GEO GROUP INC
Form 10-Q
May 04, 2007

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended April 1, 2007

OR

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

For the transition period from to

Commission file number 1-14260

The GEO Group, Inc.

(Exact name of registrant as specified in its charter)

Florida (State or other jurisdiction of incorporation or organization)	65-0043078 (I.R.S. Employer Identification No.)
One Park Place, 621 NW 53rd Street, Suite 700, Boca Raton, Florida (Address of principal executive offices)	33487 (Zip code)

(561) 893-0101
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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

Large accelerated filer o	Accelerated filer þ	Non accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

At May 1, 2007, 25,211,720 shares of the registrant s common stock were issued and outstanding.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

THE GEO GROUP, INC.
CONSOLIDATED STATEMENTS OF INCOME
FOR THE THIRTEEN WEEKS ENDED
APRIL 1, 2007 AND APRIL 2, 2006
(In thousands, except per share data)
(UNAUDITED)

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Revenues	$ 237,004	$ 185,881
Operating expenses	194,105	153,746
Depreciation and amortization	7,281	5,664
General and administrative expenses	15,053	14,009
Operating income	20,565	12,462
Interest income	3,240	2,216
Interest expense	(11,064)	(7,579)
Write off of deferred financing fees from extinguishment of debt	4,794	
Income before income taxes, minority interest, equity in earnings of affiliate and discontinued operations	7,947	7,099
Provision for income taxes	3,141	2,693
Minority interest	(92)	(9)
Equity in earnings of affiliate, net of income tax provision of $209 and $18	383	277
Income from continuing operations	5,097	4,674
Income (loss) from discontinued operations, net of tax provision (benefit) of $109 and $(65)	167	(118)
Net income	$ 5,264	$ 4,556
Weighted-average common shares outstanding:		
Basic	20,069	14,550
Diluted	20,781	15,051
Income per common share:		
Basic:		
Income from continuing operations	$ 0.25	$ 0.32
Income (loss) from discontinued operations	0.01	(0.01)
Net income per share-basic	$ 0.26	$ 0.31
Diluted:		
Income from continuing operations	$ 0.25	$ 0.31
Income (loss) from discontinued operations	0.00	(0.01)

Net income per share-diluted	$	0.25	$	0.30

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

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THE GEO GROUP, INC.
CONSOLIDATED BALANCE SHEETS
APRIL 1, 2007 AND DECEMBER 31, 2006
(In thousands, except share data)

	April 1, 2007 (Unaudited)	December 31, 2006
ASSETS		
Current Assets		
Cash and cash equivalents	$ 83,875	$ 111,520
Restricted cash	13,168	13,953
Accounts receivable, less allowance for doubtful accounts of $810 and $926	154,625	162,867
Deferred income tax asset, net	19,492	19,492
Other current assets	16,676	14,922
Total current assets	287,836	322,754
Restricted cash	15,422	19,698
Property and equipment, net	696,210	287,374
Assets held for sale	2,597	1,610
Direct finance lease receivable	41,592	39,271
Deferred income tax assets, net	4,701	4,941
Goodwill and other intangible assets, net	41,147	41,554
Other non current assets	29,503	26,251
	$ 1,119,008	$ 743,453
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 53,958	$ 48,890
Accrued payroll and related taxes	28,068	31,320
Accrued expenses	64,204	77,675
Current portion of deferred revenue		1,830
Current portion of capital lease obligations, long-term debt and non-recourse debt	16,644	12,685
Current liabilities of discontinued operations		1,303
Total current liabilities	162,874	173,703
Deferred revenue		1,755
Minority interest	1,663	1,297
Other non current liabilities	24,303	24,816
Capital lease obligations	16,415	16,621
Long-term debt	306,853	144,971
Non-recourse debt	128,573	131,680
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, 45,000,000 shares authorized, 33,253,534 and 33,248,584 issued and 25,218,284 and 19,748,584 outstanding	252	197
Additional paid-in capital	331,465	143,233
Retained earnings	204,490	201,697
Accumulated other comprehensive income	1,008	2,393
Treasury stock 8,037,500 and 13,500,000 shares	(58,888)	(98,910)
Total shareholders equity	478,327	248,610
	$ 1,119,008	$ 743,453

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

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THE GEO GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THIRTEEN WEEKS ENDED
APRIL 1, 2007 AND APRIL 2, 2006
(In thousands)
(UNAUDITED)

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Cash Flow from Operating Activities:		
Income from continuing operations	$ 5,097	$ 4,674
Adjustments to reconcile income from continuing operations to net cash provided by operating activities		
Depreciation and amortization expense	7,281	5,664
Amortization of debt issuance costs	676	281
Amortization of unearned compensation	379	
Stock-based compensation expense	194	177
Write-off of deferred financing fees	4,794	
Deferred tax expense (benefit)	240	(56)
Major maintenance reserve		57
Equity in earnings of affiliates, net of tax	(383)	(277)
Minority interests in earnings (losses) of consolidated entity	92	(515)
Income tax benefit of equity compensation	(78)	
Changes in assets and liabilities, net of acquisition		
Accounts receivable	8,242	(10,180)
Other current assets	(1,755)	2,951
Other assets	(1,624)	(642)
Accounts payable and accrued expenses	(1,615)	5,764
Accrued payroll and related taxes	(3,252)	3,375
Deferred revenue	(152)	(452)
Other liabilities	730	636
Net cash provided by operating activities of continuing operations	18,866	11,457
Net cash provided by (used in) operating activities of discontinued operations	(1,303)	73
Net cash provided by operating activities	17,563	11,530
Cash Flow from Investing Activities:		
Acquisition, net of cash acquired	(409,943)	
Change in restricted cash	5,160	(4,666)
Proceeds from sale of assets	56	19
Capital expenditures	(19,714)	(7,432)
Net cash used in investing activities	(424,441)	(12,079)
Cash Flow from Financing Activities:		
Payments on long-term debt	(214,438)	(586)
Proceeds from the exercise of stock options	111	674

