



The GEO Group, Inc.

WORLD HEADQUARTERS
One Park Place . 621 NW 53rd Street . Suite 700
Boca Raton . Florida 33487 USA
561.893.0101 866.301.4436
www.thegeogroupinc.com

THE GEO GROUP, INC. 2005 ANNUAL REPORT



The GEO Group, Inc.

2005 ANNUAL REPORT

"2005 presented our company with a number of unique opportunities

as well as a handful of unforeseen challenges. We were fortunate to

apply the innovative skills of our employees and the strengths of our

regional operating structure to overcome these challenges and

position the Company for strong growth in 2006."

George C. Zoley
Chairman and Chief Executive Officer
The GEO Group, Inc.

COMPANY PROFILE

The GEO Group, Inc. is a world leader in the delivery of correctional, detention, mental health and residential treatment services to government agencies around the globe. Through its team of approximately 11,000 professionals, The GEO Group develops and implements tailored business solutions that meet the needs of government customers throughout the world.

The GEO Group provides innovative, turnkey programs for the design, construction, financing and management of state-of-the-art correctional and detention centers, including those focused on education, substance abuse treatment, counseling, work programs and community corrections services. In addition, The GEO Group designs, constructs, finances and manages long-term care, mental health and residential treatment facilities that provide comprehensive services to residents in partnership with state and local government agencies.

The GEO Group currently provides services in the United States, Canada, Australia, South Africa, and the United Kingdom, and its worldwide operations include 61 facilities with a total design capacity of more than 49,000 beds. The GEO Group holds a global market share of 28 percent.

The GEO Group is listed on the New York Stock Exchange under the symbol GGI. For more information on The GEO Group, please visit the Company's web site at www.thegeogroupinc.com.

SHAREHOLDER INFORMATION

REGIONAL OFFICES

Eastern Region, USA

Gregory Skeens, Vice President
7111 Fairway Drive, Suite 202
Palm Beach Gardens, Florida 33418
Phone: 561-630-3400
Fax: 561-630-3416

Central Region, USA

Donald Houston, Vice President
1583 Common Street, Suite 213
New Braunfels, Texas 78130
Phone: 830-625-9000
Fax: 830-626-0108

Western Region, USA

Ed Brown, Vice President
5963 La Place Court, Suite 105
Carlsbad, California 92008
Phone: 760-930-9500
Fax: 760-930-9550

INTERNATIONAL OFFICES

The GEO Group UK Ltd

Walter MacGowan, Managing Director
Regus House, 400 Thames Valley Park Drive
Thames Valley Park, Reading RG6 1PT
United Kingdom
Phone: 44-118-963-7684
Fax: 44-118-963-7685

The GEO Group Australia Pty Ltd.

Pieter Bezuidenhout, Managing Director
Level 18, 44 Market Street
Sydney, New South Wales 2000, Australia
Phone: 61-2-9262-6100
Fax: 61-2-9262-6005

South African Custodial Services

Stephen Korabie, Managing Director
Oak Place, Woodmead Office Park
Western Service Road
Woodmead, Sandton, South Africa 2126
Phone: 27-11-802-4440
Fax: 27-11-802-4491

Other Officers

Sal A. Barbera
Vice President, Mental Health Operations
GEO Care, Inc.

Thomas F. Boyer
Vice President, Risk Management

Louis V. Carrillo
Vice President, Corporate Counsel
and Assistant Secretary

Ronald D. Champion
Vice President, International Services

Mathew J. DenAdel
Vice President, Pricing

Brian R. Evans
Vice President, Accounting
and Chief Accounting Officer

Dale W. Frick
Vice President, Project Development and
Client Relations, GEO Care, Inc.

Lauren B. Kroger
Vice President, Correctional Health Services

Charles F. Lister
Vice President, Security Operations, GEO Care, Inc.

Ron G. Maddux
Vice President, Project Development

Marcel Maier
Vice President, Tax

Amber D. Martin
Vice President, Contracts

Philip D. Mosciski
Vice President, Design Development

David A. Mustain
Vice President, Office of Professional Responsibility

James H. Reynolds
Vice President, Human Resources

Neil E. Schwartzman
Vice President and Chief Information Officer

Cloid L. Shuler
Vice President, Business Development

Gary W. Templeton
Vice President, Programs

Carlos A. Valdes-Fauli
Vice President, Design Services

David N.T. Watson
Vice President, Finance and Treasurer

Robert D. White
Vice President, Administration

CORPORATE AND SHAREHOLDER INFORMATION

Corporate and shareholder information, as well as a copy of the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, may be obtained free of charge by contacting Pablo E. Paez, Director, Corporate Relations at The GEO Group, Inc., One Park Place, 621 NW 53rd Street, Suite 700, Boca Raton, Florida 33487 or by visiting the Company's website at www.thegeogroupinc.com.

Auditors

Ernst & Young LLP
Phillips Point West Tower, Suite 1200
777 South Flagler Drive
West Palm Beach, FL 33401

Corporate Counsel

Akerman, Senterfitt & Eidson, P.A.
One Southeast Third Avenue, 28th Floor
Miami, FL 33131-1714

Transfer Agent and Registrar

Mellon Investor Services, LLC
Newport Office Center VII
480 Washington Boulevard
Jersey City, New Jersey 07310
866-210-7619
www.melloninvestor.com/isd

Notice of Annual Meeting

The Annual Shareholder Meeting for The GEO Group, Inc. will be held at the Boca Raton Resort & Club, 501 E. Camino Real, Boca Raton, Florida 33432-6127 at 9:00 a.m. on May 4, 2006.

Officer Certification

The certifications of The GEO Group, Inc.'s Chief Executive Officer and Chief Financial Officer, required under section 302 of the Sarbanes-Oxley Act of 2002, have been filed as exhibits to The GEO Group, Inc.'s Annual Report on Form 10-K. In 2005, The GEO Group, Inc.'s Chief Executive Officer submitted the annual certification to the New York Stock Exchange regarding The GEO Group, Inc.'s compliance with the New York Stock Exchange corporate governance listing standards.

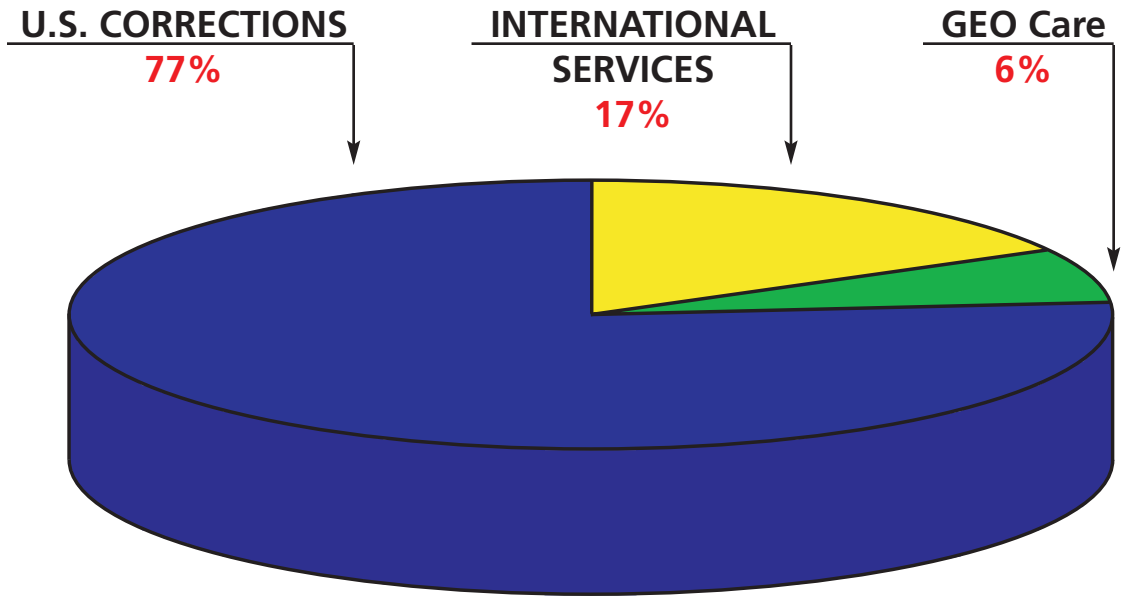
Forward-Looking Statements Safe Harbor

This report and the documents incorporated by reference herein contain "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. "Forward-looking" statements are any statements that are not based on historical information. Statements other than statements of historical facts

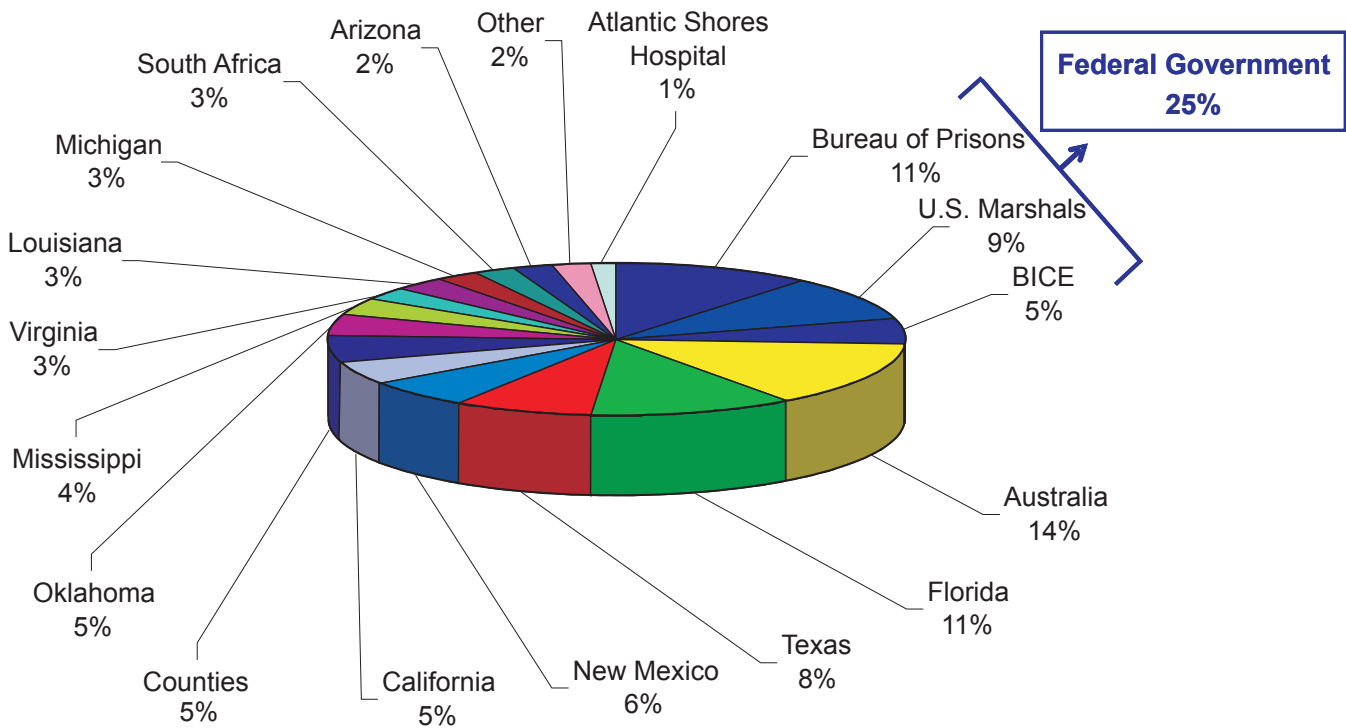
included in this report, including, without limitation, statements regarding our future financial position, business strategy, budgets, projected costs and plans and objectives of management for future operations, are "forward-looking" statements. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may," "will," "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate" or "continue" or the negative of such words or variations of such words and similar expressions. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements and we can give no assurance that such forward-looking statements will prove to be correct. Important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, or "cautionary statements," include, but are not limited to: (1) 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; (2) the instability of foreign exchange rates, exposing us to currency risks in Australia and South Africa, or other countries in which we may choose to conduct our business; (3) our ability to reactivate the Michigan Youth Correctional Facility; (4) an increase in unreimbursed labor rates; (5) our ability to expand and diversify our correctional and mental health residential treatment services; (6) our ability to win management contracts for which we have submitted proposals and to retain existing management contracts; (7) our ability to raise new project development capital given the often short-term nature of the customers' commitment to use newly developed facilities; (8) our ability to reactivate our Jena, Louisiana facility, or to sublease or coordinate the sale of the facility with the owner of the property, CentraCore Properties Trust, or CPV; (9) our ability to accurately project the size and growth of the domestic and international privatized corrections industry; (10) our ability to grow our mental health residential treatment services industry; (11) our ability to estimate the government's level of dependency on privatized correctional services; (12) our ability to develop long-term earnings visibility; (13) our ability to obtain future financing at competitive rates; (14) our exposure to rising general insurance costs; (15) our exposure to claims for which we are uninsured; (16) our exposure to rising inmate medical costs; (17) our ability to maintain occupancy rates at our facilities; (18) our ability to manage costs and expenses relating to ongoing litigation arising from our operations; (19) our ability to accurately estimate on an annual basis, loss reserves related to general liability, workers compensation and automobile liability claims; (20) our ability to identify suitable acquisitions, and to successfully complete and integrate such acquisitions on satisfactory terms; (21) the ability of our government customers to secure budgetary appropriations to fund their payment obligations to us; and (22) other factors contained in our filings with the Securities and Exchange Commission, or the SEC, including, but not limited to, those detailed in our annual report on Form 10-K, our Form 10-Qs and our Form 8-Ks filed with the SEC.

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

2005 REVENUE DISTRIBUTION BY BUSINESS UNIT



2005 REVENUE DISTRIBUTION BY CUSTOMER



To Our Shareholders:



*George C. Zoley
Chairman of the Board
Chief Executive Officer*

George C. Zoley
Chairman of the Board and
Chief Executive Officer

In many ways, 2005 was unique for our Company. Although we were faced with a handful of unforeseen challenges which negatively impacted our financial performance, we also experienced tremendous success in new business development and a successful acquisition that positioned our Company for a very positive 2006.

The first challenge came at the beginning of the first quarter when we began experiencing a lower than expected population census at our 700-bed Western Region Detention Facility in San Diego, California, which houses United States Marshals detainees. These lower population levels at the facility negatively impacted our financial performance throughout the entire year. We resolved the situation with the signing, in early 2006, of a new 10-year contract with a minimum population guarantee that eliminates our occupancy risk at the facility.

Second, we received notice that the contract for the housing of immigration detainees at our 220-bed Queens Detention Facility in New York would not be renewed by the Bureau of Immigration and Customs Enforcement. We quickly focused our efforts on finding an alternative use for the facility and were successful in transferring the contract to the Office of the Federal Detention Trustee on June 30, 2005. This allowed the United States Marshals Service to use the facility for the housing of low-security pre-trial detainees.

Our third challenge involved our employee health insurance program which experienced adverse claims development that resulted in unanticipated cost overruns during 2005. We addressed this situation by restructuring our corporate health insurance program, effective November 1, 2005, to better reflect our actual costs while maintaining the same level of quality health care coverage being provided to our employees.

Our fourth challenge came in the latter part of the year with the closure of our 500-bed Michigan Youth Correctional Facility by the Governor of the State of Michigan. While we believe that our lease contract was wrongfully terminated, we decided to take a \$21.0 million, non-cash impairment charge in the fourth quarter of the year to better reflect the book value of the facility, which now gives us the ability to market these immediately-available adult correctional beds to federal, state, and local government agencies around the country. We also decided to take a simultaneous charge of \$4.3 million to fully reserve the balance of our lease payment obligations for the 300-bed Jena, Louisiana Facility, which has been vacant for several years.

Despite these extraordinary challenges, we had a remarkable year in the area of business development with important contract awards for new correctional and residential treatment projects. Our U.S. Corrections business unit was awarded a contract by the State of Indiana Department of Correction for the management of the 2,416-bed New Castle Correctional Facility, which we transitioned into our operations on January 2, 2006. This contract award was followed by an award from the State of Florida Department of Management Services for the design, construction, financing, and operation of a new 1,500-bed adult male correctional



*Wayne H. Calabrese
Vice Chairman of the Board
President and Chief Operating Officer*

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

facility to be located in Graceville, Florida, which is expected to become operational by the fourth quarter of 2007.

Our residential treatment services subsidiary, GEO Care, also enjoyed a very successful year in the area of business development with contract awards for two new large-scale projects. The first contract award, from the State of Florida Department of Children and Families, entails the management of the 200-bed South Florida Evaluation and Treatment Center, a state forensic mental health hospital located in Miami, Florida, and the development of a new state-of-the-art replacement facility. The second contract award, from the State of New Mexico Department of Health, encompasses the management of the 230-bed Fort Bayard Medical Center, a long-term care facility located in Silver City, New Mexico, and the development of a modern replacement facility.

This growth momentum has continued into early 2006 with the recent signing of a contract by our United Kingdom subsidiary, The GEO Group UK Ltd, for the management of the 198-bed Campsfield House Immigration Removal Centre in Kidlington, England. This milestone project marks our official reentry into the UK private custodial market where we had a dominant business presence prior to the sale of our UK joint venture interest in July 2003.

Our organic business development efforts were complemented by the successful acquisition of Sarasota, Florida-based Correctional Services Corporation in November 2005. This acquisition, which achieves more than \$100 million in annual revenues, added 16 adult male correctional facilities totaling over 8,000 new beds to our operations, increasing our global market share of private correctional beds from 22 percent to 28 percent. We have been able to seamlessly transition these new facilities into our regional operating structure with only a few additional employees. Further, we signed a contract in early 2006 to house approximately 450 inmates from the State of Idaho at the 872-bed Newton County Correctional Center, a facility formerly managed by Correctional Services Corporation.

The remarkable organic growth we experienced in 2005, along with the successful integration of new facility contracts acquired through the purchase of Correctional Services Corporation, have positioned our company for significant growth in 2006 and beyond.

We currently have 4,583 new beds under development representing over \$84.0 million in annualized operating revenues. These projects are expected to be open between 2006 and late 2007. In addition, we are actively marketing approximately 3,300 immediately-available beds at a number of our facilities which would significantly enhance our financial performance.

This remarkable growth pipeline, unmatched in our industry, is based on our diversified strategy for future growth through our three business units: GEO U.S. Corrections, GEO International Services, and GEO Care Residential Treatment Services. We are hopeful of a very bright future through these efforts as well as the potential acquisition of additional companies in our core services and other related government service areas.



GEORGE C. ZOLEY
Chairman of the Board
Chief Executive Officer



JOHN G. O'ROURKE
Senior Vice President and
Chief Financial Officer



DONALD H. KEENS
Senior Vice President
International Services



JORGE A. DOMINICIS
Senior Vice President
Residential Treatment Services
President
GEO Care, Inc.



WAYNE H. CALABRESE
Vice Chairman of the Board
President and Chief Operating
Officer



JOHN J. BULFIN
Senior Vice President
General Counsel and Secretary



JOHN M. HURLEY
Senior Vice President
North American Services

SENIOR OFFICERS

BOARD OF DIRECTORS

George C. Zoley
Chairman and Chief Executive Officer
The GEO Group, Inc.

George C. Zoley serves as Chairman of the Board and Chief Executive Officer of The GEO Group, Inc. Mr. Zoley founded the Company in 1984 and continues to play a major role in the Company's worldwide operations and development of new business opportunities. Prior to founding the Company, Mr. Zoley served as manager, director, and then Vice President of Government Services at Wackenhut Services, Inc. Mr. Zoley received his Bachelor's and Master's Degrees in Public Administration from Florida Atlantic University and his Doctorate Degree in Public Administration from Nova Southeastern University.

Wayne H. Calabrese
Vice Chairman, President and
Chief Operating Officer
The GEO Group, Inc.

Wayne H. Calabrese serves as Vice Chairman of the Board, President and Chief Operating Officer of The GEO Group, Inc. Mr. Calabrese joined the Company as Vice President of Business Development in 1989 and has served in a range of increasingly senior operating positions since then. Prior to joining the Company, Mr. Calabrese was a partner in the Akron, Ohio law firm of Calabrese, Dobbins and Kepple. Mr. Calabrese received his Bachelor's Degree in Secondary Education from the University of Akron and his Juris Doctor from the University of Akron School of Law.

Norman A. Carlson
Former Director
Federal Bureau of Prisons

Norman A. Carlson has served as a Director of The GEO Group, Inc. since April 1994. Mr. Carlson retired from the Department of Justice in 1987 after serving as the Director of the Federal Bureau of Prisons for 17 years. During his 30-year career, Mr. Carlson worked at the United States Penitentiary, Leavenworth, Kansas, and at the Federal Correctional Institution, Ashland, Kentucky. Mr. Carlson was President of the American Correctional Association from 1978 to 1980. Mr. Carlson is a Fellow in the National Academy of Public Administration.



*The GEO Group's Board of Directors (from left to right):
Seated: Wayne H. Calabrese, George C. Zoley, Norman A. Carlson.
Standing: John M. Palms, Richard H. Glanton, Anne N. Foreman, John M. Perzel.*

Anne N. Foreman
Former Under Secretary
United States Air Force

Anne N. Foreman served as Under Secretary of the United States Air Force from September 1989 until January 1993. Ms. Foreman also served as General Counsel of the Department of the Air Force and as Associate Director of Presidential Personnel for National Security in the White House. Ms. Foreman earned a Bachelor's Degree, Magna Cum Laude, in History and French, and a Master's Degree in History from the University of Southern California. She received her Juris Doctor from American University and was awarded an Honorary Doctorate of Law from Troy State University.

Richard H. Glanton
Senior Vice President
Exelon Corporation

Richard H. Glanton serves as Senior Vice President of Exelon Corporation. Mr. Glanton had been a member of the Exelon Corporation Board of Directors since its inception in October 2002. Prior to joining Exelon Corporation, Mr. Glanton was a Partner in the General Corporate Group of the law firm of Reed, Smith, Shaw and McClay, LLP in Philadelphia, Pennsylvania. He received his Bachelor's Degree in English from West Georgia College (renamed State University of West Georgia) and his Juris Doctor from the University of Virginia School of Law.

John M. Palms, Ph.D.
President Emeritus
University of South Carolina

John M. Palms, Ph.D., is a Distinguished University Professor and President Emeritus at the University of South Carolina. Dr. Palms serves on the Board of Exelon Corporation and is currently the Chair of Exelon's Audit and Finance Committee. He was President at the University of South Carolina from 1991 to 2002 and President at Georgia State University from 1989 to 1991. Dr. Palms currently serves as Chairman of the Board of Trustees of the Institute for Defense Analyses and previously served in the U.S. Air Force with a Regular Commission and on the U.S. President's Selection Committee for White House Fellows.

John M. Perzel
Speaker
Pennsylvania House of Representatives

The Honorable John M. Perzel was sworn in as Pennsylvania's Speaker of the House of Representatives on April 15, 2003. Prior to being elected Speaker, Mr. Perzel served four consecutive terms as House Majority Leader. Before being elected Majority Leader in 1994, Mr. Perzel held the offices of Republican Whip, Policy Committee Chairman, and head of the House Republican Campaign Committee. Mr. Perzel was first elected to the Pennsylvania House of Representatives in 1978. Mr. Perzel earned a Bachelor's Degree from Troy State University in 1975.

ACQUISITION OF CORRECTIONAL SERVICES CORPORATION

The acquisition of Correctional Services Corporation added 16 adult correctional facilities and 8,000 correctional and detention beds to The GEO Group's North American operations, increasing the Company's private correctional bed global market share from 22 percent to 28 percent.

EXECUTING GEO'S ACQUISITION STRATEGY

During its 22 year history, The GEO Group grew from a small subsidiary to a multi-national leading provider of correctional and residential treatment services on a purely organic basis. Until July 2003, The GEO Group was constrained in its ability to access the capital markets and to pursue an effective acquisition strategy due to the presence of a majority shareholder. With the repurchase of 12 million shares of its common stock from its former majority shareholder on July 9, 2003, The GEO Group became an independent company and gained the ability to effectively access the capital markets and actively pursue accretive acquisition opportunities.

After more than two years of a diligent and disciplined pursuit of acquisition opportunities, The GEO Group successfully completed the acquisition of Sarasota, Florida-based Correctional Services Corporation on November 4, 2005. The GEO Group acquired Correctional Services Corporation for approximately \$62.0 million, or \$6.00 per common share. Simultaneous to the acquisition, The GEO Group sold the juvenile services business of Correctional Services Corporation for \$3.75 million.

