

GEO GROUP INC  
Form 10-Q  
August 09, 2012  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended July 1, 2012

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the transition period from                      to

Commission file number 1-14260

**The GEO Group, Inc.**

(Exact Name of Registrant as Specified in Its Charter)

Edgar Filing: GEO GROUP INC - Form 10-Q

**Florida**  
(State or Other Jurisdiction of

**65-0043078**  
(IRS Employer

Incorporation or Organization)

Identification No.)

**One Park Place, 621 NW 53rd Street, Suite 700,**

**Boca Raton, Florida**  
(Address of Principal Executive Offices)

**33487**  
(Zip Code)

**(561) 893-0101**

(Registrant's Telephone Number, Including Area Code)

(Former Name, Former Address and Former Fiscal Year if changed since last report)

Indicate by 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 (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

As of August 6, 2012, the registrant had 61,460,069 shares of common stock outstanding.

**Table of Contents**

**TABLE OF CONTENTS**

|   |    |
|---|----|
| <b><u>PART I - FINANCIAL INFORMATION</u></b>  | 3  |
| <b><u>ITEM 1. FINANCIAL STATEMENTS</u></b>  | 3  |
| <b><u>CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME FOR THE THIRTEEN AND TWENTY-SIX WEEKS ENDED JULY 1, 2012 AND JULY 3, 2011 (UNAUDITED)</u></b> | 3  |
| <b><u>CONSOLIDATED BALANCE SHEETS AS OF JULY 1, 2012 (UNAUDITED) AND JANUARY 1, 2012</u></b>  | 4  |
| <b><u>CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE TWENTY-SIX WEEKS ENDED JULY 1, 2012 AND JULY 3, 2011 (UNAUDITED)</u></b>                        | 5  |
| <b><u>NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS</u></b>  | 6  |
| <b><u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u></b>   | 33 |
| <b><u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u></b>  | 47 |
| <b><u>ITEM 4. CONTROLS AND PROCEDURES</u></b>   | 48 |
| <b><u>PART II - OTHER INFORMATION</u></b>   | 49 |
| <b><u>ITEM 1. LEGAL PROCEEDINGS</u></b>   | 49 |
| <b><u>ITEM 1A. RISK FACTORS</u></b>   | 49 |
| <b><u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u></b>   | 49 |
| <b><u>ITEM 3. DEFAULTS UPON SENIOR SECURITIES</u></b>   | 49 |
| <b><u>ITEM 4. MINE SAFETY DISCLOSURES</u></b>   | 49 |
| <b><u>ITEM 5. OTHER INFORMATION</u></b>   | 49 |
| <b><u>ITEM 6. EXHIBITS</u></b>  | 49 |
| <b><u>SIGNATURES</u></b>  | 50 |

**Table of Contents****PART I - FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****THE GEO GROUP, INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****FOR THE THIRTEEN AND TWENTY-SIX WEEKS ENDED****JULY 1, 2012 AND JULY 3, 2011****(In thousands, except per share data)****(Unaudited)**

|   | <b>Thirteen Weeks Ended</b> |                         | <b>Twenty-six Weeks Ended</b> |                         |
|---|-----------------------------|-------------------------|-------------------------------|-------------------------|
|   | <b>July 1,<br/>2012</b>     | <b>July 3,<br/>2011</b> | <b>July 1,<br/>2012</b>       | <b>July 3,<br/>2011</b> |
| Revenues  | \$ 412,348                  | \$ 396,804              | \$ 813,605                    | \$ 777,148              |
| Operating expenses  | 305,035                     | 299,236                 | 613,295                       | 588,257                 |
| Depreciation and amortization   | 23,807                      | 20,945                  | 46,882                        | 39,646                  |
| General and administrative expenses   | 27,043                      | 27,710                  | 54,484                        | 60,498                  |
| Operating income  | 56,463                      | 48,913                  | 98,944                        | 88,747                  |
| Interest income   | 1,761                       | 1,629                   | 3,568                         | 3,198                   |
| Interest expense  | (20,617)                    | (19,412)                | (41,424)                      | (36,373)                |
| Income before income taxes, equity in earnings of affiliates and discontinued operations                                      | 37,607                      | 31,130                  | 61,088                        | 55,572                  |
| Provision for income taxes  | 14,991                      | 12,302                  | 24,208                        | 21,674                  |
| Equity in earnings of affiliates, net of income tax provision of \$303, \$563, \$624 and \$1,587, respectively                | 430                         | 1,418                   | 1,178                         | 2,080                   |
| Income from continuing operations   | 23,046                      | 20,246                  | 38,058                        | 35,978                  |
| Income (loss) from discontinued operations, net of tax provision (benefit) of \$(359), \$577, \$(330) and \$985, respectively | (570)                       | 917                     | (523)                         | 1,565                   |
| Net income  | 22,476                      | 21,163                  | 37,535                        | 37,543                  |
| Net (income) loss attributable to noncontrolling interests  | 25                          | 415                     | (9)                           | 825                     |
| Net income attributable to The GEO Group, Inc.  | \$ 22,501                   | \$ 21,578               | \$ 37,526                     | \$ 38,368               |
| Weighted-average common shares outstanding:   |                             |                         |                               |                         |
| Basic   | 60,839                      | 64,455                  | 60,803                        | 64,373                  |
| Diluted   | 61,066                      | 64,858                  | 60,984                        | 64,787                  |
| Income per Common Share Attributable to The GEO Group, Inc.(1):   |                             |                         |                               |                         |
| Basic:  |                             |                         |                               |                         |
| Income from continuing operations   | \$ 0.38                     | \$ 0.32                 | \$ 0.63                       | \$ 0.57                 |
| Income (loss) from discontinued operations  | (0.01)                      | 0.01                    | (0.01)                        | 0.02                    |

Edgar Filing: GEO GROUP INC - Form 10-Q

|   |            |           |           |           |
|---|------------|-----------|-----------|-----------|
| Income per common share attributable to The GEO Group, Inc. - basic   | \$ 0.37    | \$ 0.33   | \$ 0.62   | \$ 0.60   |
| Diluted:  |            |           |           |           |
| Income from continuing operations   | \$ 0.38    | \$ 0.32   | \$ 0.62   | \$ 0.57   |
| Income (loss) from discontinued operations  | (0.01)     | 0.01      | (0.01)    | 0.02      |
| Income per common share attributable to The GEO Group, Inc. - diluted   | \$ 0.37    | \$ 0.33   | \$ 0.62   | \$ 0.59   |
| Other comprehensive income, net of tax:   |            |           |           |           |
| Foreign currency translation adjustments, net of tax (benefit) provision of \$(195), \$411, \$125, and \$563, respectively    | \$ (2,068) | \$ 669    | \$ (142)  | \$ 1,140  |
| Pension liability adjustment, net of tax benefit of \$19, \$6, \$38, and \$13, respectively                                   | 29         | 10        | 59        | 19        |
| Loss on derivative instrument classified as cash flow hedge, net of tax benefit of \$203, \$99, \$220 and \$196, respectively | (430)      | (180)     | (399)     | (357)     |
| Total other comprehensive income (loss), net of tax   | (2,469)    | 499       | (482)     | 802       |
| Total comprehensive income  | 20,007     | 21,662    | 37,053    | 38,345    |
| Comprehensive (income) loss attributable to noncontrolling interests  | 58         | 418       | (4)       | 835       |
| Comprehensive income attributable to The GEO Group, Inc.  | \$ 20,065  | \$ 22,080 | \$ 37,049 | \$ 39,180 |

- (1) Note that earnings per share tables may contain slight summation differences due to rounding.  
The accompanying notes are an integral part of these unaudited consolidated financial statements.

**Table of Contents****THE GEO GROUP, INC.****CONSOLIDATED BALANCE SHEETS****JULY 1, 2012 AND JANUARY 1, 2012****(In thousands, except share data)**

|  | <b>July 1, 2012<br/>(Unaudited)</b> | <b>January 1,<br/>2012</b> |
|--|-------------------------------------|----------------------------|
| <b>ASSETS</b>  |                                     |                            |
| <i>Current Assets</i>  |                                     |                            |
| Cash and cash equivalents  | \$ 68,538                           | \$ 44,753                  |
| Restricted cash and investment (including VIEs <sup>1</sup> of \$29,373 and \$35,435, respectively)  | 40,071                              | 42,535                     |
| Accounts receivable, less allowance for doubtful accounts of \$2,779 and \$2,453, respectively   | 284,431                             | 285,810                    |
| Deferred income tax assets, net  | 28,726                              | 28,726                     |
| Prepaid expenses and other current assets  | 23,383                              | 50,346                     |
| Current assets of discontinued operations  | 6,713                               | 7,159                      |
| <b>Total current assets</b>  | <b>451,862</b>                      | <b>459,329</b>             |
| <i>Restricted Cash and Investments</i> (including VIEs of \$41,270 and \$38,930, respectively)   | 60,070                              | 57,912                     |
| <i>Property and Equipment, Net</i> (including VIEs of \$160,284 and \$162,665, respectively)   | 1,718,392                           | 1,705,306                  |
| <i>Assets Held for Sale</i>  | 5,390                               | 4,363                      |
| <i>Direct Finance Lease Receivable</i>   | 29,253                              | 32,146                     |
| <i>Deferred Income Tax Assets, Net</i>   | 1,711                               | 1,711                      |
| <i>Goodwill</i>  | 508,068                             | 508,066                    |
| <i>Intangible Assets, Net</i>  | 190,743                             | 200,342                    |
| <i>Other Non-Current Assets</i>  | 83,163                              | 79,576                     |
| <i>Non-Current Assets of Discontinued Operations</i>   | 576                                 | 865                        |
| <b>Total Assets</b>  | <b>\$ 3,049,228</b>                 | <b>\$ 3,049,616</b>        |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                                     |                            |
| <i>Current Liabilities</i>   |                                     |                            |
| Accounts payable   | \$ 63,681                           | \$ 69,632                  |
| Accrued payroll and related taxes  | 37,209                              | 38,130                     |
| Accrued expenses   | 121,604                             | 126,682                    |
| Current portion of capital lease obligations, long-term debt and non-recourse debt (including VIEs of \$21,000 and \$20,770, respectively) | 59,758                              | 53,666                     |
| Current liabilities of discontinued operations   | 702                                 | 708                        |
| <b>Total current liabilities</b>   | <b>282,954</b>                      | <b>288,818</b>             |
| <i>Deferred Income Tax Liabilities</i>   | 125,209                             | 125,209                    |
| <i>Other Non-Current Liabilities</i>   | 58,938                              | 56,381                     |
| <i>Capital Lease Obligations</i>   | 12,456                              | 13,087                     |
| <i>Long-Term Debt</i>  | 1,298,030                           | 1,319,068                  |
| <i>Non-Recourse Debt</i> (including VIEs of \$101,730 and \$108,335, respectively)   | 198,995                             | 208,532                    |
| <i>Commitments and Contingencies</i> (Note 12)   |                                     |                            |
| <i>Shareholders' Equity</i>  |                                     |                            |
| Preferred stock, \$0.01 par value, 30,000,000 shares authorized, none issued or outstanding  | 854                                 | 852                        |

## Edgar Filing: GEO GROUP INC - Form 10-Q

Common stock, \$0.01 par value, 90,000,000 shares authorized, 85,447,378 and 85,185,158 issued and 61,459,663 and 61,181,172 outstanding, respectively

|  |                     |                     |
|--|---------------------|---------------------|
| Additional paid-in capital   | 730,235             | 727,297             |
| Retained earnings  | 544,290             | 507,170             |
| Accumulated other comprehensive income   | 1,453               | 1,930               |
| Treasury stock, 23,987,715 and 24,003,986 shares, at cost, at July 1, 2012 and January 1, 2012, respectively | (213,735)           | (214,031)           |
| <b>Total shareholders' equity attributable to The GEO Group, Inc.</b>  | <b>1,063,097</b>    | <b>1,023,218</b>    |
| Noncontrolling interests   | 9,549               | 15,303              |
| <b>Total shareholders' equity</b>  | <b>1,072,646</b>    | <b>1,038,521</b>    |
| <b>Total Liabilities and Shareholders' Equity</b>  | <b>\$ 3,049,228</b> | <b>\$ 3,049,616</b> |

<sup>1</sup> Variable interest entities or VIEs

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

**Table of Contents****THE GEO GROUP, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****FOR THE TWENTY-SIX WEEKS ENDED****JULY 1, 2012 AND JULY 3, 2011****(In thousands)****(Unaudited)**

|  | <b>Twenty-six Weeks Ended</b> |                         |
|--|-------------------------------|-------------------------|
|  | <b>July 1,<br/>2012</b>       | <b>July 3,<br/>2011</b> |
| <b>Cash Flow from Operating Activities:</b>  |                               |                         |
| Net Income   | \$ 37,535                     | \$ 37,543               |
| Net (income) loss attributable to noncontrolling interests   | (9)                           | 825                     |
| Net income attributable to The GEO Group, Inc.   | 37,526                        | 38,368                  |
| <b>Adjustments to reconcile net income attributable to The GEO Group, Inc. to net cash provided by operating activities:</b> |                               |                         |
| Depreciation and amortization expense  | 46,882                        | 39,646                  |
| Amortization of debt issuance costs, discount and/or premium   | 1,369                         | 640                     |
| Restricted stock expense   | 2,061                         | 1,785                   |
| Stock option expense   | 1,433                         | 1,813                   |
| Provision for doubtful accounts  | 517                           | 999                     |
| Equity in earnings of affiliates, net of tax   | (1,178)                       | (2,080)                 |
| Income tax (benefit) provision of equity compensation  | 270                           | (392)                   |
| Loss on sale of property and equipment   | 915                           | 52                      |
| Dividends received from unconsolidated joint venture   |                               | 5,402                   |
| <b>Changes in assets and liabilities, net of acquisition:</b>  |                               |                         |
| Changes in accounts receivable, prepaid expenses and other assets  | 27,137                        | 16,176                  |
| Changes in accounts payable, accrued expenses and other liabilities  | 7,820                         | (11,124)                |
| Cash provided by operating activities - continuing operations  | 124,752                       | 91,285                  |
| Cash provided by operating activities - discontinued operations  | 1,061                         | 3,977                   |
| Net cash provided by operating activities  | 125,813                       | 95,262                  |
| <b>Cash Flow from Investing Activities:</b>  |                               |                         |
| Acquisition, cash consideration, net of cash acquired  |                               | (409,607)               |
| Proceeds from sale of property and equipment   | 231                           | 619                     |
| Proceeds from sale of assets held for sale   | 297                           | 6,640                   |
| Change in restricted cash and investments  | 333                           | (11,478)                |
| Capital expenditures   | (71,853)                      | (87,362)                |
| Net cash used in investing activities  | (70,992)                      | (501,188)               |
| <b>Cash Flow from Financing Activities:</b>  |                               |                         |
| Payments on long-term debt   | (169,282)                     | (46,832)                |
| Proceeds from long-term debt   | 145,000                       | 482,260                 |
| Distribution to noncontrolling interests   | (5,758)                       | (4,012)                 |



## Edgar Filing: GEO GROUP INC - Form 10-Q

|   |           |           |
|---|-----------|-----------|
| Proceeds from the exercise of stock options                   | 396       | 2,209     |
| Payments for retirement of common stock                       | (1,035)   |           |
| Income tax (provision) benefit of equity compensation         | (270)     | 392       |
| Debt issuance costs   | (44)      | (10,771)  |
| <br>  |           |           |
| Net cash (used in) provided by financing activities           | (30,993)  | 423,246   |
| Effect of Exchange Rate Changes on Cash and Cash Equivalents  | (43)      | 469       |
| <br>  |           |           |
| Net Increase in Cash and Cash Equivalents                     | 23,785    | 17,789    |
| Cash and Cash Equivalents, beginning of period                | 44,753    | 39,664    |
| <br>  |           |           |
| Cash and Cash Equivalents, end of period                      | \$ 68,538 | \$ 57,453 |
| <br>  |           |           |
| <b>Supplemental Disclosures:</b>                              |           |           |
| Non-cash Investing and Financing activities:                  |           |           |
| Capital expenditures in accounts payable and accrued expenses | \$ 6,801  | \$ 30,870 |

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

**Table of Contents****THE GEO GROUP, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****1. BASIS OF PRESENTATION**

The GEO Group, Inc., a Florida corporation, and subsidiaries (the Company, or GEO), is a leading provider of government-outsourced services specializing in the management of correctional, detention, mental health, residential treatment and re-entry facilities, and the provision of community based services and youth services domestically and internationally. The Company develops new facilities based on contract awards, using its project development expertise and experience to design, construct and finance what it believes are state-of-the-art facilities that maximize security and efficiency. GEO provides innovative compliance technologies, industry-leading monitoring services, and evidence-based supervision and treatment programs for community-based parolees, probationers and pretrial defendants. The Company also provides secure transportation services for offender and detainee populations as contracted domestically and in the United Kingdom through its joint venture GEO Amey PECS Ltd. (GEOAmey). As of July 1, 2012, the Company's worldwide operations included the management and/or ownership of approximately 75,000 beds at 109 correctional, detention and residential treatment facilities, including projects under development, and also included the provision of monitoring of more than 70,000 offenders in a community-based environment on behalf of approximately 900 federal, state and local correctional agencies located in all 50 states.

The Company's unaudited consolidated financial statements included in this Quarterly Report on Form 10-Q have been prepared in accordance with accounting principles generally accepted in the United States and the instructions to Form 10-Q and consequently do not include all disclosures required by Form 10-K. The accounting policies followed for quarterly financial reporting are the same as those disclosed in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 1, 2012 for the fiscal year ended January 1, 2012. The accompanying January 1, 2012 consolidated balance sheet, which has been retrospectively reclassified to reflect the assets and liabilities of discontinued operations (Refer to Note 8), has been derived from those audited financial statements. Additional information may be obtained by referring to the Company's Form 10-K (File No. 001-14260). In the opinion of management, all adjustments (consisting only of normal recurring items) necessary for a fair presentation of the financial information for the interim periods reported in this Form 10-Q have been made. Results of operations for the thirteen and twenty-six weeks ended July 1, 2012 are not necessarily indicative of the results for the entire fiscal year ending December 30, 2012.

**2. GOODWILL AND OTHER INTANGIBLE ASSETS**

The Company has recorded goodwill as a result of its business combinations. Goodwill is recorded as the difference, if any, between the aggregate consideration paid for an acquisition and the fair value of the net tangible assets, other intangible assets acquired and liabilities assumed. Changes in goodwill from January 1, 2012 to July 1, 2012 are related to fluctuations in foreign currency exchange rates.

The Company has also recorded other finite and indefinite lived intangible assets as a result of business combinations and also in connection with the previous purchase of additional shares in the Company's consolidated South African joint venture. Changes in gross carrying amount from January 1, 2012 to July 1, 2012 are related to fluctuations in foreign currency exchange rates. The Company's intangible assets include facility management contracts, non-compete agreements, the BI trade name and technology as follows (in thousands):

|   | July 1, 2012          |                          | January 1, 2012     |                       |                          |                     |
|---|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
|   | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Facility management contracts           | \$ 158,588            | \$ (29,528)              | \$ 129,060          | \$ 158,604            | \$ (22,985)              | \$ 135,619          |
| Covenants not to compete                | 8,570                 | (7,872)                  | 698                 | 8,570                 | (6,347)                  | 2,223               |
| Technology                              | 21,200                | (4,215)                  | 16,985              | 21,200                | (2,700)                  | 18,500              |
| Trade name                              | 44,000                |                          | 44,000              | 44,000                |                          | 44,000              |
| <b>Total acquired intangible assets</b> | <b>\$ 232,358</b>     | <b>\$ (41,615)</b>       | <b>\$ 190,743</b>   | <b>\$ 232,374</b>     | <b>\$ (32,032)</b>       | <b>\$ 200,342</b>   |



**Table of Contents**

Amortization expense relative to the Company's finite lived intangible assets was \$4.8 million and \$9.6 million, respectively, for the thirteen and twenty-six weeks ended July 1, 2012. Amortization expense relative to the Company's finite lived intangible assets was \$5.0 million and \$9.1 million respectively, for the thirteen and twenty-six weeks ended July 3, 2011. As of July 1, 2012, the weighted average period before the next contract renewal or extension for all of the facility management contracts was approximately 1.7 years.

