify

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

the terms of any subordinated indebtedness, (xi) enter into debt agreements that contain negative pledges on its assets or covenants more restrictive than contained in the Amended Senior Credit Facility, (xii) alter the business it conducts, and (xiii) materially impair the Company's lenders' security interests in the collateral for its loans.

Events of default under the Amended Senior Credit Facility include, but are not limited to, (i) the Company's failure to pay principal or interest when due, (ii) the Company's material breach of any representations or warranty, (iii) covenant defaults, (iv) bankruptcy, (v) cross default to certain other indebtedness, (vi) unsatisfied final judgments over a specified threshold, (vii) material environmental claims which are asserted against it, and (viii) a change of control.

**Senior 8<sup>1</sup>/<sub>4</sub>% Notes**

To facilitate the completion of the purchase of the 12 million shares from Group 4 Falck, the Company amended the Senior Credit Facility and issued \$150.0 million aggregate principal amount, ten-year, 8<sup>1</sup>/<sub>4</sub>% senior unsecured notes, ("the Notes"), in a private placement pursuant to Rule 144A of the Securities Act of 1933, as amended. The Notes are general, unsecured, senior obligations. Interest is payable semi-annually on January 15 and July 15 at 8<sup>1</sup>/<sub>4</sub>%. The Notes are governed by the terms of an Indenture, dated July 9, 2003, between the Company and the Bank of New York, as trustee, referred to as the Indenture. Additionally, after July 15, 2008, the Company may redeem, at the Company's option, all or a portion of the Notes plus accrued and unpaid interest at various redemption prices ranging from 104.125% to 100.000% of the principal amount to be redeemed, depending on when the redemption occurs. The Indenture contains covenants that limit the Company's ability to incur additional indebtedness, pay dividends or distributions on its common stock, repurchase its common stock, and prepay subordinated indebtedness. The Indenture also limits the Company's ability to issue preferred stock, make certain types of investments, merge or consolidate with another company, guarantee other indebtedness, create liens and transfer and sell assets.

The Company is in compliance with all of the covenants of the Indenture governing the notes as of December 31, 2006. As of December 31, 2006, the Notes are reflected net of the original issuer's discount of approximately \$3.4 million which is being amortized over the ten year term of the Notes using the effective interest method.

**Non-Recourse Debt**

*South Texas Detention Complex:*

In February 2004, CSC was awarded a contract by the Department of Homeland Security, Bureau of Immigration and Customs Enforcement ("ICE") to develop and operate a 1,020 bed detention complex in Frio County Texas. South Texas Local Development Corporation ("STLDC") was created and issued \$49.5 million in taxable revenue bonds to finance the construction of the detention center. Additionally, CSC provided a \$5 million subordinated note to STLDC for initial development. The Company determined that it is the primary beneficiary of STLDC and consolidates the entity as a result. STLDC is the owner of the complex and entered into a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require the revenue from CSC's contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums are distributed to CSC to cover CSC's operating expenses and management fee. The bonds have a ten year term and are non-recourse to CSC and STLDC. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities resulting from its ownership. The bonds are fully insured and the sole source of payment for the bonds is the operating revenues of the center.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Included in current and non-current restricted cash is \$18.6 million as of December 31, 2006 as funds held in trust with respect to the STLDC for debt service and other reserves.

*Northwest Detention Center*

On June 30, 2003 CSC arranged financing for the construction of the Northwest Detention Center in Tacoma, Washington (the "Northwest Detention Center"), which CSC completed and opened for operation in April 2004. In connection with this financing, CSC of Tacoma LLC, a wholly owned subsidiary of CSC, issued a \$57 million note payable to the Washington Economic Development Finance Authority ("WEDFA"), an instrumentality of the State of Washington, which issued revenue bonds and subsequently loaned the proceeds of the bond issuance to CSC of Tacoma LLC for the purposes of constructing the Northwest Detention Center. The bonds are non-recourse to CSC and the loan from WEDFA to CSC of Tacoma, LLC is non-recourse to CSC. The proceeds of the loan were disbursed into escrow accounts held in trust to be used to pay the issuance costs for the revenue bonds, to construct the Northwest Detention Center and to establish debt service and other reserves.

Included in current and non-current restricted cash is \$11.1 million as of December 31, 2006 as funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.

*Australia*

In connection with the financing and management of one Australian facility, the wholly owned Australian subsidiary financed the facility's development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to us. As a condition of the loan, the Company is required to maintain a restricted cash balance of AUD 5.0 million, which, at December 31, 2006, was approximately \$3.9 million. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria.

Debt repayment schedules under capital lease obligations, long-term debt and non-recourse debt are as follows:

Fiscal Year	Capital Leases	Long Term Debt	Non Recourse	Total Annual Repayment
		(In thousands)		
2007	\$ 2,195	\$ 28	\$ 11,873	\$ 14,096
2008	2,167	28	12,571	14,766
2009	1,956	28	13,359	15,343
2010	1,932	27	14,104	16,063
2011	1,932	—	14,945	16,877
Thereafter	20,575	150,000	80,408	250,983
	<u>\$ 30,757</u>	<u>\$ 150,111</u>	<u>\$ 147,260</u>	<u>\$ 328,128</u>
Original issuer's discount	—	(3,376)	(3,707)	(7,083)
Current portion	(784)	(28)	(11,873)	(12,685)
Interest imputed on Capital Leases	(13,352)	—	—	(13,352)
Swap	—	(1,736)	—	(1,736)
Non current portion	<u>\$ 16,621</u>	<u>\$ 144,971</u>	<u>\$ 131,680</u>	<u>\$ 293,272</u>

At December 31, 2006 the Company also had outstanding seven letters of guarantee totaling approximately \$6.1 million under separate international facilities.

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

*Guarantees*

In connection with the creation of SACS, the Company entered into certain guarantees related to the financing, construction and operation of the prison. The Company guaranteed certain obligations of SACS under its debt agreements up to a maximum amount of 60.0 million South African Rand, or approximately \$8.6 million to SACS' senior lenders through the issuance of letters of credit. Additionally, SACS is required to fund a restricted account for the payment of certain costs in the event of contract termination. The Company has guaranteed the payment of 50% of amounts which may be payable by SACS into the restricted account and provided a standby letter of credit of 7.0 million South African Rand, or approximately \$1.0 million as security for the Company's guarantee. The Company's obligations under this guarantee expire upon SACS' release from its obligations in respect of the restricted account under its debt agreements. No amounts have been drawn against these letters of credit, which are included in the Company's outstanding letters of credit under its Revolving Credit Facility.

The Company has agreed to provide a loan of up to 20.0 million South African Rand, or approximately \$2.9 million (the "Standby Facility") to SACS for the purpose of financing SACS' obligations under its contract with the South African government. No amounts have been funded under the Standby Facility, and the Company does not anticipate that such funding will ever be required by SACS. The Company's obligations under the Standby Facility expire upon the earlier of full funding or SACS' release from its obligations under its debt agreements. The lenders' ability to draw on the Standby Facility is limited to certain circumstances, including termination of the contract.

The Company has also guaranteed certain obligations of SACS to the security trustee for SACS lenders. The Company secured its guarantee to the security trustee by ceding its rights to claims against SACS in respect of any loans or other finance agreements, and by pledging the Company's shares in SACS. The Company's liability under the guarantee is limited to the cession and pledge of shares. The guarantee expires upon expiration of the cession and pledge agreements.

In connection with a design, build, finance and maintenance contract, the Company guaranteed certain potential tax obligations of a special purpose entity. The potential estimated exposure of these obligations is CAD 2.5 million, or approximately \$2.2 million commencing in 2017. We have a liability of \$0.7 million and \$0.6 million related to this exposure as of December 31, 2006 and January 1, 2006, respectively. To secure this guarantee, the Company purchased Canadian dollar denominated securities with maturities matched to the estimated tax obligations in 2017 to 2021. The Company has recorded an asset and a liability equal to the current fair market value of those securities in its consolidated balance sheet.

The Company's wholly-owned Australian subsidiary financed the development of a facility and subsequent expansion in 2003, with long-term debt obligations, which are non-recourse to the Company and total \$50.0 million and \$40.3 million at December 31, 2006 and January 1, 2006, respectively. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria. As a condition of the loan, the Company is required to maintain a restricted cash balance of AUD 5.0 million, which, at December 31, 2006, was approximately \$3.9 million. This amount is included in restricted cash and the annual maturities of the future debt obligation is included in non recourse debt.

**11. Transactions with CentraCore Properties Trust ("CPT")**

On January 24, 2007, the Company completed its previously announced acquisition of CPT. As a result of the acquisition of CPT, the Company has no on going rent commitment for the facilities acquired as part of the Merger.

**THE GEO GROUP, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

During fiscal 1998, 1999 and 2000, CPT acquired 11 correctional and detention facilities operated by the Company. In 2006, CPT financed the 600-bed expansion of the Lawton Correctional Facility in Lawton Oklahoma for approximately \$20.0 million.

Simultaneous with the purchases, the Company entered into ten-year operating leases of these facilities from CPT. As the lease agreements are subject to contractual lease increases, the Company recorded operating lease expense for these leases on a straight-line basis over the term of the leases. Additionally, the lease contains three five-year renewal options based on fair market rental rates. The deferred unamortized net gain related to sales of the facilities to CPT at December 31, 2006, which is included in "Deferred Revenue" in the accompanying consolidated balance sheets is \$3.6 million with \$1.8 million short-term and \$1.8 million long-term. The balance of the deferred revenue as of December 31, 2006 will be accounted for in the purchase price allocation of the acquisition. Previously the gain was amortized over the ten-year lease terms. The Company recorded net rental expense related to the CPT leases of \$23.0 million, \$21.6 million and \$21.0 million in 2006, 2005 and 2004, respectively, excluding the Jena rental expense (See Note 12).

**12. Commitments and Contingencies**

The Company owns the 480-bed Michigan Correctional Facility in Baldwin, Michigan, referred to as the Michigan Facility. The Company operated the Michigan Facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. Separately, the Company leased the Michigan Facility, as lessor, to the State, as lessee, under a lease with an initial term of 20 years followed by two five-year options. In September 2005, the Governor of the State of Michigan closed the Michigan Facility and terminated the Company's management contract with the MDOC. In October 2005, the State of Michigan also sought to terminate its lease for the Michigan Facility. The Company believes that the State did not have the right to unilaterally terminate the Michigan Facility lease. As a result, in November 2005, the Company filed a lawsuit against the State to enforce the Company's rights under the lease. On February 24, 2006, the Ingham County Circuit Court, the trial court with jurisdiction over the case, granted summary judgment in favor of the State and against the Company and granted the Company leave to amend the complaint. The Company filed an amended complaint and on September 13, 2006, the trial court granted summary judgment on the amended complaint in favor of the State and against the Company. The Company has filed a notice of appeal and is proceeding with the appeal. The Company reviewed the Michigan Facility for impairment in accordance with FAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", and recorded an impairment charge in the fourth quarter of 2005 for \$20.9 million based on an independent appraisal of fair market value. The book value of the Michigan Facility at December 31, 2006 is \$12.6 million.

In 2005, the Company's equity affiliate, SACS, recognized a one time tax benefit of \$2.1 million related to a change in South African Tax law applicable to companies in a qualified Public Private Partnership ("PPP") with the South African Government. The tax law change had the effect that beginning in 2005 government revenues earned under the PPP are exempt from South African taxation. The one time tax benefit in part related to deferred tax liabilities that were eliminated during 2005 as a result of the change in the tax law. In February 2007 the South African legislature passed legislation that has the effect of removing the exemption from taxation on government revenues. The law change will impact the equity in earnings of affiliate beginning in 2007. The Company is in the process of fully assessing the impact of the new legislation. However, as a result of the new legislation, deferred tax liabilities will have to be established at the applicable tax rate of 29%. This is estimated to result in a one time tax charge of up to \$2.3 million in the first quarter of 2007.

During 2000, the Company's management contract at the 276-bed Jena Juvenile Justice Center in Jena, Louisiana, which is included in the U.S. corrections segment, was discontinued by the mutual agreement of the parties. Despite the discontinuation of the management contract, the Company remains responsible for

## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

payments on the Company's underlying lease of the inactive facility with CPT through January 2010. During the third quarter of 2005, the Company determined that the alternative uses being pursued were no longer probable and as a result revised its estimated sublease income and recorded an operating charge of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010 for a total reserve of \$8.6 million. This \$4.3 million charge is included in the caption "Operating Expenses" in the Consolidated Statement of Income for the fiscal year ended January 1, 2006. The balance of the reserve at December 31, 2006 of \$7.0 million will be included in the purchase price allocation of the acquisition of CPT.

**Operating Leases**

The Company leases correctional facilities, office space, computers and vehicles under non-cancelable operating leases expiring between 2007 and 2013. The future minimum commitments under these leases, exclusive of lease commitments related to CPT, are as follows:

<u>Fiscal Year</u>	<u>Annual Rental</u> <u>(In thousands)</u>
2007	\$ 10,112
2008	9,805
2009	7,325
2010	4,645
2011	2,984
Thereafter	8,037
	<u>\$ 42,908</u>

Rent expense was approximately \$25.7 million, \$24.9 million, and \$14.4 million for fiscal 2006, 2005, and 2004 respectively.

**Litigation, Claims and Assessments**

On May 19, 2006, the Company, along with Corrections Corporation of America, referred to as CCA, were sued by an individual plaintiff in the Circuit Court of the Second Judicial Circuit for Leon County, Florida (Case No. 2005CA001884). The complaint alleges that, during the period from 1995 to 2004, the Company and CCA overbilled the State of Florida by an amount of at least \$12.7 million by submitting to the State false claims for various items relating to (i) repairs, maintenance and improvements to certain facilities which the Company operates in Florida, (ii) the Company's staffing patterns in filling vacant security positions at those facilities, and (iii) the Company's alleged failure to meet the conditions of certain waivers granted to the Company by the State of Florida from the payment of liquidated damages penalties relating to the Company's staffing patterns at those facilities. The portion of the complaint relating to the Company arises out of the Company's operations at the Company's South Bay and Moore Haven, Florida correctional facilities. The complaint appears to be based largely on the same set of issues raised by a Florida Inspector General's Evaluation Report released in late June 2005, referred to as the IG Report, which alleged that the Company and CCA overbilled the State of Florida by over \$12 million.

Subsequently, the Florida Department of Management Services, referred to as the DMS, which is responsible for administering the Company's correctional contracts with the State of Florida, conducted a detailed analysis of the allegations raised by the IG Report which included a comprehensive written response to the IG Report which the Company's had prepared and delivered to the DMS. In September 2005, the DMS provided a letter to the Company stating that, although its review had not yet been fully completed, it did not find any indication of any improper conduct by the Company. On October 17, 2006, DMS provided a letter to the Company stating that its review had been completed. The Company and DMS then agreed to settle this



## THE GEO GROUP, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

matter for \$0.3 million. This amount is included in accrued expenses as of December 31, 2006. Although this determination is not dispositive of the recently initiated litigation, the Company believes it supports the Company's position that the Company has valid defenses in this matter. The Company will continue to investigate this matter and intends to defend the Company's rights vigorously. However, given the amounts claimed by the plaintiff and the fact that the nature of the allegations could cause adverse publicity to the Company, the Company believes that this matter, if settled unfavorably to the Company, could have a material adverse effect on the Company's financial condition and results of operations.

On September 15, 2006, a jury in an inmate wrongful death lawsuit in a Texas state court awarded a \$47.5 million verdict against the Company. Recently, the verdict was entered as a judgment against the Company in the amount of \$51.7 million. The lawsuit is being administered under the insurance program established by The Wackenhut Corporation, the Company's former parent company, in which the Company participated until October 2002. Policies secured by the Company under that program provide \$55 million in aggregate annual coverage. As a result, the Company believes it is fully insured for all damages, costs and expenses associated with the lawsuit and as such has not taken any reserves in connection with the matter. The lawsuit stems from an inmate death which occurred at the Company's former Willacy County State Jail in Raymondville, Texas, in April 2001, when two inmates at the facility attacked another inmate. Separate investigations conducted internally by the Company, The Texas Rangers and the Texas Office of the Inspector General exonerated the Company and its employees of any culpability with respect to the incident. The Company believes that the verdict is contrary to law and unsubstantiated by the evidence. The Company's insurance carrier has posted a superseded bond in the amount of approximately \$60.0 million to cover the judgment. On December 9, 2006, the trial court denied the Company's post trial motions and the Company filed a notice of appeal on December 18, 2006.