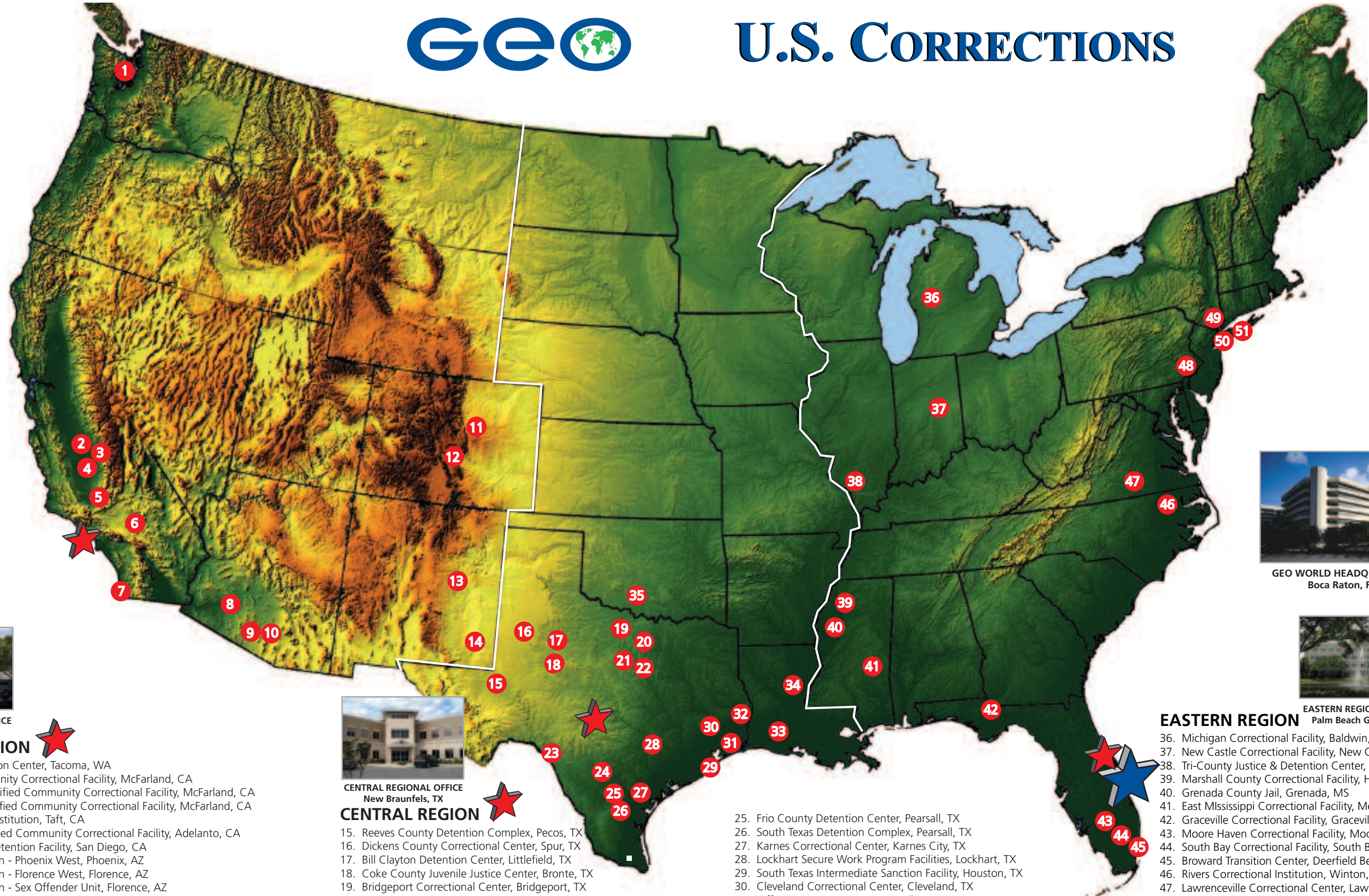
The acquisition of Correctional Services Corporation added 16 adult male correctional facilities totaling approximately 8,000 beds to The GEO Group's North American operations. These facilities generate more than \$100.0 million in annual revenues and are located in six states and represent local, state and federal customers, including the Bureau of Immigration and Customs Enforcement and the United States Marshals Service. Following the acquisition, The GEO Group's private correctional bed global market share increased from 22 percent to 28 percent.

The GEO Group will continue to pursue accretive acquisition opportunities in a diligent and disciplined fashion in the Company's core services of corrections and residential treatment as well as in other related government service areas.





U.S. CORRECTIONS



WESTERN REGIONAL OFFICE
Carlsbad, CA

WESTERN REGION

1. Northwest Detention Center, Tacoma, WA
2. McFarland Community Correctional Facility, McFarland, CA
3. Central Valley Modified Community Correctional Facility, McFarland, CA
4. Golden State Modified Community Correctional Facility, McFarland, CA
5. Taft Correctional Institution, Taft, CA
6. Desert View Modified Community Correctional Facility, Adelanto, CA
7. Western Region Detention Facility, San Diego, CA
8. Arizona State Prison - Phoenix West, Phoenix, AZ
9. Arizona State Prison - Florence West, Florence, AZ
10. Arizona State Prison - Sex Offender Unit, Florence, AZ
11. Aurora ICE Processing Center, Aurora, CO
12. Pre-Parole & Parole Revocation Center, Pueblo, CO
13. Guadalupe County Correctional Facility, Santa Rosa, NM
14. Lea County Correctional Facility, Hobbs, NM



CENTRAL REGIONAL OFFICE
New Braunfels, TX

CENTRAL REGION

15. Reeves County Detention Complex, Pecos, TX
16. Dickens County Correctional Center, Spur, TX
17. Bill Clayton Detention Center, Littlefield, TX
18. Coke County Juvenile Justice Center, Bronte, TX
19. Bridgeport Correctional Center, Bridgeport, TX
20. North Texas Intermediate Sanction Facility, Fort Worth, TX
21. Fort Worth Community Corrections Facility, Fort Worth, TX
22. Sanders Estes Unit, Venus, TX
23. Val Verde Correctional Facility, Del Rio, TX
24. Central Texas Detention Facility, San Antonio, TX



GEO WORLD HEADQUARTERS
Boca Raton, FL



EASTERN REGIONAL OFFICE
Palm Beach Gardens, FL

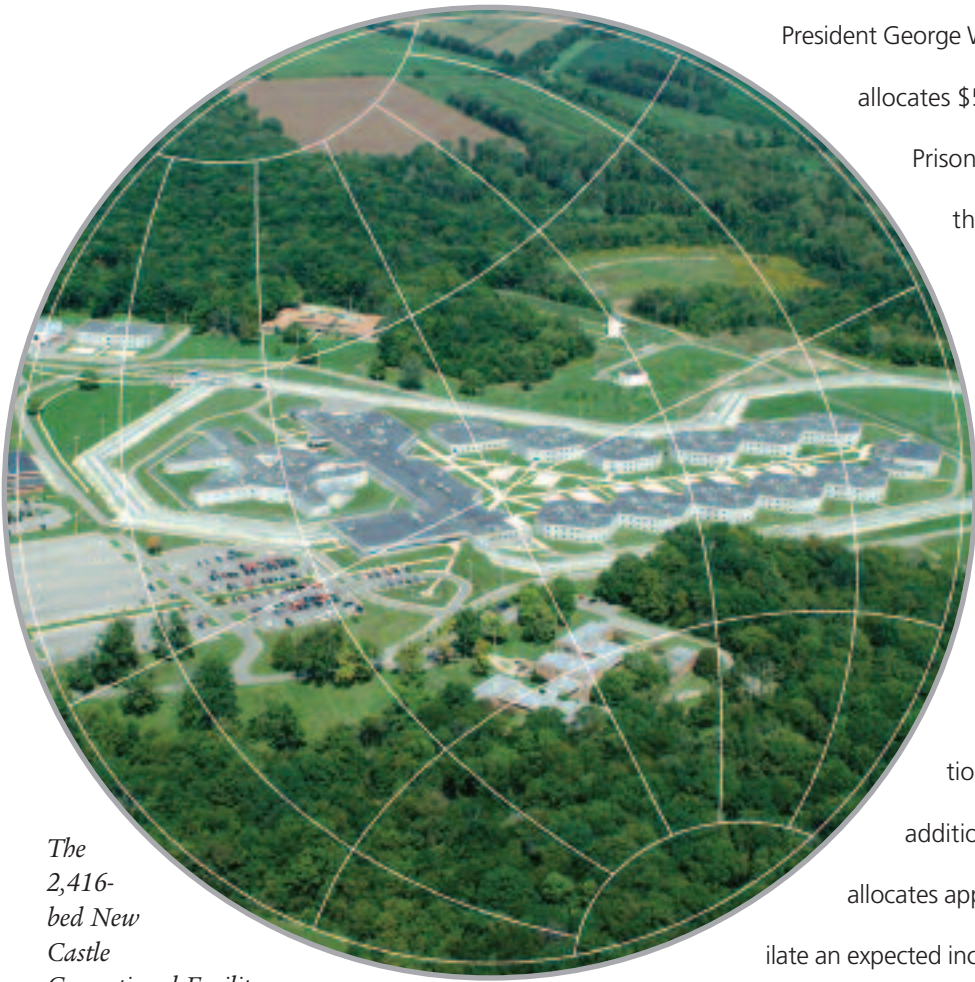
EASTERN REGION

36. Michigan Correctional Facility, Baldwin, MI
37. New Castle Correctional Facility, New Castle, IN
38. Tri-County Justice & Detention Center, Ullin, IL
39. Marshall County Correctional Facility, Holly Springs, MS
40. Grenada County Jail, Grenada, MS
41. East Mississippi Correctional Facility, Meridian, MS
42. Graceville Correctional Facility, Graceville, FL
43. Moore Haven Correctional Facility, Moore Haven, FL
44. South Bay Correctional Facility, South Bay, FL
45. Broward Transition Center, Deerfield Beach, FL
46. Rivers Correctional Institution, Winton, NC
47. Lawrenceville Correctional Center, Lawrenceville, VA
48. George W. Hill Correctional Facility, Thornton, PA
49. Brooklyn Community Correctional Center, Brooklyn, NY
50. Bronx Community Correctional Center, Bronx, NY
51. Queens Private Correctional Facility, Jamaica, NY
52. Migrant Operations Center, Guantanamo Bay, Cuba (not shown)

GEO U.S. CORRECTIONS

STRONG INDUSTRY FUNDAMENTALS SPELL CONTINUOUS GROWTH

Ongoing efforts by the United States Department of Homeland Security to secure the nation's borders and capture and detain illegal aliens in conjunction with a rapidly growing federal inmate population have resulted in increased demand for cost-efficient detention beds by the Office of the Federal Detention Trustee and the three major federal correctional/detention agencies in the United States: the Federal Bureau of Prisons, the Bureau of Immigration and Customs Enforcement, and the United States Marshals Service.

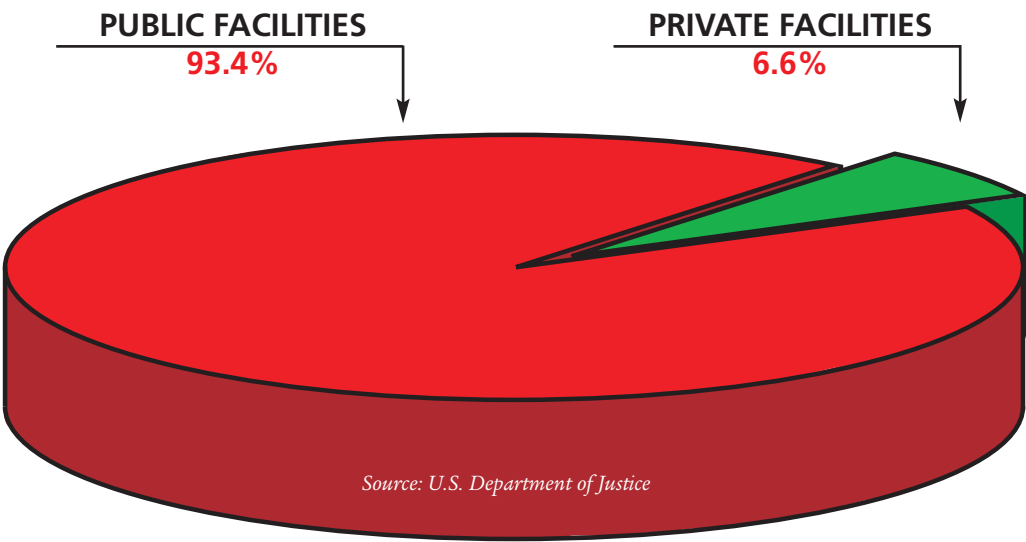


The 2,416-bed New Castle Correctional Facility in New Castle, Indiana, is the first contracted state prison operation in Indiana.

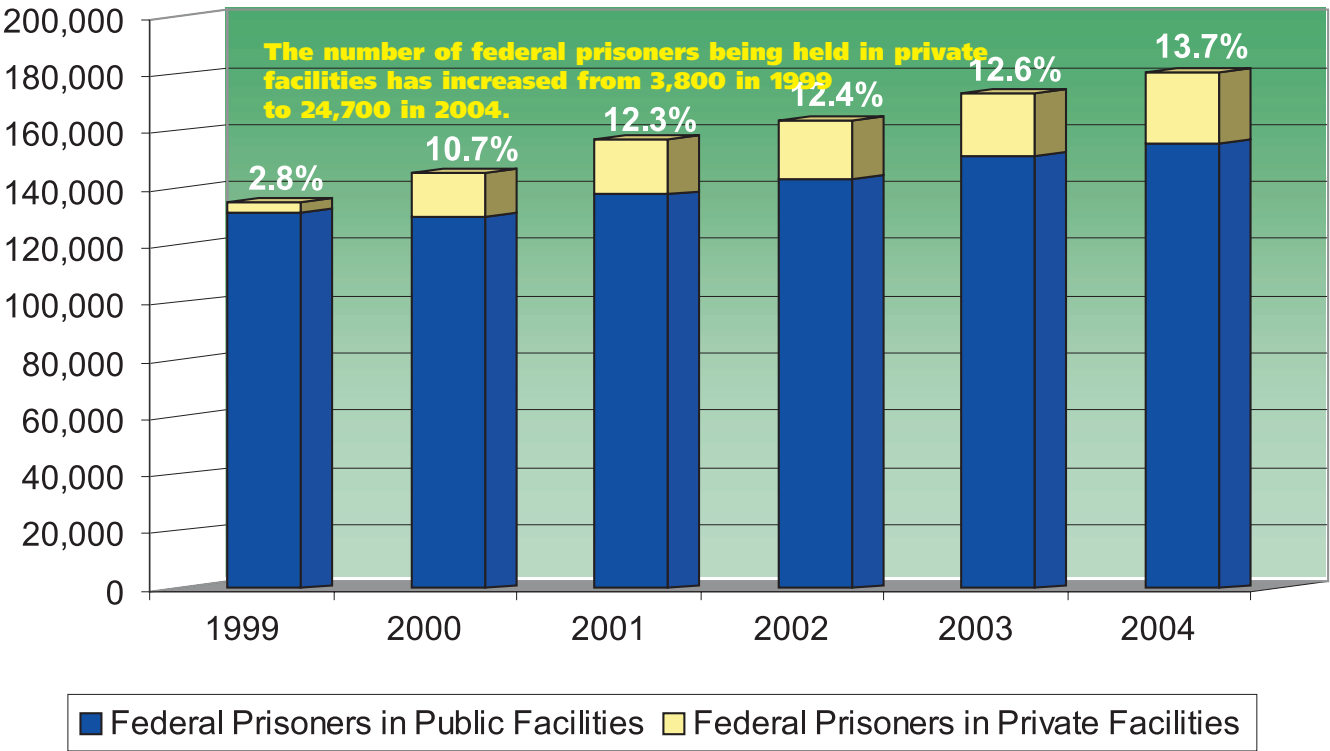
President George W. Bush's proposed budget for 2007 allocates \$5.0 billion for the Federal Bureau of Prisons and \$1.3 billion for the Office of the Federal Detention Trustee to ensure the safe detention and incarceration of a growing federal prisoner population. The President's proposed budget provides approximately \$447.0 million under the Secure Border Initiative for 6,700 new immigration detention beds as well as new immigration detention officers and agents. In addition, the President's proposed budget allocates approximately \$140.0 million to assimilate an expected increase of over 9,500 detainees under the custody of the United States Marshals Service.

MARKET POTENTIAL - CORRECTIONS

OF THE 1.5 MILLION STATE AND FEDERAL INMATES IN THE U.S., ONLY APPROXIMATELY 99,000, OR 6.6 PERCENT, ARE HELD IN PRIVATE FACILITIES.



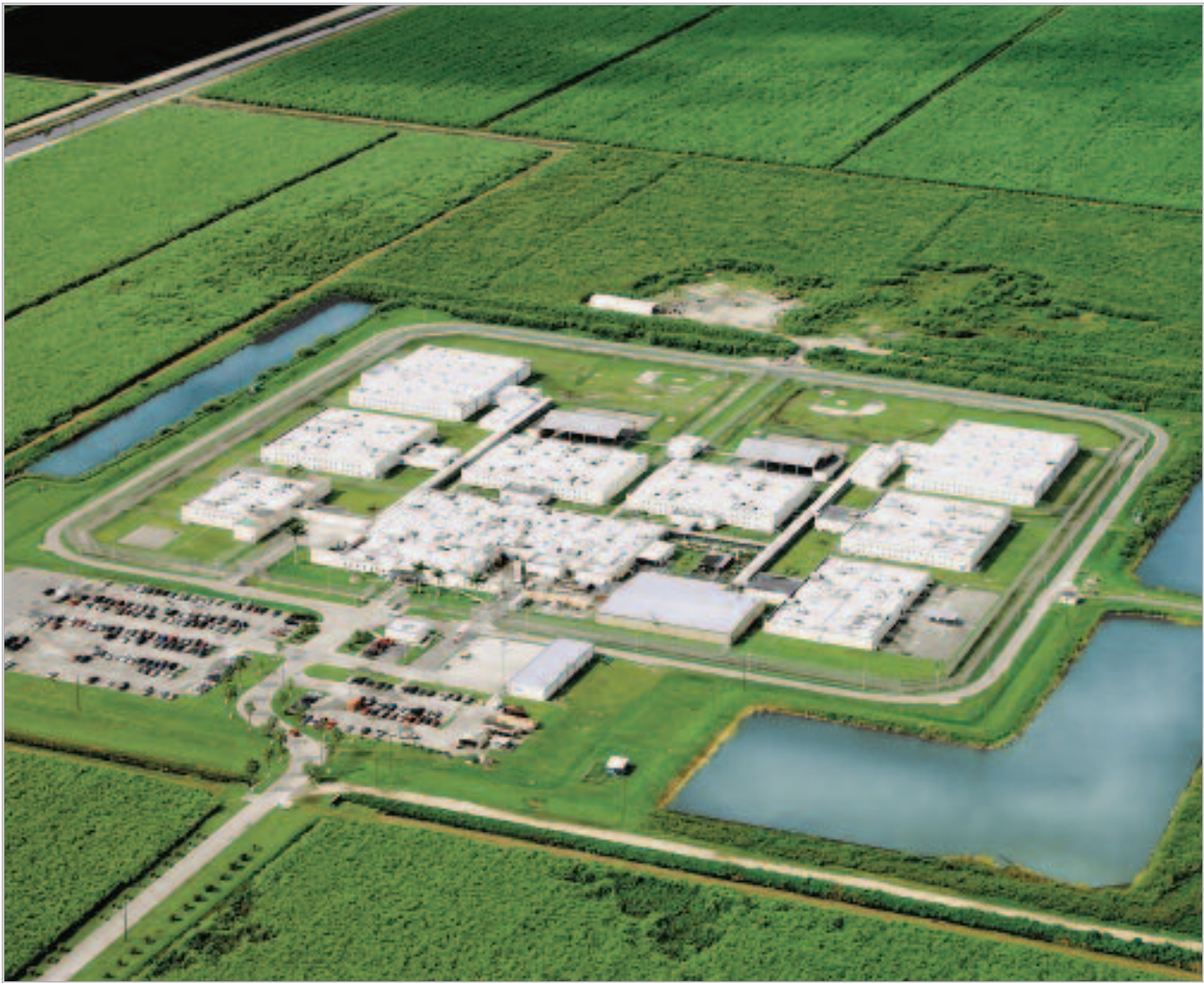
FEDERAL PRISONER POPULATION GROWTH



With 22 years of experience and a strong regional operating structure, The GEO Group is well positioned to capitalize on strong industry trends and to continue to strengthen its partnerships with federal, state and local government agencies across the country.

At the state level, overcrowding conditions and shrinking budgets continue to affect correctional systems across the country. Fifty-eight percent of the more than 2.2 million individuals incarcerated in the U.S. at year-end 2004 were held in state prisons, with the private sector housing approximately six percent of them. At the end of 2004, 24 states were operating at or above their highest detention capacity. As prison overcrowding continues to escalate, state jurisdictions throughout the U.S. are increasingly exploring partnerships with private service providers as a cost-effective alternative to the growth of their public payrolls.

The GEO Group, Inc. currently provides correctional and detention management services for 12 state customers as well as the Office of the Federal Detention Trustee and the three major federal correctional/detention agencies (the Federal Bureau of Prisons, the Bureau of Immigration and Customs Enforcement, and the United States Marshals Service). Following the acquisition of Correctional Services Corporation, The GEO Group now has contracts and awards to manage 50 domestic correctional and detention facilities totaling approximately 42,000 beds across 16 states. With 22 years of experience and a strong operating structure, The GEO Group is well positioned to capitalize on strong industry trends and to continue to strengthen its partnerships with federal, state and local government agencies across the country.



The South Bay Correctional Facility (photo top right) is a 1,861-bed adult male, medium/close custody facility. GEO has been under contract with the Florida Department of Management Services since February 3, 1997. It is one of GEO's many design/ build/finance/operate projects.

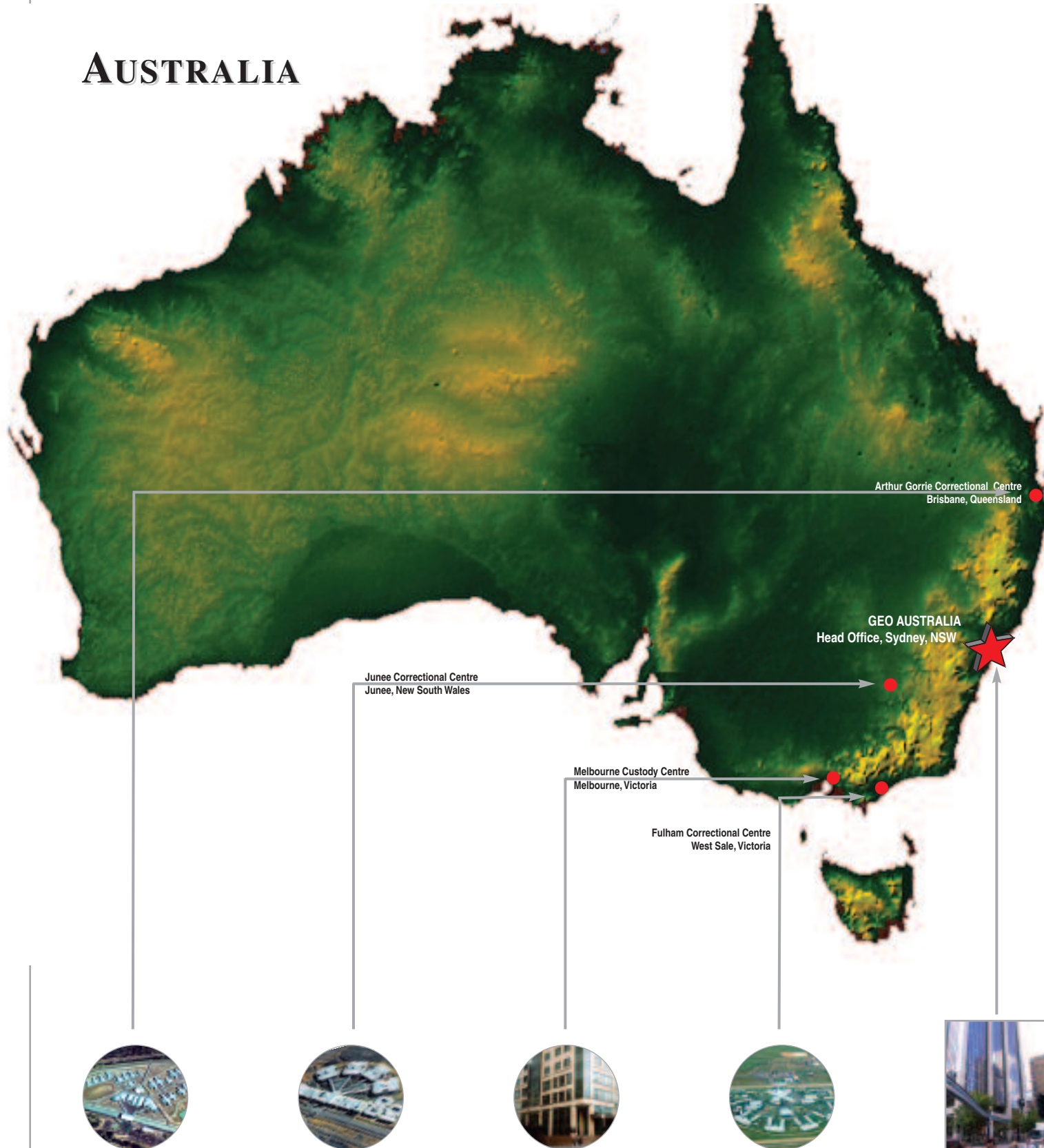
The 3,064-bed Reeves County Detention Complex (RCDC), located in Pecos, Texas (photo bottom left) is divided into three building units and houses adult male detainees for the Federal Bureau of Prisons and inmates for the Arizona Department of Corrections.

The 1,200-bed Rivers Correctional Institution in Winton, North Carolina (photo bottom right) provides services for the Federal Bureau of Prisons. The facility, designed and constructed by GEO, was completed in 365 days.