Income tax benefit of equity compensation	78	
Proceeds from long-term debt	375,000	
Debt issuance costs	(8,932)	
Proceeds from equity offering, net	227,547	
Net cash provided by financing activities	379,366	88
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(133)	(464)
Net Decrease in Cash and Cash Equivalents	(27,645)	(925)
Cash and Cash Equivalents, beginning of period	111,520	57,094
Cash and Cash Equivalents, end of period	$ 83,875	$ 56,169
Supplemental Disclosures:		
Non-cash investing and financing activities		
Extinguishment of pre-acquisition liabilities	$ 11,003	$
Total liabilities assumed in acquisition	$ 2,558	$

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

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THE GEO GROUP, INC.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The unaudited consolidated financial statements of The GEO Group, Inc., a Florida corporation (the Company), included in this Form 10-Q have been prepared in accordance with accounting principles generally accepted in the United States and the instructions to Form 10-Q and consequently do not include all disclosures required by Form 10-K. Additional information may be obtained by referring to the Company s Form 10-K for the year ended December 31, 2006. In the opinion of management, all adjustments (consisting only of normal recurring items) necessary for a fair presentation of the financial information for the interim periods reported in this Form 10-Q have been made. Results of operations for the thirteen weeks ended April 1, 2007 are not necessarily indicative of the results for the entire fiscal year ending December 30, 2007.

The accounting policies followed for quarterly financial reporting are the same as those disclosed in the Notes to Consolidated Financial Statements included in the Company s Form 10-K filed with the Securities and Exchange Commission on March 2, 2007 for the fiscal year ended December 31, 2006.

2. EQUITY OFFERING

On March 23, 2007, the Company sold in a follow-on public offering 5,462,500 shares of its common stock at a price of $43.99 per share. All shares were issued from treasury. The aggregate net proceeds to the Company (after deducting underwriter s discounts and expenses of $12.7 million) were $227.5 million. On March 26, 2007, the Company utilized $200.0 million of the net proceeds to repay outstanding debt under the term loan portion of its senior secured credit facility. The balance of the proceeds will be used for general corporate purposes, which may include working capital, capital expenditures and potential acquisitions of complementary businesses and other assets. See Note 8 Long Term Debt and Derivative Financial Instruments The Senior Credit Facility for further discussion.

3. ACQUISITION

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

As a result of the Merger, each share of common stock of CPT (collectively, the Shares) was converted into the right to receive $32.5826 in cash, inclusive of a pro-rated dividend for all quarters or partial quarters for which CPT s dividend had not yet been paid as of the closing date. In addition, each outstanding option to purchase CPT common stock (collectively, the Options) having an exercise price less than $32.00 per share was converted into the right to receive the difference between $32.00 per share and the exercise price per share of the option, multiplied by the total number of shares of CPT common stock subject to the option. The Company paid an aggregate purchase price of $421.1 million for the acquisition of CPT, inclusive of the payment of $368.3 million in exchange for the Shares and the Options, the repayment of $40.0 million in CPT debt and the payment of $12.8 million in transaction related fees. The Company financed the acquisition through the use of $365.0 million in new borrowings under a new seven year term loan, referred to as Term Loan B and approximately $65.0 million in cash on hand. The Company deferred debt issuance costs of $8.9 million related to the new $365 million term loan. These costs are being amortized over the life of the term loan. As a result of the merger, the Company will no longer have ongoing lease expense related to the properties the Company previously leased from CPT. However; the Company will have increased depreciation expense reflecting its ownership of the properties and higher interest expense as a result of borrowings used to fund the acquisition.

The allocation of the purchase price for this transaction at April 1, 2007 is preliminary. The purchase price allocations related to certain tax items are still tentative at this time and information that will enable the Company to finalize these items is expected to be received during 2007. The preliminary allocation of purchase price is summarized below (in thousands):

Current assets, net of cash acquired of $11,125	$ 1,365

Property and equipment	400,124
Other non-current assets	9
Total assets acquired	401,498
Other non-current liabilities	2,558
Total liabilities assumed	2,558
Net assets acquired, including direct transaction costs	$ 398,940

The fair values used in determining the purchase price allocation for the tangible assets were based on independent appraisal. The fair market value of the identifiable net assets acquired exceeded the cost of the acquisition by approximately $15.7 million. The excess over cost was allocated on a pro rata basis to reduce the amounts assigned related to property and equipment.

The results of operations of CPT are included in the Company s results of operations beginning after January 24, 2007. CPT is part of the Company s US Corrections reportable segment. See Note 10 for segment information. The following unaudited pro forma information combines the consolidated results of operations of the Company and CPT as if the acquisition had occurred at the beginning of fiscal year 2006 Pro forma results are not presented for the thirteen weeks ended April 2, 2007 as the acquisition was at or near the beginning of the period and the results would be immaterial:

	Thirteen Weeks Ended April 2006
Revenues	$ 186,887
Income from continuing operations	2,846
Loss from discontinued operations	(118)
Net income	2,728
Net income per share basic	
Income from continuing operations	$ 0.20
Loss from discontinued operations	(0.01)
Net income per share basic	$ 0.19
Net income per share diluted	
Loss from continuing operations	$ 0.19
Loss from discontinued operations	(0.01)
Net income per share diluted	$ 0.18

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4. EQUITY INCENTIVE PLANS

In January 2006, the Company adopted Financial Accounting Standard (FAS) No. 123(R), (FAS 123R), Share-Based Payment using the modified prospective method. Under the modified prospective method of adopting FAS No. 123(R), the Company recognizes compensation cost for all share-based payments granted after January 1, 2006, plus any prior awards granted to employees that remained unvested at that time. The Company uses a Black-Scholes option valuation model to estimate the fair value of each option awarded. The assumptions used to value options granted during the interim period were comparable to those used at December 31, 2006. The impact of forfeitures that may occur prior to vesting is also estimated and considered in the amount recognized.