In June 2004, the Company received notice of a third-party claim for property damage incurred during 2002 and 2001 at several detention facilities that the Company's Australian subsidiary formerly operated. The claim relates to property damage caused by detainees at the detention facilities. The notice was given by the Australian government's insurance provider and did not specify the amount of damages being sought. In May 2005, the Company received additional correspondence indicating that the insurance provider still intends to pursue the claim against the Company's Australian subsidiary. Although the claim is in the initial stages and the Company is still in the process of fully evaluating its merits, the Company believes that it has defenses to the allegations underlying the claim and intends to vigorously defend the Company's rights with respect to this matter. While the insurance provider has not quantified its damage claim and the outcome of this matter discussed above cannot be predicted with certainty, based on information known to date, and management's preliminary review of the claim, the Company believes that, if settled unfavorably, this matter could have a material adverse effect on the Company's financial condition, results of operations and cash flows. The Company is uninsured for any damages or costs that it may incur as a result of this claim, including the expenses of defending the claim. The Company has accrued a reserve related to this claim based on its estimate of the most probable costs that may be incurred based on the facts and circumstances known to date, and the advice of its legal counsel.

The nature of the Company's business exposes it to various types of claims or litigation against the Company, including, but not limited to, civil rights claims relating to conditions of confinement and/or mistreatment, sexual misconduct claims brought by prisoners or detainees, medical malpractice claims, claims relating to employment matters (including, but not limited to, employment discrimination claims, union grievances and wage and hour claims), property loss claims, environmental claims, automobile liability claims, indemnification claims by the customers and other third parties, contractual claims and claims for personal injury or other damages resulting from contact with the Company's facilities, programs, personnel or prisoners, including damages arising from a prisoner's escape or from a disturbance or riot at a facility. Except as otherwise disclosed above, the Company does not expect the outcome of any pending claims or legal

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

proceedings net of applicable insurance, to have a material adverse effect on its financial condition, results of operations or cash flows.

**Collective Bargaining Agreements**

The Company had approximately 14% of its workforce covered by collective bargaining agreements at December 31, 2006. Collective bargaining agreements with nine percent of employees are set to expire in less than one year.

**13. Shareholders' Equity**

**Earnings Per Share**

The table below shows the amounts used in computing earnings per share ("EPS") in accordance with FAS No. 128 and the effects on income and the weighted average number of shares of potential dilutive common stock.

Fiscal Year	2006	2005 (In thousands, except per share data)	2004
Net income	\$ 30,031	\$ 7,006	\$ 16,815
Basic earnings per share:			
Weighted average shares outstanding	17,221	14,370	14,076
Per share amount	<u>\$ 1.74</u>	<u>\$ 0.49</u>	<u>\$ 1.19</u>
Diluted earnings per share:			
Weighted average shares outstanding	17,221	14,370	14,076
Effect of dilutive securities:			
Employee and director stock options and restricted stock	651	645	531
Weighted average shares assuming dilution	<u>17,872</u>	<u>15,015</u>	<u>14,607</u>
Per share amount	<u>\$ 1.68</u>	<u>\$ 0.47</u>	<u>\$ 1.15</u>

For fiscal 2006, options to purchase 1,500 shares of the Company's common stock with an exercise price of \$27.48 per share and an expiration date of July 2016 were outstanding at December 31, 2006, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

Of 222,750 restricted shares outstanding at December 31, 2006, 35,373 were included in the computation of diluted EPS because their effect would be dilutive.

For fiscal 2005, options to purchase 24,000 shares of the Company's common stock with exercise prices ranging from \$17.92 to \$21.47 per share and expiration dates between 2006 and 2014 were outstanding at January 1, 2006, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

For fiscal 2004, options to purchase 543,671 shares of the Company's common stock with exercise prices ranging from \$14.33 to \$17.92 per share and expiration dates between 2006 and 2014 were outstanding at January 2, 2005, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**Preferred Stock**

In April 1994, the Company's Board of Directors authorized 10 million shares of "blank check" preferred stock. The Board of Directors is authorized to determine the rights and privileges of any future issuance of preferred stock such as voting and dividend rights, liquidation privileges, redemption rights and conversion privileges.

**Rights Agreement**

On October 9, 2003, the Company entered into a rights agreement with EquiServe Trust Company, N.A., as rights agent. Under the terms of the rights agreement, each share of the Company's common stock carries with it one preferred share purchase right. If the rights become exercisable pursuant to the rights agreement, each right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series A Junior Participating Preferred Stock at a fixed price, subject to adjustment. Until a right is exercised, the holder of the right has no right to vote or receive dividends or any other rights as a shareholder as a result of holding the right. The rights trade automatically with shares of our common stock, and may only be exercised in connection with certain attempts to acquire the Company. The rights are designed to protect the interests of the Company and its shareholders against coercive acquisition tactics and encourage potential acquirers to negotiate with our board of directors before attempting an acquisition. The rights may, but are not intended to, deter acquisition proposals that may be in the interests of the Company's shareholders.

**14. Equity Incentive Plans**

The Company has three stock option plans in force at December 31, 2006: The Wackenhut Corrections Corporation 1994 Stock Option Plan (Second Plan), the 1995 Non-Employee Director Stock Option Plan (Third Plan) and the Wackenhut Corrections Corporation 1999 Stock Option Plan (Fourth Plan).

Under the Second Plan and Fourth Plan, the Company may grant options to key employees for up to 2,250,000 and 1,725,000 shares of common stock, respectively. Under the terms of these plans, the exercise price per share and vesting period is determined by the language of the plan. All options that have been granted under these plans are exercisable at the fair market value of the common stock at the date of the grant. Generally, the options vest and become exercisable ratably over a four-year period, beginning immediately on the date of the grant. However, the Board of Directors has exercised its discretion and has granted options that vest 100% immediately. All options under the Second Plan and Fourth Plan expire no later than ten years after the date of the grant. The Company had 300 options available to be granted at December 31, 2006 under the Fourth Plan.

Under the Third Plan, the Company may grant up to 165,000 shares of common stock to non-employee directors of the Company. Under the terms of this plan, options are granted at the fair market value of the common stock at the date of the grant, become exercisable immediately, and expire ten years after the date of the grant.

On May 4, 2006, the Board of Directors adopted and the shareholders approved The GEO Group, Inc. 2006 Stock Incentive Plan (the "2006 Plan"). Under the 2006 Plan, the Company may grant options or restricted shares to key employees and non-employee directors for up to 450,000 shares.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A summary of the activity of the Company's stock options plans is presented below:

	Shares (In thousands)	Wtd. Avg. Exercise Price	Wtd. Avg. Remaining Contractual Term	Aggregate Intrinsic Value (In thousands)
Outstanding at December 28, 2003	2,422	\$ 9.47		
Granted	240	14.67		
Exercised	(262)	6.07		
Forfeited/Cancelled	(13)	15.29		
Options outstanding at January 2, 2005	2,387	\$ 10.33	5.7	\$ 17,647
Granted	21	21.47		
Exercised	(276)	10.88		
Forfeited/Cancelled	(22)	11.13		
Options outstanding at January 1, 2006	2,110	\$ 10.35	4.9	\$ 10,778
Granted	26	15.42		
Exercised	(487)	11.10		
Forfeited/Cancelled	(333)	14.13		
Options outstanding at December 31, 2006	1,316	\$ 9.22	5.3	\$ 37,241
Options exercisable at December 31, 2006	1,195	\$ 8.95	5.1	\$ 34,141

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (i.e., the difference between the company's closing stock price on the last trading day of fiscal year 2006 and the exercise price, times the number of shares) that would have been received by the option holders had all option holders exercised their options on December 31, 2006. This amount changes based on the fair value of the company's stock. The total intrinsic value of options exercised during the year ended December 31, 2006 was \$9.5 million.

Cash received from stock options exercises for 2006, 2005 and 2004 was \$5.4 million, \$3.0 million and \$1.6 million, respectively. Tax benefits realized from tax deductions associated with option exercises and restricted stock activity for 2006, 2005 and 2004 totaled \$2.8 million, \$0.7 million and \$0.8 million, respectively.

The weighted average grant date fair value of stock options granted during the year ended December 31, 2006, was \$0.1 million.

At December 31, 2006, the Company had \$1.4 million of unrecognized compensation costs related to non-vested stock option awards that is expected to be recognized over a weighted average period of 6.95 years.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table summarizes information about the stock options outstanding at December 31, 2006:

Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Wtd. Avg. Remaining Contractual Life	Wtd. Avg. Exercise Price	Number Exercisable	Wtd. Avg. Exercise Price
\$5.25 — \$5.25	3,000	3.3	\$ 5.25	3,000	\$ 5.25
\$5.62 — \$5.62	188,625	3.1	5.62	188,625	5.62
\$6.20 — \$6.20	223,500	4.1	6.20	223,500	6.20
\$6.34 — \$7.97	95,213	6.1	6.39	77,753	6.40
\$9.33 — \$9.33	247,091	6.3	9.33	210,001	9.33
\$10.27 — \$10.27	328,500	5.1	10.27	328,500	10.27
\$10.60 — \$15.29	154,540	6.5	13.43	104,737	13.02
\$15.39 — \$15.66	53,850	7.3	15.54	38,250	15.52
\$21.47 — \$21.47	20,250	8.1	21.47	20,250	21.47
\$27.48 — \$27.48	1,500	9.6	27.48	300	27.48
	<u>1,316,069</u>			<u>1,194,916</u>	

**Restricted Stock**

On May 4, 2006, the Company granted 225,000 shares of non-vested restricted stock under the 2006 Plan to key employees and non-employee directors. Restricted shares are converted into shares of common stock upon vesting on a one-for-one basis. The cost of these awards is determined using the fair value of the Company's common stock on the date of the grant and compensation expense is recognized over the vesting period. The restricted shares that were granted during the year have a vesting period of four years, which begins one year from the date of grant. A summary of the activity of restricted stock during the fiscal year ended December 31, 2006 is as follows:

	Shares	Wtd. Avg. Grant date Fair value
Restricted stock outstanding at January 1, 2006	—	\$ —
Granted	225,000	26.13
Vested	—	—
Forfeited/Canceled	(2,250)	26.13
Restricted stock outstanding at December 31, 2006	<u>222,750</u>	26.13

As of December 31, 2006, there was \$4.9 million of unrecognized compensation cost related to unvested restricted shares. The Company recognized \$1.0 million in compensation expense related to the restricted shares during its fiscal year ended December 31, 2006.

**15. Retirement and Deferred Compensation Plans**

The Company has two noncontributory defined benefit pension plans covering certain of the Company's executives. Retirement benefits are based on years of service, employees' average compensation for the last five years prior to retirement and social security benefits. Currently, the plans are not funded. The Company purchased and is the beneficiary of life insurance policies for certain participants enrolled in the plans.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

In 2001, the Company established non-qualified deferred compensation agreements with three key executives. These agreements were modified in 2002, and again in 2003. The current agreements provide for a lump sum payment when the executives retire, no sooner than age 55.

In September, 2006 the FASB issued FAS No. 158, “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106, and 132(R),” (“SFAS No. 158”), which requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability on its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. FAS No. 158 requires an employer to measure the funded status of a plan as of its year-end date and is first effective for fiscal 2006 for the Company and is reflected in the following presentation of the Company’s defined benefit plans. Upon adoption of this standard the Company recorded a charge of \$1.9 million, net of tax, to other comprehensive income and a \$3.3 million credit to non-current liabilities.

FAS 158 also requires an entity to measure a defined benefit postretirement plan’s assets and obligations that determine its funded status as of the end of the employer’s fiscal year, and recognize changes in the funded status of a defined benefit postretirement plan in comprehensive income in the year in which the changes occur. Since the Company currently has a measurement date of December 31 for all plans, this provision will not have a material impact in the year of adoption.

The following table summarizes key information related to these pension plans and retirement agreements which includes information as required by FAS 158. The table illustrates the reconciliation of the beginning and ending balances of the benefit obligation showing the effects during the period attributable to each of the following: service cost, interest cost, plan amendments, termination benefits, actuarial gains and losses. The assumptions used in the Company’s calculation of accrued pension costs are based on market information and the Company’s historical rates for employment compensation and discount rates, respectively.

In accordance with FAS 158, the Company has also disclosed contributions and payment of benefits related to the plans. There were no assets in the plan at December 31, 2006 or January 1, 2006. All changes as a result of the adjustments to the accumulated benefit obligation are included below and shown net of tax in the Consolidated Statement of Shareholders’ Equity and Comprehensive Income. There were no significant transactions between the employer or related parties and the plan during the period.

	2006	2005
<b>Change in Projected Benefit Obligation</b>		
Projected Benefit Obligation, Beginning of Year	\$ 15,702	\$ 14,423
Service Cost	671	437
Interest Cost	546	542
Plan Amendments	—	—
Actuarial Gain	215	332
Benefits Paid	(36)	(32)
Projected Benefit Obligation, End of Year	<u>\$ 17,098</u>	<u>\$ 15,702</u>
<b>Change in Plan Assets</b>		
Plan Assets at Fair Value, Beginning of Year	\$ —	\$ —
Company Contributions	36	32
Benefits Paid	(36)	(32)
Plan Assets at Fair Value, End of Year	<u>\$ —</u>	<u>\$ —</u>
<b>Unfunded Status of the Plan</b>	<u>\$ (17,098)</u>	<u>\$ (15,702)</u>

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	2006	2005
<b>Amounts Recognized in Accumulated Other Comprehensive Income</b>		
Unrecognized Prior Service Cost	164	N/A
Unrecognized Net Loss	3,028	N/A
Accrued Pension Cost	\$ 3,192	\$ N/A
	<u>Fiscal 2006</u>	<u>Fiscal 2005</u>
<b>Components of Net Periodic Benefit Cost</b>		
Service Cost	\$ 671	\$ 437
Interest Cost	546	542
Amortization of:		
Unrecognized Prior Service Cost	39	936
Unrecognized Net Loss	144	121
Net Periodic Pension Cost	<u>\$ 1,400</u>	<u>\$ 2,036</u>
<b>Weighted Average Assumptions for Expense</b>		
Discount Rate	5.75%	5.50%
Expected Return on Plan Assets	N/A	N/A
Rate of Compensation Increase	5.50%	5.50%

The projected benefit liability for the three plans at December 31, 2006 are as follows, \$4.1 million for the executive retirement plan, \$1.4 million for the officer retirement plan and \$11.6 million for the three key executives' plans. Although these individuals have reached the eligible age for retirement the liabilities for the plans at year-end 2006 and 2005 is included in other long-term liabilities based on actuarial assumption and expected retirement payments.

The Company has established a deferred compensation agreement for non-employee directors, which allow eligible directors to defer their compensation. Participants may elect lump sum or monthly payments to be made at least one year after the deferral is made or at the time the participant ceases to be a director. The Company recognized total compensation expense under this plan of \$0.6 million, \$(0.1) and \$0.1 million for 2006, 2005, and 2004, respectively. There were no payouts under the plan in 2006 and 2005. The liability for the deferred compensation was \$1.1 million and \$0.5 million at year-end 2006 and 2005, respectively, and is included in "Other non current liabilities" in the accompanying consolidated balance sheets. Subsequent to December 31, 2006 the Company terminated the plan and paid the participants a lump sum amount.

The Company also has a non-qualified deferred compensation plan for employees who are ineligible to participate in its qualified 401(k) plan. Eligible employees may defer a fixed percentage of their salary, which earns interest at a rate equal to the prime rate less 0.75%. The Company matches employee contributions up to \$400 each year based on the employee's years of service. Payments will be made at retirement age of 65 or at termination of employment. The Company recognized expense of \$0.2 million, \$0.1 million and \$0.1 million in 2006, 2005, and 2004, respectively. The liability for this plan at year-end 2006 and 2005 was \$2.5 million and \$2.3 million, respectively, and is included in "Other non current liabilities" in the accompanying consolidated balance sheets.

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company expects to make the following benefit payments based on eligible retirement dates:

Fiscal Year	Pension Benefits (In thousands)
2007	\$ 11,947
2008	82
2009	138
2010	149
2011	152
2012-2016	1,829
	<u>\$ 14,297</u>

16. Business Segment and Geographic Information

*Operating and Reporting Segments*

The Company conducts its business through three reportable business segments: U.S. corrections segment; international services segment; and GEO Care segment. The Company has identified these three reportable segments to reflect the current view that the Company operates three distinct business lines, each of which constitutes a material part of its overall business. This treatment also reflects how the Company has discussed its business with investors and analysts. The U.S. corrections segment primarily encompasses U.S.-based privatized corrections and detention business. The International services segment primarily consists of privatized corrections and detention operations in South Africa, Australia and the United Kingdom. This segment also operates a recently acquired United Kingdom-based prisoner transportation business and reviews opportunities to further diversify into related foreign-based governmental-outsourced services on an ongoing basis. GEO Care segment, which is operated by the Company's wholly-owned subsidiary GEO Care, Inc., comprises privatized mental health and residential treatment services business, all of which is currently conducted in the U.S.