GEO INTERNATIONAL SERVICES

AUSTRALIA



UNITED KINGDOM



AFRICA



GEO INTERNATIONAL SERVICES

REENTERING AN IMPORTANT INTERNATIONAL MARKET

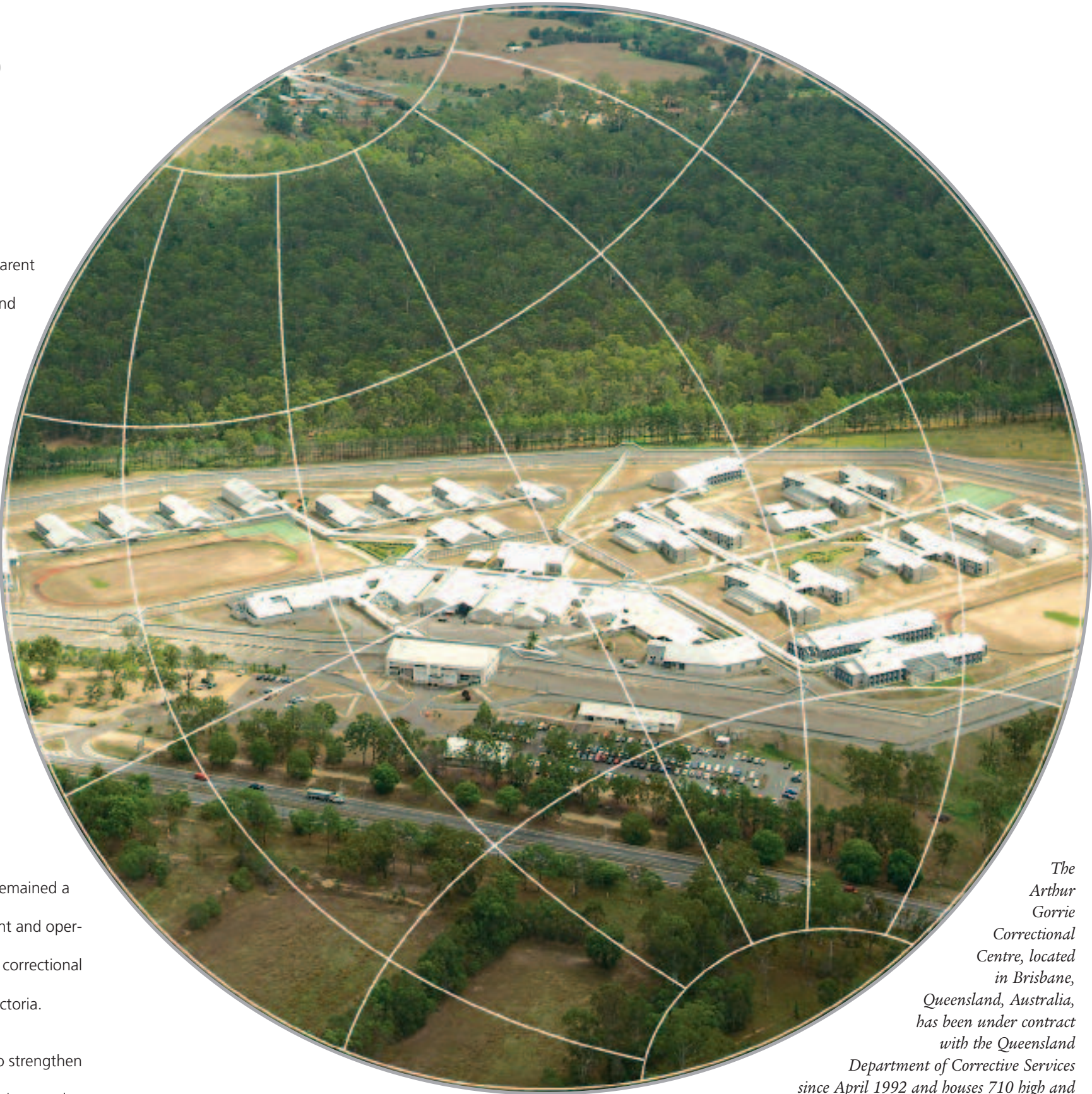
Prior to the July 2003 forced sale of its U.K. joint venture interest resulting from a change in control of its parent company, The GEO Group had a strong business presence in the United Kingdom, which represents the second largest private correctional market in the world. England, Scotland and Wales present significant new business opportunities for private correctional providers given the stated goal of the U.K. government to consider public-private partnerships for the construction and operation of all new correctional and detention facilities. In addition to the significant upside in the U.K. private correctional market, other countries in continental Europe are also exploring the potential privatization of different correctional/detention functions. In order to vigorously pursue new business opportunities in the United Kingdom and throughout Europe, The GEO Group established a wholly-owned subsidiary in the United Kingdom, The GEO Group U.K., in 2004.

The GEO Group's efforts to reestablish its once dominant business presence in the United Kingdom paid off in early 2006 when The GEO Group U.K. signed a contract for the management and operation of the 198-bed Campsfield House Immigration Removal Centre located in Kidlington, England. This milestone project marks The GEO Group's official reentry into this very important international market.

DELIVERING QUALITY SERVICES IN AUSTRALIA

Through the operations of its wholly-owned subsidiary, The GEO Group Australia Pty. Ltd., The GEO Group has remained a dominant business force in the Australian private correctional market for over a decade. Through the management and operation of three major correctional centers and one police custody center, The GEO Group Australia delivers quality correctional and detention services for the three largest state jurisdictions in Australia: New South Wales, Queensland, and Victoria.

The GEO Group's public-private partnerships with government entities in this important continent will continue to strengthen as correctional and detention government agencies in the region search for cost-effective solutions to their ongoing needs.



The Arthur Gorrie Correctional Centre, located in Brisbane, Queensland, Australia, has been under contract with the Queensland Department of Corrective Services since April 1992 and houses 710 high and maximum security male inmates.

The GEO Group, Inc. is the only publicly traded U.S. correctional company with overseas operations in the countries of Australia, South Africa, Canada, and the United Kingdom. As a proven international service provider, The GEO Group is well positioned to take advantage of new business opportunities in existing and emerging international private correctional markets.

SETTING NEW STANDARDS ON THE AFRICAN CONTINENT

In the Republic of South Africa, The GEO Group's subsidiary, South African Custodial Management (SACM), has established a remarkable public-private partnership with the Department of Correctional Services. Through its management of the 3,024-bed Kutama Sinthumule Correctional Centre, SACM has set a new standard for correctional services in South Africa, achieving ISO 9001:2000 certification in 2003 for the first time for a prison on the African continent. SACM has received several governmental and business accolades for the quality of services delivered over the past five years, including a Platinum Award for the Annual Logistics Achiever of the Year in 2004. This successful public-private partnership has placed The GEO Group and SACM in a remarkable position to strengthen their partnership with South Africa's Department of Correctional Services as new public-private partnerships are explored to alleviate the country's growing demand for correctional bed space.

The GEO Group will continue to rely on the expertise and know-how of its subsidiaries and joint ventures around the globe as it pursues new business opportunities in existing and emerging international private correctional markets.



The Kutama Sinthumule Correctional Centre (photo top right) in Louis Trichardt, Northern Province, South Africa, is a 3,024-bed maximum security prison for adult males. The South African consortium of The GEO Group and South African Custodial Services (SACS) were awarded a 25 year contract by the government.

The Junee Correctional Centre (photo bottom left) houses adult male and female inmates in New South Wales (NSW), Australia. The centre is the only privately run jail in the NSW network of 30 correctional facilities. GEO has managed the facility since its opening in 1993.

The United Kingdom Home Office, Immigration and Nationality Directorate, awarded GEO UK a contract for the total detention management of the 198-bed Campsfield House Immigration Removal Centre in Kidlington, Oxfordshire. GEO will assume operations on May 29, 2006.



GEO CARE RESIDENTIAL TREATMENT

SETTING HIGHER STANDARDS IN MENTAL HEALTH SERVICES

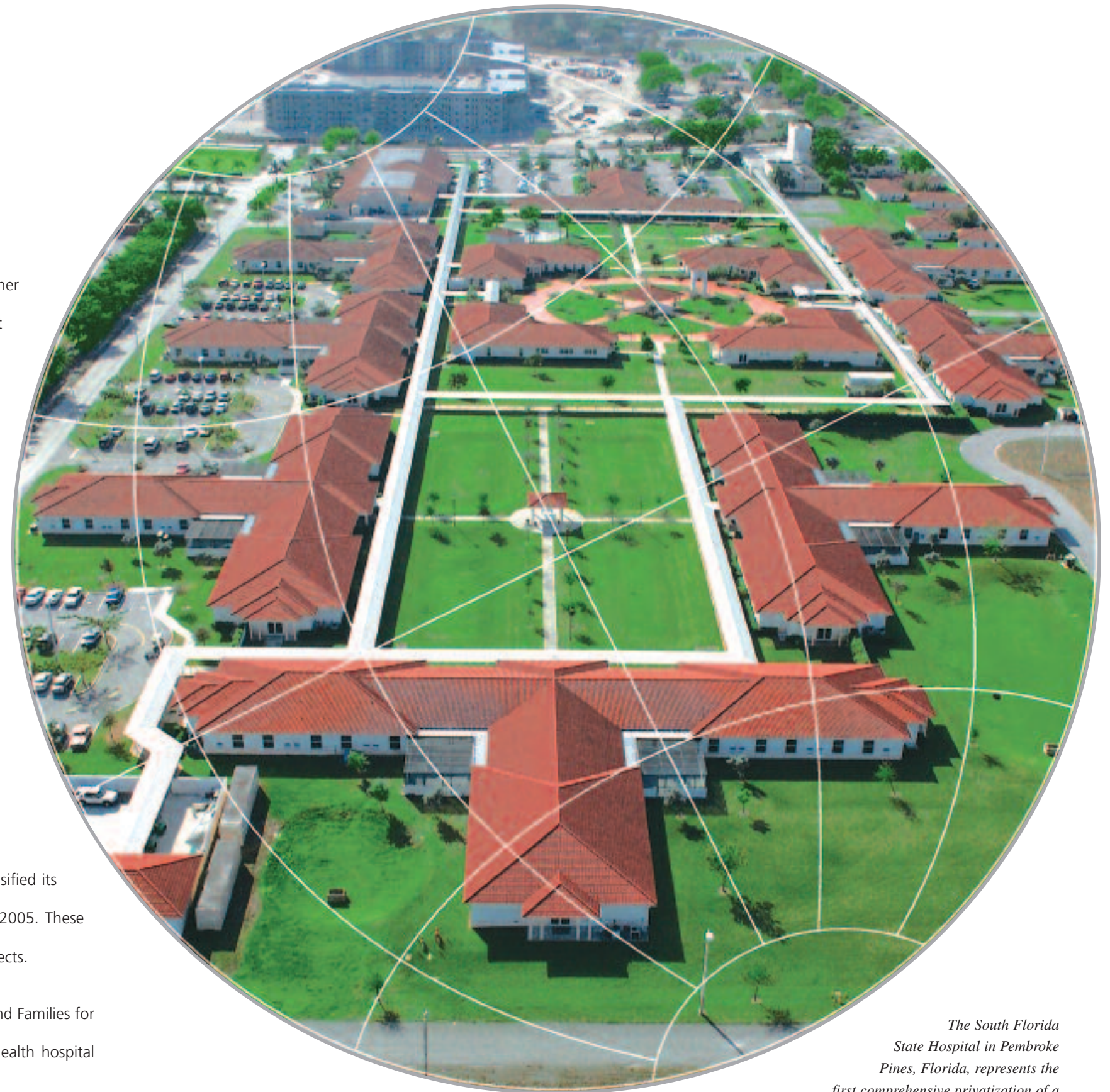
Over the past eight years, The GEO Group's wholly-owned subsidiary, GEO Care, Inc., has been setting higher standards and applying best practices in the delivery of mental health management and residential treatment services through a revolutionary public-private partnership with the State of Florida for the management and operation of the 325-bed South Florida State Hospital located in Pembroke Pines, Florida. Once a deteriorating facility, the new \$37 million South Florida State Hospital has substantially improved the quality of patient care and treatment and now leads the nation in a number of key measures used by mental health institutions to determine the quality and efficiency of treatment programs and outcomes.

One of these key measures is the number of restraint and seclusion events involving residents. Since GEO Care assumed management of the South Florida State Hospital in 1998, the number of restraint and seclusion events taking place at the facility has dramatically decreased to well below the national average, which has led the Joint Commission on Accreditation of Healthcare Organizations to recognize it nationally as a best practice in mental health services.

EXPANDING IN A GROWING MARKET

With the remarkable success of its public-private partnership at South Florida State Hospital, GEO Care intensified its efforts to promote and market its services to other state and local jurisdictions throughout the U.S. during 2005. These efforts paid dividends during the year with contract awards for two new large-scale residential treatment projects.

In the early part of 2005, GEO Care was awarded a contract by the State of Florida Department of Children and Families for the management of the 200-bed South Florida Evaluation and Treatment Center, a state forensic mental health hospital



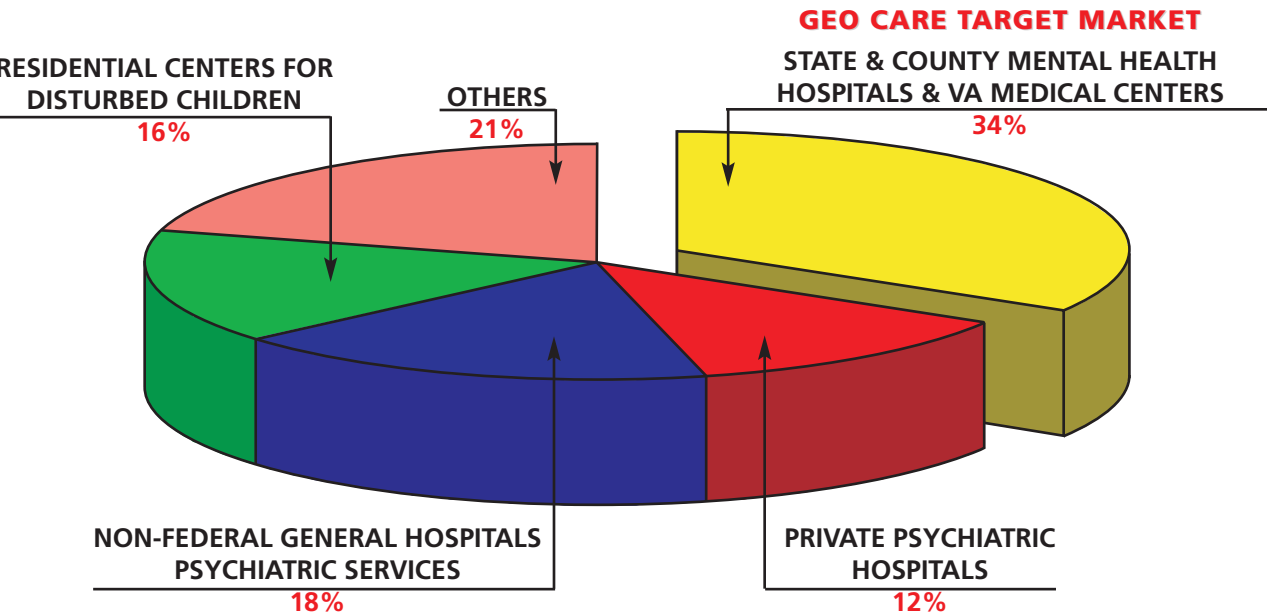
The South Florida State Hospital in Pembroke Pines, Florida, represents the first comprehensive privatization of a state psychiatric hospital in the United States.

With two important contract awards during 2005, GEO Care has more than tripled its operations. Based on this successful expansion of its business base and an ongoing pursuit of new business opportunities in other state and local jurisdictions across the country, GEO Care is poised to continue to achieve significant organic growth in an expanding market.

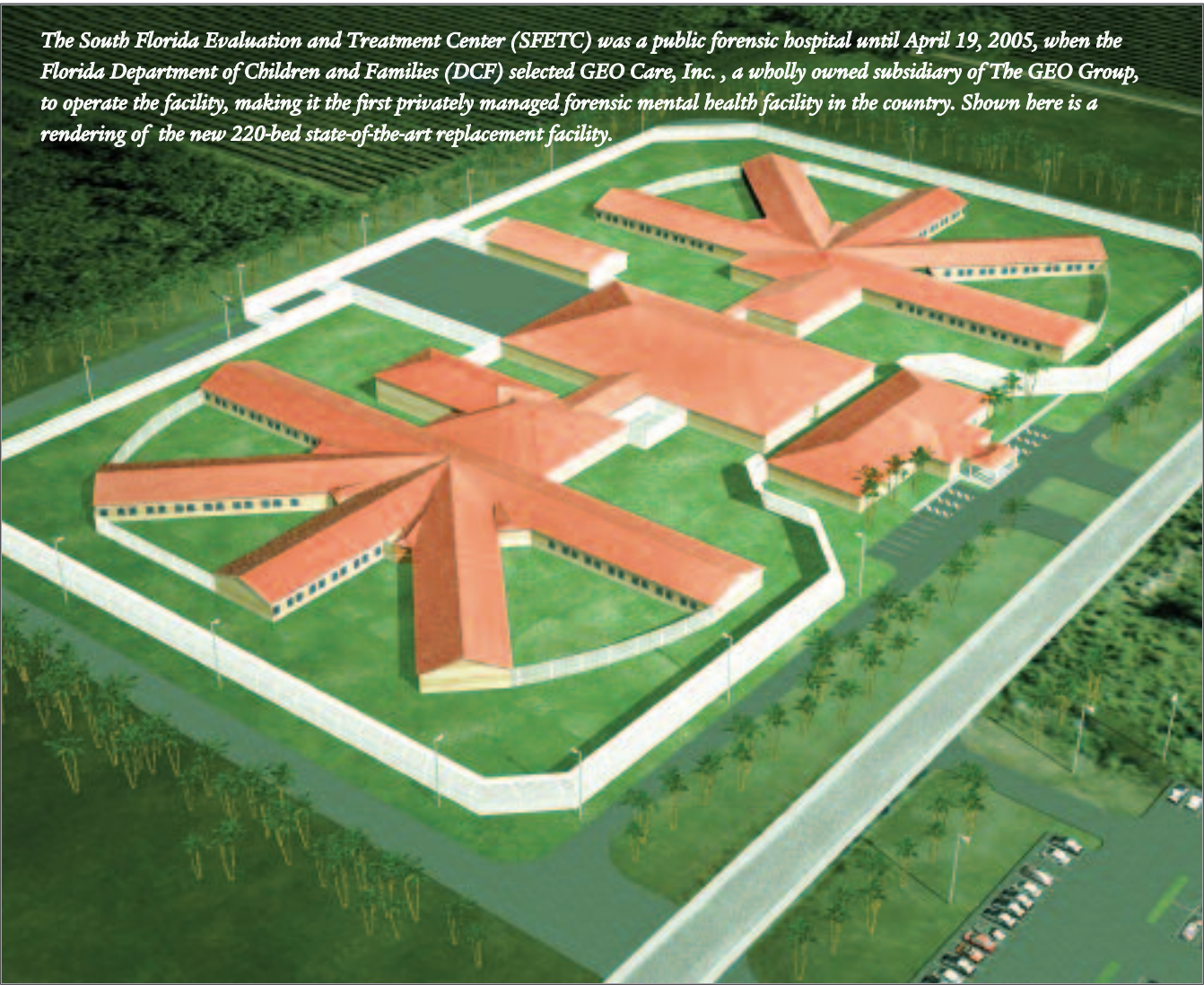
located in Miami, Florida, and for the development of a new 220-bed state-of-the-art replacement facility, which is expected to be completed by January 2008. Then, in late 2005, GEO Care received a contract award from the State of New Mexico Department of Health for the management of the 230-bed Fort Bayard Medical Center, a long-term care facility located in Silver City, New Mexico, as well as for the development of a modern 230-bed replacement facility, which is expected to be completed in 2008. GEO Care assumed management responsibilities at the South Florida Evaluation and Treatment Center and the Fort Bayard Medical Center in 2005.

These two milestone projects have more than tripled GEO Care's operations. Based on this successful expansion of its business base and an ongoing pursuit of new business opportunities in other state and local jurisdictions across the country, GEO Care is poised to continue to achieve significant organic growth in an expanding market.

24-HOUR MENTAL HEALTH ORGANIZATIONS BY NUMBER OF BEDS



Source: Center of Mental Health Services



The South Florida Evaluation and Treatment Center (SFETC) was a public forensic hospital until April 19, 2005, when the Florida Department of Children and Families (DCF) selected GEO Care, Inc. , a wholly owned subsidiary of The GEO Group, to operate the facility, making it the first privately managed forensic mental health facility in the country. Shown here is a rendering of the new 220-bed state-of-the-art replacement facility.



GEO Care managed the construction of the South Florida State Hospital's new 325-bed non-institutional, state-of-the-art residential campus style facility. Construction was completed in only 16 months.



The existing SFETC is located in downtown Miami, Florida.

FACILITIES AND OPERATIONS

U.S. Corrections

Location	Facility Type	Capacity
FEDERAL JURISDICTIONS		
Aurora ICE Processing Center (Colorado)	Adult M/F All Security Levels Immigration Detention	356
Bronx Community Correctional Center (New York)	Adult M/F Minimum Security Community/Residential	130
Brooklyn Community Correctional Center (New York)	Adult M/F Minimum Security Community/Residential	174
Broward Transition Center (Florida)	Adult M/F Minimum Security Immigration Detention	450
Guantanamo Bay Migrant Operations Center (Cuba)	Adult M/F and Juvenile Minimum Security Migrant Operations	100
Northwest Detention Center (Washington)	Adult M/F Medium/Minimum Security Immigration Detention	890
Queens Private Correctional Facility (New York)	Adult M/F Medium/Minimum Security Pre-Sentenced Detention	220
Rivers Correctional Institution (North Carolina)	Adult Male Low Security Federal Prison	1,200
South Texas Detention Complex (Texas)	Adult M/F Minimum Security Immigration Detention	1,020
Taft Correctional Institution (California)	Adult Male Low/Minimum Security Federal Prison	2,048
Western Region Detention Facility at San Diego (California)	Adult M/F High Security Pre-Sentenced Detention	700
MULTIPLE JURISDICTIONS		
Central Texas Detention Facility (Texas)	Adult M/F Medium/MinimumSecurity Detention	643
Dickens County Correctional Center (Texas)	Adult Male All Security Levels	489
Frio County Detention Center (Texas)	Adult Male/Female All Security Levels	391
Grenada County Jail (Mississippi)	Adult Male/Female All Security Levels	160
Jefferson County Downtown Jail (Texas)	Adult Male All Security Levels	500
Karnes Correctional Center (Texas)	Adult Male All Security Levels	579
Newton County Correctional Center (Texas)	Adult Male All Security Levels	872
Reeves County Detention Complex (Texas)	Adult Male Medium/Minimum Security Detention	3,064
Tri-County Justice & Detention Center (Illinois)	Adult M/F and Juvenile All Security Levels	226
Val Verde County Correctional Facility & Jail (Texas)	Adult M/F All Security Levels	784
STATE JURISDICTIONS		
Arizona		
Arizona State Prison - Florence West	Adult Male Medium/Minimum Security DWI and RTC	750
Arizona State Prison - Sex Offender Unit	Adult Male, Medium/Minimum Security	1,000
Arizona State Prison - Phoenix West	Adult Male Minimum Security DWI	450
California		
Central Valley Modified Community Correctional Facility	Adult Male Medium Security	550
Desert View Modified Community Correctional Facility	Adult Male Medium Security	568
Golden State Modified Community Correctional Facility	Adult Male Medium Security	550
McFarland Community Correctional Facility	Adult Male Minimum Security	224
Colorado		
Pre-Parole and Parole Revocation Center	Adult Male Medium Security	500
Florida		
Graceville Correctional Facility	Adult Male Medium/Close Custody	1,500
Moore Haven Correctional Facility	Adult Male Medium Security	985
South Bay Correctional Facility	Adult Male Close/Medium Security	1,862
Indiana		
New Castle Correctional Facility	Adult Male Medium/Minimum Security	2,416
Louisiana		
Allen Correctional Center	Adult Male Medium/Maximum Security	1,538
Jena Correctional Facility	Secure Correctional Facility	300
Michigan		
Michigan Correctional Facility	Secure Correctional Facility	500
Mississippi		
East Mississippi Correctional Facility	Adult Male All Security Levels Mental Health	1,000
Marshall County Correctional Facility	Adult Male Medium Security	1,000
New Mexico		
Guadalupe County Correctional Facility	Adult Male Medium Security	600
Lea County Correctional Facility	Adult Male All Security Levels	1,200
Oklahoma		
Lawton Correctional Facility	Adult Male Medium Security	2,518
Texas		
Bridgeport Correctional Center	Adult Male Minimum Security Pre-Release	520
Cleveland Correctional Center	Adult Male Minimum Security	520

Location	Facility Type	Capacity
Texas (continued)		
Coke County Juvenile Justice Center	Juvenile Male High Security	200
Fort Worth Community Corrections Facility	Adult Male/Female Minimum Security	225
Lockhart Secure Work Program Facility	Adult Male/Female Minimum Security Pre-Release	1,000
North Texas Intermediate Sanction Facility	Adult Male Minimum Security Short Term	400
Sanders Estes Unit	Adult Male Mimimum Security	1,000
South Texas Intermediate Sanction Facility	Adult Male Minimum Security Short Term	450
Virginia		
Lawrenceville Correctional Center	Adult Male Medium Security	1,536
LOCAL JURISDICTIONS		
Bill Clayton Detention Center (Texas)	Adult Male Medium Security	310
George W. Hill Correctional Facility (Pennsylvania)	Adult M/F and Juvenile All Security Levels	1,851

U.S. CORRECTIONS TOTAL

43,019

International Services

Australia		
Arthur Gorrie Correctional Centre	Local Prison and Remand Centre - All Security Levels	710
Fulham Correctional Centre	Adult Male Medium Security	777
Nalu Challenge Community	Adult Male Medium/Minimum Security	68
Junee Correctional Centre	Adult Male/Female Medium/Minimum Security	750
Melbourne Custody Centre	Court Escort and Custody Services - All Security Levels	67
South Africa		
Kutama Sinthumule Correctional Centre	Adult Male Maximum Security	3,024
United Kingdom		
Campsfield House Immigration Removal Centre	Detention Management	198

INTERNATIONAL SERVICES TOTAL

5,594

TOTAL U.S. CORRECTIONS AND INTERNATIONAL SERVICES

48,613

Residential Treatment Services

HOSPITALS		
GEO Care		
Fort Bayard Medical Center (New Mexico)	State Long Term Care Facility	230
South Florida Evaluation & Treatment Center	State Forensic Psychiatric Hospital	200
South Florida State Hospital	State Mental Health Hospital	325
RESIDENTIAL TREATMENT SERVICES TOTAL		
OTHER CONTRACTS		
Canada		
New Brunswick Youth Centre	Male/Female Youthful Offenders (Maintenance Only)	N/A
Australia		
Pacific Shores Healthcare	Health Services for the State of Victoria's Public Prisons	N/A

TOTAL BEDS UNDER MANAGEMENT

49,368

2005 FINANCIAL REVIEW

MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock trades on the New York Stock Exchange under the symbol "GGI." The following table shows the high and low prices for our common stock, as reported by the New York Stock Exchange, for each of the four quarters of fiscal years 2005 and 2004. The prices shown have been rounded to the nearest \$1/100. The approximate number of shareholders of record as of March 14, 2006, was 135

Quarter	2005		2004	
	High	Low	High	Low
First	\$ 32.20	\$ 25.60	\$ 24.23	\$ 19.80
Second	28.73	23.03	24.62	18.70
Third	28.95	25.15	21.00	17.33
Fourth	25.60	20.72	26.58	19.56

We did not pay any cash dividends on our common stock for fiscal years 2005 and 2004. We intend to retain our earnings to finance the growth and development of our business and do not anticipate paying cash dividends on our capital stock in the foreseeable future. Future dividends, if any, will depend, on our future earnings, our capital requirements, our financial condition and on such other factors as our board of directors may consider relevant. In addition, the indenture governing our \$150.0 million 81/4% senior notes due in 2013, and our \$150.0 million senior credit facility also place material restrictions on our ability to pay dividends. See "Item 7. Management's Discussion and Analysis, Cash Flow and Liquidity" and "Item 8. Financial Statements - Note 10- Debt" for further description of these restrictions.