The Company had four equity compensation plans at April 1, 2007: The Wackenhut Corrections Corporation 1994 Stock Option Plan (the 1994 Plan), the 1995 Non-Employee Director Stock Option Plan (the 1995 Plan), the Wackenhut Corrections Corporation 1999 Stock Option Plan (the 1999 Plan) and the GEO Group, Inc. 2006 Stock Incentive Plan (the 2006 Plan and, together with the 1994 Plan, the 1995 Plan and the 1999 Plan, the Company Plans). Except for 222,000 shares of restricted stock issued under the 2006 Plan as of April 1, 2007, all of the foregoing awards previously issued under the Company Plans consist of stock options. Although awards are currently outstanding under all of the Company Plans, the Company may only grant new awards under the 2006 Plan. As of April 1, 2007, the Company had the ability to issue awards with respect to 9,500 shares of common stock pursuant to the 2006 Plan.

Under the terms of the Company Plans, the vesting period and, in the case of stock options, the exercise price per share, are determined by the terms of each plan. All stock options that have been granted under the Company Plans are exercisable at the fair market value of the common stock at the date of the grant. Generally, the stock 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 to grant stock options that vest 100% immediately for the Chief Executive Officer. In addition, stock options granted to non-employee directors under the 1995 Plan become exercisable immediately. All stock options awarded under the Company Plans expire no later than ten years after the date of the grant.

The 2006 Plan was approved by the Board of Directors and by the Company s shareholders on May 4, 2006. Under the 2006 Plan, the Company may grant various different types of awards, including stock options or shares of restricted stock, to key employees and non-employee directors for up to 450,000 shares.

On May 1, 2007, the Company s Board of Directors adopted and its shareholders approved several amendments to the 2006 Plan, including an amendment providing for the issuance of an additional 250,000 shares of the Company s common stock pursuant to awards granted under the plan, and specifying that up to 150,000 of such additional shares may constitute awards other than stock options and stock appreciation rights, including shares of restricted stock.

A summary of the status of stock option awards issued and outstanding under the Company s Plans is presented below.

	April 1, 2007			
Fiscal Year	**Shares (in thousands)**	**Wtd. Avg. Exercise Price**	**Wtd. Avg. Remaining Contractual Term**	**Aggregate Intrinsic Value (in thousands)**
Outstanding at December 31, 2006	1,316	$ 9.22		$
Granted	215	42.94		
Exercised	(7)	15.35		
Forfeited/canceled				
Options outstanding at April 1, 2007	1,524	$ 13.96	5.7	$ 47,804

Options exercisable at April 1, 2007	1,264	$	10.11	5.0	$	44,501

For the thirteen week period ending April 1, 2007, the amount of stock-based compensation expense was $0.6 million. The weighted average grant date fair value of options granted during the thirteen weeks ended April 1, 2007 was $17.47 per share. The total intrinsic value of options exercised during the thirteen weeks ended April 1, 2007 was $0.2 million.

The following table summarizes information about the exercise prices and related information of stock options outstanding under the Company Plans at April 1, 2007:

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	Options Outstanding			Options Exercisable	
Exercise Prices	Number Outstanding	Wtd. Avg. Remaining Contractual Life	Wtd. Avg. Exercise Price	Number Exercisable	Wtd. Avg. Exercise Price
$5.25 - $5.25	3,000	3.1	$ 5.25	3,000	$ 5.25
$5.63 - $5.63	188,625	2.9	5.63	188,625	5.63
$6.20 - $6.20	223,500	3.9	6.20	223,500	6.20
$6.34 - $7.97	95,212	5.8	6.39	95,213	6.39
$9.33 - $9.33	247,091	6.1	9.33	210,001	9.33
$10.27 - $10.27	328,500	4.9	10.27	328,500	10.27
$10.60 - $15.39	171,191	6.3	13.61	133,518	13.51
$15.66 - $27.48	51,750	7.5	18.27	38,550	18.80
$41.25 - $41.25	20,000	9.8	41.25	4,000	41.25
$43.11 - $43.11	195,500	9.9	43.11	39,100	43.11
	1,524,369	5.7	$ 13.96	1,264,007	$ 10.11

As of April 1, 2007, the Company had $3.7 million of unrecognized compensation costs related to non-vested stock option awards that is expected to be recognized over a weighted average period of 2.8 years. Proceeds received from option exercises during the thirteen weeks ended April 1, 2007 were $0.1 million.

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Restricted Stock

During fiscal year 2006, the Company granted 225,000 shares of non-vested restricted stock under the 2006 Plan to key employees and non-employee directors. Shares of restricted stock become unrestricted shares of common stock upon vesting on a one-for-one basis. The cost of these awards is determined using the fair value of the Company s common stock on the date of the grant and compensation expense is recognized over the vesting period. The shares of restricted stock that were granted during fiscal year 2006 under the 2006 Plan vest in equal 25% increments on each of the four anniversary dates immediately following the date of grant. The following is a summary of restricted stock issued as of April 1, 2007 and changes during the thirteen weeks ended April 1, 2007 follows:

	Shares	Wtd. Avg. Grant date Fair value
Restricted stock outstanding at January 1, 2007	222,750	$ 26.13
Granted		
Vested		
Forfeited/canceled	(750)	26.13
Restricted stock outstanding at April 1, 2007	222,000	$ 26.13

During the thirteen weeks ended April 1, 2007, the Company recognized $0.4 million of compensation expense related to its outstanding shares of restricted stock and as of April 1. 2007 had $4.5 million of unrecognized compensation expense. No restricted stock was outstanding at April 2, 2006.