"Other" primarily consists of activities associated with the Company's construction business. The segment information presented in the prior periods has been reclassified to conform to the current presentation.

Fiscal Year	2006	2005 (In thousands)	2004
<b>Revenues:</b>			
U.S. corrections	\$ 612,810	\$ 473,280	\$ 455,947
International services	103,553	98,829	91,005
GEO Care	70,379	32,616	31,704
Other	74,140	8,175	15,338
Total revenues	<u>\$ 860,882</u>	<u>\$ 612,900</u>	<u>\$ 593,994</u>
<b>Depreciation and amortization:</b>			
U.S. corrections	\$ 20,848	\$ 12,980	\$ 11,298
International services	803	2,601	2,374
GEO Care	584	295	226
Other	—	—	—
Total depreciation and amortization	<u>\$ 22,235</u>	<u>\$ 15,876</u>	<u>\$ 13,898</u>



THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Fiscal Year	2006	2005 (In thousands)	2004
<b>Operating Income:</b>			
U.S. corrections	\$ 106,380	\$ 44,122	\$ 70,384
International services	8,682	10,595	13,587
GEO Care	5,996	2,317	588
Operating income from segments	121,058	57,034	84,559
Corporate Expenses	(56,268)	(48,958)	(45,879)
Other	(589)	(138)	311
Total operating income	<u>\$ 64,201</u>	<u>\$ 7,938</u>	<u>\$ 38,991</u>
<b>Segment assets:</b>			
U.S. corrections	\$ 457,545	\$ 464,813	
International services	79,641	60,827	
GEO Care	15,606	10,028	
Other	21,057	627	
Total segment assets	<u>\$ 573,849</u>	<u>\$ 536,295</u>	

Fiscal 2006 U.S. corrections operating expenses include a \$4.0 million reduction in general liability and workers compensation reserves offset by \$1.7 million in unbudgeted employee insurance reserve adjustments. Fiscal 2005 U.S. corrections segment operating expenses include net non cash charges of \$23.8 million consisting of a \$20.9 million impairment charge for the Michigan Correctional Facility and a \$4.3 million charge for the remaining obligation for the inactive Jena Facility offset by a \$1.3 million reduction in insurance reserves. Fiscal 2004 U.S. corrections segment operating expenses includes a net non cash credit of \$1.2 million, consisting of a \$4.2 million reduction in the Company's general liability, auto liability and workers' compensation insurance reserves offset by an additional provision for operating losses of approximately \$3.0 million related to the inactive facility in Jena, Louisiana.

*Pre-Tax Income Reconciliation*

Year Ended	2006	2005 (In thousands)	2004
Operating income from segments	\$ 121,058	\$ 57,034	\$ 84,559
Unallocated amounts:			
Corporate Expenses	(56,268)	(48,958)	(45,879)
Net Interest Expense	(17,544)	(13,862)	(12,570)
Costs related to early extinguishment of debt	(1,295)	(1,360)	(317)
Other	(589)	(138)	311
Income (loss) before income taxes, equity in earnings of affiliates, Discontinued operations and Minority interest	<u>\$ 45,362</u>	<u>\$ (7,284)</u>	<u>\$ 26,104</u>

**THE GEO GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

**Asset Reconciliation**

	2006	2005
Reportable segment assets	\$ 552,792	\$ 535,669
Cash	111,520	57,094
Deferred income tax	24,433	19,755
Restricted cash	33,651	26,366
Other	21,057	627
Total Assets	<u>\$ 743,453</u>	<u>\$ 639,511</u>

**Geographic Information**

The Company's international operations are conducted through the Company's wholly owned Australian subsidiaries, and one of the Company's joint ventures in South Africa, SACM. Through the Company's wholly owned subsidiary, GEO Group Australia Pty. Limited, the Company currently manages five correctional facilities, including one police custody center. Through the Company's joint venture SACM, the Company currently manages one facility.

Fiscal Year	2006	2005	2004
	(In thousands)		
<b>Revenues:</b>			
U.S. operations	\$ 757,329	\$ 514,071	\$ 502,989
Australia operations	82,156	83,335	75,947
South African operations	14,569	15,494	15,058
United Kingdom	6,828	—	—
Total revenues	<u>\$ 860,882</u>	<u>\$ 612,900</u>	<u>\$ 593,994</u>
<b>Long-lived assets:</b>			
U.S. operations	\$ 279,685	\$ 275,415	
Australia operations	6,445	6,243	
South African operations	642	578	
United Kingdom	602	—	
Total long-lived assets	<u>\$ 287,374</u>	<u>\$ 282,236</u>	

**Sources of Revenue**

The Company's derives most of its revenue from the management of privatized correction and detention facilities. The Company also derives revenue from the management of GEO Care facilities and from the construction and expansion of new and existing correctional, detention and GEO Care facilities. All of the Company's revenue is generated from external customers.

Fiscal Year	2006	2005	2004
	(In thousands)		
<b>Revenues:</b>			
Correction and detention	\$ 716,363	\$ 572,109	\$ 546,952
GEO Care	70,379	32,616	31,704
Construction	74,140	8,175	15,338
Total revenues	<u>\$ 860,882</u>	<u>\$ 612,900</u>	<u>\$ 593,994</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**Equity in Earnings of Affiliates**

Equity in earnings of affiliates for 2006, 2005 and 2004 include one of the joint ventures in South Africa, SACS. This entity is accounted for under the equity method.

A summary of financial data for SACS is as follows:

Fiscal Year	2006	2005	2004
	(In thousands)		
<b>Statement of Operations Data</b>			
Revenues	\$ 34,152	\$ 33,179	\$ 31,175
Operating income	13,301	11,969	11,118
Net income	3,124	2,866	—
<b>Balance Sheet Data</b>			
Current assets	15,396	13,212	14,250
Noncurrent assets	60,023	68,149	74,648
Current liabilities	5,282	4,187	5,094
Non current liabilities	63,919	73,645	83,474
Shareholders' equity	6,217	3,529	330

SACS commenced operation in fiscal 2002. Total equity in undistributed income/(loss) for SACS before income taxes, for fiscal 2006, 2005 and 2004 was \$3.3 million, \$0.9 million, and \$(0.1) million, respectively.

**Business Concentration**

Except for the major customers noted in the following table, no single customer provided more than 10% of the Company's consolidated revenues during fiscal 2006, 2005 and 2004:

Customer	2006	2005	2004
Various agencies of the U.S. Federal Government	30%	27%	27%
Various agencies of the State of Florida	5%	7%	12%

Concentration of credit risk related to accounts receivable is reflective of the related revenues.

**17. Income Taxes**

The United States and foreign components of income (loss) before income taxes, minority interest and equity income from affiliates are as follows:

	2006	2005	2004
	(In thousands)		
<b>Income (loss) before income taxes, minority interest, equity earnings in affiliates, and discontinued operations</b>			
United States	\$ 32,968	\$ (20,395)	\$ 9,627
Foreign	12,394	13,111	16,477
	<u>45,362</u>	<u>(7,284)</u>	<u>26,104</u>
<b>Discontinued operations:</b>			
Income (loss) from operation of discontinued business	(428)	2,022	(529)
Total	<u>\$ 44,934</u>	<u>\$ (5,262)</u>	<u>\$ 25,575</u>

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Taxes on income (loss) consist of the following components:

	2006	2005 (In thousands)	2004
<b>Federal income taxes:</b>			
Current	\$ 15,876	\$ (4,146)	\$ (72)
Deferred	(4,635)	(4,151)	2,050
	<u>11,241</u>	<u>(8,297)</u>	<u>1,978</u>
<b>State income taxes:</b>			
Current	2,667	(714)	643
Deferred	(36)	(756)	469
	<u>2,631</u>	<u>(1,470)</u>	<u>1,112</u>
<b>Foreign:</b>			
Current	3,042	(3,304)	4,226
Deferred	(409)	1,245	915
	<u>2,633</u>	<u>(2,059)</u>	<u>5,141</u>
<b>Total U.S. and foreign</b>	<u>16,505</u>	<u>(11,826)</u>	<u>8,231</u>
<b>Discontinued operations:</b>			
Income from operations of discontinued business	(151)	895	(181)
Total	<u>\$ 16,354</u>	<u>\$ (10,931)</u>	<u>\$ 8,050</u>

A reconciliation of the statutory U.S. federal tax rate (35.0%) and the effective income tax rate is as follows:

	2006	2005 (In thousands)	2004
<b>Continuing operations:</b>			
Provisions using statutory federal income tax rate	\$ 15,877	\$ (2,549)	\$ 9,136
State income taxes, net of federal tax benefit	1,466	(907)	723
Australia consolidation benefit	(228)	(6,460)	—
Basis difference PCG stock	—	—	(3,351)
UK Tax Benefit	(977)	—	—
Section 965 benefit	—	(1,704)	(197)
Non-performance based compensation	—	—	1,417
Other, net	367	(206)	503
Total continuing operations	<u>16,505</u>	<u>(11,826)</u>	<u>8,231</u>
<b>Discontinued operations:</b>			
Taxes from operations of discontinued business	(151)	895	(181)
Provision (benefit) for income taxes	<u>\$ 16,354</u>	<u>\$ (10,931)</u>	<u>\$ 8,050</u>

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The components of the net current deferred income tax asset (liability) at fiscal year end are as follows:

	2006	2005
	(In thousands)	
Book revenue not yet taxed	\$ (284)	\$ (260)
Deferred revenue	706	574
Uniforms	(337)	(158)
Deferred loan costs	301	945
Other, net	(26)	6
Allowance for doubtful accounts	357	211
Accrued vacation	4,938	4,753
Accrued liabilities	13,837	13,684
<b>Total asset (liability)</b>	<b>\$ 19,492</b>	<b>\$ 19,755</b>

The components of the net non-current deferred income tax asset (liability) at fiscal year end are as follows:

	2006	2005
	(In thousands)	
Capital losses	\$ —	\$ 5,945
Depreciation	109	(2,241)
Deferred loan costs	2,774	2,568
Deferred revenue	1,000	1,841
Bond Discount	(1,431)	(1,746)
Net operating losses	3,162	3,499
Tax credits	625	815
Intangible assets	(5,232)	(6,013)
Accrued liabilities	651	762
Deferred compensation	7,003	6,031
Residual U.S. tax liability on unrepatriated foreign earnings	(2,026)	(4,754)
Prepaid Lease	880	—
Other, net	409	261
Valuation allowance	(2,983)	(9,053)
<b>Total asset (liability)</b>	<b>\$ 4,941</b>	<b>\$ (2,085)</b>

In accordance with SFAS No. 109, Accounting for Income Taxes, deferred income taxes should be reduced by a valuation allowance if it is not more likely than not that some portion or all of the deferred tax assets will be realized. On a periodic basis, management evaluates and determines the amount of the valuation allowance required and adjusts such valuation allowance accordingly. At fiscal year end 2006 and 2005, the Company has recorded a valuation allowance of approximately \$3.0 million and \$9.1 million, respectively. At the fiscal year end 2006 and 2005, the valuation allowance includes \$0.1 million and \$6.9 million, respectively reported as part of purchase accounting relating to deferred tax assets for capital losses, federal and state net operating losses and charitable contribution carryforwards from the CSC acquisition. Current accounting pronouncements provide that a reduction of a valuation allowance related to tax assets recorded as part of purchase accounting are to reduce goodwill. At fiscal year end 2005 a full valuation allowance was provided against capital losses. Certain tax elections made during the 3rd quarter of 2006 in connection with the CSC acquisition and related sale of Youth Services International, Inc. "YSI" changed the character of tax losses

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

associated with the transactions. As a result tax losses were carried back and resulted in a federal tax refund of \$13.2 million which reduced goodwill. At fiscal year end 2006 there are no capital loss carryforwards and consequently the related valuation allowance was reduced by \$5.9 million. At fiscal year end 2006 and 2005 a partial valuation allowance was provided against net operating losses from the acquisition. At fiscal year end 2005 a partial valuation allowance was also provided against certain charitable loss carryforwards that required further investigation. The remaining valuation allowance of \$2.9 million and \$2.2 million, for 2006 and 2005, respectively, relates to deferred tax assets for foreign net operating losses and state tax credits unrelated to the CSC acquisition.

At fiscal year end 2006, the Company had \$2.2 million of net operating loss carryforwards from the CSC acquisition, which begin to expire in 2020. The utilization of these capital and net operating loss carryforwards are subject to annual usage limitations pursuant to Internal Revenue Code Section 382.

Also at fiscal year end 2006 the Company had \$7.5 million of foreign operating losses which carry forward indefinitely and state tax credits which begin to expire in 2007. The Company has recorded a full valuation allowance against these deferred tax assets.

During the fourth quarter the Company's Australian, South African and UK subsidiaries made dividend distributions in excess of their 2006 earnings in anticipation of the completion of the CPT acquisition which was consummated on January 24th, 2007. Residual US taxes in excess of foreign tax credits related to the dividend distributions of prior year foreign earnings are now currently due and to that extent are no longer reflected as part of the deferred tax liability for residual US taxes on unrepatriated foreign earnings.

During 2006 the Company's UK subsidiary received UK income tax refunds related to several tax years ending prior to 2003 totaling \$1 million. The Company provides for residual US taxes on unrepatriated foreign earnings when earned. The Company studied the impact of the UK tax refund on its foreign tax credit position under US tax law for the prior tax years at issue and concluded that it does not give rise to additional incremental US taxes that would work to offset the benefit of the UK tax refund.

As a result of tax legislation in Australia, the Company realized an income tax benefit of \$6.5 million in the fourth quarter 2005 and \$0.2 million in the third quarter 2006. The benefit is due to an elective tax step-up that in effect reestablishes tax basis that had previously been depreciated on an accelerated methodology. The permanent tax step-up was exempt from taxation and results in a decrease in the same amount in the deferred tax liability associated with the depreciable asset. Equity in earnings of affiliate in 2005 reflects a one time tax benefit of \$2.1 million related to a change in South African tax law applicable to companies in a qualified Public Private Partnership ("PPP") with the South African Government. The tax law change had the effect that beginning in 2005 Government revenues earned under the PPP are exempt from South African taxation. The one time tax benefit in part related to deferred tax liabilities that were eliminated during 2005 as a result of the change in the tax law. In February 2007 the South African legislature passed legislation that has the effect of removing the exemption from taxation on government revenues. The law change will impact the equity in earnings of affiliate beginning in 2007. The Company is in the process of fully assessing the impact of the new legislation. However, as a result of the new legislation, deferred tax liabilities will have to be established at the applicable rate of 29%. This is estimated to result in a one time tax charge of up to \$2.3 million in the first quarter of 2007.

On January 2, 2006, the Company adopted Statement of Financial Accounting Standards No. 123R, "Share-Based payment" (FAS 123R), which revises FAS 123, "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB25). SFAS 123R requires companies to recognize the cost of employee services received in exchange for awards of equity instruments based upon the grant date fair value of those awards. The Company adopted FAS 123R using the modified prospective method. Under this method the Company recognizes compensation cost for all share-based payments granted after January 1, 2006, plus any awards granted to employees prior to

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

January 2, 2006 that remain unvested at that time. The exercise of non-qualified stock options which have been granted under the Company's stock option plans give rise to compensation income which is includable in the taxable income of the applicable employees and deducted by the Company for federal and state income tax purposes. Such compensation income results from increases in the fair market value of the Company's common stock subsequent to the date of grant. The Company has elected to use the transition method described in FASB Staff Position 123(R)-3 ("FSP FAS 123(R)-3"). In accordance with FSP FAS 123(R)-3, the tax benefit on awards that vested prior to January 2, 2006 but that were exercised on or after January 2, 2006 "Fully Vested Awards" are credited directly to additional paid-in-capital. On awards that vested on or after January 2, 2006 and that were exercised on or after January 2, 2006, "Partially vested Awards" the total tax benefit first reduces the related deferred tax asset associated with the compensation cost recognized under 123(R) and any excess tax benefit, if any, is credited to additional paid-in capital. Special considerations apply and which are addressed in the FSP FAS 123(R)-3, if the ultimate tax benefit upon exercise is less than the related deferred tax asset underlying the award. At fiscal year end 2006 the deferred tax asset related to unexercised stock options was \$0.1 million.