Estimated amortization expense related to the Company's finite-lived intangible assets for the remainder of fiscal year 2012 through fiscal year 2016 and thereafter is as follows (in thousands):

| Fiscal Year       | Total<br>Amortization<br>Expense |
|-------------------|----------------------------------|
| Remainder of 2012 | \$ 8,525                         |
| 2013              | 15,195                           |
| 2014              | 14,979                           |
| 2015              | 14,949                           |
| 2016              | 14,856                           |
| Thereafter        | 78,239                           |
|                   | \$ 146,743                       |

**3. FINANCIAL INSTRUMENTS**

The following tables provide a summary of the Company's significant financial assets and liabilities carried at fair value and measured on a recurring basis as of July 1, 2012 and January 1, 2012 (in thousands):

|   | Fair Value Measurements at July 1, 2012    |   |  |   |
|---|--|---|--|---|
|   | Total Carrying<br>Value at<br>July 1, 2012 | Quoted Prices in<br>Active<br>Markets<br>(Level<br>1) | Significant Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs (Level 3) |
| <b>Assets:</b>                            |  |   |  |   |
| Interest rate swap derivative assets      | \$ 7,256                                   | \$  | \$ 7,256   | \$  |
| <b>Restricted investments:</b>            |  |   |  |   |
| Guaranteed Investment Contract            | \$ 5,742                                   | \$  | \$ 5,742   | \$  |
| Guaranteed Repurchase Agreements          | \$ 41,590                                  | \$  | \$ 41,590  | \$  |
| Rabbi Trust                               | \$ 8,941                                   | \$ 8,941  | \$   | \$  |
| Fixed income securities                   | \$ 2,081                                   | \$  | \$ 2,081   | \$  |
| <b>Liabilities:</b>                       |  |   |  |   |
| Interest rate swap derivative liabilities | \$ 589                                     | \$  | \$ 589   | \$  |

**Table of Contents**

|                                      | Fair Value Measurements at January 1, 2012 |   |   |   |
|--------------------------------------|--|---|---|---|
|                                      | Total Carrying Value at January 1, 2012    | Quoted Prices in Active Markets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| <b>Assets:</b>                       |  |   |   |   |
| Interest rate swap derivative assets | \$ 7,440                                   | \$  | \$ 7,440                                      | \$  |
| <b>Restricted investments:</b>       |  |   |   |   |
| Guaranteed Investment Contract       | \$ 5,742                                   | \$  | \$ 5,742                                      | \$  |
| Guaranteed Repurchase Agreements     | \$ 33,821                                  | \$  | \$ 33,821                                     | \$  |
| Rabbi Trust                          | \$ 8,016                                   | \$ 5,898                                  | \$ 2,118                                      | \$  |
| Fixed income securities              | \$ 2,013                                   | \$  | \$ 2,013                                      | \$  |

The Company's Level 1 investment included in the tables above as of July 1, 2012 and January 1, 2012 relates to the Company's rabbi trust established for GEO employee and employer contributions to The GEO Group Inc. Non-qualified Deferred Compensation Plan. These contributions are invested in mutual funds for which quoted market prices in active markets are available.

The Company's Level 2 financial instruments included in the tables above as of July 1, 2012 and January 1, 2012 consist of an interest rate swap asset held by the Company's Australian subsidiary, other interest rate swap assets of the Company, an investment in Canadian dollar denominated fixed income securities, a guaranteed investment contract which is a restricted investment related to CSC of Tacoma LLC and an Investment Repurchase Agreement (Repo Agreement) related to Municipal Correctional Finance, L.P. (MCF), the Company's consolidated VIE. As of July 1, 2012, the Repo Agreement consisted of guaranteed investments of \$23.8 million and \$17.8 million for the debt service reserve fund and the bond fund payment account, respectively. As of January 1, 2012 the Repo Agreement consisted of guaranteed investments of \$23.9 million and \$9.9 million for the debt service reserve fund and the bond fund payment account, respectively. The Repo Agreement is considered a Level 2 restricted investment since its fair value is estimated by using market interest rates for similar securities. The Australian subsidiary's interest rate swap asset is valued using a discounted cash flow model based on projected Australian borrowing rates. The Company's other interest rate swap assets and liabilities are based on pricing models which consider prevailing interest rates, credit risk and similar instruments. The Canadian dollar denominated securities, not actively traded, are valued using quoted rates for these and similar securities. The restricted investment in the guaranteed investment contract is valued using quoted rates for these and similar securities.

**4. FAIR VALUE OF ASSETS AND LIABILITIES**

The Company's consolidated balance sheets reflect certain financial assets and liabilities at carrying value. The following tables present the carrying values of those financial instruments and the estimated corresponding fair values at July 1, 2012 and January 1, 2012 (in thousands):

**Table of Contents**

|  | Carrying<br>Value as of<br>July 1,<br>2012 | Estimated Fair Value Measurements at July 1, 2012 |           |            |         |
|--|--|---|-----------|------------|---------|
|  |  | Total Fair<br>Value                               | Level 1   | Level 2    | Level 3 |
| <b>Assets:</b>                                     |  |   |           |            |         |
| Cash and cash equivalents                          | \$ 68,538                                  | \$ 68,538   | \$ 68,538 | \$         | \$      |
| Restricted cash                                    | 43,868                                     | 43,868  | 43,868    |            |         |
| <b>Liabilities:</b>                                |  |   |           |            |         |
| Borrowings under Senior Credit Facility            | \$ 767,632                                 | \$ 770,000  | \$        | \$ 770,000 | \$      |
| 7 <sup>3</sup> / <sub>4</sub> % Senior Notes       | 247,337                                    | 267,975   |           | 267,975    |         |
| 6.625% Senior Notes                                | 300,000                                    | 310,320   |           | 310,320    |         |
| Non-recourse debt, Australian subsidiary           | 37,434                                     | 39,135  |           | 39,135     |         |
| Other non-recourse debt, including current portion | 195,289                                    | 201,624   |           | 201,624    |         |

|  | Carrying<br>Value as of<br>January 1,<br>2012 | Estimated Fair Value Measurements at January 1, 2012 |           |            |         |
|--|---|--|-----------|------------|---------|
|  |   | Total Fair<br>Value                                  | Level 1   | Level 2    | Level 3 |
| <b>Assets:</b>                                     |   |  |           |            |         |
| Cash and cash equivalents                          | \$ 44,753                                     | \$ 44,753  | \$ 44,753 | \$         | \$      |
| Restricted cash                                    | 52,868  | 52,868   | 52,868    |            |         |
| <b>Liabilities:</b>                                |   |  |           |            |         |
| Borrowings under Senior Credit Facility            | \$ 782,962                                    | \$ 785,917   | \$        | \$ 785,917 | \$      |
| 7 <sup>3</sup> / <sub>4</sub> % Senior Notes       | 247,141                                       | 262,033  |           | 262,033    |         |
| 6.625% Senior Notes                                | 300,000                                       | 300,375  |           | 300,375    |         |
| Non-recourse debt, Australian subsidiary           | 40,345  | 41,347   |           | 41,347     |         |
| Other non-recourse debt, including current portion | 201,453                                       | 206,712  |           | 206,712    |         |

The fair values of the Company's cash and cash equivalents, and restricted cash approximates the carrying values of these assets at July 1, 2012 and January 1, 2012. Restricted cash consists of debt service funds used for payments on the Company's non-recourse debt. The fair values of the Company's 7<sup>3</sup>/<sub>4</sub>% senior unsecured notes due 2017 ( 7<sup>3</sup>/<sub>4</sub>% Senior Notes ) and the 6.625% senior unsecured notes due 2021 ( 6.625% Senior Notes ), although not actively traded, are based on published financial data for these instruments. The fair values of the Company's non-recourse debt related to South Texas Local Development Corporation ( STLDC ) and Washington Economic Development Finance Authority ( WEDFA ) are based on market prices for similar instruments. The fair value of the non-recourse debt related to the Company's Australian subsidiary is estimated using a discounted cash flow model based on current Australian borrowing rates for similar instruments. The fair value of the non-recourse debt related to MCF is estimated using a discounted cash flow model based on the Company's current borrowing rates for similar instruments. The fair value of borrowings under the Senior Credit Facility is based on an estimate of trading value considering the Company's borrowing rate, the undrawn spread and similar instruments.

**5. SHAREHOLDERS' EQUITY**

The following table presents the changes in shareholders' equity that are attributable to the Company's shareholders and to noncontrolling interests (in thousands):

**Table of Contents**

|  | Common shares |        |                            | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury shares |              | Noncontrolling Interests | Total Shareholders Equity |
|--|---------------|--------|----------------------------|-------------------|---|-----------------|--------------|--------------------------|---------------------------|
|  | Shares        | Amount | Additional Paid-In Capital |                   |   | Shares          | Amount       |                          |                           |
| Balance January 1, 2012                              | 61,181        | \$ 852 | \$ 727,297                 | \$ 507,170        | \$ 1,930                                      | 24,004          | \$ (214,031) | \$ 15,303                | \$ 1,038,521              |
| Stock option and restricted stock award transactions | 347           | 3      | 393                        |                   |   |                 |              |                          | 396                       |
| Tax provision related to equity compensation         |               |        | (270)                      |                   |   |                 |              |                          | (270)                     |
| Stock-based compensation expense                     |               |        | 3,494                      |                   |   |                 |              |                          | 3,494                     |
| Cancellation of restricted stock                     | (26)          |        |                            |                   |   |                 |              |                          |                           |
| Retirement of common stock                           | (58)          | (1)    | (628)                      | (406)             |   |                 |              |                          | (1,035)                   |
| Reissuance of treasury stock in connection with ESPP | 16            |        |                            |                   |   | (16)            | 296          |                          | 296                       |
| Other adjustments to additional paid-in capital      |               |        | (51)                       |                   |   |                 |              |                          | (51)                      |
| Distribution to non-controlling interests            |               |        |                            |                   |   |                 |              | (5,758)                  | (5,758)                   |
| Total comprehensive income                           |               |        |                            | 37,526            | (477)   |                 |              | 4                        | 37,053                    |
| Balance July 1, 2012                                 | 61,460        | \$ 854 | \$ 730,235                 | \$ 544,290        | \$ 1,453                                      | 23,988          | \$ (213,735) | \$ 9,549                 | \$ 1,072,646              |

**6. EQUITY INCENTIVE PLANS**

As of July 1, 2012, under the 2006 Stock Incentive Plan ( 2006 Plan ), the Company had 1,509,454 shares of common stock available for issuance pursuant to future awards that may be granted under the plan of which up to 681,054 shares were available for the issuance of awards other than stock options. During the twenty-six weeks ended July 1, 2012, the Company repurchased and retired 57,457 shares of fully vested employee equity awards.

**Stock Options**

The Company uses a Black-Scholes option valuation model to estimate the fair value of each option awarded. A summary of the activity of stock option awards issued and outstanding under Company Plans is as follows for the twenty-six weeks ended July 1, 2012:

| Fiscal Year                            | Shares<br>(in thousands) | Wtd. Avg.<br>Exercise<br>Price | Wtd. Avg.<br>Remaining<br>Contractual Term<br>(years) | Aggregate<br>Intrinsic<br>Value<br>(in thousands) |
|--|--------------------------|--------------------------------|---|---|
| Options outstanding at January 1, 2012 | 1,601                    | \$ 19.44                       | 6.73  | \$ 2,778  |
| Options granted                        |                          |                                |   |   |
| Options exercised                      | (62)                     | 6.41                           |   |   |
| Options forfeited/canceled/expired     | (51)                     | 22.47                          |   |   |
| Options outstanding at July 1, 2012    | 1,488                    | \$ 19.88                       | 6.36  | \$ 5,228  |

## Edgar Filing: GEO GROUP INC - Form 10-Q

|                                     |       |          |      |          |
|-------------------------------------|-------|----------|------|----------|
| Options exercisable at July 1, 2012 | 1,017 | \$ 18.38 | 5.53 | \$ 4,828 |
|-------------------------------------|-------|----------|------|----------|

No stock options were granted by the Company during the twenty-six weeks ended July 1, 2012. During the fiscal year ended January 1, 2012, the Company granted 554,350 stock options to its employees with an aggregate fair value of \$5.4 million and a weighted average exercise price of \$24.71. During the fiscal year ended January 1, 2012, 297,406 shares of common stock were issued to employees as a result of option exercises. For the twenty-six weeks ended July 1, 2012 and July 3, 2011, the amount of stock-based compensation expense related to stock options was \$1.4 million and \$1.8 million, respectively. As of July 1, 2012, the Company had \$3.1 million of unrecognized compensation costs related to non-vested stock option awards that are expected to be recognized over a weighted average period of 2.3 years.



**Table of Contents****Restricted Stock**

Shares of restricted stock become unrestricted shares of common stock upon vesting on a one-for-one basis. The cost of these awards is determined using the closing price of the Company's common stock on the date of the grant and compensation expense is recognized over the vesting period. Generally, the restricted stock awards vest in equal increments over either a three or four year period. A summary of the activity of restricted stock outstanding is as follows for the twenty-six weeks ended July 1, 2012:

|   | Shares<br>(in thousands) | Wtd. Avg.<br>Grant<br>Date<br>Fair<br>Value |
|---|--------------------------|---|
| Restricted stock outstanding at January 1, 2012 | 442                      | \$ 23.32                                    |
| Granted   | 285                      | 17.62                                       |
| Vested  | (108)                    | 24.60                                       |
| Forfeited/canceled                              | (22)                     | 22.45                                       |
| Restricted stock outstanding at July 1, 2012    | 597                      | \$ 20.62                                    |

During the twenty-six weeks ended July 1, 2012, the Company issued 285,000 restricted stock awards to its Directors and to certain senior employees. Of these awards, 205,000 are performance based awards which will be forfeited if the Company does not achieve certain targeted revenue in its fiscal year ending December 30, 2012. These performance based awards were canceled and new performance awards were granted on July 20, 2012 with revised performance targets. See Note 16 Subsequent Events for further discussion. During the fiscal year ended January 1, 2012, the Company issued 381,010 restricted stock awards to its Directors and certain senior employees. Of these awards, 205,000 were performance based awards for which the targeted revenue was achieved for the fiscal year ended January 1, 2012. For performance based awards granted prior to July 20, 2012, these grants vest over a three year period from the date of the award if the targeted revenue is achieved. The aggregate fair value of the awards issued during the twenty-six weeks ended July 1, 2012 and the fiscal year ended January 1, 2012, based on the closing price of the Company's common stock on the respective grant dates, was \$5.0 million and \$9.3 million, respectively.

During the fiscal year ended January 1, 2012, 94,530 shares of common stock were issued to employees as a result of the satisfaction of vesting requirements. For the twenty-six weeks ended July 1, 2012 and July 3, 2011, the Company recognized \$2.1 million and \$1.8 million, respectively, of compensation expense related to its restricted stock awards. As of July 1, 2012, the Company had \$9.9 million of unrecognized compensation costs related to non-vested restricted stock awards that are expected to be recognized over a weighted average period of 2.5 years.

**Employee Stock Purchase Plan**

On July 9, 2011, the Company adopted The GEO Group Inc. 2011 Employee Stock Purchase Plan (the "Plan"), subject to obtaining shareholder approval. The Plan was approved by the Company's Compensation Committee and its Board of Directors on May 4, 2011. The purpose of the Plan, which is qualified under Section 423 of the Internal Revenue Service Code of 1986, as amended, is to encourage stock ownership through payroll deductions by the employees of GEO and designated subsidiaries of GEO in order to increase their identification with the Company's goals and secure a proprietary interest in the Company's success. These deductions are used to purchase shares of the Company's Common Stock at a 5% discount from the then current market price.

The Plan, which was approved by the Company's shareholders on May 4, 2012, specifies that the share purchases for the pre-shareholder approval periods began on June 29, 2012. During the pre-shareholder approval periods, which ended on June 29, 2012, the Plan was considered to be compensatory due to an option feature contained in the Plan during that period. Stock-based compensation recorded during the pre-shareholder period was not significant. During the post-shareholder approval period the Plan no longer contains an option feature and therefore is considered to be non-compensatory. As such, no compensation expense will be recorded during the post-shareholder approval period. Share purchases for the post-shareholder approval offering periods will begin on the last day of each month. On June 29, 2012, 16,271 shares were issued out of the Company's treasury stock in connection with the pre-shareholder approval periods. The Company will offer up to 500,000 shares of its common stock for sale to eligible employees.



**Table of Contents****7. EARNINGS PER SHARE****Stock Repurchase Program**

On July 14, 2011, the Company announced that its Board of Directors approved a stock repurchase program of up to \$100.0 million of the Company's common stock effective through December 31, 2012. The stock repurchase program will be funded primarily with cash on hand, free cash flow, and borrowings under the Company's Revolving Credit Facility. The stock repurchase program is intended to be implemented through purchases made from time to time in the open market or in privately negotiated transactions, in accordance with applicable securities and stock exchange requirements. The program may also include repurchases from time to time from executive officers or directors of vested restricted stock and/or vested stock options. The stock repurchase program does not obligate the Company to purchase any specific amount of its common stock and may be suspended or extended at any time at the Company's discretion. During the fiscal year ended January 1, 2012, the Company purchased 3.9 million shares of its common stock at a cost of \$75.0 million primarily purchased with proceeds from the Company's Revolving Credit Facility. There were no repurchases of common stock under the stock repurchase program during the twenty-six weeks ended July 1, 2012.

**Earnings per share**

Basic earnings per share is computed by dividing the net income attributable to The GEO Group, Inc. shareholders by the weighted average number of outstanding shares of common stock. The calculation of diluted earnings per share is similar to that of basic earnings per share, except that the denominator includes dilutive common stock equivalents such as stock options and shares of restricted stock. Basic and diluted earnings per share (EPS) were calculated for the thirteen and twenty-six weeks ended July 1, 2012 and July 3, 2011 as follows (in thousands, except per share data):

|   | Thirteen Weeks Ended |              | Twenty-six Weeks Ended |              |
|---|----------------------|--------------|------------------------|--------------|
|   | July 1, 2012         | July 3, 2011 | July 1, 2012           | July 3, 2011 |
| Income from continuing operations   | \$ 23,046            | \$ 20,246    | \$ 38,058              | \$ 35,978    |
| Net (income) loss attributable to noncontrolling interests                | 25                   | 415          | (9)                    | 825          |
| Net income from continuing operations attributable to The GEO Group, Inc. | 23,071               | 20,661       | 38,049                 | 36,803       |
| Basic earnings per share attributable to The GEO Group, Inc.:             |                      |              |                        |              |
| Weighted average shares outstanding                                       | 60,839               | 64,455       | 60,803                 | 64,373       |
| Per share amount  | \$ 0.38              | \$ 0.32      | \$ 0.63                | \$ 0.57      |
| Diluted earnings per share attributable to The GEO Group, Inc.:           |                      |              |                        |              |
| Weighted average shares outstanding                                       | 60,839               | 64,455       | 60,803                 | 64,373       |
| Effect of dilutive securities: Stock options and restricted stock         | 227                  | 403          | 181                    | 414          |
| Weighted average shares assuming dilution                                 | 61,066               | 64,858       | 60,984                 | 64,787       |
| Per share amount  | \$ 0.38              | \$ 0.32      | \$ 0.62                | \$ 0.57      |

**Thirteen Weeks**

For the thirteen weeks ended July 1, 2012, 57,934 weighted average shares of common stock underlying options were excluded from the computation of diluted EPS because the effect would be anti-dilutive. 1,642 shares of restricted stock were anti-dilutive.

For the thirteen weeks ended July 3, 2011, 77,472 weighted average shares of common stock underlying options were excluded from the computation of diluted EPS because the effect would be anti-dilutive. No shares of restricted stock were anti-dilutive.

**Twenty-six Weeks**

## Edgar Filing: GEO GROUP INC - Form 10-Q

For the twenty-six weeks ended July 1, 2012, 112,428 weighted average shares of common stock underlying options were excluded from the computation of diluted EPS because the effect would be anti-dilutive. 1,584 shares of restricted stock were anti-dilutive.

For the twenty-six weeks ended July 3, 2011, 56,094 weighted average shares of common stock underlying options were excluded from the computation of diluted EPS because the effect would be anti-dilutive. No shares of restricted stock were anti-dilutive.

**Table of Contents****8. DISCONTINUED OPERATIONS**

The termination of any of the Company's management contracts by expiration or otherwise, may result in the classification of the assets, liabilities and cash flows associated with, and operating results of such management contracts, net of taxes, as a discontinued operation. The Company presents such events as discontinued operations so long as the financial results can be clearly identified, the operations and cash flows are completely eliminated from ongoing operations, and so long as the Company does not have any significant continuing involvement in the operations of the component after the disposal or termination transaction. Historically, the Company has classified operations as discontinued in the period they are announced as normally all continuing cash flows cease within three to six months of that date. During the thirteen weeks ended July 1, 2012, the Company discontinued operations at certain of its domestic facilities. The results of operations, net of taxes, and the assets and liabilities of these operations, each as further described below, have been retrospectively reflected in the accompanying consolidated financial statements as discontinued operations for all prior periods presented. Assets, primarily consisting of accounts receivable, and liabilities have been presented separately in the accompanying consolidated balance sheets for all prior periods presented.

**U.S. Corrections & Detention:** On April 19, 2012, the Company announced its discontinuation of its managed-only contract with the State of Mississippi, Department of Corrections for the 1,500-bed East Mississippi Correctional Facility ( East Mississippi ) effective July 19, 2012. In connection with the discontinuation of East Mississippi, the Company has also discontinued its managed-only contracts with the State of Mississippi, Department of Corrections for the 1,000-bed Marshall County Correctional Facility effective August 13, 2012, and the 1,450-bed Walnut Grove Youth Correctional Facility effective July 1, 2012. Revenues related to the discontinued operations were \$11.2 million and \$11.0 million, for the thirteen weeks ended July 1, 2012 and July 3, 2011, respectively and \$22.3 million and \$22.4 million for the twenty-six weeks ended July 1, 2012 and July 3, 2011, respectively.