We did not buy back any of our common stock during 2005. On July 9, 2003 we purchased all 12 million shares of our common stock beneficially owned by Group 4 Falck, our former 57% majority shareholder, for \$132.0 million in cash.

Equity Compensation Plan Information

The following table sets forth information about our common stock that may be issued upon the exercise of options, warrants and rights under all of our equity compensation plans as of January 1, 2006, including our 1994 Stock Option Plan, our 1994 Second Stock Option Plan, our 1999 Stock Option Plan, and our Non-Employee Director Stock Option Plan. Our shareholders have approved all of these plans.

Plan category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	1,406,657	\$ 15.53	13,000
Equity compensation plans not approved by security holders	—	—	—
Total	1,406,657	\$ 15.53	13,000

Sales of Unregistered Securities

To facilitate the completion of the share purchase from Group 4 Falck, on July 9, 2003, we issued \$150.0 million aggregate principal amount ten-year 81/4% senior notes, referred to as the Notes, in a private offering to qualified institutional buyers under Rule 144A of the Securities Act.

Subsequent to the private offering of the Notes, we filed an S-4 registration statement to register under the Securities Act of 1933 exchange notes, having substantially identical terms as the Notes, which we refer to as the Exchange Notes. The registration statement was declared effective by the SEC on November 10, 2003. We then completed an exchange offer pursuant to the registration statement, in which holders of the Notes exchanged the Notes for the Exchange Notes which are generally freely tradable, subject to certain exceptions. We did not sell any securities that were unregistered under the Securities Act of 1933 in 2004 or 2005.

SELECTED FINANCIAL DATA

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

Fiscal Year Ended: ⁽¹⁾	2005			2004		2003		2002		2001		
Results of Continuing Operations:												
Revenues	\$	612,900	100.0%	\$	593,994	100.0%	\$	549,238	100.0%	\$	490,115	100.0%
Operating income from continuing operations		7,938	1.3%		38,991	6.6%		29,500	5.4%		19,729	4.0%
Income from continuing operations	\$	5,879	1.0%	\$	17,163	2.9%	\$	36,375	6.6%	\$	17,617	3.4%
Income from continuing operations per common share:												
Basic:	\$	0.61		\$	1.83		\$	2.33		\$	0.83	
Diluted:	\$	0.59		\$	1.77		\$	2.30		\$	0.82	
Weighted Average Shares Outstanding:												
Basic		9,580			9,384			15,618			21,148	
Diluted		10,010			9,738			15,829			21,364	
Financial Condition:												
Current assets	\$	229,292		\$	222,766		\$	191,811		\$	142,839	
Current liabilities		136,519			117,478			118,704			79,360	
Total assets		639,511			480,326			505,341			405,378	
Long-term debt, including current portion (excluding non-recourse debt)		220,004			198,204			245,086			125,000	
Shareholders' equity	\$	108,594		\$	99,739		\$	77,325		\$	150,215	
Operational Data:												
Contracts/awards		59			47			43			50	
Facilities in operation		56			41			38			50	
Design capacity of contracts		48,370			34,813			38,287			40,757	
Compensated resident days(2)		12,607,525			12,458,102			11,389,821			10,591,019	
												9,943,684

(1) Our fiscal year ends on the Sunday closest to the calendar year end. The fiscal year ended January 2, 2005 contained 53 weeks. Discontinued Operations have not been included with Selected Financial Data. Information related to Discontinued Operations is listed in "Item 8. Financial Statements - Note 3 Discontinued Operations."

(2) Compensated resident days are calculated as follows: (a) for per diem rate facilities - the number of beds occupied by residents on a daily basis during the fiscal year; and (b) for fixed rate facilities - the design capacity of the facility multiplied by the number of days the facility was in operation during the fiscal year. Amounts exclude compensated resident days for United Kingdom for all of the above periods.

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

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

CSC Acquisition

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

Recent Financings

On September 14, 2005, we amended our senior secured credit facility, referred to as the Senior Credit Facility, to consist of a \$75 million, six-year term-loan bearing interest at London Interbank Offered Rate, or LIBOR plus 2.00%, and a \$100 million, five-year revolving credit facility bearing interest at LIBOR plus 2.00%. We used the borrowings under the Senior Credit Facility to fund general corporate purposes and to finance the acquisition of CSC for approximately \$62 million in cash plus transaction-related costs.

Discontinued Operations

Through our Australian subsidiary, we previously had a contract with the Department of Immigration, Multicultural and Indigenous Affairs, or DIMIA, for the management and operation of Australia's immigration centers. In 2003, the contract was not renewed, and effective February 29, 2004, we completed the transition of the contract and exited the management and operation of the DIMIA centers. The accompanying consolidated financial statements and notes reflect the operations of DIMIA as a discontinued operation in all periods presented.

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

On January 1, 2006, the last day of our 2005 fiscal year, we completed the sale of a 72 bed private mental health hospital which we owned and operated since 1997 for approximately \$11.5 million. We recognized a gain on the sale of this transaction of approximately \$1.6 million. The accompanying consolidated financial statements and notes reflect the operations of the hospital and the related sale as a discontinued operation.

Share Purchase

On July 9, 2003 we purchased all 12 million shares of our common stock beneficially owned by Group 4 Falck, our former 57% majority shareholder, for \$132.0 million in cash pursuant to the terms of a share purchase agreement, dated April 30, 2003,

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

by and among us, Group 4 Falck, our former parent company, The Wackenhut Corporation, or TWC, and Tuhnekaw, Inc., an indirect wholly-owned subsidiary of Group 4 Falck. In connection with the share purchase, we internalized several functions previously outsourced to TWC, including payroll processing, human resources management, tax and information systems.

Sale of Our Joint Venture Interest in Premier Custodial Group Limited

On July 2, 2003, we sold our one-half interest in Premier Custodial Group Limited, our former United Kingdom joint venture which we refer to as PCG, to Serco for approximately \$80.7 million, on a pretax basis.

Variable Interest Entities

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities," which addressed consolidation by a business of variable interest entities in which it is the primary beneficiary. In December 2003, the FASB issued FIN No. 46R which replaced FIN No. 46. Our 50% owned South African joint venture in South African Custodial Services Pty. Limited, which we refer to as SACS, is a variable interest entity. We determined that we are not the primary beneficiary of SACS and as a result are not required to consolidate SACS under FIN 46R. We account for SACS as an equity affiliate. SACS was established in 2001, to design, finance and build the Kutama Sinthumule Correctional Center. Subsequently, SACS was awarded a 25 year contract to design, construct, manage and finance a facility in Louis Trichardt, South Africa. SACS, based on the terms of the contract with government, was able to obtain long term financing to build the prison. The financing is fully guaranteed by the government, except in the event of default, for which it provides an 80% guarantee. "See Item 7. Financial Condition - Guarantees" for a discussion of our guarantees related to SACS. Separately, SACS entered into a long term operating contract with South African Custodial Management (Pty) Limited, which we refer to as SACM, to provide security and other management services and with SACS's joint venture partner to provide purchasing, programs and maintenance services upon completion of the construction phase, which concluded in February 2002. Our maximum exposure for loss under this contract is \$24.1 million, which represents our initial investment and the guarantees discussed in Item 7. Management's Discussion and Analysis of Financial Condition.

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

Shelf Registration Statement

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

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

applicable prospectus supplement relating to the offered securities, we anticipate using the net proceeds of each offering for general corporate purposes, including debt repayment, capital expenditures, acquisitions, business expansion, investments in subsidiaries or affiliates, and/or working capital.

Rights Agreement

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

Critical Accounting Policies

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

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

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

Revenue Recognition

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

Project development and design revenues are recognized as earned on a percentage of completion basis measured by the percentage of costs incurred to date as compared to estimated total cost for each contract. This method is used because we consider costs incurred to date to be the best available measure of progress on these contracts. Provisions for estimated losses on uncompleted contracts and changes to cost estimates are made in the period in which we determine that such losses and changes are probable. Typically, we enter into fixed price contracts and do not perform additional work unless approved change orders are in place. Costs attributable to unapproved change orders are expensed in the period in which the costs are incurred if we believe that it is not probable that the costs will be recovered through a change in the contract price. If we believe that it is probable that the costs will be recovered through a change in the contract price, costs related to unapproved change orders are expensed in

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
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the period in which they are incurred, and contract revenue is recognized to the extent of the cost incurred. Revenue in excess of the costs attributable to unapproved change orders is not recognized until the change order is approved. Contract costs include all direct material and labor costs and those indirect costs related to contract performance. Changes in job performance, job conditions, and estimated profitability, including those arising from contract penalty provisions, and final contract settlements, may result in revisions to estimated costs and income, and are recognized in the period in which the revisions are determined.

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

Reserves for Insurance Losses

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

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

Income Taxes

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

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

The provision for income taxes for the fiscal year 2005 reflects a benefit of \$1.7 million in the second quarter of 2005 related to the American Jobs Creation Act of 2004, or the AJCA. A key provision of the AJCA creates a temporary incentive for U.S. corporations to repatriate undistributed income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations. Additionally, 2005 reflects a benefit of \$6.5 million in the fourth quarter related to a step up in basis for an asset in Australia.

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Property and Equipment

As of January 1, 2006, we had approximately \$282.2 million in long-lived property and equipment. Property and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 2 to 40 years. Equipment and furniture and fixtures are depreciated over 3 to 7 years. Accelerated methods of depreciation are generally used for income tax purposes. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvement or the term of the lease. We perform ongoing evaluations of the estimated useful lives of our property and equipment for depreciation purposes. The estimated useful lives are determined and continually evaluated based on the period over which services are expected to be rendered by the asset. Maintenance and repairs are expensed as incurred.

We review long-lived assets to be held and used for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable in accordance with FAS No. 144 "Accounting for the Impairment of Disposal of Long-Lived Assets". Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell. Management has reviewed our long-lived assets and determined that there are no events requiring impairment loss recognition for the period ended January 1, 2006, other than the Michigan Facility charge. See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations "Commitments and Contingencies." Events that would trigger an impairment assessment include deterioration of profits for a business segment that has long-lived assets, or when other changes occur which might impair recovery of long-lived assets.

Idle Leased Facilities

We have entered into ten year non cancelable operating leases with CentraCore Properties Trust, or CPV, for eleven facilities with initial terms that expire at various times beginning in April 2008 and extending through 2016. In the event that our facility management contract for any of these leased facilities is terminated, we would remain responsible for payments to CPV on the underlying lease. We will account for idle periods under any such lease in accordance with FAS No. 146 "Accounting for Costs Associated with Exit or Disposal Activities." Specifically, we will review our estimate for sublease income and record a charge for the difference between the net present value of the sublease income and the lease expense over the remaining term of the lease.

Results of Operations

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

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

For the purposes of the discussion below, "2005" means the 52 week fiscal year ended January 1, 2006, "2004" means the 53 week fiscal year ended January 2, 2005, and "2003" means the 52 week fiscal year ended December 28, 2003.

Overview

GEO had diluted earnings per share of \$0.70, \$1.73 and \$2.53 in 2005, 2004, and 2003 respectively. For fiscal year 2005, the \$0.70 amount included (\$1.54) per diluted share for certain items, as detailed below, compared to the fiscal year 2004 \$1.73 amount, which included (\$0.03) per diluted share for certain items detailed below. The fiscal year 2003 \$2.53 amount included \$1.58 per diluted share for certain items detailed below. Weighted average common shares outstanding for fiscal year 2004 reflects a full year of the effect of our purchase of 12 million shares of our common stock in the third quarter 2003.

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The following table sets forth certain items before tax which we consider relevant to the discussion below of our operating results for 2005, 2004 and 2003:

	Fiscal Year		
	2005	2004	2003
(Dollars in thousands, except per share data)			
Certain Items (before income taxes)			
Michigan correctional facility write-off	\$ (20,859)	\$ —	\$ —
Insurance reduction	1,300	4,150	—
Jena, Louisiana write-off	(4,255)	(3,000)	(5,000)
DIMIA insurance reserves	—	—	(3,600)
Write-off of acquisition costs	—	(1,306)	—
Gain on sale of UK joint venture	—	—	56,094
Write-off of deferred financing fees	(1,360)	(317)	(1,989)
Certain Items	\$ (25,174)	\$ (473)	\$ 45,505
Amounts per diluted common share after-tax	\$ (1.54)	\$ (0.03)	\$ 1.58

The following table delineates where the total of certain items above are classified in our Consolidated Statements of Income.

	Fiscal Year		
	2005	2004	2003
(Dollars in thousands)			
Certain Items represented in the various lines of the Consolidated Statements of Income			
Operating Expenses	\$ (23,814)	\$ 1,150	\$ (8,600)
General and Administrative Expenses	—	(1,306)	—
Write-off of deferred financing fees	(1,360)	(317)	(1,989)
Gain on Sale of UK joint venture	—	—	56,094
Certain Items	\$ (25,174)	\$ (473)	\$ 45,505

2005 versus 2004
Revenues and Operating Expenses

	2005	% of Revenue	2004	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Revenue						
Correctional and Detention Facilities	\$ 572,109	93.3%	\$ 546,952	92.1%	\$ 25,157	4.6%
Other	\$ 40,791	6.7%	\$ 47,042	7.9%	\$ (6,251)	(13.3)%
Total	\$ 612,900	100.0%	\$ 593,994	100.0%	\$ 18,906	3.2%

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The increase in revenues in 2005 compared to 2004 is primarily attributable to five items: (i) Australian and South African revenues increased approximately \$7.8 million, \$2.6 million and \$0.2 million of which was due to the strengthening of the Australian dollar and South African Rand, respectively, and \$5.0 million of which was due to higher occupancy rates and contractual adjustments for inflation; (ii) the acquisition of CSC increased revenues \$17.3 million; (iii) the McFarland facility was idle for all of 2004 and was re-opened in January 2005 resulting in an increase in revenues of approximately \$3.1 million; (iv) domestic revenues also increased due to contractual adjustments for inflation, slightly higher occupancy rates and improved terms negotiated into a number of contracts. These increases offset a decrease in revenues due to the transition of the Queens contract from ICE to USMS, the closure of the Michigan Correctional Facility on October 14, 2005, the expiration of our operating contract for the Kyle Facility on August 31, 2005, and lower populations in our Val Verde, and San Diego Facilities; and (v) revenues decreased in 2005 because it contained 52 weeks compared to 2004, which contained 53 weeks.

The number of compensated resident days in domestic facilities increased to 10.7 million in 2005 from 10.5 million in 2004. Compensated resident days in Australian and South African facilities remained constant at 2.0 million during 2005 and 2004. We look at the average occupancy in our facilities to determine how we are managing our available beds. The average occupancy is calculated by taking compensated mandays as a percentage of capacity. The average occupancy in our domestic, Australian and South African facilities combined was 97.5% of capacity in 2005 compared to 99.3% in 2004. The decrease in the average occupancy is due to an increase in the number of beds made available to us under our contracts and lower populations in our Val Verde and San Diego facilities.

	2005	% of Revenue	2004	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Operating Expenses						
Correctional and Detention Facilities	\$ 499,924	81.6%	\$ 449,310	75.7%	\$ 50,614	11.3%
Other	\$ 40,204	6.5%	\$ 45,916	7.7%	\$ (5,712)	(12.4)%
Total	\$ 540,128	88.1%	\$ 495,226	83.4%	\$ 44,902	9.1%

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health facilities. Operating expenses for fiscal year 2005 reflect an impairment charge of \$20.9 million for the Michigan Correctional Facility. We own the 480-bed Michigan Correctional Facility and operated the facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. Separately, we leased the facility, as lessor, to the State, as lessee, under a lease with an initial term of 20 years followed by two 5-year options. On September 30, 2005, the Governor of the State of Michigan announced her decision to close the facility. As a result of the closure, our management contract with the MDOC was terminated. On October 3, 2005, the Michigan Department of Management & Budget provided a 60 day lease cancellation notice to us. See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations "Commitments and Contingencies" for further discussion relating to our Michigan Correctional Facility. Additionally, 2005 operating expenses reflect an operating charge on the Jena lease of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010.

Operating expenses in 2005 were favorably impacted by a \$3.4 million reduction in our reserves for general liability, auto liability, and workers compensation insurance. This favorable reduction was largely offset by higher than anticipated U.S. employee health insurance costs of approximately \$1.7 million, transition expenses of approximately \$0.8 million associated with our Queens New York Facility, start-up expenses at certain domestic facilities of approximately \$0.6 million and adjustments of approximately \$0.4 million to insurance reserves in our Australian operations.

The \$3.4 million reduction in insurance reserves was the result of revised actuarial projections related to loss estimates for the initial three years of our insurance program which was established on October 2, 2002. Prior to October 2, 2002, our insurance coverage was provided through an insurance program established by TWC, our former parent company. We experienced

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significant adverse claims development in general liability and workers' compensation in the late 1990's. Beginning in approximately 1999, we made significant operational changes and began to aggressively manage our risk in a proactive manner. These changes have resulted in improved claims experience and loss development, which we are realizing in our actuarial projections. As a result of improving loss trends, our independent actuary reduced its expected losses for claims arising since October 2, 2002. We adjusted our reserves in the third quarter of 2005 to reflect the actuary's improved expected loss projections. There can be no assurance that our improved claims experience and loss developments will continue. Similarly, 2004 operating expenses reflect a \$4.2 million reduction in insurance reserves also attributable to improved actuarial loss projections.

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

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

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

Other

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

Other Unallocated Operating Expenses
General and Administrative Expenses

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

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

Non Operating Expenses
Interest Income and Interest Expense

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

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

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

Costs Associated with Debt Refinancing

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

Provision for Income Taxes

	2005	% of Revenue	2004	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Income Taxes	\$ (11,826)	(1.9)%	\$ 8,231	1.4%	\$ (20,057)	(243.7)%

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

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

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

Equity in Earnings of Affiliate

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

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

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Fiscal 2004 compared with 2003
Revenues and Operating Expenses

	2004	% of Revenue	2003	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Revenue						
Correctional and Detention Facilities	\$ 546,952	92.1%	\$ 519,246	94.5%	\$ 27,706	5.3%
Other	\$ 47,042	7.9%	\$ 29,992	5.5%	\$ 17,050	56.8%
Total	\$ 593,994	100.0%	\$ 549,238	100.0%	\$ 44,756	8.1%

The increase in revenues in 2004 compared to 2003 is primarily attributable to five items: (i) Australian and South African revenues increased approximately \$17.7 million, \$9.7 million and \$2.2 million of which was due to the strengthening of the Australian dollar and South African Rand, respectively, and \$5.8 million of which was due to higher occupancy rates and contractual adjustments for inflation; (ii) revenues derived from construction increased by \$13.1 million in 2004 as compared to 2003 when construction revenue was insignificant. The construction revenue was related to our expansion of South Bay, one of the facilities that we manage, which was completed during the second quarter of 2005; (iii) the opening of new facilities, including Reeves and Sanders Estes, resulted in a \$13.1 million increase in revenue. The increase in revenues also reflects \$4.9 million of additional revenue in 2004 because the Lawrenceville Correctional Center, which opened in March 2003, was operational for the entire period; (iv) revenues increased in 2004 because it contained 53 weeks compared to 2003, which contained 52 weeks; and (v) domestic revenues also increased due to contractual adjustments for inflation, slightly higher occupancy rates and improved terms negotiated into a number of contracts. These increases were offset by \$24.6 million of lost revenue due to the non renewal in January 2004 of the management contracts for the Willacy State Jail and John R. Lindsey State Jail, and the closure of the McFarland CCF State Correctional Facility on December 31, 2003. The McFarland facility was reactivated on January 1, 2005.

The number of compensated resident days in domestic facilities increased to 10.5 million in 2004 from 9.7 million in 2003. Compensated resident days in Australian and South African facilities during 2004 increased to 2.0 million from 1.7 million for the comparable periods in 2003 primarily due to higher population levels. 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 domestic, Australian and South African facilities combined was 99.3% of capacity in 2004 compared to 97.9% in 2003. The decrease in the average occupancy is primarily due to an increase in the number of beds made available to us under our contracts.

	2004	% of Revenue	2003	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Operating Expenses						
Correctional and Detention Facilities	\$ 449,310	75.7%	\$ 438,678	79.9%	\$ 10,632	2.4%
Other	\$ 45,916	7.7%	\$ 28,340	5.1%	\$ 17,576	62.0%
Total	\$ 495,226	83.4%	\$ 467,018	85.0%	\$ 28,208	6.0%

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health facilities. Fiscal 2004 operating expenses include a \$4.2 million reduction in our general liability, auto liability and worker's compensation insurance reserves that was made in the third quarter 2004.

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

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Operating expenses in 2003 reflect a provision for operating losses of approximately \$5.0 million related to the Jena facility, and approximately \$3.0 million primarily attributable to liability insurance expenses, related to the transitioning of the DIMIA contract.

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

Other

Other primarily consists of revenues and related operating expenses associated with our mental health business and construction business. The increase in 2004 primarily relates to approximately \$13.1 of construction revenue as compared to 2003, when construction revenue was insignificant. The construction revenue is related to our expansion of the South Bay Facility, one of the facilities that we manage. The expansion was completed during the second quarter of 2005.

Other Unallocated Operating Expenses
General and Administrative Expenses

	2004	% of Revenue	2003	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
General and Administrative Expenses	\$ 45,879	7.7%	\$ 39,379	7.2%	\$ 6,500	16.5%

General and administrative expenses consist primarily of corporate management salaries and benefits, professional fees and other administrative expenses. The increase also reflects costs associated with compliance with Sarbanes-Oxley requirements for management's assessment over internal controls resulted in an increase in professional fees in 2004 of \$1.0 million. Salary expense increased \$5.0 million in 2004 as a result of increased incentive targets under our senior officer incentive plan and the internalization of functions and services previously outsourced to TWC. In addition, we were pursuing acquisition opportunities in 2004, and had capitalized direct and incremental costs related to potential acquisitions. During the fourth quarter of 2004, we determined that the related acquisitions were no longer probable, and wrote off the capitalized deferred acquisition costs of \$1.3 million. Finally, the remaining increase in general and administrative costs relates to other increases in professional fees, travel and rent expense for our corporate offices. These increases were partially offset by reduced salary expense in 2004 as compared to 2003. In May 2004, we completed payments under employment agreements with certain key executives triggered by the change in control from the sale of TWC in May 2002, resulting in a \$2.4 million reduction in salary expense in 2004.

Non Operating Expenses
Interest Income and Interest Expense

	2004	% of Revenue	2003	% of Revenue	\$ Change	% Change
(Dollars in thousands)						
Interest Income	\$ 9,568	1.6%	\$ 6,853	1.2%	\$ 2,715	39.6%
Interest Expense	\$ 22,138	3.7%	\$ 17,896	3.3%	\$ 4,242	23.7%

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

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The increase in interest expense is primarily attributable to the Notes, which began accruing interest on July 9, 2003. This resulted in a full year of interest expense in 2004 as compared to approximately six months in 2003. On June 25, 2004, we made a payment of approximately \$43.0 million on the term loan portion of our Senior Credit Facility, eliminating interest expense on the term loan for the remainder of 2004. Further, interest expense reflects higher average interest rates during 2004.

Costs Associated with Debt Refinancing

Deferred financing fees of \$0.3 million were written off in 2004 in connection with the \$43.0 million payment related to the term loan portion of the Senior Credit Facility on June 25, 2004. In 2003, the extinguishment of debt resulted in write-offs of deferred financing fees of \$2.0 million.

Sale of Joint Venture

Fiscal year 2003's results of operations includes the sale of the UK joint venture for \$80.7 million which resulted in a gain of \$56.1 million.

Provision for Income Taxes

	2004	% of Revenue	2003	% of Revenue	\$ Change	% Change
	(Dollars in thousands)					
Income Taxes	\$ 8,231	1.4%	\$ 36,852	6.7%	\$ (28,621)	(77.7)%

Provision for income taxes increased primarily due to the tax effect on the gain on sale of PCG in July 2003.

Financial Condition

Liquidity and Capital Resources

Current cash requirements consist of amounts needed for working capital, debt service, capital expenditures, supply purchases and investments in joint ventures. Our primary source of liquidity to meet these requirements is cash flow from operations and borrowings under the \$100.0 million revolving portion of our Senior Credit Facility. As of January 1, 2006, we had \$56.3 million available for borrowing under the revolving portion of the Senior Credit Facility.

We incurred substantial indebtedness in connection with the acquisition of CSC on November 4, 2005 and the share purchase in 2003. As of January 1, 2006, we had \$225.1 million of consolidated debt outstanding, excluding \$142.5 million of non-recourse debt. As of January 1, 2006, we also had outstanding eleven letters of guarantee totaling approximately \$6.5 million under separate international credit facilities. Our significant debt service obligations could, under certain circumstances, have material consequences. See "Risk Factors - Risks Related to Our High Level of Indebtedness." However, our management believes that cash on hand, cash flows from operations and our Senior Credit Facility will be adequate to support currently planned business expansion and various obligations incurred in the operation of our business, both on a near and long-term basis.