In the ordinary course of global business, there are transactions for which the ultimate tax outcome is uncertain, thus judgment is required in determining the worldwide provision for income taxes. The Company provides for income taxes on transactions based on its estimate of the probable liability. The Company adjusts its provision as appropriate for changes that impact its underlying judgments. Changes that impact provision estimates include such items as jurisdictional interpretations on tax filing positions based on the result of tax audits and general tax authority rulings.

**18. Selected Quarterly Financial Data (Unaudited)**

The Company's selected quarterly financial data is as follows (in thousands, except per share data):

	<u>First Quarter</u>	<u>Second Quarter</u>
<b>2006</b>		
Revenues	\$ 185,881	\$ 208,668
Operating income	\$ 12,462	\$ 15,957
Income from continuing operations	\$ 4,674	\$ 6,431
Loss from discontinued operations, net of tax	\$ (118)	\$ (113)
Basic earnings per share:		
Income from continuing operations	\$ 0.32	\$ 0.41
Loss from discontinued operations	\$ (0.01)	\$ (0.01)
Net income per share	\$ 0.31	\$ 0.40
Diluted earnings per share:		
Income from continuing operations	\$ 0.31	\$ 0.39
Loss from discontinued operations	\$ (0.01)	\$ (0.01)
Net income per share	\$ 0.30	\$ 0.39

THE GEO GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	<u>Third Quarter</u>	<u>Fourth Quarter</u>
Revenues	\$ 218,909	\$ 247,404
Operating income	\$ 16,985	\$ 18,797
Income from continuing operations	\$ 8,666	\$ 10,537
Loss from discontinued operations, net of tax	\$ (24)	\$ (22)
Basic earnings per share:		
Income from continuing operations	\$ 0.45	\$ 0.54
Loss from discontinued operations	\$ 0.00	\$ 0.00
Net income per share	\$ 0.45	\$ 0.54
Diluted earnings per share:		
Income from continuing operations	\$ 0.43	\$ 0.52
Loss from discontinued operations	\$ 0.00	\$ 0.00
Net income per share	\$ 0.43	\$ 0.52

	<u>First Quarter</u>	<u>Second Quarter</u>
<b>2005</b>		
Revenues	\$ 148,255	\$ 152,623
Operating income	\$ 7,373	\$ 7,588
Income from continuing operations	\$ 2,391	\$ 4,301
Income from discontinued operations, net of tax	\$ 505	\$ 173
Basic earnings per share:		
Income from continuing operations	\$ 0.17	\$ 0.30
Income from discontinued operations	\$ 0.03	\$ 0.01
Net income per share	\$ 0.20	\$ 0.31
Diluted earnings per share:		
Income from continuing operations	\$ 0.16	\$ 0.29
Income from discontinued operations	\$ 0.03	\$ 0.01
Net income per share	\$ 0.19	\$ 0.30

	<u>Third Quarter</u>	<u>Fourth Quarter(b)</u>
Revenues	\$ 147,148	\$ 164,874
Operating income (loss)	\$ 5,444	\$ (12,467)
Income (loss) from continuing operations	\$ 510(a)	\$ (1,323)(c)
Income (loss) from discontinued operations, net of tax	\$ (67)	\$ 516
Basic earnings per share:		
Income (loss) from continuing operations	\$ 0.04	\$ (0.09)
Income (loss) from discontinued operations	\$ (0.01)	\$ 0.03
Net income (loss) per share	\$ 0.03	\$ (0.06)
Diluted earnings per share:		
Income (loss) from continuing operations	\$ 0.03	\$ (0.09)
Income (loss) from discontinued operations	\$ (0.00)	\$ 0.04
Net income (loss) per share	\$ 0.03	\$ (0.05)



**THE GEO GROUP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

- 
- (a) Includes a \$4.3 million write-off for the Jena, Louisiana facility and a charge of approximately \$1.4 million related to the write-off of deferred financing fees from the extinguishment of debt.
  - (b) Includes operations of CSC from November 4, 2005 through January 1, 2006.
  - (c) Includes a \$20.9 million impairment charge for Michigan facility, a \$6.5 million tax benefit in Australia and \$2.0 million tax benefit in South Africa related to changes in law.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures**

**Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, referred to as the Exchange Act), as of the end of the period covered by this report. On the basis of this review, our management, including our Chief Executive Officer and our Chief Financial Officer, has concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective to give reasonable assurance that the information required to be disclosed in our reports filed with the Securities and Exchange Commission, or the SEC, under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and to ensure that the information required to be disclosed in the reports filed or submitted under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

It should be noted that the effectiveness of our system of disclosure controls and procedures is subject to certain limitations inherent in any system of disclosure controls and procedures, including the exercise of judgment in designing, implementing and evaluating the controls and procedures, the assumptions used in identifying the likelihood of future events, and the inability to eliminate misconduct completely. Accordingly, there can be no assurance that our disclosure controls and procedures will detect all errors or fraud. As a result, by its nature, our system of disclosure controls and procedures can provide only reasonable assurance regarding management's control objectives.

**Internal Control Over Financial Reporting**

**(a) Management's Annual Report on Internal Control Over Financial Reporting**

See "Item 8. — Financial Statements and Supplemental Data — Management's Report on Internal Control over Financial Reporting" for management's report on the effectiveness of our internal control over financial reporting as of December 31, 2006.

**(b) Attestation Report of the Registered Public Accounting Firm**

See "Item 8. — Financial Statements and Supplemental Data — Report of Independent Registered Certified Public Accountants" for the report of our independent registered public accounting firm on the effectiveness of our internal control over financial reporting as of December 31, 2006.

**(c) Changes in Internal Control over Financial Reporting**

Our management is responsible for reporting any changes in our internal control over financial reporting (as such terms is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Management believes that there have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information**

None.

**PART III**

**Items 10, 11, 12, 13 and 14**

The information required by Items 10, 11, 12 (except for the information required by Item 201(d) of Regulation S-K which is included in Part II, Item 5 of this report), 13 and 14 of Form 10-K will be contained in, and is incorporated by reference from, the proxy statement for our 2007 annual meeting of shareholders, which will be filed with the SEC pursuant to Regulation 14A within 120 days after the end of the fiscal year covered by this report.

**PART IV**

**Item 15. Exhibits, and Financial Statement Schedules**

(a)(1) *Financial Statements.*

The following consolidated financial statements of GEO are filed under Item 8 of Part II of this report:

Reports of Independent Registered Certified Public Accountants — Page 60

Consolidated Balance Sheets — December 31, 2006 and January 1, 2006 — Page 64

Consolidated Statements of Income — Fiscal years ended December 31, 2006, January 1, 2006 and January 2, 2005 — Page 63

Consolidated Statements of Cash Flows — Fiscal years ended December 31, 2006, January 1, 2006 and January 1, 2005 — Page 65

Consolidated Statements of Shareholders' Equity and Comprehensive Income — Fiscal years ended December 31, 2006, January 1, 2006, and January 2, 2005 — Page 66

Notes to Consolidated Financial Statements — Pages 67 through 104

(2) *Financial Statement Schedules.*

Schedule II — Valuation and Qualifying Accounts — Page 110

All other schedules specified in the accounting regulations of the Securities and Exchange Commission have been omitted because they are either inapplicable or not required.

(3) *Exhibits Required by Item 601 of Regulation S-K. The following exhibits are filed as part of this Annual Report:*

<u>Exhibit Number</u>	<u>Description</u>
2.1	— Agreement and Plan of Merger, dated as of September 19, 2006, among the Company, GEO Acquisition II, Inc. and CentraCore Properties Trust (incorporated herein by reference to Exhibit 2.1 of the Company's report on Form 8-K, filed on September 21, 2006)
3.1	— Amended and Restated Articles of Incorporation of the Company, dated May 16, 1994 (incorporated herein by reference to Exhibit 3.1 to the Company's registration statement on Form S-1, filed on May 24, 1994)
3.2	— Bylaws of the Company (incorporated herein by reference to Exhibit 3.2 to the Company's registration statement on Form S-1, filed on May 24, 1994)
4.1	— Indenture, dated July 9, 2003, by and between the Company and The Bank of New York, as Trustee, relating to 8 <sup>1</sup> / <sub>4</sub> % Senior Notes Due 2013 (incorporated herein by reference to Exhibit 4.1 to the Company's report on Form 8-K, filed on July 29, 2003)
4.2	— Registration Rights Agreement, dated July 9, 2003, by and among the Company Corporation and BNP Paribas Securities Corp., Lehman Brothers Inc., First Analysis Securities Corporation, SouthTrust Securities, Inc. and Comerica Securities, Inc. (incorporated herein by reference to Exhibit 4.2 to the Company's report on Form 8-K, filed on July 29, 2003)

<u>Exhibit Number</u>	<u>Description</u>
4.3	— Rights Agreement, dated as of October 9, 2003, between the Company and EquiServe Trust Company, N.A., as the Rights Agent (incorporated herein by reference to Exhibit 4.3 to the Company's report on Form 8-K, filed on July 29, 2003)
10.1	— Stock Option Plan (incorporated herein by reference to Exhibit 10.1 to the Company's registration statement on Form S-1, filed on May 24, 1994)†
10.2	— 1994 Stock Option Plan (incorporated herein by reference to Exhibit 10.2 to the Company's registration statement on Form S-1, filed on May 24, 1994)†
10.3	— Form of Indemnification Agreement between the Company and its Officers and Directors (incorporated herein by reference to Exhibit 10.3 to the Company's registration statement on Form S-1, filed on May 24, 1994)†
10.4	— Senior Officer Retirement Plan (incorporated herein by reference to Exhibit 10.4 to the Company's registration statement on Form S-1/A, filed on December 22, 1995)†
10.5	— Amendment to the Company's Senior Officer Retirement Plan (incorporated herein by reference to Exhibit 10.5 to the Company's report on Form 10-K, filed on March 23, 2005)†
10.6	— Director Deferral Plan (incorporated herein by reference to Exhibit 10.5 to the Company's registration statement on Form S-1/A, filed on December 22, 1995)†
10.7	— Senior Officer Incentive Plan (incorporated herein by reference to Exhibit 10.6 to the Company's registration statement on Form S-1/A, filed on December 22, 1995)†
10.8	— Form of Master Agreement to Lease between the Company and CPT Operating Partnership L.P. (incorporated herein by reference to Exhibit 10.2 to the Company's registration statement on Form S-11/A, filed on March 20, 1998)
10.9	— Form of Lease Agreement between CPT Operating Partnership L.P. and the Company (incorporated herein by reference to Exhibit 10.3 to the Company's registration statement on Form S-11/A, filed on March 20, 1998)
10.10	— Form of Right to Purchase Agreement between the Company and CPT Operating Partnership L.P. (incorporated herein by reference to Exhibit 10.4 to the Company's registration statement on Form S-11/A, filed on March 20, 1998)
10.11	— Form of Option Agreement between the Company and CPT Operating Partnership L.P. (incorporated herein by reference to Exhibit 10.5 to the Company's registration statement on Form S-11/A, filed on March 20, 1998)
10.12	— 1999 Stock Option Plan (incorporated herein by reference to Exhibit 10.12 to the Company's report on Form 10-K, filed on March 30, 2000)†
10.13	— Amended and Restated Employment Agreement, dated November 4, 2004, between the Company and Dr. George C. Zoley (incorporated herein by reference to Exhibit 10.1 to the Company's report on Form 10-Q, filed on November 4, 2004)†
10.14	— Amended and Restated Employment Agreement, dated November 4, 2004, between the Company and Wayne H. Calabrese (incorporated herein by reference to Exhibit 10.2 to the Company's report on Form 10-Q, filed on November 5, 2004)†
10.15	— Executive Employment Agreement, dated March 7, 2002, between the Company and John G. O'Rourke (incorporated herein by reference to Exhibit 10.17 to the Company's report on Form 10-Q, filed on May 15, 2002)†
10.16	— Executive Retirement Agreement, dated March 7, 2002, between the Company and Dr. George C. Zoley (incorporated herein by reference to Exhibit 10.18 to the Company's report on Form 10-Q, filed on May 15, 2002)†
10.17	— Executive Retirement Agreement, dated March 7, 2002, between the Company and Wayne H. Calabrese (incorporated herein by reference to Exhibit 10.19 to the Company's report on Form 10-Q, filed on May 15, 2002)†
10.18	— Executive Retirement Agreement, dated March 7, 2002, between the Company and John G. O'Rourke (incorporated herein by reference to Exhibit 10.20 to the Company's report on Form 10-Q, filed on May 15, 2002)†
10.19	— Amended Executive Retirement Agreement, dated January 17, 2003, by and between the Company and George C. Zoley (incorporated herein by reference to Exhibit 10.18 to the Company's report on Form 10-K, filed on March 20, 2003)†

[Table of Contents](#)

<u>Exhibit Number</u>	<u>Description</u>
10.20	— Amended Executive Retirement Agreement, dated January 17, 2003, by and between the Company and Wayne H. Calabrese (incorporated herein by reference to Exhibit 10.19 to the Company's report on Form 10-K, filed on March 20, 2003)†
10.21	— Amended Executive Retirement Agreement, dated January 17, 2003, by and between the Company and John G. O'Rourke (incorporated herein by reference to Exhibit 10.20 to the Company's report on Form 10-K, filed on March 20, 2003)†
10.22	— Senior Officer Employment Agreement, dated March 23, 2005, by and between the Company and John J. Bulfin (incorporated herein by reference to Exhibit 10.22 to the Company's report on Form 10-K, filed on March 23, 2005)*†
10.23	— Senior Officer Employment Agreement, dated March 23, 2005, by and between the Company and Jorge A. Dominicus (incorporated herein by reference to Exhibit 10.23 to the Company's report on Form 10-K, filed on March 23, 2005)*†
10.24	— Senior Officer Employment Agreement, dated March 23, 2005, by and between the Company and John M. Hurley (incorporated herein by reference to Exhibit 10.24 to the Company's report on Form 10-K, filed on March 23, 2005)*†
10.25	— Senior Officer Employment Agreement, dated March 23, 2005, by and between the Company and Donald H. Keens (incorporated herein by reference to Exhibit 10.25 to the Company's report on Form 10-K, filed on March 23, 2005)*†
10.26	— Office Lease, dated September 12, 2002, by and between the Company and Canpro Investments Ltd. (incorporated herein by reference to Exhibit 10.22 to the Company's report on Form 10-K, filed on March 20, 2003)
10.27	— Asset Purchase Agreement, December 9, 2005, by and between GEO Care, Inc., a Florida corporation and Atlantic Shores Hospital, LLC (incorporated herein by reference to Exhibit 10.28 to the Company's report on Form 10-K, filed on March 17, 2006)
10.28	— The GEO Group, Inc. 2006 Stock Incentive Plan*†
10.29	— Third Amended and Restated Credit Agreement, dated as of January 24, 2007, by and among The GEO Group, Inc., as Borrower, BNP Paribas, as Administrative Agent, BNP Paribas Securities Corp. as Lead Arranger and Syndication Agent, and the lenders who are, or may from time to time become, a party thereto (incorporated herein by reference to Exhibit 10.1 to the Company's report on Form 8-K, filed on January 30, 2007)
10.30	— Amendment No. 1 to the Third Amended and Restated Credit Agreement, dated as of January 31, 2007, between The GEO Group, Inc., as Borrower, and BNP Paribas, as Lender and as Administrative Agent (incorporated herein by reference to Exhibit 10.1 to the Company's report on Form 8-K, filed on February 6, 2007)
10.31	— Amendment No. 2 to the Third Amended and Restated Credit Agreement, dated as of January 31, 2007, between The GEO Group, Inc., as Borrower, and BNP Paribas, as Lender and as Administrative Agent (incorporated herein by reference to Exhibit 10.1 to the Company's report on Form 8-K, filed on February 20, 2007)
21.1	— Subsidiaries of the Company*
23.1	— Consent of Grant Thornton LLP, independent registered certified public accountants
23.2	— Consent of Ernst & Young LLP, independent registered certified public accountants*
31.1	— Rule 13a-14(a) Certification in accordance with Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	— Rule 13a-14(a) Certification in accordance with Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	— Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
32.2	— Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*

\* Filed herewith.

† Management contract or compensatory plan, contract or agreement as defined in Item 402(a)(3) of Regulation S-K.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE GEO GROUP, INC.