**9. DERIVATIVE FINANCIAL INSTRUMENTS**

The Company's primary objective in holding derivatives is to reduce the volatility of earnings and cash flows associated with changes in interest rates. The Company measures its derivative financial instruments at fair value.

As of July 1, 2012, the Company had four interest rate swap agreements in the aggregate notional amount of \$100.0 million. The Company has designated these interest rate swaps as hedges against changes in the fair value of a designated portion of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes due 2017 ( 7<sup>1</sup>/<sub>4</sub>% Senior Notes ) due to changes in underlying interest rates. These swap agreements, which have payment, expiration dates and call provisions that mirror the terms of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes, effectively convert \$100.0 million of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes into variable rate obligations. Each of the swaps has a termination clause that gives the counterparty the right to terminate the interest rate swaps at fair market value, under certain circumstances. In addition to the termination clause, the Agreements also have call provisions which specify that the lender can elect to settle the swap for the call option price. Under the agreements, the Company receives a fixed interest rate payment from the financial counterparties to the agreements equal to 7<sup>3</sup>/<sub>4</sub>% per year calculated on the notional \$100.0 million amount, while it makes a variable interest rate payment to the same counterparties equal to the three-month LIBOR plus a fixed margin of between 4.16% and 4.29%, also calculated on the notional \$100.0 million amount. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes. Total net gain (loss), entirely offset by a corresponding increase in the fair value of the variable rate portion of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes, recognized and recorded in earnings related to these fair value hedges was \$(0.1) million and \$0.2 million during the thirteen and twenty-six weeks ended July 1, 2012, respectively. As of July 1, 2012 and January 1, 2012, the swap assets' fair values were \$7.3 million and \$7.4 million, respectively and are included as Other Non-Current Assets in the accompanying consolidated balance sheets. There was no material ineffectiveness of these interest rate swaps during the fiscal periods ended July 1, 2012 or July 3, 2011.

The Company's Australian subsidiary is a party to an interest rate swap agreement to fix the interest rate on its variable rate non-recourse debt to 9.7%. The Company has determined the swap, which has a notional amount of AUD 50.9 million, payment and expiration dates, and call provisions that coincide with the terms of the non-recourse debt to be an effective cash flow hedge. Accordingly, the Company records the change in the value of the interest rate swap in accumulated other comprehensive income, net of applicable income taxes. Total unrealized losses, net of tax, recognized in the periods and recorded in accumulated other comprehensive income, net of tax, related to this cash flow hedge was \$0.4 million and \$0.4 million for the thirteen and twenty-six weeks ended July 1, 2012 respectively. The total fair value of the swap (liability) asset as of July 1, 2012 and January 1, 2012 was \$(0.6) million and \$0.0 million, respectively, and is recorded as a component of other (liabilities) assets within the accompanying consolidated balance sheets. There was no material ineffectiveness of this interest rate swap for the periods 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).

**Table of Contents****10. VARIABLE INTEREST ENTITIES**

The Company evaluates its joint ventures and other entities in which it has a variable interest (a VIE), generally in the form of investments, loans, guarantees, or equity in order to determine if it has a controlling financial interest and is required to consolidate the entity as a result. The reporting entity with a variable interest that provides the entity with a controlling financial interest in the VIE will have both of the following characteristics: (i) the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and (ii) the obligation to absorb the losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

The Company consolidates South Texas Local Development Corporation ( STLDC ), a VIE. STLDC was created to finance construction for the development of a 1,904-bed facility in Frio County, Texas. STLDC, the owner of the complex, issued \$49.5 million in taxable revenue bonds and has an operating agreement with the Company, which provides the Company with the sole and exclusive right to operate and manage the detention center. The operating agreement and bond indenture require the revenue from the contract to 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 the Company to cover operating expenses and management fees. The Company is responsible for the entire operations of the facility including the payment of all operating expenses whether or not there are sufficient revenues. The bonds have a ten-year term and are non-recourse to the Company. At the end of the ten-year term of the bonds, title and ownership of the facility transfers from STLDC to the Company. The carrying value of the facility as of July 1, 2012 and January 1, 2012 was \$26.1 million and \$26.4 million, respectively and is included in Property and Equipment in the accompanying consolidated balance sheets.

MCF was created in August 2001 as a special limited partnership for the purpose of acquiring, owning, leasing and operating low to medium security adult and juvenile correction and treatment facilities. At its inception, MCF purchased assets representing eleven facilities from certain wholly owned subsidiaries of Cornell Companies, Inc. ( Cornell ), a wholly owned GEO subsidiary, and leased those assets back to Cornell under a Master Lease Agreement (the Lease ). These assets were purchased from Cornell using proceeds from the 8.47% Revenue Bonds due 2016. Under the terms of the Lease, the Company will lease the assets for the remainder of the 20-year base term, which ends in 2021, and has options at its sole discretion to renew the Lease for up to approximately 25 additional years. MCF's sole source of revenue is from the Company and as such the Company has the power to direct the activities of the VIE that most significantly impact its performance. The Company's risk is generally limited to the rental obligations under the operating leases. This entity is included in the accompanying consolidated financial statements and all intercompany transactions are eliminated in consolidation. MCF maintains separate financial statements and all of the assets to which MCF has title are included therein. It should be noted that even though the Company consolidates MCF for accounting purposes, this VIE is a separate entity owned by unrelated third parties. MCF's assets and credit are not available to satisfy the debts and other obligations of the Company. On April 24, 2012, the Company signed a definitive agreement to purchase 100% of the partnership interests of MCF for approximately \$27 million in cash plus the release of approximately \$10 million in cash held in escrow for the benefit of MCF. In addition, in connection with the transaction, the Company will pay approximately \$67 million, net of bond cash reserves and inclusive of a net make-whole premium of approximately \$15 million, to redeem the MCF bonds. The Company expects to incur a one-time loss on extinguishment of debt in connection with the redemption of the bonds of approximately \$8 million. Closing of the transaction is conditional on the Company redeeming the outstanding MCF bonds. The Company expects to close the transaction during its third fiscal quarter of 2012.

The Company does not consolidate its 50% owned South African joint venture interest in South African Custodial Services Pty. Limited ( SACS ), a VIE. SACS joint venture investors are GEO and Kensani Corrections, Pty. Ltd; each partner owns a 50% share. The Company has determined it is not the primary beneficiary of SACS since it does not have the power to direct the activities of SACS that most significantly impact its performance. As such, the Company's investment in this entity is accounted for under the equity method of accounting. SACS was established and subsequently, in 2001, was awarded a 25-year contract to design, finance and build the Kutama Sinthumule Correctional Centre in Louis Trichardt, South Africa. To fund the construction of the prison, SACS obtained long-term financing from its equity partners and lenders, the repayment of which is fully guaranteed by the South African government, except in the event of default, in which case the government guarantee is reduced to 80%. The Company's maximum exposure for loss under this contract is limited to its investment in the joint venture of \$8.1 million at July 1, 2012 and its guarantees related to SACS discussed in Note 11 - Debt.

The Company does not consolidate its 50% owned joint venture in the United Kingdom. In February 2011, The GEO Group Limited, the Company's wholly-owned subsidiary in the United Kingdom ( GEO UK ), executed a Shareholders Agreement (the Shareholders Agreement ) with Amey Community Limited ( Amey ) and Amey UK PLC ( Amey Guarantor ) to form GEO Amey PECS Limited ( GEOAmey ), a private company limited by shares incorporated in England and Wales. GEOAmey was formed by GEO UK and Amey for the purpose of performing prisoner escort and related custody services in England and Wales. In order to form this private company, GEOAmey issued share capital of £100 divided into 100 shares of £1 each and allocated the shares 50/50 to GEO UK and Amey. GEO UK and Amey each have three directors appointed to the Board of Directors and neither party has the power to direct the activities that most significantly impact the performance of



**Table of Contents**

GEOAmeY. As such, the Company's investment in this entity is accounted for under the equity method of accounting. Both parties provide lines of credit of £12 million, or \$18.9 million as of July 1, 2012, to ensure that GEOAmeY can comply with future contractual commitments related to the performance of its operations. As of July 1, 2012, \$19.1 million, including accrued interest, was owed to the Company by GEOAmeY under the line of credit. GEOAmeY commenced operations on August 29, 2011. The Company has recorded \$0.9 million and \$1.4 million losses, net of tax impact, for GEOAmeY's operations during the thirteen and twenty-six weeks ended July 1, 2012, respectively, which is included in Equity in earnings of affiliates in the accompanying consolidated statement of comprehensive income.

**11. DEBT**

Debt outstanding as of July 1, 2012 and January 1, 2012 consisted of the following (in thousands):

|  | July 1, 2012 | January 1, 2012 |
|--|--------------|-----------------|
| Capital Lease Obligations  | \$ 13,627    | \$ 14,171       |
| Senior Credit Facility:  |              |                 |
| Term loans   | 474,000      | 482,500         |
| Discount on term loan  | (1,368)      | (1,538)         |
| Revolver   | 295,000      | 302,000         |
| <br>   |              |                 |
| Total Senior Credit Facility   | 767,632      | 782,962         |
| 6.625% Senior Notes:   |              |                 |
| Notes due in 2021  | 300,000      | 300,000         |
| 7 3/4% Senior Notes:   |              |                 |
| Notes due in 2017  | 250,000      | 250,000         |
| Discount on Notes  | (2,663)      | (2,859)         |
| Swap on Notes  | 7,256        | 7,411           |
| <br>   |              |                 |
| Total 7 3/4% Senior Notes  | 254,593      | 254,552         |
| Non-Recourse Debt :  |              |                 |
| Non-Recourse Debt  | 227,549      | 235,430         |
| Premium on Non-Recourse Debt   | 6,846        | 8,304           |
| Discount on Non-Recourse Debt  | (1,672)      | (1,936)         |
| <br>   |              |                 |
| Total Non-Recourse Debt  | 232,723      | 241,798         |
| Other debt   | 664          | 870             |
| <br>   |              |                 |
| Total debt   | 1,569,239    | 1,594,353       |
| Current portion of capital lease obligations, long-term debt and non-recourse debt | (59,758)     | (53,666)        |
| Capital Lease Obligations, long-term portion                                       | (12,456)     | (13,087)        |
| Non-Recourse Debt  | (198,995)    | (208,532)       |
| <br>   |              |                 |
| Long-Term Debt   | \$ 1,298,030 | \$ 1,319,068    |

**Senior Credit Facility**

As of July 1, 2012, the Senior Credit Facility, as amended, was comprised of: (i) a \$150.0 million Term Loan A ( Term Loan A ), currently bearing interest at LIBOR plus 3.00% and maturing August 4, 2015, (ii) a \$150.0 million Term Loan A-2 ( Term Loan A-2 ), currently bearing interest at LIBOR plus 3.00% and maturing August 4, 2015, (iii) a \$200.0 million Term Loan B ( Term Loan B ) currently bearing interest at LIBOR plus 2.75% with a LIBOR floor of 1.00% and maturing August 4, 2016, and (iv) a \$500.0 million Revolving Credit Facility ( Revolver ) currently bearing interest at LIBOR plus 3.00% and maturing August 4, 2015.

As of July 1, 2012, the Company had \$472.6 million in aggregate borrowings outstanding, net of discount, under the Term Loan A, Term Loan A-2 and Term Loan B, \$295.0 million in borrowings under the Revolver, and approximately \$56.5 million in letters of credit which leaves



## Edgar Filing: GEO GROUP INC - Form 10-Q

\$148.5 million in additional borrowing capacity under the Revolver. The weighted average interest rate on outstanding borrowings under the Senior Credit Facility as of July 1, 2012 was 3.4%.

**Table of Contents**

Indebtedness under the Revolver, the Term Loan A and the Term Loan A-2 bears interest based on the Total Leverage Ratio as of the most recent determination date, as defined, in each of the instances below at the stated rate:

**Interest Rate under the Revolver, Term Loan A and**

|                      | <b>Term Loan A-2</b>            |
|----------------------|---------------------------------|
| LIBOR borrowings     | LIBOR plus 2.00% to 3.00%.      |
| Base rate borrowings | Prime Rate plus 1.00% to 2.00%. |
| Letters of credit    | 2.00% to 3.00%.                 |
| Unused Revolver      | 0.375% to 0.50%.                |

The Senior Credit Facility requires the Company to meet certain financial covenants, including a maximum Total Leverage Ratio, a maximum Senior Secured Leverage Ratio and an Interest Coverage Ratio. The Company believes it was in compliance with all of the covenants of the Senior Credit Facility as of July 1, 2012.

***7<sup>3</sup>/<sub>4</sub>% Senior Notes***

Interest on the 7<sup>3</sup>/<sub>4</sub>% Senior Notes accrues at the stated rate. The Company pays interest semi-annually in arrears on April 15 and October 15 of each year. On or after October 15, 2013, the Company may, at its option, redeem all or a part of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes at the redemption prices set forth in the indenture governing the 7<sup>3</sup>/<sub>4</sub>% Senior Notes. The indenture governing the notes contains certain covenants, including limitations and restrictions on the Company and its restricted subsidiaries. The Company believes it was in compliance with all of the covenants of the indenture governing the 7<sup>3</sup>/<sub>4</sub>% Senior Notes as of July 1, 2012.

***6.625% Senior Notes***

Interest on the 6.625% Senior Notes accrues at the stated rate. The Company pays interest semi-annually in arrears on February 15 and August 15. On or after February 15, 2016, the Company may, at its option, redeem all or part of the 6.625% Senior Notes at the redemption prices set forth in the indenture governing the 6.625% Senior Notes. The indenture governing the notes contains certain covenants, including limitations and restrictions on the Company and its restricted subsidiaries. The Company believes it was in compliance with all of the covenants of the indenture governing the 6.625% Senior Notes as of July 1, 2012.

***Non-Recourse Debt******South Texas Detention Complex***

The Company has a debt service requirement related to the development of the South Texas Detention Complex, a 1,904-bed detention complex in Frio County, Texas. In order to finance the construction of the complex, STLDC was created and issued \$49.5 million in taxable revenue bonds. These bonds mature in February 2016 and have fixed coupon rates between 4.76% and 5.07%. Additionally, the Company is owed \$5.0 million in the form of subordinated notes by STLDC which represents the principal amount of financing provided to STLDC by CSC for initial development.

On February 1, 2012, STLDC made a payment from its restricted cash account of \$5.0 million for the current principal portion of its periodic debt service requirement in relation to the STLDC operating agreement and bond indenture. As of July 1, 2012, the remaining balance of the debt service requirement under the STLDC financing agreement is \$22.4 million, of which \$5.2 million is due within the next twelve months. Also, as of July 1, 2012, included in current restricted cash and non-current restricted cash is \$6.3 million and \$12.3 million, respectively, of 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 a detention center in Tacoma, Washington, known as the Northwest Detention Center, which was completed and opened for operation in April 2004. The Company began to operate this facility following its acquisition of CSC in November 2005. In connection with this financing, CSC formed a special purpose entity, CSC of Tacoma LLC, of which CSC is the only member, the sole purposes of which are to own, operate, mortgage, lease, finance, refinance and otherwise deal with this facility. CSC of Tacoma LLC owns the facility, as well as all of its other assets; the Company provides detention, transportation and related services for the United States Government from this facility pursuant to a Use Agreement between the Company and CSC of Tacoma LLC. The assets of CSC

## Edgar Filing: GEO GROUP INC - Form 10-Q

of Tacoma LLC are owned by CSC of Tacoma LLC. They are included in the consolidated financial statements of the Company in accordance with generally accepted accounting principles. The assets and liabilities of CSC of Tacoma LLC are recognized on the CSC of Tacoma LLC balance sheet.

**Table of Contents**

In connection with the original financing, CSC of Tacoma LLC, a wholly-owned subsidiary of CSC, issued a \$57.0 million note payable to the Washington Economic Development Finance Authority, referred to as WEDFA, an instrumentality of the State of Washington, which issued revenue bonds and subsequently loaned the proceeds of the bond issuance back to CSC for the purposes of constructing the Northwest Detention Center. The bonds are non-recourse to the Company and the loan from WEDFA to CSC is also non-recourse to the Company. These bonds mature in October 2014 and have fixed coupon rates between 4.00% and 4.10%. 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. No principal payments were made during the twenty-six weeks ended July 1, 2012. As of July 1, 2012, the remaining balance of the debt service requirement is \$19.7 million, of which \$6.3 million is classified as current in the accompanying consolidated balance sheet.

On December 9, 2011, WEDFA issued \$54.4 million of its Washington Economic Development Finance Authority Taxable Economic Development Revenue Bonds, series 2011 ( 2011 Revenue Bonds ). The 2011 Revenue Bonds were rated AA- by Standard & Poor's Ratings Services and the scheduled payment of principal and interest is guaranteed by municipal bond insurance issued by Assured Guaranty Municipal Corp. The 2011 Revenue Bonds have an average all-in cost of approximately 6.4%, including debt issuance costs and the bond discount, and maturity dates ranging from October 1, 2014 through October 1, 2021. The 2011 Revenue Bonds were issued to provide funds to make a loan to CSC of Tacoma, LLC for purposes of reimbursing GEO for costs incurred by GEO for the 2009 expansion of the Northwest Detention Facility and paying the costs of issuing the 2011 Revenue Bonds. The payment of principal and interest on the bonds is non-recourse to GEO. None of the bonds nor CSC's obligations under the loan are obligations of GEO nor are they guaranteed by GEO.

As of July 1, 2012, included in current restricted cash and non-current restricted cash is \$9.3 million and \$3.3 million, respectively, of funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.

*MCF*

MCF is obligated for the outstanding balance of the 8.47% Revenue Bonds. The bonds bear interest at a rate of 8.47% per annum and are payable in semi-annual installments of interest and annual installments of principal. All unpaid principal and accrued interest on the bonds is due on the earlier of August 1, 2016 (maturity) or as noted under the bond documents. The bonds are limited, non-recourse obligations of MCF and are collateralized by the property and equipment, bond reserves, assignment of subleases and substantially all assets related to the eleven facilities owned by MCF. The bonds are not guaranteed by the Company or its subsidiaries. As of July 1, 2012, the aggregate principal amount of these bonds was \$77.9 million, excluding the effect of the unamortized premium of \$6.8 million and net of the current portion of \$15.8 million. As of January 1, 2012, the aggregate principal amount of these bonds was \$77.9 million, excluding the effect of the unamortized premium of \$8.3 million and net of the current portion of \$15.8 million. These balances are included as Non-Recourse Debt on the accompanying consolidated balance sheets.

The 8.47% Revenue Bond indenture provides for the establishment and maintenance by MCF for the benefit of the trustee under the indenture of a debt service reserve fund. As of July 1, 2012, the debt service reserve fund has a balance of \$23.8 million. The debt service reserve fund is available to the trustee to pay debt service on the 8.47% Revenue Bonds when needed, and to pay final debt service on the 8.47% Revenue Bonds. If MCF were to default in its obligation under the 8.47% Revenue Bonds indenture, the trustee may declare the principal outstanding and accrued interest immediately due and payable. MCF has the right to cure a default of non-payment obligations. The 8.47% Revenue Bonds are subject to extraordinary mandatory redemption in certain instances upon casualty or condemnation. The 8.47% Revenue Bonds may be redeemed at the option of MCF prior to their final scheduled payment dates at par plus accrued interest plus a make-whole premium. On April 24, 2012, the Company signed a definitive agreement to purchase 100% of the partnership interests of MCF for approximately \$27 million in cash plus the release of approximately \$10 million in cash held in escrow for the benefit of MCF. In addition, in connection with the transaction, the Company will pay approximately \$67 million, net of bond cash reserves and inclusive of a net make-whole premium of approximately \$15 million, to redeem the MCF bonds. The Company expects to incur a one-time loss on extinguishment of debt in connection with the redemption of the bonds of approximately \$8 million. Closing of the transaction is conditional on the Company redeeming the outstanding MCF bonds. The Company expects to close the transaction during its third fiscal quarter of 2012.

*Australia*

The Company's wholly-owned Australian subsidiary financed the development of a facility and subsequent expansion in 2003 with long-term debt obligations. These obligations are non-recourse to the Company and total \$37.4 million (AUD 36.5 million) and \$40.3 million (AUD 39.5 million), at July 1, 2012 and January 1, 2012, 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 July 1, 2012, was \$5.1 million. This amount is included in restricted cash and the annual maturities of the future debt obligation are included in Non-Recourse Debt.