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

Our business requires us to make various capital expenditures from time to time, including expenditures related to the development of new correctional, detention and/or mental health facilities. In addition, some of our management contracts require us to make substantial initial expenditures of cash in connection with opening or renovating a facility. Generally, these initial expenditures are subsequently fully or partially recoverable as pass-through costs or are billable as a component of the per diem rates or monthly fixed fees to the contracting agency over the original term of the contract. However, we cannot assure you that any of these expenditures will, if made, be recovered. Based on current estimates of our capital needs, we anticipate that our capi-

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tal expenditures will not exceed \$10.0 million during the next 12 months. We plan to fund these capital expenditures from cash from operations or borrowings under the Senior Credit Facility.

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

The Senior Credit Facility

On September 14, 2005, we amended and restated our Senior Credit Facility, to consist of a \$75 million, six-year term-loan initially bearing interest at LIBOR plus 2.00%, and a \$100 million, five-year revolving credit facility initially bearing interest at LIBOR plus 2.00%. We used the borrowings under the Senior Credit Facility to fund general corporate purposes and to finance the acquisition of CSC, which closed on November 4, 2005 for approximately \$62 million in cash plus deal-related costs. As of January 1, 2006, we had borrowings of \$74.8 million outstanding under the term loan portion of the Senior Credit Facility, no amounts outstanding under the revolving portion of the Senior Credit Facility, and \$43.7 million outstanding in letters of credit under the revolving portion of the Senior Credit Facility.

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

Indebtedness under the revolving portion of the Senior Credit Facility bears interest at our option at the base rate plus a spread varying from 0.50% to 1.25% (depending upon a leverage-based pricing grid set forth in the Senior Credit Facility), or at LIBOR plus a spread, varying from 1.50% to 2.25% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). As of January 1, 2006, there were no borrowings currently outstanding under the revolving portion of the Senior Credit Facility. However, new borrowings would bear interest at LIBOR plus 2.00% or at the base rate plus 1.00%. Letters of credit outstanding under the revolving portion of the Senior Credit Facility bear interest at 1.50% to 2.25% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). Available capacity under the revolving portion of the Senior Credit Facility bears interest at 0.38% to 0.5%. The term loan portion of the Senior Credit Facility bears interest at our option at either the base rate plus a spread of 0.75% to 1.00%, or at LIBOR plus a spread, varying from 1.75% to 2.00% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). Borrowings under the term loan portion of the Senior Credit Facility currently bear interest at LIBOR plus a spread of 2.00%. If an event of default occurs under the Senior Credit Facility, (i) all LIBOR rate loans bear interest at the rate which is 2.00% in excess of the rate then applicable to LIBOR rate loans until the end of the applicable interest period and thereafter at a rate which is 2.00% in excess of the rate then applicable to base rate loans, and (ii) all base rate loans bear interest at a rate which is 2.00% in excess of the rate then applicable to base rate loans.

The Senior Credit Facility contains financial covenants which require us to maintain the following ratios, as computed at the end of each fiscal quarter for the immediately preceding four quarter-period: a total leverage ratio equal to or less than 3.50 to 1.00 through December 30, 2006, which reduces thereafter in 0.50 increments to 3.00 to 1.00 for the period from December 31, 2006 through December 27, 2007 and thereafter; a senior secured leverage ratio equal to or less than 2.50 to 1.00; and a fixed charge coverage ratio equal to or less than 1.05 to 1.00 until December 30, 2006, and thereafter a ratio of 1.10 to 1.00. In addition, the Senior Credit Facility prohibits us from making capital expenditures greater than \$19.0 million in the aggregate dur-

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ing any fiscal year until 2009 and \$24.0 million during each of the years 2010 and 2011, provided that to the extent that our capital expenditures during any fiscal year are less than the limit, such amount will be added to the maximum amount of capital expenditures that we can make in the following year.

The Senior Credit Facility contains certain customary representations and warranties, and certain customary covenants that restrict our ability to, among other things (i) create, incur or assume any indebtedness, (ii) incur liens, (iii) make loans and investments, (iv) engage in mergers, acquisitions and asset sales, (v) sell our assets, (vi) make certain restricted payments, including declaring any cash dividends or redeem or repurchase capital stock, except as otherwise permitted, (vii) issue, sell or otherwise dispose of our capital stock, (viii) transact with affiliates, (ix) make changes to our accounting treatment, (x) amend or modify the terms of any subordinated indebtedness (including the Notes), (xi) enter into debt agreements that contain negative pledges on our assets or covenants more restrictive than contained in the Senior Credit Facility, (xii) alter the business we conduct, and (xiii) materially impair our lenders' security interests in the collateral for our loans. Events of default under the Senior Credit Facility include, but are not limited to, (i) our failure to pay principal or interest when due, (ii) our material breach of any representations or warranty, (iii) covenant defaults, (iv) bankruptcy, (v) cross defaults to certain other indebtedness, (vi) unsatisfied final judgments over a threshold to be determined, (vii) material environmental claims which are asserted against us, and (viii) a change of control.

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

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

Senior 8^{1/4}% Notes

To facilitate the completion of the purchase of the 12 million shares from Group 4 Falck, we issued \$150.0 million aggregate principal amount, ten-year, 81/4% senior unsecured notes, which we refer to as the Notes. The Notes are general, unsecured, senior obligations of ours. Interest is payable semi-annually on January 15 and July 15 at 81/4%. The Notes are governed by the terms of an Indenture, dated July 9, 2003, between us and the Bank of New York, as trustee, referred to as the Indenture. Under the terms of the Indenture, at any time on or prior to July 15, 2006, we may redeem up to 35% of the Notes with the proceeds from equity offerings at 108.25% of the principal amount to be redeemed plus the payment of accrued and unpaid interest, and any applicable liquidated damages. Additionally, after July 15, 2008, we may redeem, at our option, all or a portion of the Notes plus accrued and unpaid interest at various redemption prices ranging from 104.125% to 100.000% of the principal amount to be redeemed, depending on when the redemption occurs. The Indenture contains certain covenants that limit our ability to incur additional indebtedness, pay dividends or distributions on our common stock, repurchase our common stock, and prepay subordinated indebtedness. The Indenture also limits our ability to issue preferred stock, make certain types of investments, merge or consolidate with another company, guarantee other indebtedness, create liens and transfer and sell assets.

The covenants governing the Notes impose significant operating and financial restrictions which may substantially restrict and adversely affect our ability to operate our business. See "Risk Factors - Risks Related to Our High Level of Indebtedness - The covenants in the indenture governing the Notes and our Senior Credit Facility impose significant operating and financial restrictions which may adversely affect our ability to operate our business." We believe that we were in compliance with all of the covenants of the Indenture governing the Notes as of January 1, 2006.

Non-Recourse Debt

South Texas Detention Complex

In February 2004, CSC was awarded a contract by ICE to develop and operate a 1,020 bed detention complex in Frio County Texas. STLDC was created and issued \$49.5 million in taxable revenue bonds to finance the construction of the detention center. Additionally, CSC provided a \$5 million subordinated note to STLDC for initial development. We determined that we are the primary beneficiary of STLDC and consolidate the entity as a result. STLDC is the owner of the complex and entered into

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a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require the revenue from CSC's contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums are distributed to CSC to cover CSC's operating expenses and management fee. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities resulting from its ownership. The bonds have a ten year term and are non-recourse to CSC and STLDC. The bonds are fully insured and the sole source of payment for the bonds is the operating revenues of the center.

Included in non-current restricted cash equivalents and investments is \$12.2 million as of January 1, 2006 as funds held in trust with respect to the STLDC for debt service and other reserves.

Northwest Detention Center

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

Included in non-current restricted cash equivalents and investments is \$1.3 million as of January 1, 2006 as funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.

Australia

In connection with the financing and management of one Australian facility, our wholly owned Australian subsidiary financed the facility's development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to us. We have consolidated the subsidiary's direct finance lease receivable from the state government and related non-recourse debt each totaling approximately \$40.3 million and \$44.7 million as of January 1, 2006 and January 2, 2005, respectively. As a condition of the loan, we are required to maintain a restricted cash balance of AUD 5.0 million, which, at January 1, 2006, was approximately \$3.7 million. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria.

Guarantees

In connection with the creation of SACS, we entered into certain guarantees related to the financing, construction and operation of the prison. We guaranteed certain obligations of SACS under its debt agreements up to a maximum amount of 60.0 million South African Rand, or approximately \$9.5 million, to SACS' senior lenders through the issuance of letters of credit. Additionally, SACS is required to fund a restricted account for the payment of certain costs in the event of contract termination. We have guaranteed the payment of 50% of amounts which may be payable by SACS into the restricted account and provided a standby letter of credit of 6.5 million South African Rand, or approximately \$1.0 million, as security for our guarantee. Our obligations under this guarantee expire upon the release from SACS of its obligations in respect of the restricted account under its debt agreements. No amounts have been drawn against these letters of credit, which are included in our outstanding letters of credit under the revolving loan portion of our Senior Credit Facility.

We have agreed to provide a loan, if necessary, of up to 20.0 million South African Rand, or approximately \$3.2 million, referred to as the Standby Facility, to SACS for the purpose of financing the obligations under the contract between SACS and the South African government. No amounts have been funded under the Standby Facility, and we do not currently anticipate that such funding will be required by SACS in the future. Our obligations under the Standby Facility expire upon the earlier of full funding or

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release from SACS of its obligations under its debt agreements. The lenders' ability to draw on the Standby Facility is limited to certain circumstances, including termination of the contract.

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

In connection with a design, build, finance and maintenance contract for a facility in Canada, we guaranteed certain potential tax obligations of a not-for-profit entity. The potential estimated exposure of these obligations is CAN\$2.5 million, or approximately \$2.1 million commencing in 2017. We have a liability of \$0.6 million and \$0.5 million related to this exposure as of January 1, 2006 and January 2, 2005, respectively. To secure this guarantee, we purchased Canadian dollar denominated securities with maturities matched to the estimated tax obligations in 2017 to 2021. We have recorded an asset and a liability equal to the current fair market value of those securities on our balance sheet. We do not currently operate or manage this facility

At January 1, 2006, we also had outstanding eleven letters of guarantee totaling approximately \$6.5 million under separate international facilities. We do not have any off balance sheet arrangements.

Interest Rate Swaps

Effective September 18, 2003, we entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. We have designated the swaps as hedges against changes in the fair value of a designated portion of the Notes due to changes in underlying interest rates. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the Notes. The agreements, which have payment and expiration dates and call provisions that coincide with the terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, we receive a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while we make a variable interest rate payment to the same counterparties equal to the six-month LIBOR plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. As of January 1, 2006 and January 2, 2005, the fair value of the swaps totaled approximately \$(1.1) million and \$0.7 million, respectively, and is included in other non-current assets and other non-current liabilities in the accompanying balance sheets. There was no material ineffectiveness of our interest rate swaps for the years ended January 1, 2006 or January 2, 2005.

Our Australian subsidiary is a party to an interest rate swap agreement to fix the interest rate on the variable rate non-recourse debt to 9.7%. We have determined the swap to be an effective cash flow hedge. Accordingly, we record the value of the interest rate swap in accumulated other comprehensive income, net of applicable income taxes. The total value of the swap liability as of January 1, 2006 and January 2, 2005 was approximately \$0.4 million and \$2.5 million, respectively, and is recorded as a component of other liabilities in the accompanying consolidated financial statements. There was no material ineffectiveness of the interest rate swaps for the fiscal years presented. We do not expect to enter into any transactions during the next twelve months which will result in the reclassification into earnings of gains or losses associated with this swap that are currently reported in accumulated other comprehensive loss.

Cash Flow

Cash and cash equivalents as of January 1, 2006 were \$57.1 million, a decrease of \$34.9 million from January 2, 2005.

Cash provided by operating activities of continuing operations in 2005, 2004 and 2003 was \$31.8 million, \$31.5 million, and \$14.4 million, respectively. Cash provided by operating activities of continuing operations in 2005 was positively impacted by impairment charges of \$20.9 million for our Michigan Correctional Facility and \$4.3 million related to our Jena facility. Cash provided by operating activities of continuing operations in 2003 was positively impacted by an increase in accounts payable and accrued expenses and other liabilities. The increase in accounts payable and other accrued expenses is attributable to the increase in value of our Australian subsidiary's accounts payable and accrued expenses due to an increase in foreign exchange rates and an increase in reserves for self insurance. The increase in other liabilities reflects an increase in the liability for the fair market value of our Australian subsidiary's interest rate swap and an increase in certain pension obligations.

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Cash provided by operating activities of continuing operations in 2005 was negatively impacted by an increase in accounts receivable. The increase in accounts receivable is attributable to the increase in value of our Australian subsidiary's accounts receivable due to an increase in foreign exchange rates, the addition of the Lawrenceville Correctional Facility and slightly higher monthly billings reflecting a general increase in facility occupancy levels.

Cash used in investing activities of continuing operations in 2005 was \$104.9 million. Cash provided by investing activities in 2004 and 2003, was \$42.1 million and \$8.3 million, respectively. Cash used in investing activities in 2005 reflect the acquisition of CSC. In 2004, there was a decrease in the restricted cash balance of \$52.0 million due to the payment of \$43.0 million of the term loan portion of the Senior Credit Facility with the net proceeds of the sale of PCG. This payment satisfied the restriction on cash imposed by the terms of the Senior Credit Facility and the remainder was reclassified to cash. Cash provided by investing activities in 2003 reflects the gross proceeds from the sale of PCG offset by restricted cash and capital expenditures in the normal course of business.

Cash provided by financing activities in 2005 was \$24.6 million. Cash used in financing activities in 2004 and 2003 was \$47.1 million and \$17.2 million, respectively. Cash provided by financing activities in 2005 reflect the payoff of \$53.4 million and the refinancing of \$75.0 million of the term loan portion of the Senior Credit Facility. Cash used in financing activities in 2004 reflect payments of \$10.0 million on borrowings under the Revolving Credit Facility, \$4.0 million in scheduled payments on the Term Loan Facility, and a one-time \$43.0 million payment on the Term Loan Facility from the net proceeds from the sale of our interest in PCG. The \$10.0 million proceeds from debt reflect borrowings under the Revolving Credit Facility in 2004.

Contractual Obligations and Off Balance Sheet Arrangements

The following is a table of certain of our contractual obligations, as of January 1, 2006, which requires us to make payments over the periods presented.

Contractual Obligations	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
(In thousands)					
Long-term debt obligations	\$ 225,114	\$ 1,051	\$ 1,500	\$ 19,125	\$ 203,438
Capital lease obligations (includes imputed interest)	32,805	2,087	4,254	3,884	22,580
Operating lease obligations	206,879	37,233	69,730	33,306	66,610
Non-recourse debt	142,479	6,707	23,171	25,868	86,733
Estimated interest payments on debt(a)	176,146	24,937	48,371	46,103	56,735
Estimated payments on interest rate swaps(a)	(76)	(10)	(20)	(20)	(26)
Other long-term liabilities	12,749	11,047	112	248	1,342
Total	\$ 796,096	\$ 83,052	\$ 147,118	\$ 128,514	\$ 437,412

(a) Due to the uncertainties of future LIBOR rates, the variable interest payments on our credit facility and swap agreements were calculated using LIBOR rates of 4.61% and 4.73% based on our bank rates as of February 24, 2006 and January 13, 2006, respectively.

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

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Commitments and Contingencies

During 2000, our management contract at the 276-bed Jena Juvenile Justice Center in Jena, Louisiana, which is included in the correction and detention facilities segment, was discontinued by the mutual agreement of the parties. Despite the discontinuation of the management contract, we remain responsible for payments on our underlying lease of the inactive facility with CentraCore Properties Trust, ("CPV") through January 2010. During the Third Quarter 2005, we determined the alternative uses being pursued were no longer probable and as a result revised our estimated sublease income and recorded an operating charge of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010 for a total reserve of \$8.6 million. However, we plan to continue our efforts to reactivate the facility.

We own the 480-bed Michigan Correctional Facility in Baldwin, Michigan, referred to as the Michigan Facility. We operated the Michigan Facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. Separately, we leased the Michigan Facility, as lessor, to the State, as lessee, under a lease with an initial term of 20 years followed by two five-year options. On September 30, 2005, the Governor of the State of Michigan announced her decision to close the Michigan Facility. As a result of the closure of the Michigan Facility, our management contract with the MDOC to operate the Michigan Facility was terminated. On October 3, 2005, the Michigan Department of Management & Budget sent us a 60 day cancellation notice to terminate the lease for the Michigan Facility. Based in part on the language of certain provisions in the lease, we believe that the Governor does not have the authority to unilaterally terminate the Michigan Facility lease. As a result, in November 2005, we filed a lawsuit against the State to enforce our rights under the lease. On February 24, 2006, the Ingham County Circuit Court, the trial court with jurisdiction over the case, granted summary judgment in favor of the State and against us and the other plaintiffs, The Village of Baldwin and Webber Township. The trial court ruled that the State lawfully cancelled the lease when the Governor exercised her line item veto of the legislative appropriation for the funding of the lease. We are in the process of appealing the summary judgment entered by the trial court. We have reviewed the Michigan Facility for impairment in accordance with FAS 144, Accounting for the Impairment or Disposal of Long-Lived Assets, and recorded an impairment charge in the fourth quarter of 2005 for \$20.9 million.

We have entered into construction contracts with the Florida Department of Management Services, or DMS, to expand the Moorehaven Correctional Facility by 235 beds, which we operate for DMS, and build the 1,500 bed Graceville Correctional Facility, which we will operate for DMS upon final completion of the construction. Payment under these construction contracts is contingent on the receipt of proceeds from bonds being issued by the State of Florida to finance the projects. Subsequent to January 1, 2006, we may incur approximately \$8.5 million in costs related to these projects prior to the financing being completed. These costs would be incurred in order to preserve construction prices and our development timeline. We expect the financing for these facilities to be completed by March 31, 2006. In the event the required financing is not completed, we will expense these costs during the first quarter of 2006 without an offsetting revenue source.

Inflation

We believe that inflation, in general, did not have a material effect on our results of operations during 2005, 2004 and 2003. While some of our contracts include provisions for inflationary indexing, inflation could have a substantial adverse effect on our results of operations in the future to the extent that wages and salaries, which represent our largest expense, increase at a faster rate than the per diem or fixed rates received by us for our management services.

Outlook

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

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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 be encouraged by the number of opportunities that have recently developed in the privatized corrections and detention industry. The need for additional bed space at the federal, state at local levels has been as strong as it has been at any time during the last decade, and we currently expect that trend to continue for the foreseeable future. Overcrowding at corrections facilities in various states and increased demand for bed space at federal prisons and detention facilities primarily resulting from government initiatives to improve immigration security are two of the factors that have contributed to the greater number of opportunities for privatization. We plan to actively bid on any new projects that fit our target profile for profitability and operational risk. Although we are pleased with the overall industry outlook, positive trends in the industry may be offset by several factors, including budgetary constraints, unanticipated contract terminations and contract non-renewals. In Michigan, the State recently cancelled our Baldwin Correctional Facility management contract based upon the Governor's veto of funding for the project. Although we do not expect this termination to represent a trend, any future unexpected terminations of our existing management contracts could have a material adverse impact on our revenues. Additionally, several of our management contracts are up for renewal and/or re-bid in 2006. Although we have historically had a relative high contract renewal rate, there can be no assurance that we will be able to renew our management contracts scheduled to expire in 2006 on favorable terms, or at all.

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

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

Operating Expenses

Operating expenses consist of those expenses incurred in the operation and management of our correctional, detention and mental health facilities. In 2005, operating expenses totaled approximately 88.1% of our consolidated revenues. Our operating expenses as a percentage of revenue in 2006 will be impacted by several factors. First, we could experience continued savings under our general liability, auto liability and workers' compensation insurance program, although the amount of these potential savings cannot be predicted. These savings, which totaled \$3.4 million in fiscal year 2005 and are now reflected in our current actuarial projections are a result of improved claims experience and loss development as compared to our results under our prior insurance program. Second, we may experience a reduction in employee healthcare costs following adjustments to our employee healthcare program in November 2005 intended to reduce costs relating to additional claims expense and increased reserve requirements. These potential reductions in operating expenses may be offset by increased start-up expenses relating to a number of new projects which we are developing, including our new Graceville prison and Moore Haven expansion project in Florida, our Clayton facility in New Mexico, our Lawton, Oklahoma prison expansion and our Florence West expansion project in Arizona. Overall, excluding start-up expenses, we anticipate that operating expenses as a percentage of our revenue will remain relatively flat, consistent with our historical performance.

With respect to our future lease expense, we intend to restructure our relationship with CPV, now known as CentraCore Properties Trust, from whom we lease eleven facilities. In 1998, the original need for our sponsorship and creation of CPV was to provide us with a means to source capital for the development of new correctional and detention facilities. This need was prompted by the fact that TWC, our former parent company at the time, would not allow us to issue stock or incur indebtedness in order to finance our growth.

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Presently, as a fully independent public company, we believe that we have a number of avenues available to us to raise capital for the development of new facilities, including the equity markets, bank debt, corporate bonds and government sponsored bonds similar to those involved in several of our new facilities under development. All of these financial avenues currently provide a lower cost of capital than our present lease rates with CPV, which are approximately 12 percent at this time. Accordingly, we believe that we have a duty to our shareholders to seek the most cost-effective available sources of capital in order to best manage and grow the company. That duty has led us to make a number of decisions.

Our first decision is to not renew GEO's 15-year Right to Purchase Agreement with CPV when it expires in 2013, thus eliminating our obligation to provide CPV with the right to acquire future company-owned facilities that are covered by that agreement. Second, we do not anticipate developing any new projects using CPV financing. We expect that for the foreseeable future we will be able to achieve a lower cost of capital by accessing development capital through government-supported bond financing or other third party financing. Third, with regard to the Jena, Louisiana facility, unless we find a new client in the very near future allowing us to reactivate the facility on a profitable basis, we will not renew that lease, which is scheduled to expire in January 2010, and we will no longer be required to make the annual lease payment of approximately \$2.1 million dollars after that date.

Fourth, with respect to the other ten facilities that we lease from CPV, seven of those leases expire in April 2008, referred to as the Expiring Leases. We have until late October 2007 to exercise our option, in our discretion, to renew each of the Expiring Leases for an additional five-year term. We are under no obligation to renew any or all of the Expiring Leases, and may renew some of the Expiring Leases without renewing others. If we opt to renew any of the Expiring Leases, the Expiring Leases will be renewed on identical terms, except that the rental rate will be equal to the fair market rental value of the facility being renewed, as mutually agreed to by us and CPT or, in the absence of such an agreement, as determined through binding arbitration.

We have acquired property in close proximity to several of the properties leased from CPV and are researching available sites near the other CPV leased properties. These steps have put us in a position to conduct a comprehensive review of government-sponsored financing and third-party ownership alternatives that may be available to us with respect to the Expiring Leases. It is possible that we may elect to not exercise our exclusive option to renew certain of the Expiring Leases upon their expiration in favor of the construction and development through government-sponsored bonds or other third party financing of new replacement facilities in close proximity to the facilities covered by the Expiring Leases. In such cases, with our customers' approval, we would transition our contracted inmate population to the new facilities prior to the expiration of the Expiring Leases in April 2008.

We believe that these decisions with respect to our relationship with CPV will best serve our shareholders' interests and allow us to better manage and grow our company by accessing the lowest cost of capital available to us.

General and Administrative Expenses

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

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Forward-Looking Statements—Safe Harbor

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

- our ability to timely build and/or open facilities as planned, profitably manage such facilities and successfully integrate such facilities into our operations without substantial additional costs;
- the instability of foreign exchange rates, exposing us to currency risks in Australia and South Africa, or other countries in which we may choose to conduct our business;
- our ability to reactivate the Michigan Correctional Facility;
- an increase in unreimbursed labor rates;
- our ability to expand and diversify our correctional and mental health residential treatment services;
- our ability to win management contracts for which we have submitted proposals and to retain existing management contracts;
- our ability to raise new project development capital given the often short-term nature of the customers' commitment to use newly developed facilities;
- our ability to reactivate our Jena, Louisiana facility, or to sublease or coordinate the sale of the facility with the owner of the property, CentraCore Properties Trust, or CPV;
- our ability to accurately project the size and growth of the domestic and international privatized corrections industry;
- our ability to grow our mental health residential treatment services industry;
- our ability to estimate the government's level of dependency on privatized correctional services;
- our ability to develop long-term earnings visibility;
- our ability to obtain future financing at competitive rates;
- our exposure to rising general insurance costs;
- our exposure to claims for which we are uninsured;
- our exposure to rising inmate medical costs;

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

- our ability to maintain occupancy rates at our facilities;
- our ability to manage costs and expenses relating to ongoing litigation arising from our operations;
- our ability to accurately estimate on an annual basis, loss reserves related to general liability, workers compensation and automobile liability claims;
- our ability to identify suitable acquisitions, and to successfully complete and integrate such acquisition on satisfactory terms;
- the ability of our government customers to secure budgetary appropriations to fund their payment obligations to us; and
- other factors contained in our filings with the Securities and Exchange Commission, or the SEC, including, but not limited to, those detailed in this annual report on Form 10-K, our Form 10-Qs and our Form 8-Ks filed with the SEC.

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

RISK FACTORS

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. Monthly payments under the Senior Credit Facility are indexed to a variable interest rate. Based on borrowings outstanding under the term loan portion of our Senior Credit Facility of \$74.8 million as of January 1, 2006, for every one percent increase in the interest rate applicable to the Senior Credit Facility, our total annual interest expense would increase by \$0.7 million.

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

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

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

Foreign Currency Exchange Rate Risk

We are exposed to market risks related to fluctuations in foreign currency exchange rates between the U.S. dollar and the Australian dollar and the South African Rand currency exchange rates. Based upon our foreign currency exchange rate exposure as of January 1, 2006 with respect to our international operations, every 10 percent change in historical currency rates would have approximately a \$2.2 million effect on our financial position and approximately a \$1.8 million impact on our results of operations over the next fiscal year.