/s/ JOHN G. O'ROURKE

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John G. O'Rourke  
Senior Vice President of Finance &  
Chief Financial Officer

Date: March 2, 2007

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

Signature	Title	Date
<hr/> <p>/s/ George C. Zoley George C. Zoley</p>	Chairman of the Board & Chief Executive Officer (principal executive officer)	March 2, 2007
<hr/> <p>/s/ John G. O'Rourke John G. O'Rourke</p>	Senior Vice President of Finance & Chief Financial Officer (principal financial officer)	March 2, 2007
<hr/> <p>/s/ Brian R. Evans Brian R. Evans</p>	Chief Accounting Officer & Controller (principal accounting officer)	March 2, 2007
<hr/> <p>/s/ Wayne H. Calabrese Wayne H. Calabrese</p>	Vice Chairman of the Board, President & Director	March 2, 2007
<hr/> <p>/s/ Norman A. Carlson Norman A. Carlson</p>	Director	March 2, 2007
<hr/> <p>/s/ Anne N. Foreman Anne N. Foreman</p>	Director	March 2, 2007
<hr/> <p>/s/ John M. Palms John M. Palms</p>	Director	March 2, 2007
<hr/> <p>/s/ Richard H. Glanton Richard H. Glanton</p>	Director	March 2, 2007
<hr/> <p>/s/ John M. Perzel John M. Perzel</p>	Director	March 2, 2007

## THE GEO GROUP, INC.

SCHEDULE II  
VALUATION AND QUALIFYING ACCOUNTS  
For the Fiscal Years Ended December 31, 2006, January 1, 2006, and January 2, 2005

<u>Description</u>	<u>Balance at Beginning of Period</u>	<u>Charged to Cost and Expenses</u>	<u>Charged to Other Accounts (In thousands)</u>	<u>Deductions, Actual Charge-Offs</u>	<u>Balance at End of Period</u>
<b>YEAR ENDED DECEMBER 31, 2006:</b>					
Allowance for doubtful accounts	\$ 224	\$ 762	\$ —	\$ (60)	\$ 926
<b>YEAR ENDED JANUARY 1, 2006:</b>					
Allowance for doubtful accounts	\$ 907	\$ —	\$ —	\$ (683)	\$ 224
<b>YEAR ENDED JANUARY 2, 2005:</b>					
Allowance for doubtful accounts	\$ 954	\$ 229	\$ —	\$ (276)	\$ 907
<b>YEAR ENDED DECEMBER 31, 2006:</b>					
Asset Replacement Reserve	\$ 723	\$ 258	\$ —	\$ (213)	\$ 768
<b>YEAR ENDED JANUARY 1, 2006:</b>					
Asset Replacement Reserve	\$ 614	\$ 290	\$ —	\$ (181)	\$ 723
<b>YEAR ENDED JANUARY 2, 2005:</b>					
Asset Replacement Reserve	\$ 417	\$ 465	\$ —	\$ (268)	\$ 614

**THE GEO GROUP, INC.  
2006 STOCK INCENTIVE PLAN**

**1. ESTABLISHMENT, EFFECTIVE DATE AND TERM**

The GEO Group, Inc., a Florida corporation hereby establishes The GEO Group, Inc. 2006 Stock Incentive Plan. The Effective Date of the Plan shall be the date that the Plan was approved by the shareholders of GEO in accordance with the laws of the State of Florida or such later date as provided in the resolutions adopting the Plan; provided, however, no Award may be granted unless and until the Plan has been approved by the shareholders of GEO. Unless earlier terminated pursuant to Section 15(k) hereof, the Plan shall terminate on the tenth anniversary of the Effective Date. Capitalized terms used herein are defined in Annex A attached hereto.

**2. PURPOSE**

The purpose of the Plan is to enable GEO to attract, retain, reward and motivate Eligible Individuals by providing them with an opportunity to acquire or increase a proprietary interest in GEO and to incentivize them to expend maximum effort for the growth and success of the Company, so as to strengthen the mutuality of the interests between the Eligible Individuals and the shareholders of GEO.

**3. ELIGIBILITY**

Awards may be granted under the Plan to any Eligible Individual, as determined by the Committee from time to time, on the basis of their importance to the business of the Company pursuant to the terms of the Plan.

**4. ADMINISTRATION**

(a) *Committee.* The Plan shall be administered by the Committee, which shall have the full power and authority to take all actions, and to make all determinations not inconsistent with the specific terms and provisions of the Plan deemed by the Committee to be necessary or appropriate to the administration of the Plan, any Award granted or any Award Agreement entered into hereunder. The Committee may correct any defect or supply any omission or reconcile any inconsistency in the Plan or in any Award Agreement in the manner and to the extent it shall deem expedient to carry the Plan into effect as it may determine in its sole discretion. The decisions by the Committee shall be final, conclusive and binding with respect to the interpretation and administration of the Plan, any Award or any Award Agreement entered into under the Plan.

(b) *Delegation to Officers or Employees.* The Committee may designate officers or employees of the Company to assist the Committee in the administration of the Plan. The Committee may delegate authority to officers or employees of the Company to grant Awards and execute Award Agreements or other documents on behalf of the Committee in connection with the administration of the Plan, subject to whatever limitations or restrictions the Committee may impose and in accordance with applicable law.

(c) *Designation of Advisors.* The Committee may designate professional advisors to assist the Committee in the administration of the Plan. The Committee may employ such legal counsel, consultants, and agents as it may deem desirable for the administration of the Plan and may rely upon any advice and any computation received from any such counsel, consultant, or agent. The Company shall pay all expenses and costs incurred by the Committee for the engagement of any such counsel, consultant, or agent.

(d) *Participants Outside the U.S.* In order to conform with the provisions of local laws and regulations in foreign countries in which the Company operates, the Committee shall have the sole discretion to (i) modify the terms and conditions of the Awards granted under the Plan to Eligible Individuals located outside the United States; (ii) establish subplans with such modifications as may be necessary or advisable under the circumstances present by local laws and regulations; and (iii) take any action which it deems advisable to



comply with or otherwise reflect any necessary governmental regulatory procedures, or to obtain any exemptions or approvals necessary with respect to the Plan or any subplan established hereunder.

(e) *Liability and Indemnification.* No Covered Individual shall be liable for any action or determination made in good faith with respect to the Plan, any Award granted hereunder or any Award Agreement entered into hereunder. The Company shall, to the maximum extent permitted by applicable law and the Articles of Incorporation and Bylaws of GEO, indemnify and hold harmless each Covered Individual against any cost or expense (including reasonable attorney fees reasonably acceptable to the Company) or liability (including any amount paid in settlement of a claim with the approval of the Company), and amounts advanced to such Covered Individual necessary to pay the foregoing at the earliest time and to the fullest extent permitted, arising out of any act or omission to act in connection with the Plan, any Award granted hereunder or any Award Agreement entered into hereunder. Such indemnification shall be in addition to any rights of indemnification such individuals may have under applicable law or under the Articles of Incorporation or Bylaws of GEO. Notwithstanding anything else herein, this indemnification will not apply to the actions or determinations made by a Covered Individual with regard to Awards granted to such Covered Individual under the Plan or arising out of such Covered Individual's own fraud or bad faith.

#### 5. SHARES OF COMMON STOCK SUBJECT TO PLAN

(a) *Shares Available for Awards.* The Common Stock that may be issued pursuant to Awards granted under the Plan shall be treasury shares or authorized but unissued shares of the Common Stock. The total number of shares of Common Stock that may be issued pursuant to Awards granted under the Plan shall be the sum of Three Hundred Thousand (300,000) shares.

(b) *Maximum Shares Issuable During a Fiscal Year.* The maximum number of shares of Common Stock that may be issued under all Awards granted in a fiscal year shall not exceed three percent (3%) of GEO's maximum authorized and outstanding shares of Common Stock at any time during said fiscal year; provided, however, that (i) such limitation shall not include any substitute grants made in settlement of any awards under any other plan sponsored by GEO or substitute grants or equity assumed in connection with a corporate transaction, and (ii) any shares of Common Stock repurchased or redeemed by GEO after any Awards have been made which have been authorized by the Board shall nevertheless be deemed to be outstanding for purposes of calculating whether there has been a violation of this Section 5(b).

(c) *Certain Limitations on Specific Types of Awards.* The granting of Awards under this Plan shall be subject to the following limitations:

(i) With respect to the shares of Common Stock reserved pursuant to this Section, a maximum of One Hundred and Fifty Thousand (150,000) of such shares may be subject to grants of Incentive Stock Options;

(ii) With respect to the shares of Common Stock reserved pursuant to this Section, a maximum of One Hundred and Fifty Thousand (150,000) of such shares may be issued in connection with Awards, other than Stock Options and Stock Appreciation Rights, that are settled in Common Stock;

(iii) With respect to the shares of Common Stock reserved pursuant to this Section, a maximum of One Hundred and Fifty Thousand (150,000) of such shares may be subject to grants of Options or Stock Appreciation Rights to any one Eligible Individual during any one fiscal year;

(iv) With respect to the shares of Common Stock reserved pursuant to this Section, a maximum of One Hundred and Fifty Thousand (150,000) of such shares may be subject to grants of Performance Shares, Restricted Stock, and Awards of Common Stock to any one Eligible Individual during any one fiscal year; and

(v) The maximum value at Grant Date of grants of Performance Units which may be granted to any one Eligible Individual during any one fiscal year shall be \$1,000,000.

(d) *Reduction of Shares Available for Awards.* Upon the granting of an Award, the number of shares of Common Stock available under this Section hereof for the granting of further Awards shall be reduced as follows:

(i) In connection with the granting of an Option or Stock Appreciation Right, the number of shares of Common Stock shall be reduced by the number of shares of Common Stock subject to the Option or Stock Appreciation Right;

(ii) In connection with the granting of an Award that is settled in Common Stock, other than the granting of an Option or Stock Appreciation Right, the number of shares of Common Stock shall be reduced by the number of shares of Common Stock subject to the Award; and

(iii) Awards settled in cash shall not count against the total number of shares of Common Stock available to be granted pursuant to the Plan.

(e) *Cancelled, Forfeited, or Surrendered Awards.* Notwithstanding anything to the contrary in this Plan, if any Award is cancelled, forfeited or terminated for any reason prior to exercise or becoming vested in full, the shares of Common Stock that were subject to such Award shall, to the extent cancelled, forfeited or terminated, immediately become available for future Awards granted under the Plan as if said Award had never been granted; provided, however, that any shares of Common Stock subject to an Award which is cancelled, forfeited or terminated in order to pay the Exercise Price, purchase price or any taxes or tax withholdings on an Award shall not be available for future Awards granted under the Plan.

(f) *Recapitalization.* If the outstanding shares of Common Stock are increased or decreased or changed into or exchanged for a different number or kind of shares or other securities of GEO by reason of any recapitalization, reclassification, reorganization, stock split, reverse split, combination of shares, exchange of shares, stock dividend or other distribution payable in capital stock of GEO or other increase or decrease in such shares effected without receipt of consideration by GEO occurring after the Effective Date, an appropriate and proportionate adjustment shall be made by the Committee to (i) the aggregate number and kind of shares of Common Stock available under the Plan, (ii) the aggregate limit of the number of shares of Common Stock that may be granted pursuant to an Incentive Stock Option, (iii) the limits on the number of shares of Common Stock that may be granted to an Eligible Employee in any one fiscal year, (iv) the calculation of the reduction of shares of Common Stock available under the Plan, (v) the number and kind of shares of Common Stock issuable upon exercise (or vesting) of outstanding Awards granted under the Plan; (vi) the Exercise Price of outstanding Options granted under the Plan, and/or (vii) the number of shares of Common Stock subject to Awards granted to Non-Employee Directors under Section 10. No fractional shares of Common Stock or units of other securities shall be issued pursuant to any such adjustment under this Section 5(f), and any fractions resulting from any such adjustment shall be eliminated in each case by rounding downward to the nearest whole share or unit. Any adjustments made under this Section 5(f) with respect to any Incentive Stock Options must be made in accordance with Code Section 424.

## 6. OPTIONS

(a) *Grant of Options.* Subject to the terms and conditions of the Plan, the Committee may grant to such Eligible Individuals as the Committee may determine, Options to purchase such number of shares of Common Stock and on such terms and conditions as the Committee shall determine in its sole and absolute discretion. Each grant of an Option shall satisfy the requirements set forth in this Section.

(b) *Type of Options.* Each Option granted under the Plan may be designated by the Committee, in its sole discretion, as either (i) an Incentive Stock Option, or (ii) a Non-Qualified Stock Option. Options designated as Incentive Stock Options that fail to continue to meet the requirements of Code Section 422 shall be re-designated as Non-Qualified Stock Options automatically on the date of such failure to continue to meet such requirements without further action by the Committee. In the absence of any designation, Options granted under the Plan will be deemed to be Non-Qualified Stock Options.

(c) *Exercise Price.* Subject to the limitations set forth in the Plan relating to Incentive Stock Options, the Exercise Price of an Option shall be fixed by the Committee and stated in the respective Award Agreement,

provided that the Exercise Price of the shares of Common Stock subject to such Option may not be less than Fair Market Value of such Common Stock on the Grant Date, or if greater, the par value of the Common Stock.

(d) *Limitation on Repricing.* Unless such action is approved by GEO's shareholders in accordance with applicable law: (i) no outstanding Option granted under the Plan may be amended to provide an Exercise Price that is lower than the then-current Exercise Price of such outstanding Option (other than adjustments to the Exercise Price pursuant to Sections 5(d) and 12); (ii) the Committee may not cancel any outstanding Option and grant in substitution therefore new Awards under the Plan covering the same or a different number of shares of Common Stock and having an Exercise Price lower than the then-current Exercise Price of the cancelled Option (other than adjustments to the Exercise Price pursuant to Sections 5(f) and 12); and (iii) the Committee may not authorize the repurchase of an outstanding Option which has an Exercise Price that is higher than the then-current fair market value of the Common Stock (other than adjustments to the Exercise Price pursuant to Sections 5(f) and 12).

(e) *Limitation on Option Period.* Subject to the limitations set forth in the Plan relating to Incentive Stock Options, Options granted under the Plan and all rights to purchase Common Stock thereunder shall terminate no later than the tenth anniversary of the Grant Date of such Options, or on such earlier date as may be stated in the Award Agreement relating to such Option. In the case of Options expiring prior to the tenth anniversary of the Grant Date, the Committee may in its discretion, at any time prior to the expiration or termination of said Options, extend the term of any such Options for such additional period as it may determine, but in no event beyond the tenth anniversary of the Grant Date thereof.

(f) *Limitations on Incentive Stock Options.* Notwithstanding any other provisions of the Plan, the following provisions shall apply with respect to Incentive Stock Options granted pursuant to the Plan.

(i) *Limitation on Grants.* Incentive Stock Options may only be granted to Section 424 Employees. The aggregate Fair Market Value (determined at the time such Incentive Stock Option is granted) of the shares of Common Stock for which any individual may have Incentive Stock Options which first become vested and exercisable in any calendar year (under all incentive stock option plans of the Company) shall not exceed \$100,000. Options granted to such individual in excess of the \$100,000 limitation, and any Options issued subsequently which first become vested and exercisable in the same calendar year, shall automatically be treated as Non-Qualified Stock Options.

(ii) *Minimum Exercise Price.* In no event may the Exercise Price of a share of Common Stock subject an Incentive Stock Option be less than 100% of the Fair Market Value of such share of Common Stock on the Grant Date.

(iii) *Ten Percent Shareholder.* Notwithstanding any other provision of the Plan to the contrary, in the case of Incentive Stock Options granted to a Section 424 Employee who, at the time the Option is granted, owns (after application of the rules set forth in Code Section 424(d)) stock possessing more than ten percent of the total combined voting power of all classes of stock of GEO, such Incentive Stock Options (i) must have an Exercise Price per share of Common Stock that is at least 110% of the Fair Market Value as of the Grant Date of a share of Common Stock, and (ii) must not be exercisable after the fifth anniversary of the Grant Date.

(g) *Vesting Schedule and Conditions.* No Options may be exercised prior to the satisfaction of the conditions and vesting schedule provided for in the Award Agreement relating thereto. Except as otherwise provided by the Committee in an Award Agreement in its sole and absolute discretion, subject to Sections 10, 12 and 13 of the Plan, Options covered by any Award under this Plan that are subject solely to a future service requirement shall vest as follows: (i) 20% of the Options subject to an Award shall vest immediately upon the Grant Date; and (ii) the remaining 80% of the Options subject to an Award shall vest over the four-year period immediately following the Grant Date in equal annual increments of 20%, with one increment vesting on each anniversary date of the Grant Date.