5. COMPREHENSIVE INCOME

The components of the Company s comprehensive income, net of tax are as follows (in thousands):

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Net income	$ 5,264	$ 4,556
Change in foreign currency translation, net of income tax (expense) benefit of $1,151, and $(833), respectively	(1,912)	1,359
Minimum pension liability adjustment, net of income tax expense of $30, and $0, respectively	46	
Unrealized gain on derivative instruments, net of income tax expense of $210, and $39, respectively	481	90
Comprehensive income	$ 3,879	$ 6,005

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6. EARNINGS PER SHARE

Basic earnings per share is computed by dividing the net income available to shareholders by the weighted average number of outstanding common shares. The calculation of diluted earnings per share is similar to that of basic earnings per share, except that the denominator includes dilutive common share equivalents such as stock options and shares of restricted stock. Basic and diluted earnings per share (EPS) were calculated for the thirteen weeks ended April 1, 2007 and April 2, 2006 as follows (in thousands, except per share data):

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Net income	$ 5,264	$ 4,556
Basic earnings per share:		
Weighted average shares outstanding	20,069	14,550
Per share amount	$ 0.26	$ 0.31
Diluted earnings per share:		
Weighted average shares outstanding	20,069	14,550
Effect of dilutive securities:		
Assumed exercise or issuance of shares relating to stock plans	712	501
Weighted average shares assuming dilution	20,781	15,051
Per share amount	$ 0.25	$ 0.30

Of 1,524,369 stock options outstanding at April 1, 2007, no options were excluded from the computation of diluted EPS because their effect would be anti-dilutive. Of 2,033,921 stock options outstanding at April 2, 2006, options to purchase 165,750 shares of the Company s common stock with exercise prices ranging from $16.71 to $21.47 per share and expiration dates between 2006 and 2015 were not included in the computation of diluted EPS because their effect would be anti-dilutive. Of 222,000 shares of restricted stock outstanding at April 1, 2007, options to purchase 141,358 shares of common stock were not included in the computation of diluted EPS because their effect would be anti-dilutive.

7. GOODWILL AND OTHER INTANGIBLE ASSETS, NET

Changes in the Company s goodwill balances for the thirteen weeks ended April 1, 2007 were as follows (in thousands):

	Balance as of December 31, 2006	Goodwill resulting from Business Combinations	Foreign Currency Translation	Balance as of April 1, 2007
U.S. Corrections	$ 23,999	$	$	$ 23,999
International Services	3,075		32	3,107
Total Segments	$ 27,074	$	$ 32	$ 27,106

No goodwill resulted from the acquisition of CPT during the first quarter of 2007.

Intangible assets consisted of the following (in thousands):

	Description		Asset Life
Facility management contracts	$	15,050	7-17 years
Covenants not to compete		1,470	4 years
	$	16,520	
Less accumulated amortization		(2,479)	
	$	14,041	

Amortization expense was $0.4 million and $0.4 million for the thirteen weeks ended April 1, 2007 and April 2, 2006, respectively. Amortization is recognized on a straight-line basis over the estimated useful life of the intangible assets.

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8. LONG TERM DEBT AND DERIVATIVE FINANCIAL INSTRUMENTS

Senior Debt

The Senior Credit Facility

On January 24, 2007, the Company completed the refinancing of its senior secured credit facility through the execution of a Third Amended and Restated Credit Agreement (the Senior Credit Facility), by and among the Company, as Borrower, BNP Paribas, as Administrative Agent, BNP Paribas Securities Corp. as Lead Arranger and Syndication Agent, and the lenders who are, or may from time to time become, a party thereto. The Senior Credit Facility consists of a $365 million, seven-year term loan (the Term Loan B) and a $150 million five-year revolver (the Revolver). The initial interest rate for the Term Loan B is at the London Interbank Offered Rate, (LIBOR) plus 1.5% and the Revolver bears interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, the Company used the $365 million in borrowings under the Term Loan B to finance its acquisition of CPT, as discussed in Note 3 Acquisition.

On March 26, 2007, the Company used $200.0 million of the aggregate net proceeds of $227.5 million from its recent offering of 5,462,500 shares of its common stock to repay debt outstanding under the Term Loan B. As a result of the debt repayment, the Company wrote off approximately $4.8 million in deferred financing fees during the quarter ended April 1, 2007. As of April 1, 2007, the Company had $165.0 million outstanding under the Term Loan B, no amounts outstanding under the Revolver, $54.2 million outstanding in letters of credit under the Revolver and $95.8 million available under the Revolver. The Company intends to use future borrowings thereunder for general corporate purposes.

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

	Interest Rate Under the Revolver
Borrowings	LIBOR plus 2.25% or base rate plus 1.25%.
Letters of credit	1.50% to 2.50%.
Available borrowings	0.38% to 0.5%.

The 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:

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

All of the obligations under the 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.

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 its assets, (vi) make certain restricted payments, including declaring any cash dividends or redeem or repurchase capital stock, except as otherwise permitted, (vii) issue, sell or otherwise dispose of capital stock, (viii) transact with affiliates, (ix) make changes in accounting treatment, (x) amend or modify the terms of any subordinated indebtedness, (xi) enter into debt agreements that contain negative pledges on its assets or covenants more restrictive than those contained in the Senior Credit Facility, (xii) alter the business it conducts, and (xiii) materially impair the Company s lenders security interests in the collateral for its loans.

Events of default under the 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 representation or warranty, (iii) covenant defaults, (iv) bankruptcy, (v) cross default to certain other indebtedness, (vi) unsatisfied final judgments over a specified threshold, (vii) material environmental state of claims which are asserted against it, and (viii) a change of control.

Senior 8 $^{1}/4$% Notes

To facilitate the completion of the purchase of the interest of the Company s former majority shareholder in 2003, the Company issued $150.0 million aggregate principal amount, ten-year, 8 $^{1}/4$% senior unsecured notes, (the Notes). 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. Additionally, after July 15, 2008, the Company may redeem, at the Company s option, all or a portion of the Notes plus accrued and unpaid interest at various redemption prices ranging from 104.125% to 100.000% of the principal amount to be redeemed, depending on when the redemption occurs. The Indenture contains covenants that limit the Company s ability to incur additional indebtedness, pay dividends or distributions on its common stock, repurchase its common stock, and prepay subordinated indebtedness. The Indenture also limits the Company s ability to issue preferred stock, make certain types of investments, merge or consolidate with another company, guarantee other indebtedness, create liens and transfer and sell assets. The Company was in compliance with all of the covenants of the Indenture governing the notes as of April 1, 2007.