Financial Statements and Supplementary Data
MANAGEMENT’S RESPONSIBILITY FOR FINANCIAL STATEMENTS

To the Shareholders of The GEO Group, Inc.:

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

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

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

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

George C. Zoley
Chairman and Chief Executive Officer

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

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

Financial Statements and Supplementary Data
MANAGEMENT’S ANNUAL REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedure may deteriorate. Management has assessed the effectiveness of the Company's internal control over financial reporting as of January 1, 2006. In making its assessment of internal control over financial reporting, management used the criteria set forth by the Committee of Sponsoring Organizations ("COSO") of the Treadway Commission in Internal Control - Integrated Framework.

On November 4, 2005, the Company completed the acquisition of Correctional Services Corporation ("CSC"), as discussed elsewhere in this report. For 2005, CSC represented 2.8% of the Company's consolidated revenue and, as of January 1, 2006, CSC represented 34.7% of the Company's total consolidated assets. In making management's assessment of the effectiveness of its internal control over financial reporting, management has excluded CSC from its report on internal control over financial reporting as management did not have sufficient time to make an assessment of CSC's internal controls using the COSO criteria in accordance with Section 404 of the Sarbanes-Oxley Act.

The Company evaluated, with the participation of its Chief Executive Officer and Chief Financial Officer, its internal control over financial reporting as of January 1, 2006, based on the COSO Internal Control - Integrated Framework. Based on this evaluation, the Company's management concluded that as of January 1, 2006, its internal control over financial reporting is effective in providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of January 1, 2006 has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report which appears on page 29.

REPORT OF INDEPENDENT REGISTERED CERTIFIED PUBLIC ACCOUNTANTS

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

We have audited the accompanying consolidated balance sheets of The GEO Group, Inc. as of January 1, 2006 and January 2, 2005, and the related consolidated statements of income, shareholders' equity and comprehensive income, and cash flows for each of the three years in the period ended January 1, 2006. Our audits also included the financial statement schedule listed in the index at item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The GEO Group, Inc. at January 1, 2006 and January 2, 2005, and the consolidated results of its operations and its cash flows for each of the three years in the period ended January 1, 2006, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of The GEO Group, Inc.'s internal control over financial reporting as of January 1, 2006, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 14, 2006 expressed an unqualified opinion thereon.

ERNST &YOUNG LLP
Fort Lauderdale, Florida
March 14, 2006

REPORT OF INDEPENDENT REGISTERED CERTIFIED PUBLIC ACCOUNTANTS

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

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting, that The GEO Group, Inc. maintained effective internal control over financial reporting as of January 1, 2006, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The GEO Group, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, management's assessment that The GEO Group, Inc. maintained effective internal control over financial reporting as of January 1, 2006, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, The GEO Group, Inc. maintained, in all material respects, effective internal control over financial reporting as of January 1, 2006, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of The GEO Group, Inc. as of January 1, 2006 and January 2, 2005, and the related consolidated statements of income, shareholders' equity and comprehensive income, and cash flows for each of the three years in the period ended January 1, 2006, of The GEO Group, Inc. and our report dated March 14, 2006 expressed an unqualified opinion thereon.

ERNST &YOUNG LLP
Fort Lauderdale, Florida
March 14, 2006

CONSOLIDATED STATEMENTS OF INCOME

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

	2005	2004	2003
(In thousands, except per share data)			
Revenues	\$ 612,900	\$ 593,994	\$ 549,238
Operating Expenses	540,128	495,226	467,018
Depreciation and Amortization	15,876	13,898	13,341
General and Administrative Expenses	48,958	45,879	39,379
Operating Income	7,938	38,991	29,500
Interest Income	9,154	9,568	6,853
Interest Expense	(23,016)	(22,138)	(17,896)
Write-off of Deferred Financing Fees from Extinguishment of Debt	(1,360)	(317)	(1,989)
Gain on Sale of UK Joint Venture	—	—	56,094
Income (loss) Before Income Taxes, Minority Interest, Equity in Earnings of Affiliates, and Discontinued Operations	(7,284)	26,104	72,562
Provision (benefit) for Income Taxes	(11,826)	8,231	36,852
Minority Interest	(742)	(710)	(645)
Equity in Earnings of Affiliates, (net of income tax provision (benefit) of \$(2,016), \$0, and \$634)	2,079	—	1,310
Income from Continuing Operations	5,879	17,163	36,375
Income (loss) from discontinued operations, (net of tax (benefit) provision of \$895, \$(181), and \$1,544)	1,127	(348)	3,644
Net Income	\$ 7,006	\$ 16,815	\$ 40,019
Weighted Average Common Shares Outstanding:			
Basic	9,580	9,384	15,618
Diluted	10,010	9,738	15,829
Earnings (loss) per Common Share:			
Basic:			
Income from continuing operations	\$ 0.61	\$ 1.83	\$ 2.33
Income (loss) from discontinued operations	0.12	(0.04)	0.23
Net income per share-basic	\$ 0.73	\$ 1.79	\$ 2.56
Diluted:			
Income from continuing operations	\$ 0.59	\$ 1.77	\$ 2.30
Income (loss) from discontinued operations	0.11	(0.04)	0.23
Net income per share-diluted	\$ 0.70	\$ 1.73	\$ 2.53

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

CONSOLIDATED BALANCE SHEETS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

	2005	2004
(In thousands, except per share data)		
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 57,094	\$ 92,005
Restricted cash	8,882	—
Short-term investments	—	10,000
Accounts receivable, less allowance for doubtful accounts of \$224 and \$907	127,612	90,386
Deferred income tax asset	19,755	12,891
Other current assets	15,826	12,083
Current assets of discontinued operations	123	5,401
Total current assets	229,292	222,766
Restricted Cash	17,484	3,908
Property and Equipment, Net	282,236	190,865
Assets Held for Sale	5,000	—
Direct Finance Lease Receivable	38,492	42,953
Goodwill and Other Intangible Assets, Net	52,127	615
Other Non Current Assets	14,880	13,282
Other Assets of Discontinued Operations	—	5,937
	\$ 639,511	\$ 480,326
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	\$ 27,762	\$ 21,039
Accrued payroll and related taxes	26,985	24,595
Accrued expenses	70,177	53,104
Current portion of deferred revenue	1,894	1,844
Current portion of capital lease obligations, long-term debt and non-recourse debt	8,441	13,736
Current liabilities of discontinued operations	1,260	3,160
Total current liabilities	136,519	117,478
Deferred Revenue	3,267	4,320
Deferred Tax Liability	2,085	8,466
Minority Interest	1,840	1,194
Other Non Current Liabilities	19,601	19,978
Capital Lease Obligations	17,072	—
Long-Term Debt	219,254	186,198
Non-Recourse Debt	131,279	42,953
Commitments and Contingencies		
Shareholders' Equity		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, none issued or outstanding	—	—
Common stock, \$0.01 par value, 30,000,000 shares authorized, 21,691,143 and 21,507,391 issued and 9,691,143 and 9,507,391 outstanding	97	95
Additional paid-in capital	70,784	67,005
Retained earnings	171,666	164,660
Accumulated other comprehensive loss	(2,073)	(141)
Treasury stock 12,000,000 shares	(131,880)	(131,880)
Total shareholders' equity	108,594	99,739
	\$ 639,511	\$ 480,326

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

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

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

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

1. Summary of Business Operations and Significant Accounting Policies

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

On November 4, 2005, the Company completed the acquisition of Correctional Services Corporation (CSC), a Florida-based provider of privatized jail, community corrections and alternative sentencing services. Management of the Company believes the acquisition is an excellent strategic fit, will have positive impact on earnings and broaden our existing client base. The acquisition was completed through the merger (the "Merger") of CSC into GEO Acquisition, Inc., a wholly owned subsidiary of the Company. Under the terms of the Merger, the Company acquired for cash, 100% of the 10.2 million outstanding shares of CSC common stock for \$6.00 per share or approximately \$62.1 million. As a result of the Merger, GEO will become responsible for supervising the operation of the sixteen adult correctional and detention facilities, totaling 8,037 beds, formerly run by CSC. Immediately following the purchase of CSC, the Company sold Youth Services International, Inc., the former juvenile services division of CSC, for \$3.75 million, \$1.75 million of which was paid in cash and the remaining \$2.0 million of which was paid in the form of a promissory note accruing interest at a rate of 6% per annum. Principal and interest are due quarterly. The annual maturities are \$0.6 million in 2006, \$0.7 million in 2007, and \$0.7 million in 2008.

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

Fiscal Year

The Company's fiscal year ends on the Sunday closest to the calendar year end. Fiscal year 2004 included 53 weeks. Fiscal years 2005 and 2003 each included 52 weeks. The Company reports the results of its South African equity affiliate, South African Custodial Services Pty. Limited, ("SACS"), and its consolidated South African entity, South African Custodial Management Pty. Limited ("SACM") on a calendar year end, due to the availability of information.

Basis of Presentation

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

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. While the Company believes that such estimates are fair when considered in conjunction with the consolidated financial statements taken as a whole, the actual amounts of such estimates, when known, will vary from these estimates. If actual results significantly differ from the Company's estimates, the Company's financial condition and results of operations could be materially impacted.

Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, restricted cash, short-term investments, accounts receivable, accounts payable and accrued expenses approximate their fair value due to the short maturity of these items. The carrying value of the Company's long-term debt related to its Senior Credit Facility (See Note 10) and non-recourse debt approximates fair value based on the variable interest rates on the debt. For the Company's 81/4% Senior Unsecured Notes, the stated value and fair value based on quoted market rates was \$150.0 million and \$147.4 million, respectively, at January 1, 2006. For the Company's non-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

recourse debt related to CSC, the stated value and fair value based on quoted market rates was \$102.2 million and \$98.4 million, respectively, at January 1, 2006.

Cash and Cash Equivalents

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

Short Term Investments

Short-term investments consist of auction rate securities classified as available-for-sale, which are stated at estimated fair value. These investments are on deposit with a major financial institution. Unrealized gains and losses, net of tax, are computed on the first-in first-out basis and are reported as a separate component of accumulated other comprehensive income (loss) in shareholders' equity until realized. There were no unrealized gains or losses at January 1, 2006 and January 2, 2005. The Company had no short-term investments at January 1, 2006.

Accounts Receivable

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

Inventories

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

Restricted Cash

The Company had \$8.9 million in current restricted cash and cash equivalents and \$17.5 million in long-term restricted cash equivalents and investments. The balances in those accounts are attributable primarily to amounts held in escrow or in trust in connection with the 1,020-bed South Texas Detention Complex in Frio County, Texas and the 890-bed Northwest Detention Center in Tacoma, Washington.

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

Costs of Acquisition Opportunities

Internal costs associated with a business combination are expensed as incurred. Direct and incremental costs related to successful negotiations where we are the acquiring company are capitalized as part of the cost of the acquisition. As of January 1, 2006 the Company had no capitalized costs. During 2004, the Company wrote off approximately \$1.3 million of costs. Costs associated with unsuccessful negotiations are expensed when it is probable that the acquisition will not occur.

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over 2 to 40 years. Equipment and furniture and fixtures are depreciated over 3 to 7 years. Accelerated methods of depreciation are generally used for income tax purposes. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvement or the term of the lease. The Company performs ongoing evaluations of the estimated useful lives of the proper-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

ty and equipment for depreciation purposes. The estimated useful lives are determined and continually evaluated based on the period over which services are expected to be rendered by the asset. Maintenance and repairs are expensed as incurred. Interest is capitalized in connection with the construction of correctional and detention facilities. Capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life. No interest cost was capitalized in 2005 or 2004.

Assets Held Under Capital Leases

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

Long-Lived Assets

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

Goodwill and Other Intangible Assets

The Company's goodwill at January 1, 2006 consisted of \$35.3 million related to the November 4, 2005 acquisition of CSC (See Note 2: Acquisition) and \$0.6 million related to its Australian subsidiary and at January 2, 2005 consisted of \$0.6 million associated with its Australian subsidiary. Goodwill related to CSC and Australia is included in the correction and detention facility segment. With the adoption of Financial Accounting Standard ("FAS") No. 142, the Company's goodwill is no longer amortized, but is subject to an annual impairment test related to the goodwill associated with the Australian subsidiary. There was no impairment of goodwill as a result of adopting FAS No. 142, "Goodwill and Other Intangible Assets" or as a result of the annual impairment test completed during the fourth quarter of 2005 and 2004 related to goodwill associated with its Australian subsidiary. The annual impairment test for the goodwill related to the acquisition of CSC will be on the first day of the fourth quarter.

Acquired intangible assets are separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, rented or exchanged, regardless of the Company's intent to do so. The Company's intangible assets were recorded in connection with the acquisition of CSC and have finite lives ranging from 4-20 years and are amortized using a straight-line method. The Company reviews finite-lived intangible assets for impairment whenever an event occurs or circumstances change which indicate that the carrying amount of such assets may not be fully recoverable. See Note 8.

Idle Facilities

The Company has entered into ten year non cancelable operating leases with CentraCore Properties Trust, or CPV, a Maryland real estate investment trust for eleven facilities with initial terms that expire at various times beginning in April 2008 and extending through 2016. In the event that the Company's facility management contract for one of these leased facilities is terminated, the Company would remain responsible for payments to CPV on the underlying lease. The Company will account for idle periods under any such lease in accordance with FAS No. 146 "Accounting for Costs Associated with Exit or Disposal Activities." Specifically, the Company reviews its estimate for sublease income and records a charge for the difference between the net present value of the sublease income and the lease expense over the remaining term of the lease.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

Variable Interest Entities

In January 2003, the Financial Accounting Standards Board ("FASB") issued Financial Interpretation FIN No. 46, "Consolidation of Variable Interest Entities," which addressed consolidation by a business of variable interest entities in which it is the primary beneficiary. In December 2003, the FASB issued FIN No. 46R which replaced FIN No. 46. Our 50% owned South African joint venture in South African Custodial Services Pty. Limited, which the Company refers to as SACS, is a variable interest entity. The Company determined that it is not the primary beneficiary of SACS and as a result it is not required to consolidate SACS under FIN 46R. The Company accounts for SACS as an equity affiliate. SACS was established in 2001, to design, finance and build the Kutama Sinthumule Correctional Center. Subsequently, SACS was awarded a 25 year contract to design, construct, manage and finance a facility in Louis Trichardt, South Africa. SACS, based on the terms of the contract with government, was able to obtain long term financing to build the prison. The financing is fully guaranteed by the government, except in the event of default, for which it provides an 80% guarantee. Separately, SACS entered into a long term operating contract with South African Custodial Management (Pty) Limited ("SACM") to provide security and other management services and with SACS' joint venture partner to provide purchasing, programs and maintenance services upon completion of the construction phase, which concluded in February 2002. The Company's maximum exposure for loss under this contract is \$24.1 million, which represents the Company's initial investment and the guarantees discussed in Note 10.

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

Deferred Revenue

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

Revenue Recognition

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

Project development and design revenues are recognized as earned on a percentage of completion basis measured by the percentage of costs incurred to date as compared to estimated total cost for each contract. This method is used because we consider costs incurred to date to be the best available measure of progress on these contracts. Provisions for estimated losses on uncompleted contracts and changes to cost estimates are made in the period in which we determine that such losses and changes are probable. Typically, the Company enters into fixed price contracts and does not perform additional work unless approved change orders are in place. Costs attributable to unapproved change orders are expensed in the period in which the costs are incurred

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if the Company believes that it is not probable that the costs will be recovered through a change in the contract price. If the Company believes that it is probable that the costs will be recovered through a change in contract price, costs related to unapproved change orders are expensed in the period in which they are incurred, and contract revenue is recognized to the extent of the costs incurred. Revenue in excess of the costs attributable to unapproved change orders is not recognized until the change order is approved. Contract costs include all direct material and labor costs and those indirect costs related to contract performance. Changes in job performance, job conditions, and estimated profitability, including those arising from contract penalty provisions, and final contract settlements, may result in revisions to estimated costs and income, and are recognized in the period in which the revisions are determined.

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

Income Taxes

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

Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding. In the computation of diluted earnings per share, the weighted-average number of common shares outstanding is adjusted for the dilutive effect of shares issuable upon exercise of stock options calculated using the treasury stock method.

Direct Finance Leases

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

Reserves for Insurance Losses

Claims for which the Company is insured arising from its U.S. operations that have an occurrence date of October 1, 2002 or earlier are handled by TWC and are fully insured up to an aggregate limit of between \$25.0 million and \$50.0 million, depending on the nature of the claim. With respect to claims for which the Company is insured arising after October 1, 2002, the Company maintains a general liability policy for all U.S. operations with \$52.0 million per occurrence and in the aggregate. On October 1, 2004 the Company increased its deductible on this general liability policy from \$1.0 million to \$3.0 million for each claim which occurs after October 1, 2004. The Company also maintains insurance in amounts the Company's management deems adequate to cover property and casualty risks, workers' compensation, medical malpractice and automobile liability. The Company's Australian subsidiary is required to carry tail insurance through 2011 related to a discontinued contract. In addition, the Company carries various types of insurance with respect to its operations in South Africa and Australia.

Since the Company's insurance policies generally have high deductible amounts (including a \$3.0 million per claim deductible under our general liability policy), losses are recorded as reported and a provision is made to cover losses incurred but not report-

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ed. Loss reserves are undiscounted and are computed based on independent actuarial studies. The Company's management uses judgments in assessing loss estimates based on actuarial studies, which include actual claim amounts and loss development considering historical and industry experience. If actual losses related to insurance claims significantly differ from our estimates, the Company's financial condition and results of operations could be materially impacted.

Debt Issuance Costs

Debt issuance costs totaling \$7.0 million and \$5.9 million at January 1, 2006, and January 2, 2005, respectively, are included in other non current assets in the consolidated balance sheets and are amortized into interest expense using the effective interest method, over the term of the related debt.

Comprehensive Income

The Company's comprehensive income is comprised of net income, foreign currency translation adjustments, unrealized gain (loss) on derivative instruments, minimum pension liability adjustment, and a reclassification adjustment for losses on UK interest rate swaps related to the sale of the UK joint venture in the Consolidated Statements of Shareholders' Equity and Comprehensive Income.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, trade accounts receivable, short-term investments, direct finance lease receivable, long-term debt and financial instruments used in hedging activities. The Company's cash management and investment policies restrict investments to low-risk, highly liquid securities, and the Company performs periodic evaluations of the credit standing of the financial institutions with which it deals. As of January 1, 2006, and January 2, 2005, the Company had no significant concentrations of credit risk except as disclosed in Note 17.

Foreign Currency Translation

The Company's foreign operations use their local currencies as their functional currencies. Assets and liabilities of the operations are translated at the exchange rates in effect on the balance sheet date and shareholders' equity is translated at historical rates. Income statement items are translated at the average exchange rates for the year. The impact of foreign currency fluctuation is included in shareholders' equity as a component of accumulated other comprehensive (loss) income and totaled \$(0.9) million at January 1, 2006 and \$2.5 million as of January 2, 2005.

Financial Instruments

In accordance with FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its related interpretations and amendments, the Company records derivatives as either assets or liabilities on the balance sheet and measures those instruments at fair value. For derivatives that are designed as and qualify as effective cash flow hedges, the portion of gain or loss on the derivative instrument effective at offsetting changes in the hedged item is reported as a component of accumulated other comprehensive income and reclassified into earnings when the hedged transaction affects earnings. Total accumulated other comprehensive loss related to these cash flow hedges was \$0.3 million and \$1.7 million as of January 1, 2006 and January 2, 2005, respectively. For derivative instruments that are designated as and qualify as effective fair value hedges, the gain or loss on the derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk is recognized in current earnings as interest income (expense) during the period of the change in fair values.

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

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Accounting for Stock-Based Compensation

The Company applies Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" in accounting for stock-based employee compensation arrangements whereby compensation cost related to stock options is generally not recognized in determining net income. Had compensation cost for the Company's stock option plans been determined pursuant to Statement of Financial Accounting Standards No. 123, "Accounting for Stock Based Compensation," the Company's net income and earnings per share would have decreased accordingly. Using the Black-Scholes option pricing model for all options granted, the Company's pro forma net income, pro forma earnings per share and pro forma weighted average fair value of options granted, with related assumptions, are as follows for the years ended January 1, 2006, January 2, 2005 and December 28, 2003 (in thousands, except per share data):(1)

Pro Forma Disclosures	2005	2004	2003
(In thousands, except per share data)			
Net income	\$ 7,006	\$ 16,815	\$ 40,019
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(397)	(765)	(935)
Pro forma net income	\$ 6,609	\$ 16,050	\$ 39,084
Basic earnings per share			
As reported	\$ 0.73	\$ 1.79	\$ 2.56
Pro forma	\$ 0.69	\$ 1.71	\$ 2.50
Diluted earnings per share			
As reported	\$ 0.70	\$ 1.73	\$ 2.53
Pro forma	\$ 0.66	\$ 1.65	\$ 2.47
Risk free interest rates	3.96%	3.25%	1.73%-2.92%
Expected lives	3-7 years	3-7 years	3-7 years
Expected volatility	39%	40%	49%
Expected dividend	—	—	—

(1)See Note 15 for more information regarding the Company's stock option plans.

In December 2004, the FASB issued FAS 123R, "Share-Based Payment," a revision of FAS 123. In March 2005, the SEC issued Staff Accounting Bulletin No. 107 (SAB 107) regarding its interpretation of FAS 123R. The standard requires companies to expense the grant-date fair value of stock options and other equity-based compensation issued to employees. In accordance with the revised statement and related guidance, the Company will begin to recognize the expense attributable to stock options granted or vested subsequent to January 1, 2006 using the modified prospective method in the first quarter of 2006. The Company will continue using the Black-Scholes valuation model and straight-line amortization of compensation expense over the requisite service period of the grant. The Company expects compensation expense during 2006 related to stock based awards consistent with the pro forma disclosures under FAS 123 above for the year ended January 1, 2006.

Recent Accounting Pronouncements

In May 2005, FASB issued FAS No. 154, "Accounting for Changes and Error Corrections". FAS No. 154 requires retrospective application to prior periods' financial statements of changes in accounting principle. It also requires that the new accounting principle be applied to the balances of assets and liabilities as of the beginning of the earliest period for which retrospective application is practicable and that a corresponding adjustment be made to the opening balance of retained earnings for that period rather than being reported in an income statement. The statement was effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of FAS No. 154 did not have a material effect on the Company's consolidated financial position or results of operations.

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In March 2005, the Financial Accounting Standards Board issued Interpretation No. 47 ("FIN 47"), Accounting for Conditional Asset Retirement Obligations. FIN 47 clarifies that an entity must record a liability for a "conditional" asset retirement obligation if the fair value of the obligation can be reasonably estimated. The provision was effective no later than the end of fiscal years ending after December 15, 2005. The application of FIN 47 did not have a material effect on the Company's financial position, results of operations, and cash flows.

2. Acquisition

Under the purchase method of accounting, the purchase price for CSC was allocated to CSC's net tangible and intangible assets based on their estimated fair values as of the date of the completion of the acquisition. The aggregate consideration for this transaction was approximately \$79.3 million, comprised of approximately \$62.1 million in cash to acquire 100% of the 10.2 million shares of outstanding common stock, approximately \$7.0 million in payments of CSC debt and direct transactions costs of approximately \$10.2 million. Independent valuation specialists have been engaged to perform valuations to assist in the determination of the fair values of a significant portion of CSC's net assets. Immediately following the purchase of CSC, the Company sold Youth Services International, Inc., the former juvenile services division of CSC, for \$3.75 million, \$1.75 million of which was paid in cash and the remaining \$2.0 million of which was paid in the form of a promissory note accruing interest at a rate of 6% per annum. Principal and interest are due quarterly. The annual maturities are \$0.6 million in 2006, \$0.7 million in 2007, and \$0.7 million in 2008. The purchase price allocations related to property and equipment, other assets, capital lease obligations and certain tax elections are still tentative as the Company has not received information from our independent valuation specialists. This information is expected to be received in the first quarter of 2006. The purchase price allocation excludes the assets of Youth Services International, Inc.

The preliminary allocation of the purchase price is summarized below (in thousands):

	Purchase Price Allocation	Asset Life
Current Assets	\$ 44,391	
Property and Equipment	110,150	Various
Intangible assets	16,520	4-20 years
Goodwill	35,317	Indefinite
Other non-current assets	17,566	
Total Assets acquired	223,934	
Current liabilities	23,565	
Other non-current liabilities	6,052	
Debt and capital lease obligations	115,027	
Total liabilities assumed	144,644	
Net assets acquired, including direct transaction costs	\$ 79,290	

None of the goodwill recorded in relation to this acquisition is deductible for tax purposes. Identifiable intangible assets purchased in the acquisition and their weighted average lives are as follows (in thousands):

	Description	Asset Life
Facility management contracts	\$ 15,050	7-20 years
Covenants not to compete	1,470	4 years
Total	\$ 16,520	

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The fair values used in determining the purchase price allocation for the intangible assets were based on independent appraisal.

The \$35.3 million of goodwill related to the acquisition was assigned to the Correctional and Detention Facilities segment. See Note 17 for segment information.

The results of operations of CSC are included in the Company's results of operations beginning after November 4, 2005. CSC is part of the Company's Correctional and Detention Facilities reportable segment. The following unaudited pro forma information combines the consolidated results of operations of the Company and CSC as if the acquisitions had occurred at the beginning of fiscal year 2004 and excludes the operations of Youth Services International, Inc. (in thousands, except per share data):

	2005	2004
Revenues	\$ 692,545	\$ 670,563
Income from continuing operations	5,719	21,662
Net income	4,402	9,571
Net income per share — basic	\$ 0.46	\$ 1.02
Net income per share — diluted	\$ 0.44	\$ 0.98

3. Discontinued Operations

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

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

On January 1, 2006, the Company completed the sale of Atlantic Shores Hospital, a 72 bed private mental health hospital which the Company owned and operated since 1997 for approximately \$11.5 million. The Company recognized a gain on the sale of this transaction of approximately \$1.6 million or \$1.0 million net of tax. Pre-tax profit related to the 72 bed private mental health hospital was \$0.1 million, \$(0.2) million and \$0.2 million in 2005, 2004 and 2003 respectively. The accompanying consolidated financial statements and notes reflect the operations of the hospital and the related sale as a discontinued operation.