**Table of Contents*****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 to SACS' senior lenders through the issuance of letters of credit for 60.0 million South African Rand. During the fiscal year ended January 1, 2012, the Company was notified by SACS' lenders that these guarantees were reduced from 60.0 million South African Rand to 34.8 million South African Rand, or \$4.3 million based on exchange rates as of July 1, 2012. Additionally, SACS was required to fund a restricted account for the payment of certain costs in the event of contract termination. As such, the Company had guaranteed the payment of 60% of amounts which may be payable by SACS into the restricted account by providing a standby letter of credit of 8.4 million South African Rand as security for this guarantee. During the fiscal year ended January 1, 2012, SACS met its obligation for the funding of the Rectification Account and the letter of credit for 8.4 million South African Rand relative to this guarantee was not renewed. In the event SACS is unable to maintain the required funding in the Rectification Account, the guarantee for the shortfall will need to be re-instated. No amounts were drawn against these letters of credit. The remaining guarantee of 34.8 million South African Rand is included as part of the value of Company's outstanding letters of credit under its Revolver as of July 1, 2012.

In addition to the above, the Company has also agreed to provide a loan, of up to 20 million South African Rand, or \$2.5 million, referred to as the Shareholder's Loan, 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 currently anticipate that such funding will be required by SACS in the future. The Company's obligations under the Shareholder's Loan expire upon the earlier of full funding or SACS' release from its obligations under its debt agreements. The lenders' ability to draw on the Shareholder's Loan 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 for a facility in Canada, the Company guaranteed certain potential tax obligations of a trust. The potential estimated exposure of these obligations is Canadian Dollar (CAD) 2.5 million, or \$2.5 million, based on exchange rates as of July 1, 2012, commencing in 2017. The Company has a liability of \$2.1 million and \$2.0 million related to this exposure included in Other Non-Current Liabilities as of July 1, 2012 and January 1, 2012, 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 equal to the current fair market value of those securities included in Other Non-Current Assets as of July 1, 2012 and January 1, 2012, respectively, on its consolidated balance sheets. The Company does not currently operate or manage this facility.

At July 1, 2012, the Company also had eight letters of guarantee outstanding under separate international facilities relating to performance guarantees of its Australian subsidiary totaling \$10.9 million.

In connection with the creation of GEOAmev, the Company and its joint venture partner guarantee the availability of working capital in equal proportion to ensure that GEOAmev can comply with current and future contractual commitments related to the performance of its operations. The Company and the 50% joint venture partner have each extended a £12 million line of credit of which £12.1 million, or \$19.1 million based on exchange rates as of July 1, 2012, was outstanding as of July 1, 2012. The Company's maximum exposure relative to the joint venture is its note receivable of \$19.1 million, including accrued interest of \$0.2 million, and future financial support necessary to guarantee performance under the contract.

Except as discussed above, the Company does not have any off balance sheet arrangements.

**12. COMMITMENTS AND CONTINGENCIES*****Litigation, Claims and Assessments***

On June 22, 2011, a jury verdict for \$6.5 million was returned against the Company in a wrongful death action brought by the Personal Representative of the Estate of Ronald Sites, a former inmate at the Company's Lawton Oklahoma Correctional Facility. On August 22, 2011, the court entered judgment against GEO in the amount of \$8.4 million, which includes pre judgment interest on the amount of the verdict from January 26, 2007, the date of the filing of the lawsuit, through the date of the jury verdict. The lawsuit, Ronald L. Sites, as the administrator of the Estate of Ronald S. Sites, deceased v. The GEO Group, Inc. was filed on January 28, 2007 in the District Court of Comanche County, State of Oklahoma, Case No. CJ-2007-



**Table of Contents**

84. It was alleged that on January 29, 2005, Mr. Sites was harmed by his cellmate as a result of the Company's negligence. The Company disagrees with the judgment and is pursuing an appeal. A supersedeas bond in the amount of \$10.0 million was posted on August 29, 2011 by the insurance company of the State of Pennsylvania, one of the Company's insurers. The Company intends to vigorously defend its rights and believes its accrual relative to this judgment is adequate. Under its insurance plan, the Company is responsible for the first \$3.0 million of liability. Aside from this amount, which the Company would pay directly from general corporate funds, the Company believes it has insurance coverage for this matter.

In June 2004, the Company received notice of a third-party claim for property damage incurred during 2001 and 2002 at several detention facilities formerly operated by its Australian subsidiary. 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 August 2007, a lawsuit (Commonwealth of Australia v. Australasian Correctional Services PTY, Limited No. SC 656) was filed against the Company in the Supreme Court of the Australian Capital Territory seeking damages of up to approximately AUD 18 million or \$18.4 million based on exchange rates as of July 1, 2012, plus interest. The Company believes that it has several defenses to the allegations underlying the litigation and the amounts sought and intends to vigorously defend its rights with respect to this matter. The Company has established a reserve based on its estimate of the most probable loss based on the facts and circumstances known to date and the advice of legal counsel in connection with this matter. Although the outcome of this matter cannot be predicted with certainty, based on information known to date and the Company's preliminary review of the claim and related reserve for loss, the Company believes that, if settled unfavorably, this matter could have a material adverse effect on its future financial condition, results of operations or 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 nature of the Company's business exposes it to various types of third-party legal 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, product liability claims, intellectual property infringement 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 its customers and other third parties, contractual claims and claims for personal injury or other damages resulting from contact with the Company's facilities, programs, electronic monitoring products, 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 proceedings to have a material adverse effect on its financial condition, results of operations or cash flows.

***Construction Commitments***

The Company is currently developing a number of projects using company financing. The Company's management estimates that these existing capital projects will cost \$125.6 million, of which \$73.4 million was spent through the second quarter of 2012. The Company estimates the remaining capital requirements related to these capital projects to be \$52.2 million, which will be spent through fiscal years 2012 and 2013. Capital expenditures related to facility maintenance costs are expected to range between \$30.0 million and \$35.0 million for fiscal year 2012. In addition to these current estimated capital requirements for 2012 and 2013, the Company is currently in the process of bidding on, or evaluating potential bids for the design, construction and management of a number of new projects. In the event that the Company wins bids for these projects and decides to self-finance their construction, its capital requirements in 2012 and/or 2013 could materially increase.

***Contract Terminations***

On March 31, 2012, the Company's contract for the management of the 130-bed Migrant Operations Center at Guantanamo Bay NAS, Cuba terminated and was transferred to another operator. The termination of this contract did not have a material impact on its financial position, results of operations and/or cash flows.

On April 10, 2012, the Company announced that the California Department of Corrections and Rehabilitation (CDCR) notified the Company that it had rescinded the previous notice of termination regarding GEO's management contract for the 625-bed Golden State Correctional Facility (Golden State). Golden State, which was previously scheduled to close on June 30, 2012, will remain in operation under the Company's current contract which is effective through December 14, 2012.

On April 19, 2012, the Company announced the discontinuation of its managed-only contract with the State of Mississippi, Department of Corrections for the 1,500-bed East Mississippi Correctional Facility (East Mississippi) effective July 19, 2012. In connection with the discontinuation of East Mississippi, the Company has also discontinued its managed-only contracts with the State of Mississippi, Department of Corrections for the 1,000-bed Marshall County Correctional Facility effective August 13, 2012, and the 1,450-bed Walnut Grove Youth Correctional Facility effective July 1, 2012. Refer to Note 8 - Discontinued Operations.





**Table of Contents**

The Company is currently marketing approximately 7,000 vacant beds at eight of its idle facilities to potential customers. The carrying values of these idle facilities totaled \$266.7 million as of July 1, 2012, excluding equipment and other assets that can be easily transferred for use at other facilities.

**13. BUSINESS SEGMENTS AND GEOGRAPHIC INFORMATION***Operating and Reporting Segments*

The Company conducts its business through four reportable business segments: the U.S. Corrections & Detention segment; the GEO Care segment; the International Services segment; and the Facility Construction & Design segment. The Company's segment revenues from external customers and a measure of segment profit are as follows (in thousands):

|                                | Thirteen Weeks Ended |                 | Twenty-six Weeks Ended |                 |
|--------------------------------|----------------------|-----------------|------------------------|-----------------|
|                                | July 1,<br>2012      | July 3,<br>2011 | July 1,<br>2012        | July 3,<br>2011 |
| Revenues:                      |                      |                 |                        |                 |
| U.S. Corrections & Detention   | \$ 246,060           | \$ 230,662      | \$ 481,094             | \$ 460,870      |
| GEO Care                       | 110,320              | 110,857         | 220,013                | 207,746         |
| International Services         | 55,968               | 55,285          | 112,498                | 108,413         |
| Facility Construction & Design |                      |                 |                        | 119             |
| Total revenues                 | \$ 412,348           | \$ 396,804      | \$ 813,605             | \$ 777,148      |
| Operating income:              |                      |                 |                        |                 |
| U.S. Corrections & Detention   | \$ 59,849            | \$ 52,881       | \$ 106,960             | \$ 107,598      |
| GEO Care                       | 21,203               | 21,443          | 39,827                 | 35,293          |
| International Services         | 2,454                | 2,322           | 6,641                  | 6,274           |
| Facility Construction & Design |                      | (23)            |                        | 80              |
| Operating income from segments | \$ 83,506            | \$ 76,623       | \$ 153,428             | \$ 149,245      |

*Pre-Tax Income Reconciliation of Segments*

The following is a reconciliation of the Company's total operating income from its reportable segments to the Company's income before income taxes and equity in earnings of affiliates (in thousands):

|   | Thirteen Weeks Ended |                 | Twenty-six Weeks Ended |                 |
|---|----------------------|-----------------|------------------------|-----------------|
|   | July 1,<br>2012      | July 3,<br>2011 | July 1,<br>2012        | July 3,<br>2011 |
| Total operating income from segments                            | \$ 83,506            | \$ 76,623       | \$ 153,428             | \$ 149,245      |
| Unallocated amounts:  |                      |                 |                        |                 |
| General and Administrative Expenses                             | (27,043)             | (27,710)        | (54,484)               | (60,498)        |
| Net interest expense  | (18,856)             | (17,783)        | (37,856)               | (33,175)        |
| Income before income taxes and equity in earnings of affiliates | \$ 37,607            | \$ 31,130       | \$ 61,088              | \$ 55,572       |

*Equity in Earnings of Affiliates*

Equity in earnings of affiliates includes the Company's 50% owned joint ventures in SACS, located in South Africa, and GEOAmev, located in the United Kingdom. Our investments in these entities are accounted for under the equity method of accounting. The Company's investments in these entities are presented as a component of Other Non-Current Assets in the accompanying consolidated balance sheets.

## Edgar Filing: GEO GROUP INC - Form 10-Q

As of July 1, 2012 and January 1, 2012 and for the thirteen and twenty-six weeks ended July 1, 2012 and July 3, 2011, SACS was considered to be a significant subsidiary and as such, summarized financial data is included below as follows (in thousands):

**Table of Contents**

|                                     | Thirteen Weeks Ended |              | Twenty-six Weeks Ended |              |
|-------------------------------------|----------------------|--------------|------------------------|--------------|
|                                     | July 1, 2012         | July 3, 2011 | July 1, 2012           | July 3, 2011 |
| <b>Statement of Operations Data</b> |                      |              |                        |              |
| Revenues                            | \$ 11,651            | \$ 12,830    | \$ 23,496              | \$ 25,001    |
| Operating income                    | 4,706                | 5,369        | 9,474                  | 10,129       |
| Net income                          | 2,641                | 2,837        | 5,232                  | 4,160        |

|                         | July 1, 2012              | January 1, 2012 |
|-------------------------|---------------------------|-----------------|
|                         | <b>Balance Sheet Data</b> |                 |
| Current assets          | \$22,774                  | \$21,068        |
| Non-current assets      | 37,317                    | 39,110          |
| Current liabilities     | 3,331                     | 3,645           |
| Non-current liabilities | 40,473                    | 45,237          |
| Shareholders' equity    | 16,287                    | 11,296          |

As of July 1, 2012 and January 1, 2012, the Company's investment in SACS was \$8.1 million and \$5.6 million, respectively.

The Company has recorded \$0.9 million and \$1.4 million in losses, net of tax impact, for GEOAmeys operations during the thirteen and twenty-six weeks ended July 1, 2012, which is included in Equity in earnings of affiliates in the accompanying consolidated statement of comprehensive income. As of July 1, 2012, the Company's investment in GEOAmeys was \$(3.8) million, and represents its share of reported losses.

**14. BENEFIT PLANS**

The following table summarizes key information related to the Company's pension plans and retirement agreements (in thousands):

**Table of Contents**

|   | Twenty-six Weeks<br>Ended July 1, 2012 | Fiscal Year Ended<br>January 1, 2012 |
|---|--|--------------------------------------|
| <b>Change in Projected Benefit Obligation</b>     |  |                                      |
| Projected benefit obligation, beginning of period | \$ 16,879                              | \$ 13,830                            |
| Service cost                                      | 387                                    | 645                                  |
| Interest cost                                     | 393                                    | 667                                  |
| Actuarial gain                                    |  | 1,922                                |
| Benefits paid                                     | (79)                                   | (185)                                |
| <br>  |  |                                      |
| Projected benefit obligation, end of period       | \$ 17,580                              | \$ 16,879                            |
| <br><b>Change in Plan Assets</b>                  |  |                                      |
| Plan assets at fair value, beginning of period    | \$                                     | \$                                   |
| Company contributions                             | 79                                     | 185                                  |
| Benefits paid                                     | (79)                                   | (185)                                |
| Plan assets at fair value, end of period          | \$                                     | \$                                   |
| <br>  |  |                                      |
| <b>Unfunded Status of the Plan</b>                | <b>\$ (17,580)</b>                     | <b>\$ (16,879)</b>                   |

|  | Thirteen Weeks<br>Ended |                 | Twenty-six<br>Weeks Ended |                 |
|--|-------------------------|-----------------|---------------------------|-----------------|
|  | July 1,<br>2012         | July 3,<br>2011 | July 1,<br>2012           | July 3,<br>2011 |
| <b>Components of Net Periodic Benefit Cost</b> |                         |                 |                           |                 |
| Service cost                                   | \$ 193                  | \$ 161          | \$ 387                    | \$ 322          |
| Interest cost                                  | 197                     | 167             | 393                       | 334             |
| Amortization of prior service cost             |                         |                 |                           |                 |
| Net loss                                       | 48                      | 16              | 97                        | 32              |
| <br>   |                         |                 |                           |                 |
| Net periodic pension cost                      | \$ 438                  | \$ 344          | \$ 877                    | \$ 688          |

The long-term portion of the pension liability as of July 1, 2012 and January 1, 2012 was \$17.4 million and \$16.7 million, respectively, and is included in Other Non-Current Liabilities in the accompanying consolidated balance sheets.

**15. RECENT ACCOUNTING STANDARDS**

The Company implemented the following accounting standards in the twenty-six weeks ended July 1, 2012:

In May 2011, the FASB issued ASU No. 2011-04 which provides a consistent definition of fair value in US GAAP and International Financial Reporting Standards (IFRS) and ensures that their respective fair value measurement and disclosure requirements are the same (except for minor differences in wording and style). The amendments change certain fair value measurement principles and enhance the disclosure requirements particularly for level 3 fair value measurements. The standard became effective for the Company during interim and annual periods beginning after December 15, 2011 and has been applied prospectively, where applicable. The implementation of this standard in the twenty-six weeks ended July 1, 2012 did not have a material impact on its financial position, results of operation and cash flows.

In June 2011, the FASB issued ASU No. 2011-05 which requires an entity to present all non-owner changes in stockholders' equity either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. Regardless of whether an entity chooses to present comprehensive income in a single continuous statement or in two separate but consecutive statements, the entity is required to present on the face of the financial statements reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement(s) where the components of net income and the components of other comprehensive income are presented. This standard became effective for the Company in fiscal years, and interim periods within those years, beginning after December 15, 2011 and was applied retrospectively. The implementation of this standard in the twenty-six weeks ended July 1, 2012 did not have a material impact on its financial position, results of operation and cash flows.

## Edgar Filing: GEO GROUP INC - Form 10-Q

In December 2011, the FASB issued ASU 2011-12 in order to defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments. No other requirements in ASU 2011-05 were affected by this ASU, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but

---

**Table of Contents**

consecutive financial statements. ASU 2011-12 is effective for the Company in fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company's implementation of ASU 2011-12 in the twenty-six weeks ended July 1, 2012 did not have a material impact on the Company's financial position, results of operation or cash flows. The Company does not expect the future impact of this standard, once the deferral period is over, to have a material impact on the Company's financial position, results of operation or cash flows.

In July 2012, the FASB issued ASU 2012-02 which is intended to simplify how an entity tests indefinite-lived intangible assets for impairment. Under the revised guidance, an entity has the option first to assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the indefinite-lived intangible asset is impaired. If, after assessing the totality of facts and circumstances, an entity concludes that it is not more likely than not that the indefinite-lived intangible asset is impaired, then the entity is not required to take further action. However, if an entity concludes otherwise, then it is required to determine the fair value with the carrying amount in accordance with Subtopic 350-30. Under the amendments in this update, an entity has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative impairment test. An entity will be able to resume performing the qualitative assessment in any subsequent period. The amendments are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted, including for annual and interim impairment tests performed as of a date before July 27, 2012, if a public entity's financial statements for the most recent annual or interim period have not yet been issued. The Company does not believe that the implementation of this standard will have a material impact on its financial position, results of operations or cash flows.

**16. SUBSEQUENT EVENTS*****Restricted Stock Awards***

On July 20, 2012, the Compensation Committee of the Board of Directors adopted resolutions providing that all future performance-based equity grants under GEO's equity incentive plans will be subject to multiple annual performance metrics. Such annual metrics for performance-based awards will include earnings-per-share performance and return on capital employed results. Such metrics will not include revenue for future performance-based awards (Refer to Note 6 - Equity Incentive Plans). In connection with the resolution, the Compensation Committee canceled the restricted stock awards previously granted on March 12, 2012 to certain executive officers. In lieu of the canceled awards, the Compensation Committee granted new restricted stock awards on July 20, 2012 to these same executive officers covering the same number of shares of restricted stock as were granted in March 2012. The vesting of these new restricted stock grants will be subject to the achievement by GEO of two annual performance metrics as follows: (i) up to 75% of the shares of restricted stock in each award can vest annually or cumulatively if GEO meets certain earnings per share performance targets during years 2012, 2013 and 2014; and (ii) up to 25% of the shares of restricted stock in each award can vest annually if GEO meets certain return on capital performance targets in 2012, 2013 and 2014. Based on the terms of the agreement, the Company does not expect there to be any incremental compensation cost related to the modified awards.

***Dividends***

On August 7, 2012, the Board of Directors declared a dividend of \$.20 per share to shareholders of record on August 21, 2012 to be paid out on September 7, 2012.

***Operating Tax Refund***

In the Third Quarter 2012, the Company received net refunds in the amount of \$6.0 million, not related to income taxes, for certain previously disputed tax claims in various jurisdictions.

**17. CONDENSED CONSOLIDATING FINANCIAL INFORMATION**

The Company's 6.625% Senior Notes and 7<sup>1</sup>/<sub>4</sub>% Senior Notes are fully and unconditionally guaranteed on a joint and several senior unsecured basis by the Company and certain of its wholly-owned domestic subsidiaries (the "Subsidiary Guarantors"). The following condensed consolidating financial information, which has been prepared in accordance with the requirements for presentation of Rule 3-10(d) of Regulation S-X promulgated under the Securities Act, presents the condensed consolidating financial information separately for:

- (i) The GEO Group, Inc., as the issuer of the Notes;

- (ii) The Subsidiary Guarantors, on a combined basis, which are 100% owned by The GEO Group, Inc., and which are guarantors of the Notes;



**Table of Contents**

- (iii) The Company's other subsidiaries, on a combined basis, which are not guarantors of the Notes (the **Subsidiary Non-Guarantors**);
  
- (iv) Consolidating entries and eliminations representing adjustments to (a) eliminate intercompany transactions between or among the Company, the **Subsidiary Guarantors** and the **Subsidiary Non-Guarantors** and (b) eliminate the investments in the Company's subsidiaries; and
  
- (v) The Company and its subsidiaries on a consolidated basis.