Non-Recourse Debt

South Texas Detention Complex

On February 1, 2007, the Company made a payment of $4.1 million for the current portion of our periodic debt service requirement in relation to the South Texas Local Development Corporation (STLDC) operating agreement and bond indenture. As of April 1, 2007, the remaining balance of the debt service requirement is $45.3 million, out of which $4.3 million is due within the next twelve months. Previously, in February 2004, Correctional Services Corporation (CSC), which the Company acquired in November 2005, 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. STLDC was created and issued $49.5 million in taxable revenue bonds to finance the construction of the detention center. Additionally, CSC provided $5.0 million of subordinated notes to STLDC for initial development. We determined that we are the primary beneficiary of STLDC and consolidate the entity as a result. STLDC is the owner of the complex and entered into a development agreement with CSC to oversee the development of the complex. In addition, STLDC entered into an operating agreement providing CSC the sole and exclusive right to operate and manage the complex. The operating agreement and bond indenture require the revenue from CSC s contract with ICE be used to fund the periodic debt service requirements as they become due. The net revenues, if any, after various expenses such as trustee fees, property taxes and insurance premiums are distributed to CSC to cover CSC s operating expenses and management fee. CSC is responsible for the entire operations of the facility including all operating expenses and is required to pay all operating expenses whether or not there are sufficient revenues. STLDC has no liabilities 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 is $5.5 million as of April 1, 2007 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, referred to as 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, referred to as 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 $5.9 million as of April 1, 2007 as funds held in trust with respect to the Northwest Detention Center for debt service and other reserves.
Australia
In connection with the financing and management of one Australian facility, the Company s wholly owned Australian subsidiary financed the facility s development and subsequent expansion in 2003 with long-term debt obligations, which are non-recourse to us. As a condition of the loan, the Company is required to maintain a restricted cash balance of Australian Dollar (AUD) 5.0 million, which, at April 1, 2007, was approximately $4.0 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 South African Custodial Services Ltd., referred to as SACS, the Company entered into certain guarantees related to the financing, construction and operation of the prison. The Company guaranteed certain obligations of SACS under its debt agreements up to a maximum amount of 60.0 million South African Rand, or approximately $8.3 million, to SACS senior lenders through the issuance of letters of credit. Additionally, SACS is required to fund a restricted account for the payment of certain costs in the event of contract termination. The Company has guaranteed the payment of 50% of amounts which may be payable by SACS into the restricted account and provided a standby letter of credit of 7.0 million South African Rand, or approximately $1.0 million, as security for its guarantee. The Company s 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 the Company s outstanding letters of credit under its Revolver.
The Company has agreed to provide a loan, of up to 20.0 million South African Rand, or approximately $2.8 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. The Company s obligations under the Standby Facility expire upon the earlier of full funding or SACS s release from its obligations under its debt agreements. The lenders ability to draw on the Standby Facility is limited to certain circumstances, including termination of the contract.
The Company has also guaranteed certain obligations of SACS to the security trustee for SACS lenders. The Company secured its guarantee to the security trustee by ceding its rights to claims against SACS in respect of any loans or other finance agreements, and by pledging the Company s shares in SACS. The Company s liability under the guarantee is limited to the cession and pledge of shares. The guarantee expires upon expiration of the cession and pledge agreements.
In connection with a design, build, finance and maintenance contract for a facility in Canada, the Company guaranteed certain potential tax obligations of a not-for-profit entity. The potential estimated exposure of these obligations is Canadian Dollar (CAN) 2.5 million, or approximately $2.2 million commencing in 2017. The Company has a liability of $0.7 million related to this exposure as of April 1, 2007 and December 31, 2006. To secure this guarantee, the Company has 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 does not currently operate or manage this facility.

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 $51.1 million and $50.0 million at April 1, 2007 and December 31, 2006, respectively. The term of the non-recourse debt is through 2017 and it bears interest at a variable rate quoted by certain Australian banks plus 140 basis points. Any obligations or liabilities of the subsidiary are matched by a similar or corresponding commitment from the government of the State of Victoria. As a condition of the loan, the Company is required to maintain a restricted cash balance of AUD 5.0 million, which, at April 1, 2007, was approximately $4.0 million. This amount is included in restricted cash and the annual maturities of the future debt obligation is included in non recourse debt.

At April 1, 2007, the Company also had outstanding seven letters of guarantee totaling approximately $6.3 million under separate international facilities. The Company does not have any off balance sheet arrangements.

Derivatives

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 LIBOR plus a fixed margin of 3.45%, also calculated on the notional $50.0 million amount. As of April 1, 2007 and December 31, 2006 the fair value of the swaps totaled approximately $(1.3) million and $(1.7) million, respectively, and are included in other non-current 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 period ended April 1, 2007.

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 asset as of April 1, 2007 and December 31, 2006 was approximately $3.9 million and $3.2 million, respectively, and was recorded as a component of other assets within the consolidated financial statements. There was no material ineffectiveness of the Company s interest rate swap for the fiscal periods presented. The Company does not expect to enter into any transactions during the next twelve months which would result in the reclassification into earnings of losses associated with this swap currently reported in accumulated other comprehensive loss.

9. COMMITMENTS AND CONTINGENCIES

In 2005, the Company s equity affiliate, SACS, recognized a one time tax benefit of $2.1 million related to a change in South African Tax law applicable to companies in a qualified Public Private Partnership (PPP) with the South African Government. The tax law change had the effect that beginning in 2005 government revenues earned under the PPP are exempt from South African taxation. The one time tax benefit in part related to deferred tax liabilities that were eliminated during 2005 as a result of the change in the tax law. In February 2007, the South African legislature passed legislation that has the effect of removing the exemption from taxation on government revenues. As a result of the new legislation, SACS will be subject to South African taxation going forward at the applicable tax rate of 29%. The increase in the applicable income tax rate results in an increase in net deferred tax liabilities which were calculated at a rate of 0% during the period the government revenues were exempt. The effect of the increase in the deferred tax liability of the equity affiliate is a charge to equity in earnings of affiliate in the amount of $2.4 million. The law change also has the effect of reducing a previously recorded liability for unrecognized tax benefits as provided under FIN 48, Accounting for Uncertainties in Income Taxes resulting in an increase to equity in earnings of affiliate. The respective decrease and increase to equity in earnings of affiliate are substantially offsetting in nature.