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

	2005	2004	2003
		(In thousands)	
Revenues — DIMIA	\$ 20	\$ 6,040	\$ 62,673
Revenues — Auckland	7,256	12,940	10,492
Revenues — Atlantic Shores	8,602	7,614	7,711

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4. Property and Equipment

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

	Useful Life	2005	2004
	(Years)		
		(In thousands)	
Land	—	\$ 6,195	\$ 2,699
Buildings and improvements	2 to 40	258,008	168,855
Leasehold improvements	1 to 15	45,356	40,126
Equipment	3 to 7	32,541	23,106
Furniture and fixtures	3 to 7	9,309	3,432
		\$ 351,409	\$ 238,218
Less accumulated depreciation and amortization		(69,173)	(47,353)
		\$ 282,236	\$ 190,865

At January 1, 2006, the Company had \$17.3 million of assets recorded under capital leases including \$16.6 million related to buildings and improvements, \$0.6 million related to equipment and \$0.1 million related to leasehold improvements with accumulated amortization of \$0.1 million. There were no assets under capital leases at January 2, 2005.

5. Assets Held for Sale

In conjunction with the acquisition of CSC, the Company acquired a building and assets associated with a program that had been discontinued by CSC in October 2003. These assets meet the criteria to be classified as held for sale per the guidance of FAS No. 144 and have been recorded at their net realizable value at November 4, 2005. No depreciation has been recorded related to these assets in accordance with FAS No. 144.

6. Investment in Direct Finance Leases

The Company's investment in direct finance leases relates to the financing and management of one Australian facility. The Company's wholly-owned Australian subsidiary financed the facility's development with long-term debt obligations, which are non-recourse to the Company. The Company's financial statements reflect the consolidated Australian's subsidiary's direct finance lease receivable from the state government and related non-recourse debt each totaling approximately \$40.3 million and \$44.7 as of January 1, 2006 and January 2, 2005, respectively.

The future minimum rentals to be received are as follows:

Fiscal Year	Annual Repayment
	(In thousands)
2006	\$ 5,630
2007	5,660
2008	5,705
2009	5,744
2010	5,792
Thereafter	39,433
Total minimum obligation	\$ 67,964
Less unearned interest income	(27,670)
Less current portion of direct finance lease	(1,802)
Investment in direct finance lease	\$ 38,492

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7. Derivative Financial Instruments

Effective September 18, 2003, the Company entered into interest rate swap agreements in the aggregate notional amount of \$50.0 million. The Company has designated the swaps as hedges against changes in the fair value of a designated portion of the Notes due to changes in underlying interest rates. Changes in the fair value of the interest rate swaps are recorded in earnings along with related designated changes in the value of the Notes. The agreements, which have payment and expiration dates and call provisions that coincide with the terms of the Notes, effectively convert \$50.0 million of the Notes into variable rate obligations. Under the agreements, the Company receives a fixed interest rate payment from the financial counterparties to the agreements equal to 8.25% per year calculated on the notional \$50.0 million amount, while the Company makes a variable interest rate payment to the same counterparties equal to the six-month London Interbank Offered Rate, ("LIBOR") plus a fixed margin of 3.45%, also calculated on the notional \$50.0 million amount. As of January 1, 2006 and January 2, 2005, the fair value of the swaps totaled approximately \$(1.1) million and \$0.7 million and is included in other non-current assets or liabilities and as an adjustment to the carrying value of the Notes in the accompanying balance sheets. There was no material ineffectiveness of the Company's interest rate swaps for the fiscal year ended January 1, 2006.

The Company's Australian subsidiary is a party to an interest rate swap agreement to fix the interest rate on the variable rate non-recourse debt to 9.7%. The Company has determined the swap to be an effective cash flow hedge. Accordingly, the Company records the value of the interest rate swap in accumulated other comprehensive income, net of applicable income taxes. The total value of the swap liability as of January 1, 2006 and January 2, 2005 was approximately \$0.4 million and \$2.5 million, respectively, and is recorded as a component of other liabilities in the accompanying consolidated financial statements. There was no material ineffectiveness of the Company's interest rate swaps for the fiscal years presented. The Company does not expect to enter into any transactions during the next twelve months which would result in the reclassification into earnings of losses associated with this swap currently reported in accumulated other comprehensive loss.

The Company's former 50% owned joint venture operating in the United Kingdom was a party to several interest rate swaps to fix the interest rate on its variable rate credit facility. The Company previously determined the swaps to be effective cash flow hedges and upon the initial adoption of FAS No. 133 on January 1, 2001, the Company recognized a \$12.1 million reduction of shareholders' equity. In fiscal 2003, in connection with the sale of the 50% owned joint venture in the UK, the Company reclassified the remaining balance of approximately \$13.3 million from accumulated other comprehensive loss into earnings as a reduction of the gain on sale of the UK joint venture.

8. Goodwill and Other Intangible Assets, Net

As of January 1, 2006 and January 2, 2005, the Company had \$35.9 million and \$0.6 million of goodwill, respectively.

Intangible assets, net consisted of the following (in thousands):

	Useful Life in Years	2005
Facility Management Contracts	7-20	\$ 15,050
Covenants not to compete	4	1,470
		\$ 16,520
Less Accumulated Amortization		(289)
		\$ 16,231

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Amortization expense was \$0.3 million for the fiscal year ended 2005. Amortization is recognized on a straight-line basis over the estimated useful life of the intangible assets. Estimated amortization expense for fiscal 2006 through fiscal 2010 and thereafter are as follows:

Fiscal Year	Expense Amortization
	(In thousands)
2006	\$ 1,754
2007	1,754
2008	1,754
2009	1,693
2010	1,387
Thereafter	7,889
	\$ 16,231

9. Accrued Expenses

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

	2005	2004
Accrued interest	\$ 7,193	\$ 5,476
Accrued bonus	4,369	5,608
Accrued insurance	25,923	15,686
Accrued taxes	882	1,522
Jena idle facility lease reserve	8,257	5,847
Other	23,553	18,965
Total	\$ 70,177	\$ 53,104

10. Debt

Debt consisted of the following (dollars in thousands):

	2005	2004
Capital Lease Obligations	\$ 17,755	\$ —
Senior Credit Facility:		
Term loan	\$ 74,813	\$ 51,521
Senior 8¼% Notes:		
Notes Due in 2013	\$ 150,000	\$ 150,000
Discount on Notes	(3,735)	(4,063)
Swap on Notes	(1,074)	746
Total Senior 8¼% Notes	\$ 145,191	\$ 146,683
Non Recourse Debt:		
Non recourse debt	\$ 142,479	\$ 44,683
Discount on bonds	(4,493)	—
Total non recourse debt	137,986	44,683
Other debt	301	—
Total debt	\$ 376,046	\$ 242,887
Current portion of capital lease obligations, long-term debt and non-recourse debt	(8,441)	(13,736)
Capital lease obligations	(17,072)	—
Non recourse debt	(131,279)	(42,953)
Long term debt	\$ 219,254	\$ 186,198

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The Senior Credit Facility

On September 14, 2005, the Company amended its senior secured credit facility (the "Senior Credit Facility"), to consist of a \$75 million, six-year term-loan bearing interest at London Interbank Offered Rate, ("LIBOR") plus 2.00%, and a \$100 million, five-year revolving credit facility bearing interest at LIBOR plus 2.00%. The Company used the borrowings under the Senior Credit Facility to fund general corporate purposes and to finance the acquisition of Correctional Services Corporation ("CSC") for approximately \$62 million plus transaction-related costs. The acquisition of CSC closed in the fourth quarter of 2005. As of January 1, 2006, the Company had borrowings of \$74.8 million outstanding under the term loan portion of the Senior Credit Facility, no amounts outstanding under the revolving portion of the Senior Credit Facility, and \$43.7 million outstanding in letters of credit under the revolving portion of the Senior Credit Facility. As of January 1, 2006 the Company had \$56.3 million available for borrowings under the revolving portion of the Senior Credit Facility.

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

Indebtedness under the Revolving Credit Facility bears interest at the Company's option at the base rate plus a spread varying from 0.50% to 1.25% (depending upon a leverage-based pricing grid set forth in the Senior Credit Facility), or at LIBOR plus a spread, varying from 1.50% to 2.25% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). As of January 1, 2006, there were no borrowings outstanding under the Revolving Credit Facility. However, new borrowings would bear interest at LIBOR plus 2.00% or at the base rate plus 1.00%. Letters of credit outstanding under the revolving portion of the Senior Credit Facility bear interest at 1.50% to 2.25% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). Available capacity under the revolving portion of the Senior Credit Facility bears interest at 0.38% to 0.5%. The Term Loan Facility bears interest at the Company's option at the base rate plus a spread of 0.75% to 1.00%, or at LIBOR plus a spread, varying from 1.75% to 2.00% (depending upon a leverage-based pricing grid, as defined in the Senior Credit Facility). Borrowings under the Term Loan Facility currently bear interest at LIBOR plus a spread of 2.00%. If an event of default occurs under the Senior Credit Facility, (i) all LIBOR rate loans bear interest at the rate which is 2.00% in excess of the rate then applicable to LIBOR rate loans until the end of the applicable interest period and thereafter at a rate which is 2.00% in excess of the rate then applicable to base rate loans, and (ii) all base rate loans bear interest at a rate which is 2.00% in excess of the rate then applicable to base rate loans.

The Senior Credit Facility contains financial covenants which require the Company to maintain the following ratios, as computed at the end of each fiscal quarter for the immediately preceding four quarter-period: a total leverage ratio equal to or less than 3.50 to 1.00 through December 30, 2006, which reduces thereafter in 0.50 increments to 3.00 to 1.00 for the period from December 31, 2006 through December 27, 2007 and thereafter; a senior secured leverage ratio equal to or less than 2.50 to 1.00; and a fixed charge coverage ratio equal to or less than 1.05 to 1.00 until December 30, 2006, and thereafter a ratio of 1.10 to 1.00. In addition, the Senior Credit Facility prohibits the Company from making capital expenditures greater than \$19.0 million in the aggregate during any fiscal year until 2009 and \$24.0 million during each of the years 2010 and 2011, provided that to the extent that the Company's capital expenditures during any fiscal year are less than the limit, such amount will be added to the maximum amount of capital expenditures that the Company can make in the following year.

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

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ments that contain negative pledges on the Company's assets or covenants more restrictive than contained in the Senior Credit Facility, (xii) alter the business the Company conducts, and (xiii) materially impair the Company's lenders' security interests in the collateral for the Company's loans. The covenants in the Senior Credit Facility can substantially restrict the Company's business operations.

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

Senior 8^{1/4}% Notes

To facilitate the completion of the purchase of the 12 million shares from Group 4 Falck, the Company amended the Senior Credit Facility and issued \$150.0 million aggregate principal amount, ten-year, 8 1/4% senior unsecured notes, ("the Notes"), in a private placement pursuant to Rule 144A of the Securities Act of 1933, as amended. The Notes are general, unsecured, senior obligations. Interest is payable semi-annually on January 15 and July 15 at 8 1/4%. The Notes are governed by the terms of an Indenture, dated July 9, 2003, between the Company and the Bank of New York, as trustee, referred to as the Indenture. Under the terms of the Indenture, at any time on or prior to July 15, 2006, the Company may redeem up to 35% of the Notes with the proceeds from equity offerings at 108.25% of the principal amount to be redeemed plus the payment of accrued and unpaid interest, and any applicable liquidated damages. Additionally, after July 15, 2008, the Company may redeem, at the Company's option, all or a portion of the Notes plus accrued and unpaid interest at various redemption prices ranging from 104.125% to 100.000% of the principal amount to be redeemed, depending on when the redemption occurs. The Indenture contains covenants that limit the Company's ability to incur additional indebtedness, pay dividends or distributions on its common stock, repurchase its common stock, and prepay subordinated indebtedness. The Indenture also limits the Company's ability to issue preferred stock, make certain types of investments, merge or consolidate with another company, guarantee other indebtedness, create liens and transfer and sell assets. On June 25, 2004, as required by the terms of the Indenture governing the Notes, the Company used \$43.0 million of the net proceeds from the sale of PCG to permanently reduce the Senior Credit Facility, and wrote off approximately \$0.3 million in deferred financing costs related to this payment.

The Company is in compliance with all of the covenants of the Indenture governing the notes as of January 1, 2006.

Non-Recourse Debt

South Texas Detention Complex

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

Included in non-current restricted cash equivalents and investments is \$12.2 million as of January 1, 2006 as funds held in trust with respect to the STLDC for debt service and other reserves.

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Northwest Detention Center

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

Included in non-current restricted cash equivalents and investments is \$1.3 million as of January 1, 2006 as funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.

Australia

In connection with the financing and management of one Australian facility, our wholly owned Australian subsidiary financed the facility's development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to us. We have consolidated the subsidiary's direct finance lease receivable from the state government and related non-recourse debt each totaling approximately \$40.3 million and \$44.7 million as of January 1, 2006 and January 2, 2005, respectively. As a condition of the loan, we are required to maintain a restricted cash balance of AUD 5.0 million, which, at January 1, 2006, was approximately \$3.7 million. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria.

As of January 1, 2006, the Notes are reflected net of the original issuer's discount of approximately \$3.7 million which is being amortized over the ten year term of the Notes using the effective interest method.

Fiscal Year	Capital Leases	Long Term Debt	Non Recourse	Total Annual Repayment
(In thousands)				
2006	\$ 2,087	\$ 1,051	\$ 6,707	\$ 9,845
2007	2,135	750	11,272	14,157
2008	2,119	750	11,899	14,768
2009	1,975	750	12,606	15,331
2010	1,909	18,375	13,262	33,546
Thereafter	22,580	203,438	86,733	312,751
	<u>\$ 32,805</u>	<u>\$ 225,114</u>	<u>\$ 142,479</u>	<u>\$ 400,398</u>
Original issuer’s discount	—	(3,735)	(4,493)	(8,228)
Current portion	(683)	(1,051)	(6,707)	(8,441)
Interest imputed on Capital Leases	(15,050)	—	—	(15,050)
Swap	—	(1,074)	—	(1,074)
Non current portion	<u>\$ 17,072</u>	<u>\$ 219,254</u>	<u>\$ 131,279</u>	<u>\$ 367,605</u>

At January 1, 2006 the Company also had outstanding eleven letters of guarantee totaling approximately \$6.5 million under separate international facilities.

Guarantees

In connection with the creation of SACS, the Company entered into certain guarantees related to the financing, construction and operation of the prison. The Company guaranteed certain obligations of SACS under its debt agreements up to a maximum amount of 60.0 million South African Rand, or approximately \$9.5 million to SACS' senior lenders through the issuance of let-

ters of credit. Additionally, SACS is required to fund a restricted account for the payment of certain costs in the event of contract termination. The Company has guaranteed the payment of 50% of amounts which may be payable by SACS into the restricted account and provided a standby letter of credit of 6.5 million South African Rand, or approximately \$1.0 million as security for the Company's guarantee. The Company's obligations under this guarantee expire upon SACS' release from its obligations in respect of the restricted account under its debt agreements. No amounts have been drawn against these letters of credit, which are included in the Company's outstanding letters of credit under its Revolving Credit Facility.

The Company has agreed to provide a loan of up to 20.0 million South African Rand, or approximately \$3.2 million (the "Standby Facility") to SACS for the purpose of financing SACS' obligations under its contract with the South African government. No amounts have been funded under the Standby Facility, and the Company does not anticipate that such funding will ever be required by SACS. The Company's obligations under the Standby Facility expire upon the earlier of full funding or SACS' release from its obligations under its debt agreements. The lenders' ability to draw on the Standby Facility is limited to certain circumstance, including termination of the contract.

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

In connection with a design, build, finance and maintenance contract, the Company guaranteed certain potential tax obligations of a special purpose entity. The potential estimated exposure of these obligations is CAN\$2.5 million, or approximately \$2.1 million commencing in 2017. To secure this guarantee, the Company purchased Canadian dollar denominated securities with maturities matched to the estimated tax obligations in 2017 to 2021. The Company has recorded an asset and a liability equal to the current fair market value of those securities on its balance sheet.

The Company's wholly-owned Australian subsidiary financed the development of a facility and subsequent expansion in 2003, with long-term debt obligations, which are non-recourse to the Company and total \$40.3 million and \$44.7 million at January 1, 2006 and January 2, 2005, 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 January 1, 2006, was approximately \$3.7 million. This amount is included in restricted cash and the annual maturities of the future debt obligation is included in non recourse debt. The debt amortization schedule requires annual repayments of \$1.8 million in 2006, \$2.0 million in 2007, \$2.3 million in 2008, \$2.5 million in 2009, \$2.8 million in 2010 and \$28.9 million thereafter. CSC non-recourse requires annual repayments of \$4.9 million in 2006, \$9.3 million in 2007, \$9.7 million in 2008, \$10.1 million in 2009, \$10.3 million in 2010 and \$57.9 million thereafter.

11. Transactions with CentraCore Properties Trust ("CPV")

During fiscal 1998, 1999 and 2000, CPV acquired 11 correctional and detention facilities operated by the Company. There have been no purchase and sale transactions between the Company and CPV since 2000.

Simultaneous with the purchases, the Company entered into ten-year operating leases of these facilities from CPV. As the lease agreements are subject to contractual lease increases, the Company records operating lease expense for these leases on a straight-line basis over the term of the leases. Additionally, the lease contains three five-year renewal options based on fair market rental rates. The deferred unamortized net gain related to sales of the facilities to CPV at January 1, 2006, which is included in "Deferred Revenue" in the accompanying consolidated balance sheets is \$5.2 million with \$1.9 million short-term and \$3.3 million long-term. The gain is being amortized over the ten-year lease terms. The Company recorded net rental expense related to the CPV leases of \$21.6 million, \$21.0 million and \$20.0 million in 2005, 2004 and 2003, respectively, excluding the Jena rental expense (See Note 12).

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The future minimum lease commitments under the leases for these eleven facilities are as follows:

Fiscal Year	Annual Rental
	(In thousands)
2006	\$ 25,750
2007	27,292
2008	20,022
2009	10,617
2010	8,203
Thereafter	48,267
	<u>\$ 140,151</u>

The Company operates the 1,918-bed Lawton Correctional Facility in Lawton Oklahoma and leases the facility under a ten year non-cancelable operating lease from CentraCore Properties Trust (CPV). The Company completed the construction of a 300-bed expansion to the original 1,618 bed facility in 1999 and capitalized the expansion as a leasehold improvement. On May 27, 2005 the Company entered into an amended lease agreement with CPV which includes the purchase by CPV of the 300 bed expansion for \$3.5 million and an additional 600-bed expansion for \$23.0 million. The Company recognized a \$1.0 million gain on the sale of the existing 300-bed expansion which is being deferred and amortized over the new lease term. The Company accounts for the construction of the new 600-bed expansion in accordance with EITF 97-10 "The Effect of Lessee Involvement in Asset Construction" and capitalized the construction costs through the completion of construction. On January 1, 2006, the Company had capitalized \$8.9 million of construction costs. The Company expects the construction of the new 600-bed expansion to be completed sometime during the third quarter 2006, after which time a new ten year non-cancelable operating lease with CPV for the entire Lawton Correctional Facility will become effective.

In February 2005, the Company appointed a new board member who previously served on CPV's board of directors. Subsequently on February 8, 2006, the director resigned from the Company's board of directors.

12. Commitments and Contingencies

During 2000, the Company's management contract at the 276-bed Jena Juvenile Justice Center in Jena, Louisiana, which is included in the correction and detention facilities segment, was discontinued by the mutual agreement of the parties. Despite the discontinuation of the management contract, the Company remains responsible for payments on the Company's underlying lease of the inactive facility with CPV through January 2010. During the third quarter of 2005, the Company determined the alternative uses being pursued were no longer probable and as a result revised its estimated sublease income and recorded an operating charge of \$4.3 million, representing the remaining obligation on the lease through the contractual term of January 2010 for a total reserve of \$8.6 million. This \$4.3 million charge is included in the caption "Operating Expenses" in the Consolidated Statement of Income for the fiscal year ended January 1, 2006. However, the Company will continue its effort to reactivate the facility.

The Company owns the 480-bed Michigan Correctional Facility in Baldwin, Michigan, referred to as the Michigan Facility. The Company operated the Michigan Facility from 1999 until October 2005 pursuant to a management contract with the Michigan Department of Corrections, or the MDOC. Separately, the Company leased the Michigan Facility, as lessor, to the State, as lessee, under a lease with an initial term of 20 years followed by two five-year options. On September 30, 2005, the Governor of the State of Michigan announced her decision to close the Michigan Facility. As a result of the closure of the Michigan Facility, the Company's management contract with the MDOC to operate the Michigan Facility was terminated. On October 3, 2005, the Michigan Department of Management & Budget sent the Company a 60 day cancellation notice to terminate the lease for the Michigan Facility. Based in part on the language of certain provisions in the lease, the Company believes that the Governor does not have the authority to unilaterally terminate the Michigan Facility lease. As a result, in November 2005, the Company filed

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a lawsuit against the State to enforce the Company's rights under the lease. On February 24, 2006, the Ingham County Circuit Court, the trial court with jurisdiction over the case, granted summary judgment in favor of the State and against the Company and the other plaintiffs, The Village of Baldwin and Webber Township. The trial court ruled that the State lawfully cancelled the lease when the Governor exercised her line item veto of the legislative appropriation for the funding of the lease. The Company is in the process of appealing the summary judgment entered by the trial court. The Company has reviewed the Michigan Facility for impairment in accordance with FAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", and recorded an impairment charge in the fourth quarter of 2005 for \$20.9 million based on an independent appraisal of fair market value.

The Company has entered into construction contracts with the Florida Department of Management Services ("DMS") to expand the Moorehaven Correctional Facility by 235 beds, which the Company operates for DMS, and build the 1,500 bed Graceville Correctional Facility, which the Company will operate for DMS upon final completion of the construction. Payment under these construction contracts is contingent on the receipt of proceeds from bonds being issued by the state of Florida to finance the projects. Subsequent to January 1, 2006, the Company incurred approximately \$8.5 million in costs related to these projects prior to the financing being completed. We expect the financing to be completed by March 31, 2006. In the event the required financing is not completed, the Company will expense these costs during the first quarter of 2006 without an offsetting revenue source.

Operating Leases

The Company leases correctional facilities, office space, computers and vehicles under non-cancelable operating leases expiring between 2005 and 2013. The future minimum commitments under these leases exclusive of lease commitments related to CPV, are as follows:

Fiscal Year	Annual Rental
	(In thousands)
2006	\$ 11,483
2007	11,353
2008	11,063
2009	8,583
2010	5,903
Thereafter	18,343
	<u>\$ 66,728</u>

Rent expense was approximately \$24.9 million, \$14.4 million, and \$12.5 million for fiscal 2005, 2004, and 2003 respectively.

Litigation, Claims and Assessments

The Company was defending a wage and hour class action lawsuit (Salas et al v. WCC) filed on December 26, 2001 in California state court by ten current and former employees. In January 2005, this lawsuit was settled by a satisfaction of judgment and a release of all claims executed by the plaintiffs which was filed with the Superior Court of California in Kern County. As part of the settlement, the Company made a cash payment of approximately \$3.1 million and is required to provide certain non-cash considerations to current California employees who were included in the lawsuit. The non-cash considerations include a designated number of paid days off according to longevity of employment, modifications to the Company's human resources department, and changes in certain operational procedures at the Company's correctional facilities in California. The settlement encompasses all current and former employees in California through the approval date of the settlement and constitutes a full and final settlement of all actual and potential wage and hour claims against the Company in California for the period preceding July 29, 2004.

In June 2004, the Company received notice of a third-party claim for property damage incurred during 2002 and 2001 at several detention facilities that the Company's Australian subsidiary formerly operated pursuant to its discontinued operation. The

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

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

Collective Bargaining Agreements

The Company had approximately twenty percent of its workforce covered by collective bargaining agreements at January 1, 2006. Collective bargaining agreements with nine percent of employees are set to expire in less than one year.

13. Share Purchase

On July 9, 2003, the Company purchased all 12 million shares of the Company's common stock beneficially owned by Group 4 Falck, the Company's former 57% majority shareholder, for \$132.0 million in cash.

In April 1994, the Company's Board of Directors authorized 10,000,000 shares of "blank check" preferred stock. The Board of Directors is authorized to determine the rights and privileges of any future issuance of preferred stock such as voting and dividend rights, liquidation privileges, redemption rights and conversion privileges.

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14. Earnings Per Share

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

Fiscal Year	2005	2004	2003
	(In thousands, except per share data)		
Net income	\$ 7,006	\$ 16,815	\$ 40,019
Basic earnings per share:			
Weighted average shares outstanding	9,580	9,384	15,618
Per share amount	\$ 0.73	\$ 1.79	\$ 2.56
Diluted earnings per share:			
Weighted average shares outstanding	9,580	9,384	15,618
Effect of dilutive securities:			
Employee and director stock options	430	354	211
Weighted average shares assuming dilution	10,010	9,738	15,829
Per share amount	\$ 0.70	\$ 1.73	\$ 2.53

For fiscal 2005, options to purchase 16,000 shares of the Company's common stock with exercise prices ranging from \$26.88 to \$32.20 per share and expiration dates between 2006 and 2014 were outstanding at January 1, 2006, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

For fiscal 2004, options to purchase 362,447 shares of the Company's common stock with exercise prices ranging from \$21.50 to \$26.88 per share and expiration dates between 2006 and 2014 were outstanding at January 2, 2005, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

For fiscal 2003, options to purchase 735,600 shares of the Company's common stock with exercise prices ranging from \$15.40 to \$29.56 per share and expiration dates between 2006 and 2012 were outstanding at December 28, 2003, but were not included in the computation of diluted EPS because their effect would be anti-dilutive.