**Table of Contents****CONDENSED CONSOLIDATING BALANCE SHEET**

(dollars in thousands)

(unaudited)

|  |                        |                                      | As of July 1, 2012                        |                       |                     |
|--|------------------------|--------------------------------------|---|-----------------------|---------------------|
|  | The GEO Group, Inc.    | Combined<br>Subsidiary<br>Guarantors | Combined<br>Non-Guarantor<br>Subsidiaries | Eliminations          | Consolidated        |
|  | (Dollars in thousands) |                                      |   |                       |                     |
| <b>ASSETS</b>  |                        |                                      |   |                       |                     |
| Cash and cash equivalents  | 43,081                 | \$ 4,550                             | \$ 20,907                                 | \$                    | \$ 68,538           |
| Restricted cash and investments  |                        | 1,350                                | 38,721                                    |                       | 40,071              |
| Accounts receivable, less allowance for doubtful accounts                          | 122,746                | 138,653                              | 23,032                                    |                       | 284,431             |
| Deferred income tax assets, net  | 13,891                 | 11,047                               | 3,788                                     |                       | 28,726              |
| Prepaid expenses and other current assets  | 6,878                  | 7,094                                | 10,565                                    | (1,154)               | 23,383              |
| Current assets of discontinued operations  | 4,740                  | 1,973                                |   |                       | 6,713               |
| <b>Total current assets</b>  | <b>191,336</b>         | <b>164,667</b>                       | <b>97,013</b>                             | <b>(1,154)</b>        | <b>451,862</b>      |
| Restricted Cash and Investments  | 8,941                  |                                      | 51,129                                    |                       | 60,070              |
| Property and Equipment, Net  | 638,967                | 830,739                              | 248,686                                   |                       | 1,718,392           |
| Assets Held for Sale   | 3,083                  | 2,307                                |   |                       | 5,390               |
| Direct Finance Lease Receivable  |                        |                                      | 29,253                                    |                       | 29,253              |
| Intercompany Receivable  | 378,861                | 14,380                               | 12,708                                    | (405,949)             |                     |
| Deferred Income Tax Assets, Net  |                        |                                      | 1,711                                     |                       | 1,711               |
| Goodwill   | 34                     | 507,272                              | 762                                       |                       | 508,068             |
| Intangible Assets, Net   |                        | 188,957                              | 1,786                                     |                       | 190,743             |
| Investment in Subsidiaries   | 1,317,002              | 16,615                               |   | (1,333,617)           |                     |
| Other Non-Current Assets   | 38,680                 | 81,700                               | 37,104                                    | (74,321)              | 83,163              |
| Non-Current Assets of Discontinued Operations                                      | \$ 541                 | \$ 35                                | \$  | \$                    | \$ 576              |
| <b>Total Assets</b>  | <b>\$ 2,577,445</b>    | <b>\$ 1,806,672</b>                  | <b>\$ 480,152</b>                         | <b>\$ (1,815,041)</b> | <b>\$ 3,049,228</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                        |                                      |   |                       |                     |
| Accounts payable   | \$ 27,396              | \$ 33,154                            | \$ 3,131                                  | \$                    | \$ 63,681           |
| Accrued payroll and related taxes  | 2,829                  | 16,911                               | 17,469                                    |                       | 37,209              |
| Accrued expenses   | 73,968                 | 21,626                               | 27,164                                    | (1,154)               | 121,604             |
| Current portion of capital lease obligations, long-term debt and non-recourse debt | 24,606                 | 1,424                                | 33,728                                    |                       | 59,758              |
| Current liabilities of discontinued operations                                     | 546                    | 156                                  |   |                       | 702                 |
| <b>Total current liabilities</b>   | <b>129,345</b>         | <b>73,271</b>                        | <b>81,492</b>                             | <b>(1,154)</b>        | <b>282,954</b>      |
| Deferred Income Tax Liabilities  | 42,879                 | 82,296                               | 34  |                       | 125,209             |
| Intercompany Payable   | 12,708                 | 375,695                              | 17,546                                    | (405,949)             |                     |
| Other Non-Current Liabilities  | 31,692                 | 26,798                               | 74,769                                    | (74,321)              | 58,938              |
| Capital Lease Obligations  |                        | 12,456                               |   |                       | 12,456              |
| Long-Term Debt   | 1,297,724              | 306                                  |   |                       | 1,298,030           |
| Non-Recourse Debt  |                        |                                      | 198,995                                   |                       | 198,995             |
| Commitments & Contingencies  |                        |                                      |   |                       |                     |

Edgar Filing: GEO GROUP INC - Form 10-Q

|   |                     |                     |                   |                       |                     |  |
|---|---------------------|---------------------|-------------------|-----------------------|---------------------|--|
| Shareholders' Equity:                             |                     |                     |                   |                       |                     |  |
| The GEO Group, Inc. Shareholders' Equity          | 1,063,097           | 1,226,841           | 106,776           | (1,333,617)           | 1,063,097           |  |
| Noncontrolling Interests                          |                     | 9,009               | 540               |                       | 9,549               |  |
| Total Shareholders' Equity                        | 1,072,646           | 1,235,850           | 107,316           | (1,343,166)           | 1,072,646           |  |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>\$ 2,577,445</b> | <b>\$ 1,806,672</b> | <b>\$ 480,152</b> | <b>\$ (1,815,041)</b> | <b>\$ 3,049,228</b> |  |

**Table of Contents****CONDENSED CONSOLIDATING BALANCE SHEET**

(dollars in thousands)

(unaudited)

|  | As of January 1, 2012  |                                      |   |                       | Consolidated        |
|--|------------------------|--------------------------------------|---|-----------------------|---------------------|
|  | The GEO Group, Inc.    | Combined<br>Subsidiary<br>Guarantors | Combined<br>Non-Guarantor<br>Subsidiaries | Eliminations          |                     |
|  | (Dollars in thousands) |                                      |   |                       |                     |
| <b>ASSETS</b>  |                        |                                      |   |                       |                     |
| Cash and cash equivalents  | \$ 15,085              | \$ 3,155                             | \$ 26,513                                 | \$                    | \$ 44,753           |
| Restricted cash and investments  |                        |                                      | 42,535                                    |                       | 42,535              |
| Accounts receivable, less allowance for doubtful accounts                          | 123,426                | 139,574                              | 22,810                                    |                       | 285,810             |
| Deferred income tax assets, net  | 14,063                 | 10,875                               | 3,788                                     |                       | 28,726              |
| Prepaid expenses and other current assets  | 17,170                 | 23,791                               | 10,539                                    | (1,154)               | 50,346              |
| Current assets of discontinued operations  | 5,021                  | 2,138                                |   |                       | 7,159               |
| <b>Total current assets</b>  | <b>174,765</b>         | <b>179,533</b>                       | <b>106,185</b>                            | <b>(1,154)</b>        | <b>459,329</b>      |
| Restricted Cash and Investments  | 8,016                  |                                      | 49,896                                    |                       | 57,912              |
| Property and Equipment, Net  | 620,124                | 834,345                              | 250,837                                   |                       | 1,705,306           |
| Assets Held for Sale   | 3,083                  | 1,280                                |   |                       | 4,363               |
| Direct Finance Lease Receivable  |                        |                                      | 32,146                                    |                       | 32,146              |
| Intercompany Receivable  | 386,026                | 14,305                               | 14,028                                    | (414,359)             |                     |
| Deferred Income Tax Assets, Net  |                        |                                      | 1,711                                     |                       | 1,711               |
| Goodwill   | 34                     | 507,272                              | 760                                       |                       | 508,066             |
| Intangible Assets, Net   |                        | 198,477                              | 1,865                                     |                       | 200,342             |
| Investment in Subsidiaries   | 1,333,885              | 9,784                                |   | (1,343,669)           |                     |
| Other Non-Current Assets   | 40,695                 | 73,480                               | 31,022                                    | (65,621)              | 79,576              |
| Non-Current Assets of Discontinued Operations                                      | \$ 697                 | \$ 168                               | \$  | \$                    | \$ 865              |
| <b>Total Assets</b>  | <b>\$ 2,567,325</b>    | <b>\$ 1,818,644</b>                  | <b>\$ 488,450</b>                         | <b>\$ (1,824,803)</b> | <b>\$ 3,049,616</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                        |                                      |   |                       |                     |
| Accounts payable   | \$ 47,159              | \$ 18,531                            | \$ 3,942                                  | \$                    | \$ 69,632           |
| Accrued payroll and related taxes  | 2,855                  | 18,273                               | 17,002                                    |                       | 38,130              |
| Accrued expenses   | 69,585                 | 33,500                               | 24,751                                    | (1,154)               | 126,682             |
| Current portion of capital lease obligations, long-term debt and non-recourse debt | 19,037                 | 1,363                                | 33,266                                    |                       | 53,666              |
| Current liabilities of discontinued operations                                     | 542                    | 166                                  |   |                       | 708                 |
| <b>Total current liabilities</b>   | <b>139,178</b>         | <b>71,833</b>                        | <b>78,961</b>                             | <b>(1,154)</b>        | <b>288,818</b>      |
| Deferred Income Tax Liabilities  | 42,879                 | 82,296                               | 34  |                       | 125,209             |
| Intercompany Payable   | 14,027                 | 378,005                              | 22,327                                    | (414,359)             |                     |
| Other Non-Current Liabilities  | 29,384                 | 28,654                               | 63,964                                    | (65,621)              | 56,381              |
| Capital Lease Obligations  |                        | 13,087                               |   |                       | 13,087              |
| Long-Term Debt   | 1,318,639              | 429                                  |   |                       | 1,319,068           |
| Non-Recourse Debt  |                        |                                      | 208,532                                   |                       | 208,532             |
| Commitments & Contingencies  |                        |                                      |   |                       |                     |

Edgar Filing: GEO GROUP INC - Form 10-Q

|   |                     |                     |                   |                       |                     |  |
|---|---------------------|---------------------|-------------------|-----------------------|---------------------|--|
| Shareholders' Equity:                             |                     |                     |                   |                       |                     |  |
| The GEO Group, Inc. Shareholders' Equity          | 1,023,218           | 1,229,553           | 114,116           | (1,343,669)           | 1,023,218           |  |
| Noncontrolling Interests                          |                     | 14,787              | 516               |                       | 15,303              |  |
| Total Shareholders' Equity                        | 1,023,218           | 1,244,340           | 114,632           | (1,343,669)           | 1,038,521           |  |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>\$ 2,567,325</b> | <b>\$ 1,818,644</b> | <b>\$ 488,450</b> | <b>\$ (1,824,803)</b> | <b>\$ 3,049,616</b> |  |

**Table of Contents****CONDENSED CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME**

(dollars in thousands)

(unaudited)

|   | For the Thirteen Weeks Ended July 1, 2012 |                       |                            |              |              |
|---|---|-----------------------|----------------------------|--------------|--------------|
|   |   | Combined              | Combined                   |              |              |
|   | The GEO Group, Inc.                       | Subsidiary Guarantors | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
| Revenues  | \$ 153,754                                | \$ 217,573            | \$ 61,400                  | \$ (20,379)  | \$ 412,348   |
| Operating expenses  | 130,229                                   | 145,784               | 49,401                     | (20,379)     | 305,035      |
| Depreciation and amortization   | 7,390                                     | 14,255                | 2,162                      |              | 23,807       |
| General and administrative expenses   | 9,609                                     | 13,597                | 3,837                      |              | 27,043       |
| Operating income  | 6,526                                     | 43,937                | 6,000                      |              | 56,463       |
| Interest income   | 7,848                                     | 393                   | 1,661                      | (8,141)      | 1,761        |
| Interest expense  | (16,836)                                  | (7,926)               | (3,996)                    | 8,141        | (20,617)     |
| Income (loss) before income taxes and equity in earnings of affiliates                        | (2,462)                                   | 36,404                | 3,665                      |              | 37,607       |
| Provision (benefit) for income taxes  | (663)                                     | 14,089                | 1,565                      |              | 14,991       |
| Equity in earnings of affiliates, net of income tax provision                                 |   |                       | 430                        |              | 430          |
| Income (loss) from continuing operations before equity in income of consolidated subsidiaries | (1,799)                                   | 22,315                | 2,530                      |              | 23,046       |
| Income from consolidated subsidiaries, net of income tax provision                            | 24,845                                    |                       |                            | (24,845)     |              |
| Income from continuing operations   | 23,046                                    | 22,315                | 2,530                      | (24,845)     | 23,046       |
| Net income (loss) from discontinued operations  | (570)                                     | 85                    |                            | (85)         | (570)        |
| Net income  | 22,476                                    | 22,400                | 2,530                      | (24,930)     | 22,476       |
| Net loss attributable to noncontrolling interests   |   |                       | 25                         |              | 25           |
| Net income attributable to The GEO Group, Inc.  | \$ 22,476                                 | \$ 22,400             | \$ 2,555                   | \$ (24,930)  | \$ 22,501    |
| Net income  | \$ 22,476                                 | \$ 22,400             | \$ 2,530                   | \$ (24,930)  | \$ 22,476    |
| Other comprehensive income (loss), net of tax   | \$ 29                                     | \$                    | \$ (2,498)                 | \$           | \$ (2,469)   |
| Comprehensive income  | \$ 22,505                                 | \$ 22,400             | \$ 32                      | \$ (24,930)  | \$ 20,007    |
| Comprehensive loss attributable to noncontrolling interests                                   | \$  |                       | \$ 58                      | \$           | \$ 58        |
| Comprehensive income attributable to The GEO Group, Inc.                                      | \$ 22,505                                 | \$ 22,400             | \$ 90                      | \$ (24,930)  | \$ 20,065    |

**Table of Contents****CONDENSED CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME**

(dollars in thousands)

(unaudited)

|   | For the Thirteen Weeks Ended July 3, 2011 |                       |                            |              |              |
|---|---|-----------------------|----------------------------|--------------|--------------|
|   |   | Combined              | Combined                   |              |              |
|   | The GEO Group, Inc.                       | Subsidiary Guarantors | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
| Revenues  | \$ 138,571                                | \$ 220,016            | \$ 57,514                  | \$ (19,297)  | \$ 396,804   |
| Operating expenses  | 126,590                                   | 145,399               | 46,544                     | (19,297)     | 299,236      |
| Depreciation and amortization   | 4,668                                     | 14,401                | 1,876                      |              | 20,945       |
| General and administrative expenses   | 9,520                                     | 14,459                | 3,731                      |              | 27,710       |
| Operating income (loss)   | (2,207)                                   | 45,757                | 5,363                      |              | 48,913       |
| Interest income   | 7,767                                     | 413                   | 1,562                      | (8,113)      | 1,629        |
| Interest expense  | (15,886)                                  | (7,983)               | (3,656)                    | 8,113        | (19,412)     |
| Income (loss) before income taxes and equity in earnings of affiliates                        | (10,326)                                  | 38,187                | 3,269                      |              | 31,130       |
| Provision (benefit) for income taxes  | (3,902)                                   | 14,756                | 1,448                      |              | 12,302       |
| Equity in earnings of affiliates, net of income tax provision                                 |   |                       | 1,418                      |              | 1,418        |
| Income (loss) from continuing operations before equity in income of consolidated subsidiaries | (6,424)                                   | 23,431                | 3,239                      |              | 20,246       |
| Income from consolidated subsidiaries, net of income tax provision                            | 26,670                                    |                       |                            | (26,670)     |              |
| Income from continuing operations   | 20,246                                    | 23,431                | 3,239                      | (26,670)     | 20,246       |
| Net income from discontinued operations   | 917                                       | 236                   |                            | (236)        | 917          |
| Net income  | 21,163                                    | 23,667                | 3,239                      | (26,906)     | 21,163       |
| Net loss attributable to noncontrolling interests   |   | 1                     | 414                        |              | 415          |
| Net income attributable to The GEO Group, Inc.  | \$ 21,163                                 | \$ 23,668             | \$ 3,653                   | \$ (26,906)  | \$ 21,578    |
| Net income  | \$ 21,163                                 | \$ 23,667             | \$ 3,239                   | \$ (26,906)  | \$ 21,163    |
| Other comprehensive income, net of tax  | 10  |                       | 489                        |              | 499          |
| Comprehensive income  | \$ 21,173                                 | \$ 23,667             | \$ 3,728                   | \$ (26,906)  | \$ 21,662    |
| Comprehensive loss attributable to noncontrolling interests                                   |   | 1                     | 417                        |              | 418          |
| Comprehensive income attributable to The GEO Group, Inc.                                      | \$ 21,173                                 | \$ 23,668             | \$ 4,145                   | \$ (26,906)  | \$ 22,080    |

**Table of Contents**

|   | For the Twenty-six Weeks Ended July 1, 2012 |                                      |   |              |              |
|---|---|--------------------------------------|---|--------------|--------------|
|   | The GEO Group, Inc.                         | Combined<br>Subsidiary<br>Guarantors | Combined<br>Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
| Revenues  | \$ 294,370                                  | \$ 436,476                           | \$ 123,174                                    | \$ (40,415)  | \$ 813,605   |
| Operating expenses  | 261,460                                     | 294,875                              | 97,375  | (40,415)     | 613,295      |
| Depreciation and amortization   | 14,244                                      | 28,318                               | 4,320   |              | 46,882       |
| General and administrative expenses   | 18,780                                      | 27,846                               | 7,858   |              | 54,484       |
| Operating income  | (114)                                       | 85,437                               | 13,621  |              | 98,944       |
| Interest income   | 15,655                                      | 886                                  | 3,262   | (16,235)     | 3,568        |
| Interest expense  | (33,754)                                    | (15,837)                             | (8,068)                                       | 16,235       | (41,424)     |
| Income (loss) before income taxes and equity in earnings of affiliates                        | (18,213)                                    | 70,486                               | 8,815   |              | 61,088       |
| Provision (benefit) for income taxes  | (6,323)                                     | 26,993                               | 3,538   |              | 24,208       |
| Equity in earnings of affiliates, net of income tax provision                                 |   |                                      | 1,178   |              | 1,178        |
| Income (loss) from continuing operations before equity in income of consolidated subsidiaries | (11,890)                                    | 43,493                               | 6,455   |              | 38,058       |
| Income from consolidated subsidiaries, net of income tax provision                            | 49,948                                      |                                      |   | (49,948)     |              |
| Income from continuing operations   | 38,058                                      | 43,493                               | 6,455   | (49,948)     | 38,058       |
| Net income (loss) from discontinued operations  | (523)                                       | 223                                  |   | (223)        | (523)        |
| Net income  | 37,535                                      | 43,716                               | 6,455   | (50,171)     | 37,535       |
| Net income attributable to noncontrolling interests   |   |                                      | (9)   |              | (9)          |
| Net income attributable to The GEO Group, Inc.  | \$ 37,535                                   | \$ 43,716                            | \$ 6,446                                      | \$ (50,171)  | \$ 37,526    |
| Net income  | \$ 37,535                                   | \$ 43,716                            | \$ 6,455                                      | \$ (50,171)  | \$ 37,535    |
| Other comprehensive income (loss), net of tax   | 59  |                                      | (541)   |              | (482)        |
| Comprehensive income  | \$ 37,594                                   | \$ 43,716                            | \$ 5,914                                      | \$ (50,171)  | \$ 37,053    |
| Comprehensive loss attributable to noncontrolling interests                                   |   |                                      | (4)   |              | (4)          |
| Comprehensive income attributable to The GEO Group, Inc.                                      | \$ 37,594                                   | \$ 43,716                            | \$ 5,910                                      | \$ (50,171)  | \$ 37,049    |



**Table of Contents**

For the Twenty-six Weeks Ended July 3, 2011

|   | The GEO Group, Inc. | Combined<br>Subsidiary<br>Guarantors | Combined<br>Non-Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|---|---------------------|--------------------------------------|---|--------------|--------------|
| Revenues  | \$ 273,812          | \$ 427,970                           | \$ 113,015                                | \$ (37,649)  | \$ 777,148   |
| Operating expenses  | 251,024             | 286,276                              | 88,606                                    | (37,649)     | 588,257      |
| Depreciation and amortization   | 8,855               | 27,059                               | 3,732                                     |              | 39,646       |
| General and administrative expenses   | 20,964              | 31,367                               | 8,167                                     |              | 60,498       |
| Operating income (loss)   | (7,031)             | 83,268                               | 12,510                                    |              | 88,747       |
| Interest income   | 13,504              | 737                                  | 3,025                                     | (14,068)     | 3,198        |
| Interest expense  | (29,239)            | (13,922)                             | (7,280)                                   | 14,068       | (36,373)     |
| Income (loss) before income taxes and equity in earnings of affiliates                        | (22,766)            | 70,083                               | 8,255                                     |              | 55,572       |
| Provision (benefit) for income taxes  | (8,709)             | 27,080                               | 3,303                                     |              | 21,674       |
| Equity in earnings of affiliates, net of income tax provision                                 |                     |                                      | 2,080                                     |              | 2,080        |
| Income (loss) from continuing operations before equity in income of consolidated subsidiaries | (14,057)            | 43,003                               | 7,032                                     |              | 35,978       |
| Income from consolidated subsidiaries, net of income tax provision                            | 50,035              |                                      |   | (50,035)     |              |
| Income from continuing operations   | 35,978              | 43,003                               | 7,032                                     | (50,035)     | 35,978       |
| Net income from discontinued operations   | 1,565               | 503                                  |   | (503)        | 1,565        |
| Net income  | 37,543              | 43,506                               | 7,032                                     | (50,538)     | 37,543       |
| Net loss attributable to noncontrolling interests   |                     | 2                                    | 823                                       |              | 825          |
| Net income attributable to The GEO Group, Inc.  | \$ 37,543           | \$ 43,508                            | \$ 7,855                                  | \$ (50,538)  | \$ 38,368    |
| Net income  | \$ 37,543           | \$ 43,506                            | \$ 7,032                                  | \$ (50,538)  | \$ 37,543    |
| Other comprehensive income  | 19                  |                                      | 783                                       |              | 802          |
| Comprehensive income  | 37,562              | 43,506                               | 7,815                                     | (50,538)     | 38,345       |
| Comprehensive loss attributable to noncontrolling interests                                   |                     | 9                                    | 826                                       |              | 835          |
| Comprehensive income attributable to The GEO Group, Inc.                                      | \$ 37,562           | \$ 43,515                            | \$ 8,641                                  | \$ (50,538)  | \$ 39,180    |