(h) *Exercise.* When the conditions to the exercise of an Option have been satisfied, the Participant may exercise the Option only in accordance with the following provisions. The Participant shall deliver to GEO a

written notice stating that the Participant is exercising the Option and specifying the number of shares of Common Stock which are to be purchased pursuant to the Option, and such notice shall be accompanied by payment in full of the Exercise Price of the shares for which the Option is being exercised, by one or more of the methods provided for in the Plan. Said notice must be delivered to GEO at its principal office and addressed to the attention of John J. Bulfin, General Counsel, The GEO Group Inc., 621 NW 53rd Street, Suite 700, Boca Raton, Florida 33487. An attempt to exercise any Option granted hereunder other than as set forth in the Plan shall be invalid and of no force and effect.

(i) *Payment.* Payment of the Exercise Price for the shares of Common Stock purchased pursuant to the exercise of an Option shall be made by one of the following methods:

(i) by cash, certified or cashier's check, bank draft or money order;

(ii) through the delivery to GEO of shares of Common Stock which have been previously owned by the Participant for the requisite period necessary to avoid a charge to GEO's earnings for financial reporting purposes; such shares shall be valued, for purposes of determining the extent to which the Exercise Price has been paid thereby, at their Fair Market Value on the date of exercise; without limiting the foregoing, the Committee may require the Participant to furnish an opinion of counsel acceptable to the Committee to the effect that such delivery would not result in GEO incurring any liability under Section 16(b) of the Exchange Act; or

(iii) by any other method which the Committee, in its sole and absolute discretion and to the extent permitted by applicable law, may permit, including, but not limited to, any of the following: (A) through a "cashless exercise sale and remittance procedure" pursuant to which the Participant shall concurrently provide irrevocable instructions (1) to a brokerage firm approved by the Committee to effect the immediate sale of the purchased shares and remit to GEO, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate Exercise Price payable for the purchased shares plus all applicable federal, state and local income, employment, excise, foreign and other taxes required to be withheld by the Company by reason of such exercise and (2) to GEO to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale; or (B) by any other method as may be permitted by the Committee.

(j) *Termination of Employment, Disability or Death.* Unless otherwise provided in an Award Agreement, upon the termination of the employment or other service of a Participant with Company for any reason, all of the Participant's outstanding Options (whether vested or unvested) shall be subject to the rules of this paragraph. Upon such termination, the Participant's unvested Options shall expire. Notwithstanding anything in this Plan to the contrary, the Committee may provide, in its sole and absolute discretion, that following the termination of employment or other service of a Participant with the Company for any reason (i) any unvested Options held by the Participant that vest solely upon a future service requirement shall vest in whole or in part, at any time subsequent to such termination of employment or other service, and or (ii) a Participant or the Participant's estate, devisee or heir at law (whichever is applicable), may exercise an Option, in whole or in part, at any time subsequent to such termination of employment or other service and prior to the termination of the Option pursuant to its terms. Unless otherwise determined by the Committee, temporary absence from employment because of illness, vacation, approved leaves of absence or military service shall not constitute a termination of employment or other service.

(i) *Termination for Reason Other Than Cause, Disability or Death.* If a Participant's termination of employment or other service is for any reason other than death, Disability, Cause or a voluntary termination within ninety (90) days after occurrence of an event which would be grounds for termination of employment or other service by the Company for Cause, any Option held by such Participant, may be exercised, to the extent exercisable at termination, by the Participant at any time within a period not to exceed ninety (90) days from the date of such termination, but in no event after the termination of the Option pursuant to its terms.

(ii) *Disability.* If a Participant's termination of employment or other service with the Company is by reason of a Disability of such Participant, the Participant shall have the right at any time within a period

not to exceed one (1) year after such termination, but in no event after the termination of the Option pursuant to its terms, to exercise, in whole or in part, any vested portion of the Option held by such Participant at the date of such termination; *provided, however*, that if the Participant dies within such period, any vested Option held by such Participant upon death shall be exercisable by the Participant's estate, devisee or heir at law (whichever is applicable) for a period not to exceed one (1) year after the Participant's death, but in no event after the termination of the Option pursuant to its terms.

(iii) *Death*. If a Participant dies while in the employment or other service of the Company, the Participant's estate or the devisee named in the Participant's valid last will and testament or the Participant's heir at law who inherits the Option has the right, at any time within a period not to exceed one (1) year after the date of such Participant's death, but in no event after the termination of the Option pursuant to its terms, to exercise, in whole or in part, any portion of the vested Option held by such Participant at the date of such Participant's death.

(iv) *Termination for Cause*. In the event the termination is for Cause or is a voluntary termination within ninety (90) days after occurrence of an event which would be grounds for termination of employment or other service by the Company for Cause (without regard to any notice or cure period requirement), any Option held by the Participant at the time of such termination shall be deemed to have terminated and expired upon the date of such termination.

## 7. STOCK APPRECIATION RIGHTS

(a) *Grant of Stock Appreciation Rights*. Subject to the terms and conditions of the Plan, the Committee may grant to such Eligible Individuals as the Committee may determine, Stock Appreciation Rights, in such amounts and on such terms and conditions as the Committee shall determine in its sole and absolute discretion. Each grant of a Stock Appreciation Right shall satisfy the requirements as set forth in this Section.

(b) *Terms and Conditions of Stock Appreciation Rights*. Unless otherwise provided in an Award Agreement, the terms and conditions (including, without limitation, the limitations on the Exercise Price, exercise period, repricing and termination) of the Stock Appreciation Right shall be substantially identical (to the extent possible taking into account the differences related to the character of the Stock Appreciation Right) to the terms and conditions that would have been applicable under Section 6 above were the grant of the Stock Appreciation Rights a grant of an Option.

(c) *Exercise of Stock Appreciation Rights*. Stock Appreciation Rights shall be exercised by a Participant only by written notice delivered to the General Counsel of GEO, specifying the number of shares of Common Stock with respect to which the Stock Appreciation Right is being exercised.

(d) *Payment of Stock Appreciation Right*. Unless otherwise provided in an Award Agreement, upon exercise of a Stock Appreciation Right, the Participant or Participant's estate, devisee or heir at law (whichever is applicable) shall be entitled to receive payment, in cash, in shares of Common Stock, or in a combination thereof, as determined by the Committee in its sole and absolute discretion. The amount of such payment shall be determined by multiplying the excess, if any, of the Fair Market Value of a share of Common Stock on the date of exercise over the Fair Market Value of a share of Common Stock on the Grant Date, by the number of shares of Common Stock with respect to which the Stock Appreciation Rights are then being exercised. Notwithstanding the foregoing, the Committee may limit in any manner the amount payable with respect to a Stock Appreciation Right by including such limitation in the Award Agreement.

## 8. RESTRICTED STOCK

(a) *Grant of Restricted Stock*. Subject to the terms and conditions of the Plan, the Committee may grant to such Eligible Individuals as the Committee may determine, Restricted Stock, in such amounts and on such terms and conditions as the Committee shall determine in its sole and absolute discretion. Each grant of Restricted Stock shall satisfy the requirements as set forth in this Section.

(b) *Restrictions*. The Committee shall impose such restrictions on any Restricted Stock granted pursuant to the Plan as it may deem advisable including, without limitation; time based vesting restrictions, or the

attainment of Performance Goals. Except as otherwise provided by the Committee in an Award Agreement in its sole and absolute discretion, subject to Sections 10, 12 and 13 of the Plan, Restricted Stock covered by any Award under this Plan that are subject solely to a future service requirement shall vest over the four-year period immediately following the Grant Date in equal annual increments of 25%, with one increment vesting on each anniversary date of the Grant Date. Shares of Restricted Stock subject to the attainment of Performance Goals will be released from restrictions only after the attainment of such Performance Goals has been certified by the Committee in accordance with Section 9(c).

(c) *Certificates and Certificate Legend.* With respect to a grant of Restricted Stock, the Company may issue a certificate evidencing such Restricted Stock to the Participant or issue and hold such shares of Restricted Stock for the benefit of the Participant until the applicable restrictions expire. The Company may legend the certificate representing Restricted Stock to give appropriate notice of such restrictions. In addition to any such legends, each certificate representing shares of Restricted Stock granted pursuant to the Plan shall bear the following legend:

“The sale or other transfer of the shares of stock represented by this certificate, whether voluntary, involuntary, or by operation of law, are subject to certain terms, conditions, and restrictions on transfer as set forth in The GEO Group, Inc. 2006 Stock Incentive Plan (the “Plan”), and in an Agreement entered into by and between the registered owner of such shares and The GEO Group, Inc. (the “Company”), dated (the “Award Agreement”). A copy of the Plan and the Award Agreement may be obtained from the Secretary of the Company.”

(d) *Removal of Restrictions.* Except as otherwise provided in the Plan, shares of Restricted Stock shall become freely transferable by the Participant upon the lapse of the applicable restrictions. Once the shares of Restricted Stock are released from the restrictions, the Participant shall be entitled to have the legend required by paragraph (c) above removed from the share certificate evidencing such Restricted Stock and the Company shall pay or distribute to the Participant all dividends and distributions held in escrow by the Company with respect to such Restricted Stock.

(e) *Shareholder Rights.* Unless otherwise provided in an Award Agreement, until the expiration of all applicable restrictions, (i) the Restricted Stock shall be treated as outstanding, (ii) the Participant holding shares of Restricted Stock may exercise full voting rights with respect to such shares, and (iii) the Participant holding shares of Restricted Stock shall be entitled to receive all dividends and other distributions paid with respect to such shares while they are so held. If any such dividends or distributions are paid in shares of Common Stock, such shares shall be subject to the same restrictions on transferability and forfeitability as the shares of Restricted Stock with respect to which they were paid. Notwithstanding anything to the contrary, at the discretion of the Committee, all such dividends and distributions may be held in escrow by the Company (subject to the same restrictions on forfeitability) until all restrictions on the respective Restricted Stock have lapsed.

(f) *Termination of Service.* Unless otherwise provided in an Award Agreement, if a Participant’s employment or other service with the Company terminates for any reason, all unvested shares of Restricted Stock held by the Participant and any dividends or distributions held in escrow by GEO with respect to such Restricted Stock shall be forfeited immediately and returned to the Company. Notwithstanding this paragraph, all grants of Restricted Stock that vest solely upon the attainment of Performance Goals shall be treated pursuant to the terms and conditions that would have been applicable under Section 9(c) as if such grants of Restricted Stock were Awards of Performance Shares. Notwithstanding anything in this Plan to the contrary, the Committee may provide, in its sole and absolute discretion, that following the termination of employment or other service of a Participant with the Company for any reason, any unvested shares of Restricted Stock held by the Participant that vest solely upon a future service requirement shall vest in whole or in part, at any time subsequent to such termination of employment or other service.

## 9. PERFORMANCE SHARES AND PERFORMANCE UNITS

(a) *Grant of Performance Shares and Performance Units.* Subject to the terms and conditions of the Plan, the Committee may grant to such Eligible Individuals as the Committee may determine, Performance Shares

and Performance Units, in such amounts and on such terms and conditions as the Committee shall determine in its sole and absolute discretion. Each grant of a Performance Share or a Performance Unit shall satisfy the requirements as set forth in this Section.

(b) *Performance Goals.* Performance Goals will be based on one or more of the following criteria, as determined by the Committee in its absolute and sole discretion: (i) the attainment of certain target levels of, or a specified increase in, GEO's enterprise value or value creation targets; (ii) the attainment of certain target levels of, or a percentage increase in, GEO's after-tax or pre-tax profits including, without limitation, that attributable to GEO's continuing and/or other operations; (iii) the attainment of certain target levels of, or a specified increase relating to, GEO's operational cash flow or working capital, or a component thereof; (iv) the attainment of certain target levels of, or a specified decrease relating to, GEO's operational costs, or a component thereof (v) the attainment of a certain level of reduction of, or other specified objectives with regard to limiting the level of increase in all or a portion of bank debt or other of GEO's long-term or short-term public or private debt or other similar financial obligations of GEO, which may be calculated net of cash balances and/or other offsets and adjustments as may be established by the Committee; (vi) the attainment of a specified percentage increase in earnings per share or earnings per share from GEO's continuing operations; (vii) the attainment of certain target levels of, or a specified percentage increase in, GEO's net sales, revenues, net income or earnings before income tax or other exclusions; (viii) the attainment of certain target levels of, or a specified increase in, GEO's return on capital employed or return on invested capital; (ix) the attainment of certain target levels of, or a percentage increase in, GEO's after-tax or pre-tax return on shareholder equity; (x) the attainment of certain target levels in the fair market value of GEO's Common Stock; (xi) the growth in the value of an investment in the Common Stock assuming the reinvestment of dividends; and/or (xii) the attainment of certain target levels of, or a specified increase in, EBITDA (earnings before income tax, depreciation and amortization). In addition, Performance Goals may be based upon the attainment by a subsidiary, division or other operational unit of GEO of specified levels of performance under one or more of the measures described above. Further, the Performance Goals may be based upon the attainment by GEO (or a subsidiary, division, facility or other operational unit of GEO) of specified levels of performance under one or more of the foregoing measures relative to the performance of other corporations. To the extent permitted under Code Section 162(m) of the Code (including, without limitation, compliance with any requirements for shareholder approval), the Committee may, in its sole and absolute discretion: (i) designate additional business criteria upon which the Performance Goals may be based; (ii) modify, amend or adjust the business criteria described herein; or (iii) incorporate in the Performance Goals provisions regarding changes in accounting methods, corporate transactions (including, without limitation, dispositions or acquisitions) and similar events or circumstances. Performance Goals may include a threshold level of performance below which no Award will be earned, levels of performance at which an Award will become partially earned and a level at which an Award will be fully earned.

(c) *Terms and Conditions of Performance Shares and Performance Units.* The applicable Award Agreement shall set forth (i) the number of Performance Shares or the dollar value of Performance Units granted to the Participant; (ii) the Performance Period and Performance Goals with respect to each such Award; (iii) the threshold, target and maximum shares of Common Stock or dollar values of each Performance Share or Performance Unit and corresponding Performance Goals, and (iv) any other terms and conditions as the Committee determines in its sole and absolute discretion. The Committee shall establish, in its sole and absolute discretion, the Performance Goals for the applicable Performance Period for each Performance Share or Performance Unit granted hereunder. Performance Goals for different Participants and for different grants of Performance Shares and Performance Units need not be identical. Unless otherwise provided in an Award Agreement, the Participants' rights as a shareholder in Performance Shares shall be substantially identical to the terms and conditions that would have been applicable under Section 8 above if the Performance Shares were Restricted Stock. Unless otherwise provided in an Award Agreement, a holder of Performance Units is not entitled to the rights of a holder of Common Stock.

(d) *Determination and Payment of Performance Units or Performance Shares Earned.* As soon as practicable after the end of a Performance Period, the Committee shall determine the extent to which Performance Shares or Performance Units have been earned on the basis of the Company's actual performance

in relation to the established Performance Goals as set forth in the applicable Award Agreement and shall certify these results in writing. As soon as practicable after the Committee has determined that an amount is payable or should be distributed with respect to a Performance Share or a Performance Unit, the Committee shall cause the amount of such Award to be paid or distributed to the Participant or the Participant's estate, devisee or heir at law (whichever is applicable). Unless otherwise provided in an Award Agreement, the Committee shall determine in its sole and absolute discretion whether payment with respect to the Performance Share or Performance Unit shall be made in cash, in shares of Common Stock, or in a combination thereof. For purposes of making payment or a distribution with respect to a Performance Share or Performance Unit, the cash equivalent of a share of Common Stock shall be determined by the Fair Market Value of the Common Stock on the day the Committee designates the Performance Shares or Performance Units to be payable.

(e) *Termination of Employment.* Unless otherwise provided in an Award Agreement, if a Participant's employment or other service with the Company terminates for any reason, all of the Participant's outstanding Performance Shares and Performance Units shall be subject to the rules of this Section.

(i) *Termination for Reason Other Than Death or Disability.* If a Participant's employment or other service with the Company terminates prior to the expiration of a Performance Period with respect to any Performance Units or Performance Shares held by such Participant for any reason other than death or Disability, the outstanding Performance Units or Performance Shares held by such Participant for which the Performance Period has not yet expired shall terminate upon such termination and the Participant shall have no further rights pursuant to such Performance Units or Performance Shares.