15. Stock Options

The Company has four stock option plans: The Wackenhut Corrections Corporation 1994 Stock Option Plan (First Plan), the Wackenhut Corrections Corporation 1994 Stock Option Plan (Second Plan), the 1995 Non-Employee Director Stock Option Plan (Third Plan) and the Wackenhut Corrections Corporation 1999 Stock Option Plan (Fourth Plan). The Wackenhut Corrections Corporation 1994 Stock Option Plan (First Plan) has expired and has no outstanding stock options.

Under the Second Plan and Fourth Plan, the Company may grant options to key employees for up to 1,500,000 and 1,150,000 shares of common stock, respectively. Under the terms of these plans, the exercise price per share and vesting period is determined at the sole discretion of the Board of Directors. All options that have been granted under these plans are exercisable at the fair market value of the common stock at the date of the grant. Generally, the options vest and become exercisable ratably over a four-year period, beginning immediately on the date of the grant. However, the Board of Directors has exercised its discretion and has granted options that vest 100% immediately. All options under the Second Plan and Fourth Plan expire no later than ten years after the date of the grant.

Under the Third Plan, the Company may grant up to 110,000 shares of common stock to non-employee directors of the Company. Under the terms of this plan, options are granted at the fair market value of the common stock at the date of the grant, become exercisable immediately, and expire ten years after the date of the grant.

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A summary of the status of the Company's stock option plans is presented below.

Fiscal Year	2005		2004		2003	
	Shares	Wtd. Avg. Exercise Price	Shares	Wtd. Avg. Exercise Price	Shares	Wtd. Avg. Exercise Price
Outstanding at beginning of year	1,591,509	\$ 15.49	1,614,374	\$ 14.21	1,410,306	\$ 14.26
Granted	13,500	32.20	160,374	22.00	305,000	12.67
Exercised	183,752	16.32	174,839	9.10	86,932	8.93
Forfeited/ Cancelled	14,600	16.70	8,400	22.93	14,000	17.36
Options outstanding at end of year	1,406,657	15.53	1,591,509	15.49	1,614,374	14.21
Options exercisable at end of year	1,260,492	\$ 15.32	1,381,692	\$ 15.26	1,443,032	\$ 14.39

The following table summarizes information about the stock options outstanding at January 1, 2006:

Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Wtd. Avg. Remaining Contractual Life	Wtd. Avg. Exercise Price	Number Exercisable	Wtd. Avg. Exercise Price
\$7.88 - \$7.88	2,000	4.3	\$ 7.88	2,000	\$ 7.88
\$8.44 - \$8.44	184,500	4.1	8.44	184,500	8.44
\$9.30 - \$9.30	172,500	5.1	9.30	172,500	9.30
\$9.51 - \$12.51	80,091	7.1	9.61	56,807	9.65
\$14.00 - \$14.00	184,182	7.3	14.00	134,732	14.00
\$14.69 - \$14.69	15,000	3.7	14.69	15,000	14.69
\$15.40 - \$15.40	264,000	6.1	15.40	264,000	15.40
\$15.90 - \$18.63	176,137	4.3	18.43	160,753	18.44
\$20.25 - \$22.93	159,000	3.7	22.30	120,600	22.10
\$23.00 - \$32.20	169,247	4.4	25.09	149,600	25.32
	1,406,657	5.2	\$ 15.53	1,260,492	\$ 15.32

The Company had 13,000 options available to be granted at January 1, 2006 under the aforementioned stock plans.

16. Retirement and Deferred Compensation Plans

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

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

The following table summarizes key information related to these pension plans and retirement agreements which includes information as required by FAS 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits". The table illustrates the reconciliation of the beginning and ending balances of the benefit obligation showing the effects during the period attributable to each of the following: service cost, interest cost, plan amendments, termination benefits, actuarial gains and losses. The assumptions used in the Company's calculation of accrued pension costs are based on market information and the Company's historical rates for employment compensation and discount rates, respectively.

In accordance with FAS 132, the Company has also disclosed contributions and payment of benefits related to the plans. There were no assets in the plan at January 1, 2006 or January 2, 2005. All changes as a result of the adjustments to the accumulated benefit obligation are included below and shown net of tax in the Consolidated Statement of Shareholders' Equity and Comprehensive Income. There were no significant transactions between the employer or related parties and the plan during the period.

	2005	2004
Change in Projected Benefit Obligation		
Projected Benefit Obligation, Beginning of Year	\$ 14,423	\$ 13,408
Service Cost	437	313
Interest Cost	542	836
Plan Amendments	—	—
Actuarial Gain (Loss)	332	(102)
Benefits Paid	(32)	(32)
Projected Benefit Obligation, End of Year	\$ 15,702	\$ 14,423
Change in Plan Assets		
Plan Assets at Fair Value, Beginning of Year	\$ —	\$ —
Company Contributions	32	32
Benefits Paid	(32)	(32)
Plan Assets at Fair Value, End of Year	\$ —	\$ —
Reconciliation of Prepaid (Accrued) and Total Amount Recognized		
Funded Status of the Plan	\$ (15,702)	\$ (14,423)
Unrecognized Prior Service Cost	204	1,141
Unrecognized Net Loss	2,930	2,719
Accrued Pension Cost	\$ (12,568)	\$ (10,563)
Accrued Benefit Liability	(12,568)	(11,748)
Intangible Asset	—	1,141
Accumulated Other Comprehensive Income	—	44
Total Recognized	\$ (12,568)	\$ (10,563)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

	Fiscal 2005	Fiscal 2004
Components of Net Periodic Benefit Cost		
Service Cost	\$ 437	\$ 314
Interest Cost	542	836
Amortization of:		
Unrecognized Prior Service Cost	936	1,078
Unrecognized Net Loss	121	404
Net Periodic Pension Cost	\$ 2,036	\$ 2,632
Weighted Average Assumptions for Expense		
Discount Rate	5.50%	5.75%
Expected Return on Plan Assets	N/A	N/A
Rate of Compensation Increase	5.50%	5.50%

The accumulated benefit obligation for all defined benefit plans was \$12.6 million and \$11.7 million at January 1, 2006 and January 2, 2005, respectively. The accrued benefit liability for the three plans at January 1, 2006 are as follows, \$1.7 million for the executive retirement plan, \$0.8 million for the officer retirement plan and \$10.1 million for the three key executives' plans.

The Company has established a deferred compensation agreement for non-employee directors, which allow eligible directors to defer their compensation in either the form of cash or stock. Participants may elect lump sum or monthly payments to be made at least one year after the deferral is made or at the time the participant ceases to be a director. The Company recognized total compensation expense under this plan of \$(0.1) million, \$0.1 and \$0.1 million for 2005, 2004, and 2003, respectively. Payouts under the plan were \$0.0 and \$0.1 million in 2005 and 2004 respectively. The liability for the deferred compensation was \$0.5 million and \$0.5 million at year-end 2005 and 2004, respectively, and is included in "Accrued expenses" in the accompanying consolidated balance sheets.

The Company also has a non-qualified deferred compensation plan for employees who are ineligible to participate in its qualified 401(k) plan. Eligible employees may defer a fixed percentage of their salary, which earns interest at a rate equal to the prime rate less 0.75%. The Company matches employee contributions up to \$400 each year based on the employee's years of service. Payments will be made at retirement age of 65 or at termination of employment. The Company recognized expense of \$0.1 million, \$0.1 million and \$0.1 million in 2005, 2004, and 2003, respectively. The liability for this plan at year-end 2005 and 2004 was \$2.3 million and \$2.1 million, respectively, and is included in accrued expense in the accompanying consolidated balance sheets.

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

Fiscal Year	Pension Benefits
	(In thousands)
2006	\$ 11,047
2007	53
2008	59
2009	118
2010	130
2011-2015	1,342
	\$ 12,749

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

17. Business Segment and Geographic Information

Operating and Reporting Segment

The Company operates in one industry segment encompassing the development and management of privatized government institutions located in the United States, Australia, South Africa and the United Kingdom. The segment information presented in the prior periods has been reclassified to conform to the current presentation.

Fiscal Year	2005	2004	2003
	(In thousands)		
Revenues:			
Correction and detention facilities	\$ 572,109	\$ 546,952	\$ 519,246
Other	40,791	47,042	29,992
Total revenues	\$ 612,900	\$ 593,994	\$ 549,238
Depreciation and amortization:			
Correction and detention facilities	\$ 15,617	\$ 13,672	\$ 13,237
Other	259	226	104
Total depreciation and amortization	\$ 15,876	\$ 13,898	\$ 13,341
Operating Income:			
Correction and detention facilities	\$ 7,646	\$ 38,092	\$ 27,952
Other	292	899	1,548
Total operating income	\$ 7,938	\$ 38,991	\$ 29,500
Segment assets:			
Correction and detention facilities	\$ 525,625	\$ 343,505	
Other	10,671	18,017	
Total segment assets	\$ 536,296	\$ 361,522	

Fiscal 2005 segment operating expenses include net non cash charges of \$23.8 million consisting of a \$20.9 million impairment charge for the Michigan Correctional Facility and a \$4.3 million charge for the remaining obligation for the inactive Jena Facility offset by a \$1.3 million reduction in insurance reserves.

Fiscal 2004 segment operating expenses includes a net non cash credit of \$1.2 million, consisting of a \$4.2 million reduction in our general liability, auto liability and worker's compensation insurance reserves offset by an additional provision for operating losses of approximately \$3.0 million related to our inactive facility in Jena, Louisiana. Fiscal 2003 operating expenses include net non cash charges of \$8.6 million in 2003, consisting of a provision for operating losses of approximately \$5.0 million related to the Jena facility, and approximately \$3.6 million primarily attributable to liability insurance expenses, related to the transitioning of the DIMIA contract in Australia.

Pre-Tax Income Reconciliation

Year Ended	2005	2004	2003
	(In thousands)		
Total operating income from segment	\$ 7,646	\$ 38,092	\$ 27,952
Unallocated amounts:			
Net Interest Expense	(13,862)	(12,570)	(11,043)
Gain on sale of UK Joint Venture	—	—	56,094
Costs related to early extinguishment of debt	(1,360)	(317)	(1,989)
Other	292	899	1,548
Income (loss) before income taxes, equity in earnings of affiliates, Discontinued operations and Minority interest	\$ (7,284)	\$ 26,104	\$ 72,562

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

Asset Reconciliation

	2005	2004
Total segment assets	\$ 525,625	\$ 343,505
Cash	57,094	92,005
Short term investments	—	10,000
Deferred income tax-current	19,755	12,891
Restricted cash	26,366	3,908
Other	10,671	18,017
Total Assets	\$ 639,511	\$ 480,326

Geographic Information

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

Fiscal Year	2005	2004	2003
(In thousands)			
Revenues:			
U.S. operations	\$ 514,071	\$ 502,989	\$ 475,043
Australia operations	83,335	75,947	61,571
South African operations	15,494	15,058	12,624
Total revenues	\$ 612,900	\$ 593,994	\$ 549,238
Long-lived assets:			
U.S. operations	\$ 275,415	\$ 183,655	
Australia operations	6,243	6,916	
South African operations	578	294	
Total long-lived assets	\$ 282,236	\$ 190,865	

Sources of Revenue

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

Fiscal Year	2005	2004	2003
(In thousands)			
Revenues:			
Correction and detention facilities	\$ 572,109	\$ 546,952	\$ 519,246
Mental health	32,616	31,704	29,911
Construction	8,175	15,338	81
Total revenues	\$ 612,900	\$ 593,994	\$ 549,238

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Equity in Earnings of Affiliates

Equity in earnings of affiliates for 2005 and 2004 include one of our joint ventures in South Africa, SACS. Equity in earnings of affiliates for 2003 represent the operations of the Company's 50% owned joint ventures in the United Kingdom (Premier Custodial Group Limited) and SACS. These entities and their subsidiaries are accounted for under the equity method.

The Company sold its interest in Premier Custodial Group Limited on July 2, 2003 for approximately \$80.7 million and recognized a gain of approximately \$56.0 million. Total equity in the undistributed earnings for Premier Custodial Group Limited, before income taxes, for fiscal 2003, and 2002 was \$3.0 million, and \$10.2 million, respectively.

The following table summarizes certain financial information pertaining to this joint venture for the period from December 30, 2002 through the date of sale of the UK joint venture on July 2, 2003 and for the fiscal year ended December 29, 2002 (in thousands):

	2003
Statement of Operations Data	
Revenues	\$ 104,080
Operating loss	\$ (2,981)
Net income	\$ 3,486

A summary of financial data for SACS is as follows:

Fiscal Year	2005	2004	2003
(In thousands)			
Statement of Operations Data			
Revenues	\$ 33,179	\$ 31,175	\$ 24,801
Operating income	11,969	11,118	7,528
Net (loss) income	2,866	—	(817)
Balance Sheet Data			
Current assets	13,212	14,250	8,154
Noncurrent assets	68,149	74,648	61,342
Current liabilities	4,187	5,094	2,896
Non current liabilities	73,645	83,474	69,749
Shareholders' equity (deficit)	3,529	330	(3,150)

SACS commenced operation in fiscal 2002. Total equity in undistributed loss for SACS before income taxes, for fiscal 2005, 2004 and 2003 was \$0.9 million, \$(0.1) million, and \$(0.4) million, respectively.

Business Concentration

Except for the major customers noted in the following table, no single customer provided more than 10% of the Company's consolidated revenues during fiscal 2005, 2004 and 2003:

Customer	2005	2004	2003
Various agencies of the U.S. Federal Government	27%	27%	27%
Various agencies of the State of Texas	8%	9%	12%
Various agencies of the State of Florida	7%	12%	12%

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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18. Income Taxes

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

	2005	2004	2003
	(In thousands)		
Income (loss) before income taxes, minority interest, equity earnings in affiliates, and discontinued operations			
United States	\$ (20,395)	\$ 9,627	\$ 61,064
Foreign	13,111	16,477	11,498
	<u>(7,284)</u>	<u>26,104</u>	<u>72,562</u>
Discontinued operations:			
Income (loss) from operation of discontinued business	2,022	(529)	5,188
Total	<u>\$ (5,262)</u>	<u>\$ 25,575</u>	<u>\$ 77,750</u>

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

	2005	2004	2003
	(In thousands)		
Federal income taxes:			
Current	\$ (4,146)	\$ (72)	\$ 29,182
Deferred	<u>(4,151)</u>	<u>2,050</u>	<u>1,790</u>
	<u>(8,297)</u>	<u>1,978</u>	<u>30,972</u>
State income taxes:			
Current	(714)	643	2,332
Deferred	<u>(756)</u>	<u>469</u>	<u>226</u>
	<u>(1,470)</u>	<u>1,112</u>	<u>2,558</u>
Foreign:			
Current	(3,304)	4,226	5,108
Deferred	<u>1,245</u>	<u>915</u>	<u>(1,786)</u>
	<u>(2,059)</u>	<u>5,141</u>	<u>3,322</u>
Total U.S. and foreign	<u>(11,826)</u>	<u>8,231</u>	<u>36,852</u>
Discontinued operations:			
Income from operations of discontinued business	895	(181)	1,544
Total	<u>\$ (10,931)</u>	<u>\$ 8,050</u>	<u>\$ 38,396</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	2005	2004	2003
	(In thousands)		
Continuing operations:			
Provisions using statutory federal income tax rate	\$ (2,549)	\$ 9,136	\$ 25,396
State income taxes, net of federal tax benefit	(907)	723	1,650
Australia consolidation benefit	(6,460)	—	—
Basis difference PCG stock	—	(3,351)	8,639
Section 965 benefit	(1,704)	(197)	—
Non-performance based compensation	—	1,417	—
Other, net	<u>(206)</u>	<u>503</u>	<u>1,167</u>
Total continuing operations	<u>(11,826)</u>	<u>8,231</u>	<u>36,852</u>
Discontinued operations:			
Taxes from operations of discontinued business	895	(181)	1,544
Provision (benefit) for income taxes	<u>\$ (10,931)</u>	<u>\$ 8,050</u>	<u>\$ 38,396</u>

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

	2005	2004
	(In thousands)	
Revenue not yet taxed	\$ (260)	\$ —
Deferred revenue	574	—
Uniforms	(158)	(207)
Deferred loan costs	945	—
Other, net	6	—
Allowance for doubtful accounts	211	426
Accrued vacation	4,753	2,644
Accrued liabilities	<u>13,684</u>	<u>10,028</u>
Total	<u>\$ 19,755</u>	<u>\$ 12,891</u>

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

	2005	2004
	(In thousands)	
Capital losses	\$ 5,945	\$ —
Depreciation	(2,241)	(9,808)
Deferred loan costs	2,568	—
Deferred revenue	1,841	2,886
Bond Discount	(1,746)	—
Net operating losses	3,499	1,587
Tax credits	815	—
Intangible assets	(6,013)	—
Accrued liabilities	762	—
Deferred compensation	6,031	5,231
Residual U.S. tax liability on unrepatriated foreign earnings	(4,754)	(4,611)
Foreign deferred tax assets	—	(2,277)
Other, net	261	113
Valuation allowance	<u>(9,053)</u>	<u>(1,587)</u>
Total liability	<u>\$ (2,085)</u>	<u>\$ (8,466)</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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In accordance with SFAS No. 109, Accounting for Income Taxes, deferred income taxes should be reduced by a valuation allowance if it is not more likely than not that some portion or all of the deferred tax assets will be realized. On a periodic basis, management evaluates and determines the amount of the valuation allowance required and adjusts such valuation allowance accordingly. At fiscal year end 2005, the Company has recorded a valuation allowance of approximately \$9.1 million. The valuation allowance includes \$6.9 million reported as part of purchase accounting relating to deferred tax assets for capital losses, federal and state net operating losses and charitable contribution carryforwards from the CSC acquisition. A full valuation allowance was provided against capital losses and a partial valuation allowance was provided against net operating losses and charitable contribution carryovers from the acquisition. The remaining valuation allowance of \$2.2 million relates to deferred tax assets for foreign net operating losses and state tax credits unrelated to the CSC acquisition.

At fiscal year end 2005, the Company had \$15.1 million of capital loss and \$4.2 million of net operating loss carryforwards from the CSC acquisition. The capital loss carryforwards begin to expire in 2007 and the net operating loss carryforwards begin to expire in 2020. The utilization of these capital and net operating loss carryforwards are subject to annual usage limitations pursuant to Internal Revenue Code Section 382.

Also at fiscal year end the Company had \$6.1 million of foreign operating losses which carry forward indefinitely and state tax credits which begin to expire in 2006. The Company has recorded a full valuation allowance against these deferred tax assets.

As a result of tax legislation in Australia, the Company realized an income tax benefit of \$6.5 million in the fourth quarter 2005. The benefit is due to an elective tax step-up that in effect reestablishes tax basis that had previously been depreciated on an accelerated methodology. The permanent tax step-up was exempt from taxation and results in a decrease in the same amount in the deferred tax liability associated with the depreciable asset. Equity in earnings of affiliate in 2005 reflects a one time tax benefit of \$2.1 million related to a change in South African tax law applicable to companies in a qualified Public Private Partnership ("PPP") with the South African Government. Beginning in 2005 Government revenues earned under the PPP are exempt from South African taxation. Additionally, prior year temporary differences that gave rise to deferred tax liabilities of the affiliate are exempt from tax in the future. Consequently, the affiliate eliminated these deferred tax liabilities which contributed to the one time tax benefit.

On October 22, 2004, the President of the United States signed into law the American Jobs Creation Act of 2004 ("AJCA"). A key provision of the AJCA creates a temporary incentive for U.S. corporations to repatriate undistributed income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations. In December 2004, the Company repatriated approximately \$17.3 million in incentive dividends and recognized an income tax benefit of \$1.7 million and \$0.2 million in 2005 and 2004, respectively.

During 2004, the Company adjusted its tax provision to reflect an adjustment to its treatment of certain executive compensation. During the fiscal years ended 2003 and 2002, along with the period ending June 27, 2004, the Company calculated its tax provision as if its executive bonus plan met the Internal Revenue Service code section 162(m) requirements for deductibility. During 2004, the Company discovered that the plan did not meet certain specific requirements of section 162(m). The Company recognized \$1.4 million of additional tax provision under section 162(m) for 2004, including \$0.6 million to correct its tax provision for the fiscal years ended 2003 and 2002.

The 2004 income tax expense includes a benefit from the realization of approximately \$3.4 million of foreign tax credits related to the gain on sale of PCG in July 2003. This benefit was realized in 2004 as a result of the Company completing its analysis of its earnings and profits in PCG and determining the amount of available foreign tax credits which could be applied against the gain from the sale.

The exercise of non-qualified stock options which have been granted under the Company's stock option plans give rise to compensation which is includable in the taxable income of the applicable employees and deducted by the Company for federal and state income tax purposes. Such compensation results from increases in the fair market value of the Company's common stock subsequent to the date of grant. In accordance with APB No. 25, such compensation is not recognized as an expense for financial accounting purposes and related tax benefits are credited directly to additional paid-in-capital.

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

19. Related Party Transactions with The Wackenhut Corporation

Related party transactions occurred in the past in the normal course of business between the Company and TWC. Such transactions included the purchase of goods and services and corporate costs for management support, office space, insurance and interest expense. No related party transactions occurred during fiscal years 2005 and 2004.

The Company incurred the following expenses related to transactions with TWC in 2003 (in thousands):

Fiscal Year	
General and administrative expenses	\$ 1,750
Rent	501
	<u>\$ 2,251</u>

General and administrative expenses represented charges for management and support services. TWC previously provided various general and administrative services to the Company under a services agreement, including payroll services, human resources support, tax services and information technology support services through December 31, 2002. Beginning January 1, 2003, the only service provided was for information technology support through year-end 2003. The Company began handling information technology support services internally effective January 1, 2004, and no longer relies on TWC for any services. All of the services formerly provided by TWC to the Company were pursuant to negotiated annual rates with TWC based upon the level of service to be provided under the services agreement. The Company believes that such rates were on terms no less favorable than the Company could obtain from unaffiliated third parties.

The Company also leased office space from TWC for its corporate headquarters under a non-cancelable operating lease that expired February 11, 2011. This lease was terminated effective July 19, 2003 as a result of the share purchase agreement.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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20. Selected Quarterly Financial Data (Unaudited)

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

	First Quarter	Second Quarter
2005		
Revenues	\$ 148,255	\$ 152,623
Operating income	\$ 7,373	\$ 7,588
Income from continuing operations	\$ 2,391	\$ 4,301
Income from discontinued operations, net of tax	\$ 505	\$ 173
Basic earnings per share		
Income from continuing operations	\$ 0.25	\$ 0.45
Income from discontinued operations	\$ 0.05	\$ 0.02
Net income per share	\$ 0.30	\$ 0.47
Diluted earnings per share		
Income from continuing operations	\$ 0.24	\$ 0.43
Income from discontinued operations	\$ 0.05	\$ 0.02
Net income per share	\$ 0.29	\$ 0.45
	Third Quarter	Fourth Quarter(b)
Revenues	\$ 147,148	\$ 164,874
Operating income (loss)	\$ 5,444	\$ (12,467)
Income (loss) from continuing operations	\$ 510(a)	\$ (1,323)(c)
Income (loss) from discontinued operations, net of tax	\$ (67)	\$ 516
Basic earnings per share		
Income (loss) from continuing operations	\$ 0.06	\$ (0.13)
Income (loss) from discontinued operations	\$ (0.01)	\$ 0.05
Net income (loss) per share	\$ 0.05	\$ (0.08)
Diluted earnings per share		
Income (loss) from continuing operations	\$ 0.05	\$ (0.13)
Income (loss) from discontinued operations	\$ (0.01)	\$ 0.05
Net income (loss) per share	\$ 0.04	\$ (0.08)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 1, 2006, January 2, 2005, and December 28, 2003

	First Quarter	Second Quarter
2004		
Revenues	\$ 140,837	\$ 145,062
Operating income	\$ 7,373	\$ 9,992
Income from continuing operations	\$ 1,899	\$ 3,657
Income (loss) from discontinued operations, net of tax	\$ 395	\$ (25)
Basic earnings per share		
Income from continuing operations	\$ 0.21	\$ 0.39
Income from discontinued operations	\$ 0.04	\$ 0.00
Net income per share	\$ 0.25	\$ 0.39
Diluted earnings per share		
Income from continuing operations	\$ 0.20	\$ 0.37
Income from discontinued operations	\$ 0.04	\$ 0.00
Net income per share	\$ 0.24	\$ 0.37
	Third Quarter	Fourth Quarter(e)
Revenues	\$ 146,501	\$ 161,594
Operating income	\$ 13,785	\$ 7,841
Income from continuing operations	\$ 5,681(d)	\$ 5,926(f)
Loss from discontinued operations, net of tax	\$ (46)	\$ (697)
Basic earnings per share		
Income from continuing operations	\$ 0.61	\$ 0.62
Loss from discontinued operations	\$ (0.01)	\$ (0.07)
Net income per share	\$ 0.60	\$ 0.55
Diluted earnings per share		
Income from continuing operations	\$ 0.59	\$ 0.60
Loss from discontinued operations	\$ (0.01)	\$ (0.07)
Net income per share	\$ 0.58	\$ 0.53

- (a) Includes a \$4.3 million write-off for our Jena, Louisiana facility and a charge of approximately \$1.4 million related to the write-off of deferred financing fees from the extinguishment of debt.
- (b) Includes operations of CSC from November 4, 2005 through January 1, 2006.
- (c) Includes a \$20.9 million impairment charge for Michigan facility, a \$6.5 million tax benefit in Australia and \$2.0 million tax benefit in South Africa related to changes in law.
- (d) Includes a \$4.2 million pre-tax reduction in our general liability, auto liability and worker's compensation insurance reserves.
- (e) Includes 14 weeks of operations.
- (f) Includes a \$3.0 million write-off for our Jena, Louisiana facility