Legal Proceedings

Florida Department of Management Services Matter

On May 19, 2006, the Company, along with Corrections Corporation of America, referred to as CCA, were sued by an individual plaintiff in the Circuit Court of the Second Judicial Circuit for Leon County, Florida (Case No. 2005CA001884). The complaint alleges that, during the period from 1995 to 2004, the Company and CCA overbilled the State of Florida by an amount of at least

$12.7 million by submitting to the State false claims for various items relating to (i) repairs, maintenance and improvements to certain facilities which the Company operates in Florida, (ii) the Company s staffing patterns in filling vacant security positions at those facilities, and (iii) the Company s alleged failure to meet the conditions of certain waivers granted to the Company by the State of Florida from the payment of liquidated damages penalties relating to the Company s staffing patterns at those facilities. The portion of the complaint relating to the Company arises out of the Company s operations at the Company s South Bay and Moore Haven, Florida correctional facilities. The complaint appears to be based largely on the same set of issues raised by a Florida Inspector General s Evaluation Report released in late June 2005, referred to as the IG Report, which alleged that the Company and CCA overbilled the State of Florida by over $12.0 million.

Subsequently, the Florida Department of Management Services, referred to as the DMS, which is responsible for administering the Company s correctional contracts with the State of Florida, conducted a detailed analysis of the allegations raised by the IG Report which included a comprehensive written response to the IG Report which the Company s had prepared and delivered to the DMS. In September 2005, the DMS provided a letter to the Company stating that, although its review had not yet been fully completed, it did not find any indication of any improper conduct by the Company. On October 17, 2006, DMS provided a letter to the Company stating that its review had been completed. The Company and DMS then agreed to settle this matter for $0.3 million. This amount was accrued at December 31, 2006 and paid in the first quarter of 2007. Although this determination is not dispositive of the recently initiated litigation, the Company believes it supports the Company s position that the Company has valid defenses in this matter. The Florida Department of Law Enforcement is currently investigating this matter and the Company is cooperating with the investigation. The Company will continue to monitor this matter and intends to defend its rights vigorously. However, given the amounts claimed by the plaintiff and the fact that the nature of the allegations could cause adverse publicity to the Company, the Company believes that this matter, if settled unfavorably to the Company, could have a material adverse effect on the Company s financial condition and results of operations.

Texas Wrongful Death Action

On September 15, 2006, a jury in an inmate wrongful death lawsuit in a Texas state court awarded a $47.5 million verdict against the Company. Recently, the verdict was entered as a judgment against the Company in the amount of $51.7 million. The lawsuit is being administered under the insurance program established by The Wackenhut Corporation, the Company s former parent company, in which the Company participated until October 2002. Policies secured by the Company under that program provide $55 million in aggregate annual coverage. As a result, the Company believes it is fully insured for all damages, costs and expenses associated with the lawsuit and as such has not taken any reserves in connection with the matter. The lawsuit stems from an inmate death which occurred at the Company s former Willacy County State Jail in Raymondville, Texas, in April 2001, when two inmates at the facility attacked another inmate. Separate investigations conducted internally by the Company, The Texas Rangers and the Texas Office of the Inspector General exonerated the Company and its employees of any culpability with respect to the incident. The Company believes that the verdict is contrary to law and unsubstantiated by the evidence. The Company s insurance carrier has posted a supersedeas bond in the amount of approximately $60 million to cover the judgment. On December 9, 2006, the trial court denied the Company s post trial motions and the Company filed a notice of appeal on December 18, 2006.

Other Legal Proceedings

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.

10. BUSINESS SEGMENT AND GEOGRAPHIC INFORMATION

Operating and Reporting Segments

The Company conducts its business through three reportable business segments: its U.S. corrections segment; its international services segment; and its GEO Care segment. The Company has identified these three reportable segments to reflect the current view that the Company operates three distinct business lines, each of which constitutes a material part of its overall business. This treatment also

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reflects how the Company has discussed its business with investors and analysts. The U.S. corrections segment primarily encompasses U.S.-based privatized corrections and detention business. The international services segment primarily consists of privatized corrections and detention operations in South Africa, Australia and the United Kingdom. This segment also operates our recently acquired United Kingdom-based prisoner transportation business and reviews opportunities to further diversify into related foreign-based governmental-outsourced services on an ongoing basis. The GEO Care segment, which is operated by the Company s wholly-owned subsidiary GEO Care, Inc., comprises privatized mental health and residential treatment services business, all of which is currently conducted in the United States. Other primarily consists of activities associated with the Company s construction business. Set forth below is certain financial and other information regarding each of the Company s reportable segments. The segment information presented below with respect to prior periods has been reclassified to conform to the Company s current presentation.

	Thirteen Weeks Ended	
	April 1, 2007	**April 2, 2006**
Revenues:		
U.S. corrections	$ 164,349	$ 146,764
International services	28,842	23,112
GEO Care	22,134	14,902
Other	21,679	1,103
Total revenues	$ 237,004	$ 185,881
Depreciation and amortization:		
U.S. corrections	$ 6,834	$ 4,914
International services	259	650
GEO Care	188	100
Other		
Total depreciation and amortization	$ 7,281	$ 5,664
Operating income:		
U.S. corrections	$ 32,404	$ 22,429
International services	1,739	1,822
GEO Care	1,636	2,217
Other	(161)	3
Operating income from segments	35,618	26,471
Corporate expenses	(15,053)	(14,009)
Total operating income	$ 20,565	$ 12,462

	April 1, 2007	**December 31, 2006**
Segment assets:		
U.S. corrections	$ 867,311	$ 457,545
International services	83,459	79,641
GEO Care	16,262	15,606

Other	15,318	21,057
Total segment assets	$ 982,350	$ 573,849

Pre-Tax Income Reconciliation of Segments

The following is a reconciliation of the Company s total operating income from its reportable segments to the Company s income before income taxes, equity in earnings of affiliates, discontinued operations and minority interest, in each case, during the thirteen weeks ended April 1, 2007 and April 2, 2006, respectively.