**Table of Contents****CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS****(dollars in thousands)****(unaudited)**

|  | <b>For the Twenty-six Weeks Ended July 1, 2012</b> |   |  |                     |
|--|--|---|--|---------------------|
|  | <b>The GEO Group, Inc.</b>                         | <b>Combined<br/>Subsidiary<br/>Guarantors</b> | <b>Combined<br/>Non-Guarantor<br/>Subsidiaries</b> | <b>Consolidated</b> |
| <b>Cash Flow from Operating Activities:</b>                  |  |   |  |                     |
| Net cash provided by operating activities                    | \$ 98,491  | \$ 17,218                                     | \$ 10,104  | \$ 125,813          |
| <b>Cash Flow from Investing Activities:</b>                  |  |   |  |                     |
| Proceeds from sale of property and equipment                 |  | 162   | 69   | 231                 |
| Proceeds from sale of assets held for sale                   |  | 297   |  | 297                 |
| Change in restricted cash and investments                    |  |   | 333  | 333                 |
| Capital expenditures   | (54,024)   | (15,589)                                      | (2,240)  | (71,853)            |
| Net cash (used in) provided by investing activities          | (54,024)   | (15,130)                                      | (1,838)  | (70,992)            |
| <b>Cash Flow from Financing Activities:</b>                  |  |   |  |                     |
| Payments on long-term debt                                   | (160,556)  | (693)   | (8,033)  | (169,282)           |
| Proceeds from long-term debt                                 | 145,000  |   |  | 145,000             |
| Distribution to noncontrolling interests                     |  |   | (5,758)  | (5,758)             |
| Proceeds from the exercise of stock options                  | 396  |   |  | 396                 |
| Income tax provision of equity compensation                  | (270)  |   |  | (270)               |
| Payments for retirement of common stock                      | (1,035)  |   |  | (1,035)             |
| Debt issuance costs  | (6)  |   | (38)   | (44)                |
| Net cash used in financing activities                        | (16,471)   | (693)   | (13,829)   | (30,993)            |
| Effect of Exchange Rate Changes on Cash and Cash Equivalents |  |   | (43)   | (43)                |
| Net (Decrease) Increase in Cash and Cash Equivalents         | 27,996   | 1,395   | (5,606)  | 23,785              |
| Cash and Cash Equivalents, beginning of period               | 15,085   | 3,155   | 26,513   | 44,753              |
| Cash and Cash Equivalents, end of period                     | \$ 43,081  | \$ 4,550                                      | \$ 20,907  | \$ 68,538           |

**Table of Contents****CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS**

(dollars in thousands)

(unaudited)

|   | For the Twenty-six Weeks Ended July 3, 2011 |                                      |   |              |
|---|---|--------------------------------------|---|--------------|
|   | The GEO Group, Inc.                         | Combined<br>Subsidiary<br>Guarantors | Combined<br>Non-Guarantor<br>Subsidiaries | Consolidated |
| <b>Cash Flow from Operating Activities:</b>                     |   |                                      |   |              |
| Net cash provided by (used in) operating activities             | \$ 64,488                                   | \$ (1,202)                           | \$ 31,976                                 | \$ 95,262    |
| <b>Cash Flow from Investing Activities:</b>                     |   |                                      |   |              |
| Acquisition, cash consideration, net of cash acquired           | (409,607)                                   |                                      |   | (409,607)    |
| Proceeds from sale of property and equipment                    |   | 619                                  |   | 619          |
| Proceeds from assets held for sale                              |   | 6,640                                |   | 6,640        |
| Change in restricted cash and investments                       |   |                                      | (11,478)                                  | (11,478)     |
| Capital expenditures  | (82,994)                                    | (3,236)                              | (1,132)                                   | (87,362)     |
| Net cash (used in) provided by investing activities             | (492,601)                                   | 4,023                                | (12,610)                                  | (501,188)    |
| <b>Cash Flow from Financing Activities:</b>                     |   |                                      |   |              |
| Payments on long-term debt                                      | (38,638)                                    | (576)                                | (7,618)                                   | (46,832)     |
| Proceeds from long-term debt                                    | 482,260                                     |                                      |   | 482,260      |
| Distribution to noncontrolling interests                        |   |                                      | (4,012)                                   | (4,012)      |
| Proceeds from the exercise of stock options                     | 2,209                                       |                                      |   | 2,209        |
| Income tax benefit of equity compensation                       | 392   |                                      |   | 392          |
| Debt issuance costs   | (10,771)                                    |                                      |   | (10,771)     |
| Net cash provided by (used in) financing activities             | 435,452                                     | (576)                                | (11,630)                                  | 423,246      |
| Effect of Exchange Rate Changes on Cash and Cash<br>Equivalents |   |                                      | 469                                       | 469          |
| Net Increase in Cash and Cash Equivalents                       | 7,339                                       | 2,245                                | 8,205                                     | 17,789       |
| Cash and Cash Equivalents, beginning of period                  | 2,614                                       | 221                                  | 36,829                                    | 39,664       |
| Cash and Cash Equivalents, end of period                        | \$ 9,953                                    | \$ 2,466                             | \$ 45,034                                 | \$ 57,453    |

---

**Table of Contents**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

**Forward-Looking Information**

This Quarterly Report on Form 10-Q 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 variations 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;

our ability to fulfill our debt service obligations and its impact on our liquidity;

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 activate the inactive beds at our idle facilities;

our ability to maintain occupancy rates at our facilities;

an increase in unreimbursed labor rates;

our ability to expand, diversify and grow our correctional, detention, mental health, residential treatment, re-entry, community-based services, youth services, monitoring services, evidence-based supervision and treatment programs and secure transportation services businesses;

our ability to win management contracts for which we have submitted proposals, retain existing management contracts and meet any performance standards required by such management contracts;

our ability to control operating costs associated with contract start-ups;

our ability to raise new project development capital given the often short-term nature of the customers' commitment to use newly developed facilities;

## Edgar Filing: GEO GROUP INC - Form 10-Q

our ability to estimate the government's level of dependency on privatized correctional services;

our ability to accurately project the size and growth of the U.S. and international privatized corrections industry;

our ability to successfully respond to delays encountered by states privatizing correctional services and cost savings initiatives implemented by a number of states;

our ability to develop long-term earnings visibility;

our ability to identify suitable acquisitions, and to successfully complete and integrate such acquisitions on satisfactory terms, and estimate the synergies to be achieved as a result of such acquisitions;

our exposure to the impairment of goodwill and other intangible assets as a result of our acquisitions;

our ability to successfully conduct our operations through joint ventures;

**Table of Contents**

our ability to obtain future financing on satisfactory terms or at all, including our ability to secure the funding we need to complete ongoing capital projects;

our exposure to political and economic instability and other risks impacting our international operations;

our exposure to risks impacting our information systems, including those that may cause an interruption, delay or failure in the provision of our services;

our exposure to rising general insurance costs;

our exposure to state and federal income tax law changes internationally and domestically and our exposure as a result of federal and international examinations of our tax returns or tax positions;

our exposure to claims for which we are uninsured;

our exposure to rising employee and inmate medical costs;

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;

the ability of our government customers to secure budgetary appropriations to fund their payment obligations to us and continue to operate under our existing agreements and/ or renew our existing agreements;

our ability to consummate the acquisition of the partnership interests in MCF during the third quarter of 2012;

our ability to pay quarterly dividends consistent with our expectations as to timing and amounts;

our analysis of the advantages and disadvantages of a REIT conversion, the results of our private letter ruling request to the IRS and our expectations as to the timing of completing a REIT conversion;

our ability to comply with government regulations and applicable contractual requirements;

our ability to acquire, protect or maintain our intellectual property; and

## Edgar Filing: GEO GROUP INC - Form 10-Q

other factors contained in our filings with the Securities and Exchange Commission, or the SEC, including, but not limited to, those detailed in this Quarterly Report on Form 10-Q, our Annual Report on Form 10-K and our Current Reports on Form 8-K 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 Quarterly Report on Form 10-Q.

### **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 above under **Forward Looking Information** and under **Part I - Item 1A. Risk Factors** in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012. The discussion should be read in conjunction with our unaudited consolidated financial statements and notes thereto included in this Quarterly Report on Form 10-Q. For the purposes of this discussion and analysis, we refer to the thirteen weeks ended July 1, 2012 as **Second Quarter 2012**, and we refer to the thirteen weeks ended July 3, 2011 as **Second Quarter 2011**. We refer to the twenty-six weeks ended July 1, 2012 as **First Half 2012** and the twenty-six weeks ended July 3, 2011 as **First Half 2011**.

We are a leading provider of government-outsourced services specializing in the management of correctional, detention, mental health, residential treatment and re-entry facilities, and the provision of community based services and youth services 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, mental health, residential treatment and community based re-entry facilities. We offer counseling,

---

**Table of Contents**

education and/or treatment to inmates with alcohol and drug abuse problems at most of the domestic facilities we manage. We are also a provider of innovative compliance technologies, industry-leading monitoring services, and evidence-based supervision and treatment programs for community-based parolees, probationers and pretrial defendants. Additionally, we have an exclusive contract with the U.S. Immigration and Customs Enforcement, which we refer to as ICE, to provide supervision and reporting services designed to improve the participation of non-detained aliens in the immigration court system. We 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. We also provide secure transportation services for offender and detainee populations as contracted domestically and in the United Kingdom through our joint venture, GEO Amey PECS Ltd., which we refer to as GEOAmey.

We acquired two companies, Cornell Companies, Inc. and BII Holding Corporation, during the past two years that have had, and we believe will continue to have, a significant impact on our business. As a result of these acquisitions, we expect to benefit from the increased scale and diversification of service offerings. Our acquisition in August 2010 of Cornell Companies, Inc., which we refer to as Cornell and we refer to this transaction as the Cornell Acquisition, added scale to our presence in the U.S. correctional and detention market, and combined Cornell's adult community-based and youth treatment services into GEO Care's behavioral healthcare services platform to create a leadership position in this growing market. Our acquisition on February 10, 2011 of BII Holding, the indirect owner of 100% of the equity interests of B.I. Incorporated, which we refer to as BI and refer to this transaction as the BI Acquisition, provides us with the ability to offer turn-key solutions to our customers in managing the full lifecycle of an offender from arraignment to reintegration into the community, which we refer to as the corrections lifecycle. As of July 1, 2012, our worldwide operations included the management and/or ownership of approximately 75,000 beds at 109 correctional, detention and residential treatment facilities, including idle facilities and projects under development and also included the provision of monitoring of more than 70,000 offenders in a community-based environment on behalf of approximately 900 federal, state and local correctional agencies located in all 50 states.

We provide a diversified scope of services on behalf of our government clients:

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 working with governments to deliver quality care, innovative programming and active patient treatment, primarily in state-owned mental healthcare facilities;

our community-based services involve supervision of adult parolees and probationers and the provision of temporary housing, programming, employment assistance and other services with the intention of the successful reintegration of residents into the community;

our youth services include residential, detention and shelter care and community-based services along with rehabilitative, educational and treatment programs;

our monitoring services provide our governmental clients with innovative compliance technologies, industry-leading monitoring services, and evidence-based supervision and treatment programs for community-based parolees, probationers and pretrial defendants; including services provided under the Intensive Supervision Appearance Program, which we refer to as ISAP, to ICE for the provision of services designed to improve the participation of non-detained aliens in the immigration court system;

we develop new facilities, using our project development experience to design, construct and finance what we believe are state-of-the-art facilities that maximize security and efficiency; and

we provide secure transportation services for offender and detainee populations as contracted domestically, and internationally, our joint venture GEOAmey is responsible for providing prisoner escort and custody services in the United Kingdom, including all of Wales and



## Edgar Filing: GEO GROUP INC - Form 10-Q

all of England except London and The East of England.

We maintained an average company-wide facility occupancy rate of 95.7% for the twenty-six weeks ended July 1, 2012, excluding facilities that are either idle or under development.

Reference is made to Part II, Item 7 of our Annual Report on Form 10-K filed with the SEC on March 1, 2012, for further discussion and analysis of information pertaining to our financial condition and results of operations for the fiscal year ended January 1, 2012.

---

## **Table of Contents**

### **Fiscal 2012 Developments**

#### **Contract Awards, Activations and Terminations**

The following contract awards and facility activations are expected to occur during fiscal year 2012:

On June 1, 2011, we announced that the City of Adelanto, California had signed a contract with us for the housing of federal immigration detainees at our 650-bed Detention Facility in Adelanto, California, which we purchased from the City of Adelanto in June of 2010, and at a 650-bed facility expansion, which we are constructing, to be located on land immediately adjacent to the facility. We completed the renovation and retrofitting of the existing 650-bed facility and began the initial intake of 650 detainees in August 2011. We expect to complete the new 650-bed expansion and begin the intake of the additional 650 detainees by August 2012.

On April 10, 2012, we announced that the California Department of Corrections and Rehabilitation, which we refer to as the CDCR, rescinded its previous notice of termination regarding our management contract for the 625-bed Golden State Correctional Facility. We will continue to manage this contract under our agreement with CDCR which currently expires in December 2012.

The following contract terminations occurred during fiscal year 2012:

On March 31, 2012, our contract for the management of the 130-bed Migrant Operations Center at Guantanamo Bay NAS, Cuba terminated and was transferred to another operator. We do not expect that the termination of this contract will have a material impact on our financial position, results of operations and/ or cash flows.

On April 19, 2012, the Company announced the discontinuation of its managed-only contract with the State of Mississippi, Department of Corrections for the 1,500-bed East Mississippi Correctional Facility ( East Mississippi ) effective July 19, 2012. In connection with the discontinuation of East Mississippi, the Company also discontinued its managed-only contracts with the State of Mississippi, Department of Corrections for the 1,000-bed Marshall County Correctional Facility effective August 13, 2012, and the 1,450-bed Walnut Grove Youth Correctional Facility effective July 1, 2012. Revenues related to the discontinued operations were \$11.2 million and \$11.0 million, for the thirteen weeks ended July 1, 2012 and July 3, 2011, respectively and \$22.3 million and \$22.4 million for the twenty-six weeks ended July 1, 2012 and July 3, 2011, respectively.

We are currently marketing approximately 7,000 vacant beds at 8 of our idle facilities to potential customers. The carrying values of these idle facilities totaled \$266.7 million as of July 1, 2012, excluding equipment and other assets that can be easily transferred for use at other facilities.

#### **Partnership Interests in Municipal Corrections Finance, L.P.**

On April 24, 2012, we signed a definitive agreement to purchase 100% of the partnership interests in Municipal Corrections Finance, L.P., which we refer to as MCF, for approximately \$27 million in cash plus the release of approximately \$10 million in cash held in escrow for the benefit of MCF. In addition, in connection with the transaction, the Company will pay approximately \$67 million, net of bond cash reserves and inclusive of a net make-whole premium of approximately \$15 million, to redeem the MCF bonds. The Company expects to incur a one-time loss on extinguishment of debt in connection with the redemption of the bonds of approximately \$8 million. Closing of the transaction is conditional on the Company redeeming the outstanding MCF bonds. We expect to close the transaction during our third fiscal quarter of 2012.

#### **Approval of The GEO Group Inc. 2011 Employee Stock Purchase Plan**

On May 4, 2012, our shareholders approved The GEO Group Inc. 2011 Employee Stock Purchase Plan. The Compensation Committee and Board of Directors had previously approved the Plan on May 4, 2011 and the Plan became effective on July 9, 2011, subject to obtaining shareholder approval. Eligible employees were allowed to participate in the Plan as of July 9, 2011, but no shares of common stock were issuable pursuant to the Plan prior to obtaining shareholder approval. Shares were issued to participating employees for the pre-shareholder approval offering periods on June 29, 2012 and shares will be issued to participating employees for the post-shareholder approval offering periods on the last day of each month.

#### **Potential REIT Conversion**

As previously disclosed, we are evaluating a potential conversion into a real estate investment trust ( REIT ). We have engaged legal advisors and financial advisors to assist us with this comprehensive review. In mid-July 2012, we submitted a request to the United States Internal Revenue

## Edgar Filing: GEO GROUP INC - Form 10-Q

Service for a private letter ruling in order to better inform our Board of Directors regarding the potential advantages and disadvantages of a REIT conversion and to determine whether we would qualify to convert to a REIT. Once we and our advisors complete the comprehensive analysis being performed regarding a potential REIT conversion, our Board of Directors will be adequately informed and in a position to determine whether to move forward with a REIT conversion. If our Board of Directors concludes that it is in our best interest to proceed with the REIT conversion, we would seek to complete the conversion by the earliest conversion date which is January 2013, however, due to the short timeframe, the REIT conversion could be delayed until the next available conversion date which is January 2014. We would expect to seek shareholder approval to implement provision in our charter that would be consistent with a public REIT structure.

### **Critical Accounting Policies**

The accompanying unaudited 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 revenue and expenses during the reporting period. We routinely evaluate our estimates based on historical experience and on various other assumptions that management believes

**Table of Contents**

are reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. During the twenty-six weeks ended July 1, 2012, we did not experience any changes in estimates inherent in the preparation of our financial statements and, at this time, do not anticipate any changes during the fiscal year ending December 30, 2012. A summary of our significant accounting policies is contained in Note 1 to our financial statements included in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012.

**RESULTS OF OPERATIONS**

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and the notes to our unaudited consolidated financial statements included in Part I, Item 1, of this Quarterly Report on Form 10-Q. The results of operations presented herein do not include the results of operations related to the Company's discontinued operations for all periods presented. Refer to Note 8 of the Quarterly Report on Form 10-Q.

**Comparison of Thirteen Weeks Ended July 1, 2012 and Thirteen Weeks Ended July 3, 2011**

For the purposes of the discussion below, Second Quarter 2012 refers to the thirteen weeks ended July 1, 2012 and Second Quarter 2011 refers to the thirteen weeks ended July 3, 2011.

**Revenues**

|   | 2012       | % of Revenue | 2011<br>(Dollars in thousands) | % of Revenue | \$ Change | % Change |
|---|------------|--------------|--------------------------------|--------------|-----------|----------|
| <b>U.S. Corrections &amp; Detention</b>   | 246,060    | 59.6%        | \$ 230,662                     | 58.2%        | \$ 15,398 | 6.7%     |
| <b>GEO Care</b>                           | 110,320    | 26.8%        | 110,857                        | 27.9%        | (537)     | (0.5)%   |
| <b>International Services</b>             | 55,968     | 13.6%        | 55,285                         | 13.9%        | 683       | 1.2%     |
| <b>Facility Construction &amp; Design</b> |            | %            |                                | %            |           | %        |
| <b>Total</b>                              | \$ 412,348 | 100.0%       | \$ 396,804                     | 100.0%       | \$ 15,544 | 3.9%     |

**U.S. Corrections & Detention**

Revenues increased in Second Quarter 2012 compared to Second Quarter 2011 primarily due to aggregate increases of \$15.9 million due to the activation and intake of inmates at the 650-bed Adelanto ICE Processing Center East ( Adelanto East ) in August 2011, the 1,500-bed Riverbend Correctional Facility ( Riverbend ) in December 2011, and the 600-bed Karnes Civil Detention Center ( Karnes ) in March 2012. We also experienced aggregate increases in revenues of \$8.7 million at certain of our facilities primarily due to increases in population and/or rates. These increases were partially offset by an aggregate decrease of \$11.0 million primarily due to contract terminations and other decreases related to lower populations at some facilities.

The number of compensated mandays in U.S. Corrections & Detention facilities was 4.2 million in Second Quarter 2012 and 4.0 million in Second Quarter 2011. We experienced an aggregate increase of approximately 320,000 mandays as a result of our new contracts discussed above and also as a result of population increases at certain facilities. These increases were offset by decreases resulting from contract terminations. 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. Detention & Corrections facilities was 96.4% and 95.9% of capacity in Second Quarter 2012 and Second Quarter 2011 respectively, excluding idle facilities.

**GEO Care**

The decrease in revenues for GEO Care in Second Quarter 2012 compared to Second Quarter 2011 is primarily attributable to decreases in revenues of \$3.7 million related to our terminated contracts. These decreases were partially offset by increases of \$0.9 million due to new electronic monitoring contracts of BI and an increase of \$2.4 million primarily due to population increases at certain facilities.

**International Services**

## Edgar Filing: GEO GROUP INC - Form 10-Q

Revenues for our International Services segment during Second Quarter 2012 increased by \$0.7 million over Second Quarter 2011 primarily due to the following factors: (i) aggregate increases at our Australian subsidiary of \$1.7 million related to population increases, contractual increases linked to the inflationary index and the provision of additional services under certain contracts; (ii) an increase of \$3.4 million due to the provision of additional services at Harmondsworth Immigration Removal Centre ( Harmondsworth ) located in London, England and the assumption of operations at the 217-bed Dungavel House

**Table of Contents**

Immigration Removal Centre ( Dungavel ) on September 25, 2011; and (iii) an increase of \$0.5 million at our South Africa subsidiary primarily due to increases in the inflationary index. These increases were partially offset by: (i) decreases of \$3.4 million as a result of foreign exchange rate fluctuations; and (ii) a decrease in revenues of \$1.6 million related to our terminated contract for the operation of the Campsfield House Removal Centre ( Campsfield House ).