(ii) *Termination of Employment for Death or Disability.* If a Participant's employment or other service with the Company terminates by reason of the Participant's death or Disability prior to the end of a Performance Period, the Participant, or the Participant's estate, devisee or heir at law (whichever is applicable) shall be entitled to a payment of the Participant's outstanding Performance Units and Performance Share at the end of the applicable Performance Period, pursuant to the terms of the Plan and the Participant's Award Agreement; *provided, however,* that the Participant shall be deemed to have earned only that proportion (to the nearest whole unit or share) of the Performance Units or Performance Shares granted to the Participant under such Award as the number of full months of the Performance Period which have elapsed since the first day of the Performance Period for which the Award was granted to the end of the month in which the Participant's termination of employment or other service, bears to the total number of months in the Performance Period, subject to the attainment of the Performance Goals associated with the Award as certified by the Committee. The right to receive any remaining Performance Units or Performance Shares shall be canceled and forfeited.

#### **10. VESTING OF AWARD GRANTS TO NON-EMPLOYEE DIRECTORS**

Notwithstanding the minimum vesting provisions in Section 6(g) and 8(b) of the Plan, any Award granted to a Non-Employee Director in lieu of cash compensation shall not be subject to any minimum vesting requirements.

#### **11. OTHER AWARDS**

Awards of shares of Common Stock, phantom stock, restricted stock units and other awards that are valued in whole or in part by reference to, or otherwise based on, Common Stock, may also be made, from time to time, to Eligible Individuals as may be selected by the Committee. Such Common Stock may be issued in satisfaction of awards granted under any other plan sponsored by the Company or compensation payable to an Eligible Individual. In addition, such awards may be made alone or in addition to or in connection with any other Award granted hereunder. The Committee may determine the terms and conditions of any such award. Each such award shall be evidenced by an Award Agreement between the Eligible Individual and the Company which shall specify the number of shares of Common Stock subject to the award, any consideration therefore, any vesting or performance requirements and such other terms and conditions as the Committee shall determine in its sole and absolute discretion.



## 12. CHANGE IN CONTROL

Unless otherwise provided in an Award Agreement, upon the occurrence of a Change in Control of GEO, the Committee may in its sole and absolute discretion, provide on a case by case basis that (i) some or all outstanding Awards may become immediately exercisable or vested, without regard to any limitation imposed pursuant to this Plan, (ii) that all Awards shall terminate, provided that Participants shall have the right, immediately prior to the occurrence of such Change in Control and during such reasonable period as the Committee in its sole discretion shall determine and designate, to exercise any vested Award in whole or in part, (iii) that all Awards shall terminate, provided that Participants shall be entitled to a cash payment equal to the Change in Control Price with respect to shares subject to the vested portion of the Award net of the Exercise Price thereof (if applicable), (iv) provide that, in connection with a liquidation or dissolution of GEO, Awards shall convert into the right to receive liquidation proceeds net of the Exercise Price (if applicable) and (v) any combination of the foregoing. In the event that the Committee does not terminate or convert an Award upon a Change in Control of GEO, then the Award shall be assumed, or substantially equivalent Awards shall be substituted, by the acquiring, or succeeding corporation (or an affiliate thereof).

## 13. CHANGE IN STATUS OF PARENT OR SUBSIDIARY

Unless otherwise provided in an Award Agreement or otherwise determined by the Committee, in the event that an entity or business unit which was previously a part of the Company is no longer a part of the Company, as determined by the Committee in its sole discretion, the Committee may, in its sole and absolute discretion: (i) provide on a case by case basis that some or all outstanding Awards held by a Participant employed by or performing service for such entity or business unit may become immediately exercisable or vested, without regard to any limitation imposed pursuant to this Plan; (ii) provide on a case by case basis that some or all outstanding Awards held by a Participant employed by or performing service for such entity or business unit may remain outstanding, may continue to vest, and/or may remain exercisable for a period not exceeding one (1) year, subject to the terms of the Award Agreement and this Plan; and/or (iii) treat the employment or other services of a Participant employed by such entity or business unit as terminated if such Participant is not employed by GEO or any entity that is a part of the Company immediately after such event.

## 14. REQUIREMENTS OF LAW

(a) *Violations of Law.* The Company shall not be required to sell or issue any shares of Common Stock under any Award if the sale or issuance of such shares would constitute a violation by the individual exercising the Award, the Participant or the Company of any provisions of any law or regulation of any governmental authority, including without limitation any provisions of the Sarbanes-Oxley Act, and any other federal or state securities laws or regulations. Any determination in this connection by the Committee shall be final, binding, and conclusive. The Company shall not be obligated to take any affirmative action in order to cause the exercise of an Award, the issuance of shares pursuant thereto or the grant of an Award to comply with any law or regulation of any governmental authority.

(b) *Registration.* At the time of any exercise or receipt of any Award, the Company may, if it shall determine it necessary or desirable for any reason, require the Participant (or Participant's heirs, legatees or legal representative, as the case may be), as a condition to the exercise or grant thereof, to deliver to the Company a written representation of present intention to hold the shares for their own account as an investment and not with a view to, or for sale in connection with, the distribution of such shares, except in compliance with applicable federal and state securities laws with respect thereto. In the event such representation is required to be delivered, an appropriate legend may be placed upon each certificate delivered to the Participant (or Participant's heirs, legatees or legal representative, as the case may be) upon the Participant's exercise of part or all of the Award or receipt of an Award and a stop transfer order may be placed with the transfer agent. Each Award shall also be subject to the requirement that, if at any time the Company determines, in its discretion, that the listing, registration or qualification of the shares subject to the Award upon any securities exchange or under any state or federal law, or the consent or approval of any governmental regulatory body, is necessary or desirable as a condition of or in connection with, the issuance or purchase of the shares thereunder, the Award may not be exercised in whole or in part and the restrictions on an Award

may not be removed unless such listing, registration, qualification, consent or approval shall have been effected or obtained free of any conditions not acceptable to the Company in its sole discretion. The Participant shall provide the Company with any certificates, representations and information that the Company requests and shall otherwise cooperate with the Company in obtaining any listing, registration, qualification, consent or approval that the Company deems necessary or appropriate. The Company shall not be obligated to take any affirmative action in order to cause the exercisability or vesting of an Award, to cause the exercise of an Award or the issuance of shares pursuant thereto, or to cause the grant of Award to comply with any law or regulation of any governmental authority.

(c) *Withholding.* The Committee may make such provisions and take such steps as it may deem necessary or appropriate for the withholding of any taxes that the Company is required by any law or regulation of any governmental authority, whether federal, state or local, domestic or foreign, to withhold in connection with the grant or exercise of an Award, or the removal of restrictions on an Award including, but not limited to: (i) the withholding of delivery of shares of Common Stock until the holder reimburses the Company for the amount the Company is required to withhold with respect to such taxes; (ii) the canceling of any number of shares of Common Stock issuable in an amount sufficient to reimburse the Company for the amount it is required to so withhold; (iii) withholding the amount due from any such person's wages or compensation due to such person; or (iv) requiring the Participant to pay the Company cash in the amount the Company is required to withhold with respect to such taxes.

(d) *Governing Law.* The Plan shall be governed by, and construed and enforced in accordance with, the laws of the State of Florida.

## 15. GENERAL PROVISIONS

(a) *Award Agreements.* All Awards granted pursuant to the Plan shall be evidenced by an Award Agreement. Each Award Agreement shall specify the terms and conditions of the Award granted and shall contain any additional provisions as the Committee shall deem appropriate, in its sole and absolute discretion (including, to the extent that the Committee deems appropriate, provisions relating to confidentiality, non-competition, non-solicitation and similar matters). The terms of each Award Agreement need not be identical for Eligible Individuals provided that all Award Agreements comply with the terms of the Plan.

(b) *Purchase Price.* To the extent the purchase price of any Award granted hereunder is less than par value of a share of Common Stock and such purchase price is not permitted by applicable law, the per share purchase price shall be deemed to be equal to the par value of a share of Common Stock.

(c) *Dividends and Dividend Equivalents.* Except as provided by the Committee in its sole and absolute discretion or as otherwise provided in Section 5(d) and subject to Section 8(e) of the Plan, a Participant shall not be entitled to receive, currently or on a deferred basis, cash or stock dividends, Dividend Equivalents, or cash payments in amounts equivalent to cash or stock dividends on shares of Commons Stock covered by an Award which has not vested or an Option. The Committee in its absolute and sole discretion may credit a Participant's Award with Dividend Equivalents with respect to any Awards. To the extent that dividends and distributions relating to an Award are held in escrow by the Company, or Dividend Equivalents are credited to an Award, a Participant shall not be entitled to any interest on any such amounts. The Committee may not grant Dividend Equivalents to an Award subject to performance-based vesting to the extent that the grant of such Dividend Equivalents would limit the Company's deduction of the compensation payable under such Award for federal tax purposes pursuant to Code Section 162(m).

(d) *Deferral of Awards.* The Committee may from time to time establish procedures pursuant to which a Participant may elect to defer, until a time or times later than the vesting of an Award, receipt of all or a portion of the shares of Common Stock or cash subject to such Award and to receive Common Stock or cash at such later time or times, all on such terms and conditions as the Committee shall determine. The Committee shall not permit the deferral of an Award unless counsel for GEO determines that such action will not result in adverse tax consequences to a Participant under Section 409A of the Code. If any such deferrals are permitted, then notwithstanding anything to the contrary herein, a Participant who elects to defer receipt of Common Stock shall not have any rights as a shareholder with respect to deferred shares of Common Stock unless and

until shares of Common Stock are actually delivered to the Participant with respect thereto, except to the extent otherwise determined by the Committee.

(e) *Prospective Employees.* Notwithstanding anything to the contrary, any Award granted to a Prospective Employee shall not become vested prior to the date the Prospective Employee first becomes an employee of the Company.

(f) *Issuance of Certificates; Shareholder Rights.* GEO shall deliver to the Participant a certificate evidencing the Participant's ownership of shares of Common Stock issued pursuant to the exercise of an Award as soon as administratively practicable after satisfaction of all conditions relating to the issuance of such shares. A Participant shall not have any of the rights of a shareholder with respect to such Common Stock prior to satisfaction of all conditions relating to the issuance of such Common Stock, and, except as expressly provided in the Plan, no adjustment shall be made for dividends, distributions or other rights of any kind for which the record date is prior to the date on which all such conditions have been satisfied.

(g) *Transferability of Awards.* A Participant may not Transfer an Award other than by will or the laws of descent and distribution. Awards may be exercised during the Participant's lifetime only by the Participant. No Award shall be liable for or subject to the debts, contracts, or liabilities of any Participant, nor shall any Award be subject to legal process or attachment for or against such person. Any purported Transfer of an Award in contravention of the provisions of the Plan shall have no force or effect and shall be null and void, and the purported transferee of such Award shall not acquire any rights with respect to such Award. Notwithstanding anything to the contrary, the Committee may in its sole and absolute discretion permit the Transfer of an Award to a Participant's "family member" as such term is defined in the Form 8 Registration Statement under the Securities Act of 1933, as amended, under such terms and conditions as specified by the Committee. In such case, such Award shall be exercisable only by the transferee approved of by the Committee. To the extent that the Committee permits the Transfer of an Incentive Stock Option to a "family member", so that such Option fails to continue to satisfy the requirements of an incentive stock option under the Code such Option shall automatically be re-designated as a Non-Qualified Stock Option.

(h) *Buyout and Settlement Provisions.* Except as prohibited in Section 6(d) of the Plan, the Committee may at any time on behalf of GEO offer to buy out any Awards previously granted based on such terms and conditions as the Committee shall determine which shall be communicated to the Participants at the time such offer is made.

(i) *Use of Proceeds.* The proceeds received by GEO from the sale of Common Stock pursuant to Awards granted under the Plan shall constitute general funds of GEO.

(j) *Modification or Substitution of an Award.* Subject to the terms and conditions of the Plan, the Committee may modify outstanding Awards. Notwithstanding the following, no modification of an Award shall adversely affect any rights or obligations of the Participant under the applicable Award Agreement without the Participant's consent. The Committee in its sole and absolute discretion may rescind, modify, or waive any vesting requirements or other conditions applicable to an Award. Notwithstanding the foregoing, without the approval of the shareholders of GEO in accordance with applicable law, an Award may not be modified to reduce the exercise price thereof nor may an Award at a lower price be substituted for a surrender of an Award, provided that (i) the foregoing shall not apply to adjustments or substitutions in accordance with Section 5 or Section 12, and (ii) if an Award is modified, extended or renewed and thereby deemed to be in issuance of a new Award under the Code or the applicable accounting rules, the exercise price of such Award may continue to be the original Exercise Price even if less than Fair Market Value of the Common Stock at the time of such modification, extension or renewal.

(k) *Amendment and Termination of Plan.* The Board may, at any time and from time to time, amend, suspend or terminate the Plan as to any shares of Common Stock as to which Awards have not been granted; *provided, however,* that the approval of the shareholders of GEO in accordance with applicable law and the Articles of Incorporation and Bylaws of GEO shall be required for any amendment: (i) that changes the class of individuals eligible to receive Awards under the Plan: (ii) that increases the maximum number of shares of Common Stock in the aggregate that may be subject to Awards that are granted under the Plan (except as

permitted under Section 5 or Section 12 hereof): (iii) the approval of which is necessary to comply with federal or state law (including without limitation Section 162(m) of the Code and Rule 16b-3 under the Exchange Act) or with the rules of any stock exchange or automated quotation system on which the Common Stock may be listed or traded; or (iv) that proposed to eliminate a requirement provided herein that the shareholders of GEO must approve an action to be undertaken under the Plan. Except as permitted under Section 5 or Section 12 hereof, no amendment, suspension or termination of the Plan shall, without the consent of the holder of an Award, alter or impair rights or obligations under any Award theretofore granted under the Plan. Awards granted prior to the termination of the Plan may extend beyond the date the Plan is terminated and shall continue subject to the terms of the Plan as in effect on the date the Plan is terminated.

(l) *Section 409A of the Code.* With respect to Awards subject to Section 409A of the Code, this Plan is intended to comply with the requirements of such Section, and the provisions hereof shall be interpreted in a manner that satisfies the requirements of such Section and the related regulations, and the Plan shall be operated accordingly. If any provision of this Plan or any term or condition of any Award would otherwise frustrate or conflict with this intent, the provision, term or condition will be interpreted and deemed amended so as to avoid this conflict.

(m) *Notification of 83(b) Election.* If in connection with the grant of any Award, any Participant makes an election permitted under Code Section 83(b), such Participant must notify the Company in writing of such election within ten (10) days of filing such election with the Internal Revenue Service.

(n) *Detrimental Activity.* All Awards shall be subject to cancellation by the Committee in accordance with the terms of this Section 15(n) if the Participant engages in any Detrimental Activity. To the extent that a Participant engages in any Detrimental Activity at any time prior to, or during the one year period after, any exercise or vesting of an Award but prior to a Change in Control, the Company shall, upon the recommendation of the Committee, in its sole and absolute discretion, be entitled to (i) immediately terminate and cancel any Awards held by the Participant that have not yet been exercised, and/or (ii) with respect to Awards of the Participant that have been previously exercised, recover from the Participant at any time within two (2) years after such exercise but prior to a Change in Control (and the Participant shall be obligated to pay over to the Company with respect to any such Award previously held by such Participant): (A) with respect to any Options exercised, an amount equal to the excess of the Fair Market Value of the Common Stock for which any Option was exercised over the Exercise Price paid (regardless of the form by which payment was made) with respect to such Option; (B) with respect to any Award other than an Option, any shares of Common Stock granted and vested pursuant to such Award, and if such shares are not still owned by the Participant, the Fair Market Value of such shares on the date they were issued, or if later, the date all vesting restrictions were satisfied; and (C) any cash or other property (other than Common Stock) received by the Participant from the Company pursuant to an Award. Without limiting the generality of the foregoing, in the event that a Participant engages in any Detrimental Activity at any time prior to any exercise of an Award and the Company exercises its remedies pursuant to this Section 15(n) following the exercise of such Award, such exercise shall be treated as having been null and void, provided that the Company will nevertheless be entitled to recover the amounts referenced above.

(o) *Disclaimer of Rights.* No provision in the Plan, any Award granted hereunder, or any Award Agreement entered into pursuant to the Plan shall be construed to confer upon any individual the right to remain in the employ of or other service with the Company or to interfere in any way with the right and authority of the Company either to increase or decrease the compensation of any individual, including any holder of an Award, at any time, or to terminate any employment or other relationship between any individual and the Company. The grant of an Award pursuant to the Plan shall not affect or limit in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structure or to merge, consolidate, dissolve or liquidate, or to sell or transfer all or any part of its business or assets.