	Thirteen Weeks Ended	
	April 1, 2007	**April 2, 2006**
Total operating income from segments	$ 35,618	$ 26,471
Unallocated amounts:		
Corporate expenses	(15,053)	(14,009)
Net interest expense	(7,824)	(5,363)
Write off of deferred financing fees from extinguishment of debt	(4,794)	
Income before income taxes, equity in earnings of affiliates, Discontinued operations and minority interest	$ 7,947	$ 7,099

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Asset Reconciliation of Segments

The following is a reconciliation of the Company s reportable segment assets to the Company s total assets as of April 1, 2007 and December 31, 2006, respectively.

	April 1, 2007	December 31, 2006
Reportable segment assets	$ 967,032	$ 552,792
Cash	83,875	111,520
Deferred tax asset, net	24,193	24,433
Restricted cash	28,590	33,651
Other	15,318	21,057
Total Assets	$ 1,119,008	$ 743,453

Sources of Revenue

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

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Revenues:		
Correction and detention	$ 193,191	$ 169,876
GEO Care	22,134	14,902
Construction	21,679	1,103
Total revenues	$ 237,004	$ 185,881

Equity in Earnings of Affiliate

Equity in earnings of affiliate includes our joint venture in South Africa, SACS. This entity is accounted for under the equity method of accounting.

A summary of financial data for SACS is as follows (in thousands):

	Thirteen Weeks Ended	
	April 1, 2007	April 2, 2006
Statement of Operations Data		
Revenues	$ 8,380	$ 8,862
Operating income	3,357	3,343
Net income	796	561
Balance Sheet Data		
Current assets	11,985	10,728
Non current assets	51,463	69,850
Current liabilities	4,914	4,477
Non current liabilities	57,479	71,895
Shareholders equity	1,055	4,206

SACS commenced operations in fiscal 2002. Total equity in undistributed income for SACS before income taxes, as of April 1, 2007 and April 2, 2006 was $1.2 million and $0.6 million, respectively.

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11. BENEFIT 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 Company adopted FAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R), (FAS 158) at December 31, 2006. FAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability on its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. FAS 158 requires an employer to measure the funded status of a plan as of its year-end date.

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

In accordance with FAS 158, the Company has disclosed contributions and payment of benefits related to the plans. There were no assets in the plan at April 1, 2007 or December 31, 2006. All changes as a result of the adjustments to the accumulated benefit obligation are included below and are shown net of tax as a component of comprehensive income in Note 5 Comprehensive Income. There were no significant transactions between the employer or related parties and the plan during the period.

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

	April 1, 2007	**December 31, 2006**
	(in thousands)	
Change in Projected Benefit Obligation		
Projected benefit obligation, beginning of period	$ 17,098	$ 15,702
Service cost	138	671
Interest cost	126	546
Plan amendments		
Actuarial gain		215
Benefits paid		(36)
Projected benefit obligation, end of period	$ 17,362	$ 17,098
Change in Plan Assets		
Plan assets at fair value, beginning of period	$	$
Company contributions	11	36
Benefits paid	(11)	(36)

Plan assets at fair value, end of period	$	$
Unfunded Status of the Plan	$ (17,362)	$ (17,098)
Amounts Recognized in Accumulated Other Comprehensive Income		
Unrecognized prior service cost	153	164
Unrecognized net loss	3,068	3,028
Accrued pension cost	$ 3,221	$ 3,192

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		April 1, 2007		April 2, 2006
Components of Net Periodic Benefit Cost				
Service cost	$	138	$	132
Interest cost		125		244
Amortization of:				
Unrecognized prior service cost		10		10
Unrecognized net loss		76		36
Net periodic pension cost	$	349	$	422
Weighted Average Assumptions for Expense				
Discount rate		5.75%		5.50%
Expected return on plan assets		N/A		N/A
Rate of compensation increase		5.50%		5.50%

12. RECENT ACCOUNTING PRONOUNCEMENTS

In February 2007, the Financial Accounting Standards Board (FASB) issued FAS No. 159 (FAS 159), Fair Value Option for Financial Assets and Financial Liabilities, which permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of FAS 159 is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The fair value option established by FAS 159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. FAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact this standard will have on its financial condition, results of operations, cash flows or disclosures.

In September 2006, the Financial Accounting Standards Board (FASB) issued FAS No. 157 (FAS 157), Fair Value Measurements, which establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. FAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. FAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact this standard will have on its financial condition, results of operations, cash flows or disclosures.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). The Company adopted the provisions of FIN 48, on January 1, 2007. Previously, the Company had accounted for tax contingencies in accordance with Statement of Financial Accounting Standards 5, *Accounting for Contingencies.* As required by FIN 48, which clarifies Statement 109, *Accounting for Income Taxes,* the Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. At the adoption date, the Company applied FIN 48 to all tax positions for which the statute of limitations remained open. As a result of the implementation of FIN 48, the Company recognized an increase of approximately a $2.5 million in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007, balance of retained earnings.

The amount of unrecognized tax benefits as of January 1, 2007, was $5.7 million. That amount includes $3.4 million of unrecognized tax benefits which, if ultimately recognized, will reduce the Company s annual effective tax rate. As a result of a South African tax law change enacted during the first quarter of 2007, a liability for unrecognized tax benefits in the amount of $2.4 million is no longer required resulting in a material change in unrecognized tax benefits. The reduction in the liability resulted in an increase to equity in earnings of affiliate. See Note 9

Commitments and Contingencies for a discussion of the tax law change.