**Operating Expenses**

|   | 2012       | % of<br>Segment<br>Revenues | 2011       | % of<br>Segment<br>Revenues | \$ Change | % Change |
|---|------------|-----------------------------|------------|-----------------------------|-----------|----------|
| (Dollars in thousands)                    |            |                             |            |                             |           |          |
| <b>U.S. Corrections &amp; Detention</b>   | \$ 170,467 | 69.3%                       | \$ 164,568 | 71.3%                       | \$ 5,899  | 3.6%     |
| <b>GEO Care</b>                           | 81,610     | 74.0%                       | 82,232     | 74.2%                       | (622)     | (0.8)%   |
| <b>International Services</b>             | 52,958     | 94.6%                       | 52,413     | 94.8%                       | 545       | 1.0%     |
| <b>Facility Construction &amp; Design</b> |            | %                           | 23         | %                           | (23)      | (100.0)% |
| <b>Total</b>                              | \$ 305,035 | 74.0%                       | \$ 299,236 | 75.4%                       | \$ 5,799  | 1.9%     |

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health and GEO Care facilities and expenses incurred in our Facility Construction & Design segment.

**U.S. Corrections & Detention**

The increase in operating expenses for U.S. Corrections & Detention reflects the following: (i) the activation and intake of inmates at Adelanto East, Riverbend and Karnes which contributed an aggregate increase to operating expenses of \$10.5 million; and (ii) increases of \$3.6 million at certain of our facilities primarily related to population increases, higher levels of required staffing and additional medical costs. These increases were partially offset by aggregate decreases in operating expenses of \$8.2 million due to contract terminations. Overall, we experienced a decrease in operating expenses as a percentage of revenue primarily due to a \$2.7 million accrual in Second Quarter 2011 due to the verdict entered against us at a GEO Oklahoma state correctional facility, as well as higher startup related costs in Second Quarter 2011 for new facilities opened.

**GEO Care**

Operating expenses for GEO Care decreased by \$0.6 million during Second Quarter 2012 from Second Quarter 2011 primarily due to contract terminations. These decreases were partially offset by non-recurring recoveries related to accounts receivable and an insurance settlement for property damage at an acquired facility in Second Quarter 2011.

**International Services**

Operating expenses for our International Services segment during Second Quarter 2012 increased \$0.5 million over the prior year due to: (i) the impacts of foreign currency exchange rates of \$(1.1) million; and (ii) a decrease in operating expenses at our Australian subsidiary of \$(1.0) million in Second Quarter 2012 which is primarily related to non-recurring international bid costs incurred during Second Quarter 2011. We also experienced a net increase of \$2.6 million in operating expenses in the United Kingdom primarily due to the opening of Dungavel partially offset by the termination of our contract for the management of Campsfield House effective in May 2011.

**Table of Contents****Depreciation and Amortization**

|   | 2012      | % of<br>Segment<br>Revenue | 2011<br>(Dollars in thousands) | % of<br>Segment<br>Revenue | \$ Change | % Change |
|---|-----------|----------------------------|--------------------------------|----------------------------|-----------|----------|
| <b>U.S. Corrections &amp; Detention</b>   | 15,744    | 6.4%                       | \$ 13,213                      | 5.7%                       | \$ 2,531  | 19.2%    |
| <b>GEO Care</b>                           | 7,507     | 6.8%                       | 7,182                          | 6.5%                       | 325       | 4.5%     |
| <b>International Services</b>             | 556       | 1.0%                       | 550                            | 1.0%                       | 6         | 1.1%     |
| <b>Facility Construction &amp; Design</b> |           | %                          |                                |                            |           | %        |
| <b>Total</b>                              | \$ 23,807 | 5.8%                       | \$ 20,945                      | 5.3%                       | \$ 2,862  | 13.7%    |

**U.S. Corrections & Detention**

U.S. Corrections & Detention depreciation and amortization expense increased by \$2.5 million in Second Quarter 2012 compared to Second Quarter 2011 primarily as a result of the completion of construction projects in 2011.

**GEO Care**

The increase in depreciation and amortization expense for GEO Care in Second Quarter 2012 compared to Second Quarter 2011 is primarily due to an increase in monitoring and other equipment at BI in 2012 related to certain contract wins.

**International Services**

Depreciation and amortization expense increased slightly in Second Quarter 2012 over Second Quarter 2011 primarily from increases in capital expenditures at our Australian subsidiary and also from fluctuations in foreign exchange rates. These increases were partially offset by a decrease in depreciation expense due to the termination of our Campsfield House management contract effective May 2011.

**Other Unallocated Operating Expenses**

|  | 2012      | % of<br>Revenue | 2011<br>(Dollars in thousands) | % of<br>Revenue | \$ Change | % Change |
|--|-----------|-----------------|--------------------------------|-----------------|-----------|----------|
| <b>General and Administrative Expenses</b> | \$ 27,043 | 6.6%            | \$ 27,710                      | 7.0%            | \$ (667)  | (2.4)%   |

General and administrative expenses comprise substantially all of our other unallocated operating expenses including primarily corporate management salaries and benefits, professional fees and other administrative expenses. The decrease in general and administrative expenses in Second Quarter 2012 compared to Second Quarter 2011 was due to \$0.9 million of nonrecurring start-up and acquisition related costs in 2011. Excluding the impact of acquisition related costs, general and administrative expenses are slightly lower as a percentage of revenues in Second Quarter 2012 as a result of lower professional fees and other miscellaneous expenses. We anticipate that general and administrative expenses, excluding any acquisition related costs, as a percentage of revenue will be slightly lower in fiscal 2012 than in fiscal 2011.

**Non Operating Expenses****Interest Income and Interest Expense**

|  | 2012 | % of<br>Revenue | 2011 | % of<br>Revenue | \$ Change | % Change |
|--|------|-----------------|------|-----------------|-----------|----------|
|--|------|-----------------|------|-----------------|-----------|----------|

Edgar Filing: GEO GROUP INC - Form 10-Q

(Dollars in thousands)

|                         |           |      |           |      |          |      |
|-------------------------|-----------|------|-----------|------|----------|------|
| <b>Interest Income</b>  | \$ 1,761  | 0.4% | \$ 1,629  | 0.4% | \$ 132   | 8.1% |
| <b>Interest Expense</b> | \$ 20,617 | 5.0% | \$ 19,412 | 4.9% | \$ 1,205 | 6.2% |

The majority of our interest income generated in Second Quarter 2012 and Second Quarter 2011 is from the cash balances at our foreign subsidiaries.



**Table of Contents**

The increase in interest expense of \$1.2 million is attributable to more indebtedness outstanding in Second Quarter 2012 compared to Second Quarter 2011. We incurred aggregate increases in interest expense of \$1.7 million due to greater outstanding borrowings under our Senior Credit Facility and due to the issuance of non-recourse debt by our wholly owned subsidiary in December 2011. These increases were partially offset by decreases in interest expense aggregating \$0.5 million primarily due to lower outstanding borrowings on certain of our other non-recourse debt. Outstanding borrowings, net of discount and swap, at July 1, 2012 and July 3, 2011, excluding non-recourse debt and capital lease liabilities, were \$1,322.9 million and \$1,252.6 million, respectively.

**Provision for Income Taxes**

|                     | 2012                   | Effective Rate | 2011      | Effective Rate | \$ Change | % Change |
|---------------------|------------------------|----------------|-----------|----------------|-----------|----------|
|                     | (Dollars in thousands) |                |           |                |           |          |
| <b>Income Taxes</b> | \$ 14,991              | 39.9%          | \$ 12,302 | 39.5%          | \$ 2,689  | 21.9%    |

The effective tax rate for Second Quarter 2012 was 39.9% compared to an effective tax rate of 39.5% for the same period in the prior year. The expiration of the federal Work-Opportunity-Tax-Credit legislation at the end of 2011 has an unfavorable impact on our effective tax rate of approximately one-half percent in 2012. We estimate our annual effective tax rate for fiscal year 2012 to be in the range of 39% to 40%.

**Equity in Earnings of Affiliates**

|   | 2012                   | % of Revenue | 2011     | % of Revenue | \$ Change | % Change |
|---|------------------------|--------------|----------|--------------|-----------|----------|
|   | (Dollars in thousands) |              |          |              |           |          |
| <b>Equity in Earnings of Affiliates</b> | \$ 430                 | 0.1%         | \$ 1,418 | 0.4%         | \$ (988)  | (69.7)%  |

Equity in earnings of affiliates, presented net of income taxes, represents the earnings (loss) of SACS and GEOAmeY, respectively. Overall, we experienced a decrease in equity in earnings of affiliates during Second Quarter 2012 compared to Second Quarter 2011, which is primarily due to an \$0.9 million loss from the operations of GEOAmeY, which began operating in August 2011.

**Comparison of Twenty-six Weeks Ended July 1, 2012 and Twenty-six Weeks Ended July 3, 2011****Revenues**

|                                | 2012                   | % of Revenue  | 2011              | % of Revenue  | \$ Change        | % Change    |
|--------------------------------|------------------------|---------------|-------------------|---------------|------------------|-------------|
|                                | (Dollars in thousands) |               |                   |               |                  |             |
| U.S. Corrections & Detention   | \$ 481,094             | 59.2%         | \$ 460,870        | 59.3%         | \$ 20,224        | 4.4%        |
| GEO Care                       | 220,013                | 27.0%         | 207,746           | 26.7%         | 12,267           | 5.9%        |
| International Services         | 112,498                | 13.8%         | 108,413           | 14.0%         | 4,085            | 3.8%        |
| Facility Construction & Design |                        | %             | 119               | %             | (119)            | (100.0)%    |
| <b>Total</b>                   | <b>\$ 813,605</b>      | <b>100.0%</b> | <b>\$ 777,148</b> | <b>100.0%</b> | <b>\$ 36,457</b> | <b>4.7%</b> |

**U.S. Corrections & Detention**

Revenues increased in First Half 2012 as compared to First Half 2011 primarily due to aggregate increases of \$21.7 million due to the activation and intake of inmates at Adelanto East, Riverbend and Karnes. We also experienced aggregate increases in revenues of \$18.5 million at certain of our facilities primarily due to increases in population and/or rates. These increases were partially offset by an aggregate decrease of \$23.2 million due to contract terminations and other decreases primarily related to lower populations at some facilities.

The number of compensated mandays in U.S. Corrections & Detention facilities was 8.2 million in First Half 2012 as compared to 8.0 million in First Half 2011. We experienced an aggregate increase of approximately 540,000 mandays as a result of our new contracts discussed above and also as a result of population increases at certain facilities. These increases were offset by decreases resulting from contract terminations. We

## Edgar Filing: GEO GROUP INC - Form 10-Q

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. Detention & Corrections facilities was 96.2% and 94.8% of capacity in First Half 2012 and First Half 2011 respectively, excluding idle facilities.

**Table of Contents***GEO Care*

The increase in revenues for GEO Care in First Half 2012 as compared to First Half 2011 is primarily attributable to a full six months of revenues generated by BI in 2012 compared to approximately four and a half months of revenues in 2011 which contributed to an increase of \$15.2 million. We also experienced an increase in revenues of \$4.5 million at certain of our facilities primarily due to increases in population and/or rates. These increases were partially offset by a decrease in revenues of \$7.6 million related to our terminated contracts.

*International Services*

Revenues for our International Services segment during First Half 2012 increased by \$4.1 million over First Half 2011 primarily due to the following factors: (i) aggregate increases at our Australian subsidiary of \$3.7 million related to population increases, contractual increases linked to the inflationary index and the provision of additional services under certain contracts; (ii) an increase of \$5.5 million due to the provision of additional services at Harmondsworth and the assumption of operations at Dungavel on September 25, 2011; and (iii) an increase of \$0.5 million at our South Africa subsidiary primarily due to increases in the inflationary index. These increases were partially offset by: (i) decreases of \$2.1 million as a result of foreign exchange rate fluctuations; and (ii) a decrease in revenues of \$4.0 million related to our terminated contract for the operation of Campsfield House effective in May 2011.

*Operating Expenses*

|                                | 2012              | % of<br>Segment<br>Revenues | 2011<br>(Dollars in thousands) | % of<br>Segment<br>Revenues | \$<br>Change     | % Change    |
|--------------------------------|-------------------|-----------------------------|--------------------------------|-----------------------------|------------------|-------------|
| U.S. Corrections & Detention   | \$ 343,228        | 71.3%                       | \$ 327,230                     | 71.0%                       | \$ 15,998        | 4.9%        |
| GEO Care                       | 165,323           | 75.1%                       | 159,926                        | 77.0%                       | 5,397            | 3.4%        |
| International Services         | 104,744           | 93.1%                       | 101,062                        | 93.2%                       | 3,682            | 3.6%        |
| Facility Construction & Design |                   | %                           | 39                             | 32.8%                       | (39)             | (100.0)%    |
| <b>Total</b>                   | <b>\$ 613,295</b> | <b>75.4%</b>                | <b>\$ 588,257</b>              | <b>75.7%</b>                | <b>\$ 25,038</b> | <b>4.3%</b> |

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health and GEO Care facilities and expenses incurred in our Facility Construction & Design segment.

*U.S. Corrections & Detention*

The increase in operating expenses for U.S. Corrections & Detention reflects the following: (i) the activation and intake of inmates at Adelanto East, Riverbend and Karnes which contributed an aggregate increase to operating expenses of \$22.5 million, including \$3.6 million in nonrecurring start-up costs; and (ii) increases of \$7.4 million at certain of our facilities primarily related to population increases, higher levels of required staffing and additional medical costs. These increases were partially offset by aggregate decreases in operating expenses of \$13.9 million due to contract terminations.

*GEO Care*

Operating expenses for GEO Care increased \$5.4 million during First Half 2012 from First Half 2011 primarily due to BI which was operating for two full quarters during First Half 2012 compared to a partial two quarters during First Half 2011 as BI was acquired in February 2011. We also experienced an increase in operating expenses during First Half 2012 for the operation of Montgomery County which opened in March 2011. These increases were partially offset by a decrease in operating expenses for terminated contracts. During First Half 2012, we experienced a decrease in operating expenses as a percentage of revenue due to improved margins resulting from our acquisition of BI and also due to nonrecurring start up costs incurred in First Half 2011 for the opening of Montgomery County.

*International Services*

## Edgar Filing: GEO GROUP INC - Form 10-Q

Operating expenses for our International Services segment during the First Half of 2012 increased \$3.6 million over the prior year due to: (i) the impacts of foreign currency exchange rates of \$(2.1) million; and (ii) an increase in operating expenses at our Australian and South African subsidiaries of \$2.8 million related to increases in population and additional services

**Table of Contents**

provided at certain of those facilities. We also experienced a net increase of \$2.9 million in operating expenses in the United Kingdom primarily due to the opening of Dungavel on September 25, 2011, partially offset by the termination of our contract for the management of Campsfield House effective in May 2011.

**Depreciation and Amortization**

|   | 2012      | % of<br>Segment<br>Revenue | 2011<br>(Dollars in thousands) | % of<br>Segment<br>Revenue | \$ Change | % Change |
|---|-----------|----------------------------|--------------------------------|----------------------------|-----------|----------|
| <b>U.S. Corrections &amp; Detention</b>   | \$ 30,906 | 6.4%                       | \$ 26,042                      | 5.7%                       | \$ 4,864  | 18.7%    |
| <b>GEO Care</b>                           | 14,863    | 6.8%                       | 12,527                         | 6.0%                       | 2,336     | 18.6%    |
| <b>International Services</b>             | 1,113     | 1.0%                       | 1,077                          | 1.0%                       | 36        | 3.3%     |
| <b>Facility Construction &amp; Design</b> |           | %                          |                                | %                          |           | %        |
| <b>Total</b>                              | \$ 46,882 | 5.8%                       | \$ 39,646                      | 5.1%                       | \$ 7,236  | 18.3%    |

**U.S. Corrections & Detention**

U.S. Corrections & Detention depreciation and amortization expense increased by \$4.9 million in First Half 2012 compared to the First Half 2011 primarily as a result of the completion of construction projects in 2011 and 2012.

**GEO Care**

The increase in depreciation and amortization expense for GEO Care in First Half 2012 compared to First Half 2011 is primarily due to an increase in monitoring and other equipment at BI in 2012 related to certain contract wins and amortization of BI intangible assets. As BI was acquired in February 2011, First Half 2011 does not include a full six months of depreciation and amortization for BI.

**International Services**

Depreciation and amortization expense increased slightly in First Half 2012 over First Half 2011 primarily due to increases in capital expenditures at our Australian subsidiary and also from fluctuations in foreign exchange rates. These increases were partially offset by a decrease in depreciation expense due to the termination of our Campsfield House management contract effective May 2011.

**Other Unallocated Operating Expenses**

|  | 2012      | % of<br>Revenue | 2011<br>(Dollars in thousands) | % of<br>Revenue | \$ Change  | % Change |
|--|-----------|-----------------|--------------------------------|-----------------|------------|----------|
| <b>General and Administrative Expenses</b> | \$ 54,484 | 6.7%            | \$ 60,498                      | 7.8%            | \$ (6,014) | (9.9)%   |

General and administrative expenses comprise substantially all of our other unallocated operating expenses including primarily corporate management salaries and benefits, professional fees and other administrative expenses. The decrease in general and administrative expenses in First Half 2012 compared to First Half 2011 was due to \$5.7 million of nonrecurring start-up and acquisition related costs in 2011. Excluding the impact of acquisition related costs, general and administrative expenses are slightly lower as a percentage of revenues in First Half 2012 as a result of lower professional fees and other miscellaneous expenses. We anticipate that general and administrative expenses, excluding any acquisition related costs, as a percentage of revenue will be slightly lower in fiscal 2012 than in fiscal 2011.

**Table of Contents****Non Operating Expenses****Interest Income and Interest Expense**

|                  | 2012                   | % of<br>Revenue | 2011      | % of<br>Revenue | \$ Change | % Change |
|------------------|------------------------|-----------------|-----------|-----------------|-----------|----------|
|                  | (Dollars in thousands) |                 |           |                 |           |          |
| Interest Income  | \$ 3,568               | 0.4%            | \$ 3,198  | 0.4%            | \$ 370    | 11.6%    |
| Interest Expense | \$ 41,424              | 5.1%            | \$ 36,373 | 4.7%            | \$ 5,051  | 13.9%    |

The majority of our interest income generated in the First Half of 2012 and the First Half of 2011 is from the cash balances at our foreign subsidiaries.

The increase in interest expense of \$5.1 million is attributable to more indebtedness outstanding in First Half 2012 compared to the First Half 2011. We incurred \$2.1 million in additional expense during the First Half 2012 due to the issuance of our 6.625% Senior Notes in February 2011. We also incurred aggregate increases in interest expense of \$3.8 million due to greater outstanding borrowings under our Senior Credit Facility and due to the issuance of non-recourse debt by our wholly owned subsidiary in December 2011. These increases were partially offset by decreases in interest expense aggregating \$0.8 million primarily due to lower outstanding borrowings on certain of our other non-recourse debt. Outstanding borrowings, net of discount and swap, at July 1, 2012 and July 3, 2011, excluding non-recourse debt and capital lease liabilities, were \$1,322.9 million and \$1,252.6 million, respectively.

**Provision for Income Taxes**

|              | 2012                   | Effective Rate | 2011      | Effective Rate | \$ Change | % Change |
|--------------|------------------------|----------------|-----------|----------------|-----------|----------|
|              | (Dollars in thousands) |                |           |                |           |          |
| Income Taxes | \$ 24,208              | 39.6%          | \$ 21,674 | 39.0%          | \$ 2,534  | 11.7%    |

The effective tax rate for First Half 2012 was 39.6% compared to an effective tax rate of 39.0% for the same period in the prior year which included certain discrete items. Excluding the discrete items, the effective tax rate for the same period in the prior year would have been 39.4%. The expiration of the federal Work-Opportunity-Tax-Credit legislation at the end of 2011 has an unfavorable impact on our effective tax rate of approximately one-half percent in 2012. We estimate our annual effective tax rate for fiscal year 2012 to be in the range of 39% to 40%.

**Equity in Earnings of Affiliates**

|                                  | 2012                   | % of<br>Revenue | 2011     | % of<br>Revenue | \$ Change | % Change |
|----------------------------------|------------------------|-----------------|----------|-----------------|-----------|----------|
|                                  | (Dollars in thousands) |                 |          |                 |           |          |
| Equity in Earnings of Affiliates | \$ 1,178               | 0.1%            | \$ 2,080 | 0.3%            | \$ (902)  | (43.4)%  |

Equity in earnings of affiliates, presented net of income taxes, represents the earnings (loss) of SACS and GEOAmeY, respectively. Overall, we experienced a decrease in equity in earnings of affiliates due to a \$1.4 million net loss from the operations of GEOAmeY, which began operating in August 2011. This loss was partially offset by an increase in net earnings from SACS of \$0.5 million.