(p) *Unfunded Status of Plan.* The Plan is intended to constitute an "unfunded" plan for incentive and deferred compensation. With respect to any payments as to which a Participant has a fixed and vested interest

but which are not yet made to such Participant by the Company, nothing contained herein shall give any such Participant any rights that are greater than those of a general creditor of the Company.

(q) *Nonexclusivity of Plan.* The adoption of the Plan shall not be construed as creating any limitations upon the right and authority of the Board to adopt such other incentive compensation arrangements (which arrangements may be applicable either generally to a class or classes of individuals or specifically to a particular individual or individuals) as the Board in its sole and absolute discretion determines desirable.

(r) *Other Benefits.* No Award payment under the Plan shall be deemed compensation for purposes of computing benefits under any retirement plan of the Company or any agreement between a Participant and the Company, nor affect any benefits under any other benefit plan of the Company now or subsequently in effect under which benefits are based upon a Participant's level of compensation.

(s) *Headings.* The section headings in the Plan are for convenience only; they form no part of this Agreement and shall not affect its interpretation.

(t) *Pronouns.* The use of any gender in the Plan shall be deemed to include all genders, and the use of the singular shall be deemed to include the plural and vice versa, wherever it appears appropriate from the context.

(u) *Successors and Assigns.* The Plan shall be binding on all successors of the Company and all successors and permitted assigns of a Participant, including, but not limited to, a Participant's estate, devisee, or heir at law.

(v) *Severability.* If any provision of the Plan or any Award Agreement shall be determined to be illegal or unenforceable by any court of law in any jurisdiction, the remaining provisions hereof and thereof shall be severable and enforceable in accordance with their terms, and all provisions shall remain enforceable in any other jurisdiction.

(w) *Notices.* Any communication or notice required or permitted to be given under the Plan shall be in writing, and mailed by registered or certified mail or delivered by hand, to GEO, to its principal place of business, attention: John J. Bulfin, General Counsel, The GEO Group Inc., and if to the holder of an Award, to the address as appearing on the records of the Company.

**ANNEX A**  
**DEFINITIONS**

“Award” means any Common Stock, Option, Performance Share, Performance Unit, Restricted Stock, Stock Appreciation Right or any other award granted pursuant to the Plan.

“Award Agreement” means a written agreement entered into by GEO and a Participant setting forth the terms and conditions of the grant of an Award to such Participant.

“Board” means the board of directors of GEO.

“Cause” means, with respect to a termination of employment or other service with the Company, a termination of employment or other service due to a Participant’s dishonesty, fraud, insubordination, willful misconduct, refusal to perform services (for any reason other than illness or incapacity) or materially unsatisfactory performance of the Participant’s duties for the Company; *provided, however*, that if the Participant and the Company have entered into an employment agreement or consulting agreement which defines the term Cause, the term Cause shall be defined in accordance with such agreement with respect to any Award granted to the Participant on or after the effective date of the respective employment or consulting agreement. The Committee shall determine in its sole and absolute discretion whether Cause exists for purposes of the Plan.

“Change in Control” shall be deemed to occur upon:

(a) any “person” as such term is used in Sections 13(d) and 14(d) of the Exchange Act (other than GEO, any trustee or other fiduciary holding securities under any employee benefit plan of the Company, or any company owned, directly or indirectly, by the shareholders of GEO in substantially the same proportions as their ownership of common stock of GEO), is or becomes the “beneficial owner” (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of GEO representing thirty percent (30%) or more of the combined voting power of GEO’s then outstanding securities;

(b) during any period of two (2) consecutive years, individuals who at the beginning of such period constitute the Board, and any new director (other than a director designated by a person who has entered into an agreement with the Company to effect a transaction described in paragraph (a), (c), or (d) of this Section) whose election by the Board or nomination for election by GEO’s shareholders was approved by a vote of at least two-thirds of the directors then still in office who either were directors at the beginning of the two-year period or whose election or nomination for election was previously so approved, cease for any reason to constitute at least a majority of the Board;

(c) a merger, consolidation, reorganization, or other business combination of GEO with any other entity, other than a merger or consolidation which would result in the voting securities of GEO outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than fifty percent (50%) of the combined voting power of the voting securities of GEO or such surviving entity outstanding immediately after such merger or consolidation; *provided, however*, that a merger or consolidation effected to implement a recapitalization of GEO (or similar transaction) in which no person acquires more than twenty-five percent (25%) of the combined voting power of GEO’s then outstanding securities shall not constitute a Change in Control; or

(d) the shareholders of GEO approve a plan of complete liquidation of GEO or the consummation of the sale or disposition by GEO of all or substantially all of GEO’s assets other than (x) the sale or disposition of all or substantially all of the assets of GEO to a person or persons who beneficially own, directly or indirectly, at least fifty percent (50%) or more of the combined voting power of the outstanding voting securities of GEO at the time of the sale or (y) pursuant to a spin-off type transaction, directly or indirectly, of such assets to the shareholders of GEO.

However, to the extent that Section 409A of the Code would cause an adverse tax consequence to a Participant using the above definition, the term “Change in Control” shall have the meaning ascribed to the

phrase "Change in the Ownership or Effective Control of a Corporation or in the Ownership of a Substantial Portion of the Assets of a Corporation" under Treasury Department Proposed Regulation 1.409A-3(g)(5), as revised from time to time in either subsequent proposed or final regulations, and in the event that such regulations are withdrawn or such phrase (or a substantially similar phrase) ceases to be defined, as determined by the Committee.

"Change in Control Price" means the price per share of Common Stock paid in any transaction related to a Change in Control of GEO.

"Code" means the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

"Committee" means a committee or sub-committee of the Board consisting of two or more members of the Board, none of whom shall be an officer or other salaried employee of the Company, and each of whom shall qualify in all respects as a "non-employee director" as defined in Rule 16b-3 under the Exchange Act, and as an "outside director" for purposes of Code Section 162(m). If no Committee exists, the functions of the Committee will be exercised by the Board; *provided, however*, that a Committee shall be created prior to the grant of Awards to a Covered Employee and that grants of Awards to a Covered Employee shall be made only by such Committee. Notwithstanding the foregoing, with respect to the grant of Awards to non-employee directors, the Committee shall be the Board.

"Common Stock" means the common stock, par value \$0.01 per share, of GEO.

"Company" means The GEO Group, Inc., a Florida corporation, the subsidiaries of The GEO Group, Inc., and all other entities whose financial statements are required to be consolidated with the financial statements of The GEO Group, Inc. pursuant to United States generally accepted accounting principles, and any other entity determined to be an affiliate of The GEO Group, Inc. as determined by the Committee in its sole and absolute discretion.

"Covered Employee" means "covered employee" as defined in Code Section 162(m)(3).

"Covered Individual" means any current or former member of the Committee, any current or former officer or director of the Company, or any individual designated pursuant to Section 4(c).

"Detrimental Activity" means any of the following: (i) the disclosure to anyone outside the Company, or the use in other than the Company's business, without written authorization from the Company, of any confidential information or proprietary information, relating to the business of the Company, acquired by a Participant prior to a termination of the Participant's employment or service with the Company; (ii) activity while employed or providing services that is classified by the Company as a basis for a termination for Cause; (iii) the Participant's Disparagement, or inducement of others to do so, of the Company or its past or present officers, directors, employees or services; or (iv) any other conduct or act determined by the Committee, in its sole discretion, to be injurious, detrimental or prejudicial to the interests of the Company. For purposes of subparagraph (i) above, the Chief Executive Officer and the General Counsel of the Company shall each have authority to provide the Participant with written authorization to engage in the activities contemplated thereby and no other person shall have authority to provide the Participant with such authorization.

"Disability" means a "permanent and total disability" within the meaning of Code Section 22(e)(3); *provided, however*, that if a Participant and the Company have entered into an employment or consulting agreement which defines the term Disability for purposes of such agreement, Disability shall be defined pursuant to the definition in such agreement with respect to any Award granted to the Participant on or after the effective date of the respective employment or consulting agreement. The Committee shall determine in its sole and absolute discretion whether a Disability exists for purposes of the Plan.

"Disparagement" means making any comments or statements to the press, the Company's employees, clients or any other individuals or entities with whom the Company has a business relationship, which could adversely affect in any manner: (i) the conduct of the business of the Company (including, without limitation, any products or business plans or prospects), or (ii) the business reputation of the Company or any of its products, or its past or present officers, directors or employees.

“Dividend Equivalents” means an amount equal to the cash dividends paid by the Company upon one share of Common Stock subject to an Award granted to a Participant under the Plan.

“Effective Date” shall mean the date that the Plan was approved by the shareholders of GEO in accordance with applicable law or such later date as provided in the resolutions adopting the Plan.

“Eligible Individual” means any employee, officer, director (employee or non-employee director) or consultant of the Company and any Prospective Employee to whom Awards are granted in connection with an offer of future employment with the Company.

“Exchange Act” means the Securities Exchange Act of 1934, as amended.

“Exercise Price” means the purchase price per share of each share of Common Stock subject to an Award.

“Fair Market Value” means, unless otherwise required by the Code, as of any date, the last sales price reported for the Common Stock on the day immediately prior to such date (i) as reported by the national securities exchange in the United States on which it is then traded, or (ii) if not traded on any such national securities exchange, as quoted on an automated quotation system sponsored by the National Association of Securities Dealers, Inc., or if the Common Stock shall not have been reported or quoted on such date, on the first day prior thereto on which the Common Stock was reported or quoted; *provided, however*, that the Committee may modify the definition of Fair Market Value to reflect any changes in the trading practices of any exchange or automated system sponsored by the National Association of Securities Dealers, Inc. on which the Common Stock is listed or traded. If the Common Stock is not readily traded on a national securities exchange or any system sponsored by the National Association of Securities Dealers, Inc., the Fair Market Value shall be determined in good faith by the Committee.

“GEO” means The GEO Group, Inc., a Florida corporation.

“Grant Date” means the date on which the Committee approves the grant of an Award or such later date as is specified by the Committee and set forth in the applicable Award Agreement.

“Incentive Stock Option” means an “incentive stock option” within the meaning of Code Section 422.

“Non-Employee Director” means a director of GEO who is not an active employee of the Company.

“Non-Qualified Stock Option” means an Option which is not an Incentive Stock Option.

“Option” means an option to purchase Common Stock granted pursuant to Sections 6 of the Plan.

“Participant” means any Eligible Individual who holds an Award under the Plan and any of such individual’s successors or permitted assigns.

“Performance Goals” means the specified performance goals which have been established by the Committee in connection with an Award.

“Performance Period” means the period during which Performance Goals must be achieved in connection with an Award granted under the Plan.

“Performance Share” means a right to receive a fixed number of shares of Common Stock, or the cash equivalent, which is contingent on the achievement of certain Performance Goals during a Performance Period.

“Performance Unit” means a right to receive a designated dollar value, or shares of Common Stock of the equivalent value, which is contingent on the achievement of Performance Goals during a Performance Period.

“Person” shall mean any person, corporation, partnership, joint venture or other entity or any group (as such term is defined for purposes of Section 13(d) of the Exchange Act), other than a Parent or Subsidiary.

“Plan” means this The GEO Group, Inc. 2006 Stock Incentive Plan.



“Prospective Employee” means any individual who has committed to become an employee of the Company within sixty (60) days from the date an Award is granted to such individual.

“Restricted Stock” means Common Stock subject to certain restrictions, as determined by the Committee, and granted pursuant to Section 8 hereunder.

“Section 424 Employee” means an employee of GEO or any “subsidiary corporation” or “parent corporation” as such terms are defined in and in accordance with Code Section 424. The term “Section 424 Employee” also includes employees of a corporation issuing or assuming any Options in a transaction to which Code Section 424(a) applies.

“Stock Appreciation Right” means the right to receive all or some portion of the increase in value of a fixed number of shares of Common Stock granted pursuant to Section 7 hereunder.

“Transfer” means, as a noun, any direct or indirect, voluntary or involuntary, exchange, sale, bequeath, pledge, mortgage, hypothecation, encumbrance, distribution, transfer, gift, assignment or other disposition or attempted disposition of, and, as a verb, directly or indirectly, voluntarily or involuntarily, to exchange, sell, bequeath, pledge, mortgage, hypothecate, encumber, distribute, transfer, give, assign or in any other manner whatsoever dispose or attempt to dispose of.

The GEO Group, Inc. Subsidiaries

GEO International Holdings, Inc.  
GEO RE Holdings LLC  
WCC Financial, Inc.  
WCC Development, Inc.  
WCC/FL/01, Inc.  
WCC/FL/02, Inc.  
GEO Design Services, Inc.  
GEO Care, Inc.  
The GEO Group UK Ltd.  
Premier Custodial Development Ltd.  
South African Custodial Holdings Pty Ltd.  
GEO NZ Limited  
The GEO Group Australasia Pty, Ltd.  
GEO Australasia Pty, Ltd.  
The GEO Group Australia Pty, Ltd.  
Premier Employment Services Pty, Ltd.  
Australasian Correctional Investment Pty, Ltd.  
Pacific Rim Employment Pty, Ltd.  
Strategic Healthcare Solutions Pty, Ltd.  
Wackenhut Corrections Corporation N.V.  
Canadian Correctional Management, Inc.  
Miramichi Youth Center Management, Inc.  
Wackenhut Corrections Puerto Rico, Inc.  
Correctional Services Corporation  
FF&E, Inc.  
CPT Limited Partner LLC  
CPT Operating Partnership LP  
Correctional Properties Prison Finance LLC  
Public Properties Development & Leasing LLC  
GEO Holdings I, Inc.

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We have issued our report dated February 27, 2007, accompanying the consolidated financial statements and schedules included in the Annual Report of The GEO Group, Inc. (which report expressed an unqualified opinion and contains an explanatory paragraph relating to the adoption of Statement of Financial Accounting Standards No. 123(R) and Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans) on Form 10-K for the year ended December 31, 2006. We hereby consent to the incorporation by reference of said report in the Registration Statements of The GEO Group, Inc. on Form S-3 (File No. 333-111003, effective January 26, 2004) and Forms S-8 (File No. 333-79817, effective June 2, 1999, File No. 333-17265, effective December 4, 1996, File No. 333-09977, effective August 12, 1996 and File No. 333-09981, effective August 12, 1996).

/s/ Grant Thornton LLP

Miami, FL  
February 27, 2007

**CONSENT OF INDEPENDENT REGISTERED CERTIFIED PUBLIC ACCOUNTANTS**

We consent to the incorporation by reference in the Registration Statement (Form S-4 No. 333-107709) of The GEO Group, Inc. in the related Prospectus, the Registration Statement (Form S-3 No. 333-111003) and in the related Prospectus, the Registration Statement (Form S-8 No. 333-79817) pertaining to the 1999 Stock Option Plan, the Registration Statement (Form S-8 No. 333-17265) pertaining to the Employees' 401 (k) and Retirement Plan, the Registration Statement (Form S-8 No. 333-09977) pertaining to the Wackenhut Corrections Corporation Stock Option Plan, and the Registration Statement (Form S-8 No. 333-09981) pertaining to the Nonemployee Director Stock Option Plan of Wackenhut Corrections Corporation of our report dated March 14, 2006, with respect to the consolidated financial statements and schedule of The GEO Group, Inc., included in this Annual Report (Form 10-K) for the year ended December 31, 2006.

/s/ Ernst & Young LLP

West Palm Beach, Florida  
February 27, 2007

## CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, George C. Zoley, certify that:

1. I have reviewed this annual report on Form 10-K of The GEO Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f), for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

/s/ George C. Zoley

George C. Zoley  
Chief Executive Officer

Date: March 2, 2007

## CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, John G. O'Rourke, certify that:

1. I have reviewed this annual report on Form 10-K of The GEO Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f), for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

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/s/ John G. O'Rourke  
John G. O'Rourke  
Chief Financial Officer

Date: March 2, 2007

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-  
OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of The GEO Group, Inc. (the "Company") for the fiscal year ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, I George C. Zoley, Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ George C. Zoley

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George C. Zoley  
*Chief Executive Officer*

Date: March 2, 2007

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-  
OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of The GEO Group, Inc. (the "Company") for the fiscal year ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, I John G. O'Rourke, Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ John G. O'Rourke

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John G. O'Rourke  
*Chief Financial Officer*

Date: March 2, 2007