**Financial Condition****Capital Requirements**

Our current cash requirements consist of amounts needed for working capital, debt service, supply purchases, investments in joint ventures, and capital expenditures related to either the development of new correctional, detention, mental health, residential treatment and re-entry facilities, or the maintenance of existing 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

## Edgar Filing: GEO GROUP INC - Form 10-Q

the contract. In connection with GEOAmeY, our newly formed joint venture in the United Kingdom, we and our joint venture partner have each provided a line of credit of £12.0 million, or \$18.9 million, based on exchange rates, as of July 1, 2012, for GEOAmeY's operations. As of July 1, 2012, \$19.1 million, including accrued interest of \$0.2 million was owed to us by GEOAmeY under the line of credit. Also, on April 24, 2012, the Company signed a definitive agreement to purchase 100% of the partnership interests of MCF for approximately \$27 million in cash plus the release of approximately \$10 million in cash held in escrow for

**Table of Contents**

the benefit of MCF. In addition, in connection with the transaction, the Company will pay approximately \$67 million, net of bond cash reserves and inclusive of a net make-whole premium of approximately \$15 million, to redeem the MCF bonds. Additional capital needs may also arise in the future with respect to possible acquisitions, other corporate transactions or other corporate purposes.

We are currently developing a number of projects using company financing. We estimate that these existing capital projects will cost approximately \$125.6 million, of which \$73.4 million was spent through the twenty-six weeks ended July 1, 2012. We have future committed capital projects for which we estimate our remaining capital requirements to be approximately \$52.2 million, which will be spent in fiscal years 2012 and 2013. Capital expenditures related to facility maintenance costs are expected to range between \$30.0 million and \$35.0 million for fiscal year 2012. In addition to these current estimated capital requirements for 2012 and 2013, we are currently in the process of bidding on, or evaluating potential bids for the design, construction and management of a number of new projects. In the event that we win bids for these projects and decide to self-finance their construction, our capital requirements in 2012 and/or 2013 could materially increase.

***Liquidity and Capital Resources***

As of July 1, 2012, the Senior Credit Facility, as amended, was comprised of: (i) a \$150.0 million Term Loan A bearing interest at LIBOR plus 3.00% and maturing August 4, 2015, (ii) a \$150.0 million Term Loan A-2 bearing interest at LIBOR plus 3.00% and maturing August 4, 2015, (iii) a \$200.0 million Term Loan B, bearing interest at LIBOR plus 2.75% with a LIBOR floor of 1.00% and maturing August 4, 2016 and (iv) the Revolver of \$500.0 million bearing interest at LIBOR plus 3.00% and maturing August 4, 2015. As of July 1, 2012, we had \$136.9 million outstanding under the Term Loan A, \$140.6 million outstanding under the Term Loan A-2, \$196.5 million outstanding under the Term Loan B, net of \$1.4 million discount, and our \$500.0 million Revolving Credit Facility had \$295.0 million outstanding in loans, \$56.5 million outstanding in letters of credit and \$148.5 million available for borrowings. We also had the ability to borrow \$250.0 million under the accordion feature of our Senior Credit Facility subject to lender demand and market conditions.

In October 2009, we completed an offering of \$250.0 million in aggregate principal of our 7<sup>3</sup>/<sub>4</sub>% Senior Notes due 2017, which we refer to as the 7<sup>3</sup>/<sub>4</sub>% Senior Notes. Interest on the 7<sup>3</sup>/<sub>4</sub>% Senior Notes accrues interest at the stated rate. We pay interest semi-annually in arrears on April 15 and October 15 of each year. On or after October 15, 2013, we may, at our option, redeem all or a part of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes at the redemption prices set forth in the indenture governing the 7<sup>3</sup>/<sub>4</sub>% Senior Notes.

In connection with our acquisition of BI in February 2011, we completed an offering of \$300.0 million in aggregate principal of our 6.625% Senior Notes due 2021, which we refer to as the 6.625% Senior Notes. Interest on the 6.625% Senior Notes accrues at the stated rate. We pay interest semi-annually in arrears on February 15 and August 15. On or after February 15, 2016, we may, at our option, redeem all or part of the 6.625% Senior Notes at the redemption prices set forth in the indenture governing the 6.625% Senior Notes.

In addition to the debt outstanding under the Senior Credit Facility, the 7<sup>3</sup>/<sub>4</sub>% Senior Notes and the 6.625% Senior Notes discussed above, we also have significant debt obligations which, although these obligations are non-recourse to us, require cash expenditures for debt service. Our significant debt obligations could have material consequences. See Risk Factors - Risks Related to Our High Level of Indebtedness in Item 1A of our Form 10-K. We are exposed to various commitments and contingencies which may have a material adverse effect on our liquidity. See Part II - Item 1. Legal Proceedings. We also have guaranteed certain obligations for our South African joint venture and other of our international subsidiaries. These non-recourse obligations, commitments and contingencies and guarantees are further discussed in Notes 10, 11 and 12 to the financial statements and also are further described in the Company's 2011 Annual Report on Form 10-K.

We are also considering opportunities for future business and/or asset acquisitions. If we are successful in our pursuit of these new projects, our cash on hand, cash flows from operations and borrowings under the existing Senior Credit Facility may not provide sufficient liquidity to meet our capital needs through 2013 and we could be forced to seek additional financing or refinance our existing indebtedness. There can be no assurance that any such financing or refinancing would be available to us on terms equal to or more favorable than our current financing terms, or at all. In the future, our access to capital and ability to compete for future capital-intensive projects will also be dependent upon, among other things, our ability to meet certain financial covenants in the indenture governing the 7<sup>3</sup>/<sub>4</sub>% Senior Notes, the indenture governing the 6.625% Senior Notes and our Senior Credit Facility. A substantial decline in our financial performance could limit our access to capital pursuant to these covenants and have a material adverse affect on our liquidity and capital resources and, as a result, on our financial condition and results of operations. In addition to these foregoing potential constraints on our capital, a number of state government agencies have been suffering from budget deficits and liquidity issues. While we expect to be in compliance with our debt covenants, if these constraints were to intensify, our liquidity could be materially adversely impacted as could our ability to remain in compliance with these debt covenants.



---

**Table of Contents**

On July 14, 2011, our Board of Directors approved a stock repurchase program of up to \$100.0 million of our common stock effective through December 31, 2012. During the fiscal year ended January 1, 2012, we repurchased 3.9 million shares of our common stock at a cost of \$75.0 million primarily with proceeds from our Revolver. The remaining \$25.0 million of repurchases that may be made under the stock repurchase program will be funded primarily with cash on hand, free cash flow, and/ or borrowings under our Revolver. The stock repurchase program is intended to be implemented through repurchases made from time to time in the open market or in privately negotiated transactions, in accordance with applicable securities and stock exchange requirements. The program may also include repurchases from time to time from executive officers or directors of vested restricted stock and/or vested stock options. The stock repurchase program does not obligate us to purchase any specific amount of our common stock and may be suspended or extended at any time at our discretion.

In February 2012, our Board adopted a dividend policy. In May 2012, our Board determined to accelerate the implementation of our dividend policy to the third quarter of 2012 and to increase the estimated quarterly dividend beginning in the fourth quarter of 2012. Under the dividend policy, we anticipate that we will pay quarterly dividends beginning in the third quarter of 2012 in the amount of \$.20 per share subject to capital availability and periodic determinations by our Board that cash dividends are in the best interests of our shareholders and are in compliance with all laws and our agreements applicable to the declaration of cash dividends, including our indentures and Senior Credit Facility. Based on 61.5 million shares outstanding as of July 1, 2012, quarterly cash dividends of \$.20 per share would have resulted in quarterly cash dividends of \$12.3 million. Based on our current capitalization, we do not believe that making dividend payments will materially adversely impact our liquidity. We believe we have the ability to declare quarterly cash dividends, as well as continue to fund the stock repurchase program, our working capital, our debt service requirements, and our maintenance and growth capital expenditure requirements, while maintaining sufficient liquidity for other corporate purposes.

We plan to fund all of our capital needs, including our capital expenditures, from cash on hand, cash from operations, borrowings under our Senior Credit Facility and any other financings which our management and Board of Directors, in their discretion, may consummate. Currently, our primary source of liquidity to meet these requirements is cash flow from operations and borrowings under the \$500.0 million Revolver. Our management believes that cash on hand, cash flows from operations and availability under our Senior Credit Facility will be adequate to support our capital requirements for 2012 and 2013 disclosed under *Capital Requirements* above.

***Executive Retirement Agreement***

We have a non-qualified deferred compensation agreement with our Chief Executive Officer, which we refer to as our CEO. The current agreement provides for a lump sum payment upon retirement, no sooner than age 55. As of January 1, 2012, our CEO had reached age 55 and was eligible to receive the payment upon retirement. If our CEO had retired as of July 1, 2012, the Company would have had to pay him \$6.0 million including a tax gross-up relating to the retirement payment equal to \$2.2 million. Based on our current capitalization, we do not believe that making this payment would materially adversely impact our liquidity.

***Cash Flow***

Cash and cash equivalents as of July 1, 2012 were \$68.5 million, an increase of \$23.8 million from January 1, 2012.

Cash provided by operating activities from continuing operations amounted to \$124.7 million in First Half 2012 versus cash provided by operating activities from continuing operations of \$91.3 million in First Half 2011. Cash provided by operating activities from continuing operations represents the fiscal year to date net income plus depreciation and amortization, stock-based compensation expense, changes in working capital and adjusted for other non-cash charges and income. The cash flows from operations in First Half 2012 was also positively impacted by a decrease in accounts receivable, prepaid expenses and other current assets.

Cash used in investing activities of amounted to \$71.0 million in First Half 2012 compared to cash used in investing activities of \$501.2 million in First Half 2011. Cash used in investing activities in First Half 2012 was primarily the result of capital expenditures of \$71.9 million. Cash used in investing activities in First Half 2011 primarily reflects our cash consideration for the purchase of BI for \$409.6 million and capital expenditures of \$87.4 million. Cash used in investing activities may be impacted during 2012 by capital expenditures and business and/or asset acquisitions.

Cash used in financing activities in First Half 2012 amounted to \$31.0 million compared to cash provided by financing activities of \$423.2 million in First Half 2011. Cash used in financing activities in the First Half 2012 reflects payments of \$169.3 million on indebtedness offset by \$145.0 million of borrowings under our Revolver. We also made a cash distribution of \$5.8 million to the partners of MCF. Cash provided by financing activities in First Half 2011 reflects proceeds from our



## **Table of Contents**

Senior Credit Facility of \$180.0 million, proceeds of \$300.0 million from the issuance of our 6.625% Senior Notes and \$2.3 million of debt related to our acquisition of BI, offset by payments on indebtedness of \$38.6 million, payments on non-recourse debt of \$7.6 million and other debt payments of \$0.6 million. We also made a cash distribution of \$4.0 million to the partners of MCF and paid \$10.8 million in debt issuance costs associated with the financing of the BI Acquisition. Cash used in financing activities may increase by up to \$25.0 million if our management determines that the repurchase of our common stock is an appropriate use of capital resources. Further uses of cash in financing activities are expected to result from the payment of dividends in our third and fourth fiscal quarters. Cash provided by financing activities will increase as a result of any financing related to the above mentioned investing and financing activities.

## **Outlook**

The following discussion 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 statements. Please refer to Part I - Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012, the Forward-Looking Statements - Safe Harbor section in our Annual Report on Form 10-K, as well as the other disclosures contained in our Annual Report on Form 10-K, and the

Forward-Looking Information section in this Form 10-Q 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.

## *Revenue*

Domestically, we continue to pursue a number of opportunities in the privatized corrections and detention industry. Overcrowding at corrections facilities in various states and increased demand for bed space at federal prisons and detention facilities are two of the factors that have contributed to the opportunities for privatization. We are currently competing on procurements at the state level which represent approximately 2,700 correctional beds. In New Hampshire, we have responded to a state procurement for a new correctional facility totaling approximately 1,700 beds. In Arizona, we responded to a procurement the State had issued which was intended for 2,000 in-state beds. The State has since decided to initially award contracts for 1,000 in-state beds under the procurement. We continue to be encouraged by opportunities as discussed above; however any positive trends may, to some extent, be adversely impacted by government budgetary constraints in the future. While state fiscal conditions continue to improve at a slow and steady pace and revenue performance remains positive in most states, the number of states reporting spending overruns in fiscal year 2012 has grown from 11 to 21 states since fall 2011 according to a Spring 2012 survey by the National Conference of State Legislatures. As a result of budgetary pressures, state correctional agencies may pursue a number of cost savings initiatives which may include the early release of inmates, changes to parole laws and sentencing guidelines, and reductions in per diem rates and/or the scope of services provided by private operators. These potential cost savings initiatives could have a material adverse impact on our current operations and/or our ability to pursue new business opportunities. Effective October 1, 2011, the State of California began implementing its Criminal Justice Realignment Plan, which has delegated tens of thousands of low level state offenders to local county jurisdictions in California. As a result of this decision, the California Department of Corrections and Rehabilitation cancelled our agreements for the housing of low level state offenders at three of our California community correctional facilities. In January 2012, we also received notice from the CDCR of its intention to terminate the contract at Golden State Medium Community Correctional Facility however, this termination was rescinded in April 2012 and we will continue to manage the facility under the original contract through December 14, 2012. We plan to market the idle facilities to federal, state and local jurisdictions in California. Additionally, if state budgetary constraints, as discussed above, persist or intensify, our state customers' ability to pay us may be impaired and/or we may be forced to renegotiate our management contracts on less favorable terms and our financial condition, results of operations or cash flows could be materially adversely impacted. 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, contract non-renewals, and/or contract re-bids. Although we have historically had a relatively high contract renewal rate, there can be no assurance that we will be able to renew our expiring management contracts on favorable terms, or at all. Also, while we are pleased with our track record in re-bid situations, we cannot assure that we will prevail in any such future situations.

Internationally, the government in the United Kingdom has an active procurement for the private management of nine existing prison facilities which total approximately 6,000 beds. We began competition for these opportunities in the fourth quarter of 2011 and submitted our initial proposal on April 24, 2012. Contract awards are expected to be announced in fall of 2012. Also in the United Kingdom, in April 2012, the Ministry of Justice issued an invitation to negotiate for an electronic monitoring project which is expected to be awarded in January 2013. We believe there will be additional opportunities in the United Kingdom such as additional market testing of prisons, electronic monitoring of offenders and community corrections. We are exploring other opportunities in international markets and will continue to actively bid on any opportunities that fit our target profile for profitability and operational risk.



**Table of Contents**

With respect to our mental health, residential treatment, youth services, electronic monitoring services, and re-entry services business conducted through our GEO Care business segment, we are currently pursuing a number of business development opportunities. In connection with our merger with Cornell in August 2010 and our acquisition of BI in February 2011, we have significantly expanded GEO Care's operations by adding 37 facilities, 7 nonresidential service centers, and 35 Day Reporting Centers. We also expanded the service offerings of GEO Care by adding electronic monitoring services, community re-entry and immigration related supervision services. Through both organic growth and acquisitions, and subsequent to our acquisition of BI in February 2011, we have been able to grow GEO Care's business to approximately 6,500 beds and approximately 70,000 offenders under community supervision. Several states including Texas, Georgia, Louisiana, South Carolina, North Carolina, Pennsylvania, Virginia and others have indicated a desire to privatize one or more state psychiatric hospitals. We are currently competing on formal procurements for state psychiatric hospitals and/or residential treatment facilities in the states of Texas, North Carolina, and Virginia. Relative to opportunities for community-based re-entry centers, we expect to compete for several formal solicitations from the BOP for re-entry centers across the country and are also working with our existing local and state correctional clients to leverage new opportunities for both residential facilities as well as non-residential day reporting centers. 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 contracts to provide services to our governmental clients. Labor and related cost represented 61.4% of our operating expenses in First Half 2012. Additional significant operating expenses include food, utilities and inmate medical costs. In First Half 2012, operating expenses totaled 75.4% of our consolidated revenues. Our operating expenses as a percentage of revenue in 2012 will be impacted by the opening of any new or existing facilities as a result of the cost of transitioning and/or start-up operations related to a facility opening. During 2012, we will incur carrying costs for facilities that are either currently vacant or are expected to become vacant in 2012. The carrying costs associated with the approximately 7,000 beds we are currently marketing are expected to be \$14.8 million, including depreciation of \$7.6 million. We will also experience increases as a result of the amortization of intangible assets acquired in connection with our acquisition of BI. In addition to these factors, we expect to experience overall increases in operating expenses in 2012 as a result of a full year of BI's operations. As of July 1, 2012, our worldwide operations include the management and/or ownership of approximately 75,000 beds at 109 correctional, detention and residential treatment, youth services and community-based facilities including idle facilities and projects under development and also include the provision of monitoring of approximately 70,000 offenders in a community-based environment on behalf of approximately 900 federal, state and local correctional agencies located in all 50 states.

*General and Administrative Expenses*

General and administrative expenses consist primarily of corporate management salaries and benefits, professional fees and other administrative expenses. In First Half 2012, general and administrative expenses totaled 6.7% of our consolidated revenues. We expect general and administrative expenses as a percentage of revenue in 2012 to decrease as a result of cost savings initiatives and decreases in nonrecurring integration costs related to our acquisitions of Cornell and BI. During 2011, we incurred approximately \$6.4 million in nonrecurring integration costs. We expect business development costs to remain consistent 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 from time to time on the evaluation of potential acquisition targets.

**ITEM 3. 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 Senior Credit Facility of \$767.6 million and \$56.5 million in outstanding letters of credit, as of July 1, 2012, for every one percent increase in the average interest rate applicable to the Senior Credit Facility, our total annual interest expense would increase by \$7.7 million.

As of July 1, 2012, we had four interest rate swap agreements in the aggregate notional amount of \$100.0 million. These interest rate swaps, which have payment, expiration dates and call provisions that mirror the terms of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes, effectively convert \$100.0 million of the 7<sup>3</sup>/<sub>4</sub>% Senior Notes into variable rate obligations. Under these interest rate swaps, we



---

**Table of Contents**

receive a fixed interest rate payment from the financial counterparties to the agreements equal to  $7\frac{3}{4}\%$  per year calculated on the notional \$100.0 million amount, while we make a variable interest rate payment to the same counterparties equal to the three-month LIBOR plus a fixed margin of between 4.16% and 4.29%, also calculated on the notional \$100.0 million amount. For every one percent increase in the interest rate applicable to our aggregate notional \$100.0 million of swap agreements relative to the  $7\frac{3}{4}\%$  Senior Notes, our annual interest expense would increase by \$1.0 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 also exposed to market risks related to fluctuations in foreign currency exchange rates between the U.S. dollar, the Australian dollar, the Canadian dollar, the South African Rand and the British Pound currency exchange rates. Based upon our foreign currency exchange rate exposure at July 1, 2012, every 10 percent change in historical currency rates would have approximately a \$6.4 million effect on our financial position and approximately a \$0.7 million impact on our results of operations during First Half 2012.

**ITEM 4. CONTROLS AND PROCEDURES.****(a) Evaluation of 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 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.

**(b) Changes in Internal Control Over Financial Reporting.**

Our management is responsible to report 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. 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.





**Table of Contents**

**PART II - OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS.**

The information required herein is incorporated by reference from Note 11 - Commitments and Contingencies in the Notes to the Unaudited Consolidated Financial Statements included in Part I of this Quarterly Report on Form 10-Q.

**ITEM 1A. RISK FACTORS.**

Item 1A of Part I of our Annual Report on Form 10-K for the year ended January 1, 2012, includes a detailed discussion of the risk factors that could materially affect our business, financial condition or future prospects.

**ITEM 2. UNREGISTERED SALES OF SECURITIES AND USE OF PROCEEDS.**

Not applicable.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

Not applicable.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION.**

Not Applicable

**ITEM 6. EXHIBITS.**

(A) Exhibits

|         |   |
|---------|---|
| 10.41   | The GEO Group, Inc. 2011 Employee Stock Purchase Plan (1) |
| 31.1    | SECTION 302 CEO Certification.                            |
| 31.2    | SECTION 302 CFO Certification.                            |
| 32.1    | SECTION 906 CEO Certification.                            |
| 32.2    | SECTION 906 CFO Certification.                            |
| 101.INS | XBRL Instance Document                                    |
| 101.SCH | XBRL Taxonomy Extension Schema                            |

## Edgar Filing: GEO GROUP INC - Form 10-Q

|         |   |
|---------|---|
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase  |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase   |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase        |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

(1) Incorporated herein by reference from the Company's Form S-8, filed on May 4, 2012.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: August 8, 2012

THE GEO GROUP, INC.

/s/ Brian R. Evans

Brian R. Evans

Senior Vice President & Chief Financial Officer

(duly authorized officer and principal financial officer)