The Company is subject to income taxes in the U.S. federal jurisdiction, and various states and foreign jurisdictions. Tax regulations within each jurisdiction are subject to interpretation of the related tax laws and regulations and require significant judgment to apply. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for the years before 2002.

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The Internal Revenue Service commenced an examination of the Company s U.S. income tax returns for 2002 through 2004 in the third quarter of 2005 that is anticipated to be completed during 2008. The Company does not expect to recognize any further significant changes to the total amount of unrecognized tax benefits during the remaining quarters of the year.

In adopting FIN 48, the Company changed its previous method of classifying interest and penalties related to unrecognized tax benefits as income tax expense to classifying interest accrued as interest expense and penalties as operating expenses. Because the transition rules of FIN 48 do not permit the retroactive restatement of prior period financial statements, the Company s first quarter 2006 financial statements continue to reflect interest and penalties on unrecognized tax benefits as income tax expense. The Company accrued approximately $0.9 million for the payment of interest and penalties at January 1, 2007. Subsequent changes to accrued interest and penalties have not been significant.

13. SUBSEQUENT EVENTS

On April 26, 2007, the Company announced that the Federal Bureau of Prisons awarded a contract for the management of the 2,048-bed Taft Correctional Institution, which has been managed by the Company since 1997, to another private operator. The management contract, which was competitively re-bid, will be transitioned to the alternative operator effective August 20, 2007. The Company does not expect the loss of this contract to have a material adverse effect on its financial condition or results of operations.

On May 1, 2007, the Company s shareholders approved several amendments to the GEO Group, Inc. 2006 Stock Incentive Plan, including an amendment providing for the issuance of an additional 250,000 shares of GEO common stock pursuant to awards granted under the plan, and specifying that up to 150,000 of such additional shares may constitute awards other than stock options and stock appreciation rights, including shares of restricted stock.

On May 1, 2007, the Company s Board of Directors declared a two-for-one stock split of the Company s common stock. The stock split will take effect on June 1, 2007 with respect to stockholders of record on May 17, 2007. Following the stock split, the Company s shares outstanding will increase from 25.2 million to 50.4 million.

THE GEO GROUP, INC.

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

Forward-Looking Information

This report, our other filings with the Securities and Exchange Commission, which we refer to as the SEC, and our earnings press release dated May 1, 2007 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, estimat the negative of such words or variations of such words and similar expressions. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements and we can give no assurance that such forward-looking statements will prove to be correct. Important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, or cautionary statements, include, but are not limited to:

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

our exposure to rising employee and inmate medical costs;

our ability to maintain occupancy rates at our facilities;

our ability to manage costs and expenses relating to ongoing litigation arising from our operations;

our ability to accurately estimate on an annual basis, loss reserves related to general liability, workers compensation and automobile liability claims;

our ability to identify suitable acquisitions, and to successfully complete and integrate such 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 SEC including, but not limited to, those detailed in this quarterly report on Form 10-Q, our annual report on Form 10-K and our 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.

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 under Risk Factors in our Form 10-K for the year ended December 31, 2006, filed with the Securities and Exchange Commission on March 2, 2007. The discussion should be read in conjunction with our unaudited consolidated financial statements and notes thereto included in this Form 10-Q.

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

As of April 1, 2007, we operated a total of 58 correctional, detention and mental health and residential treatment facilities and had over 58,000 beds under management or for which we had been awarded contracts. We maintained an average facility occupancy rate of 97.2% for the thirteen weeks ended April 1, 2007 excluding our vacant Michigan and Jena facilities.

Reference is made to Part II, Item 7 of our annual report on Form 10-K filed with the SEC on March 2, 2007, for further discussion and analysis of information pertaining to our financial condition and results of operations for the fiscal year ended December 31, 2006.

Recent Developments

On January 24, 2007, we completed the acquisition of CentraCore Properties Trust, which we refer to as CPT, pursuant to the merger of CPT with and into GEO Acquisition II, Inc., our wholly-owned subsidiary. We paid an aggregate purchase price of $421.1 million for the acquisition of CPT, inclusive of the payment of $368.3 million in exchange for the outstanding CPT common stock and stock options, the repayment of $40.0 million in CPT debt and the payment of $12.8 million in transaction related fees. We financed the acquisition through the use of $365.0 million in new borrowings under a new Term Loan B and $65.0 million in cash on hand. The Company deferred debt issuance costs of $8.9 million related to the new $365 million term loan. These costs are being amortized over the life of the term loan. As a result of the merger we will no longer have ongoing lease expense related to the properties we previously leased from CPT. However, we will have increased depreciation expense reflecting our ownership of the properties and higher interest expense as a result of borrowings used to fund the acquisition.

Recent Financings

On January 24, 2007, in connection with our acquisition of CPT, we completed the refinancing of our senior credit facility through the execution of an amended senior credit facility, which we refer to as the Senior Credit Facility. The Senior Credit Facility initially consisted of a $365.0 million seven-year term loan, referred to as the Term Loan B, and a $150 million five-year revolver, referred to as the Revolver. The initial interest rate for the Term Loan B is LIBOR plus 1.50% and any future borrowings under the Revolver would bear interest at LIBOR plus 2.25% or at the base rate plus 1.25%. On January 24, 2007, we used the $365.0 million in borrowings under the Term Loan B to finance our acquisition of CPT.

On March 23, 2007, we sold in a follow-on public equity offering 5,462,500 shares of our common stock at a price of $43.99 per share. All shares were issued from treasury. The aggregate net proceeds to us from the offering (after deducting underwriter s discounts and expenses of $12.7 million) were $227.5 million. On March 26, 2007, we utilized $200.0 million of the net proceeds from the offering to repay outstanding debt under the Term Loan B portion of the Senior Credit Facility. As a result, as of April 1, 2007, we had reduced our total Term Loan B borrowings to $165.0 million. We intend to use the balance of the proceeds from the offering for general corporate purposes, which may include working capital, capital expenditures and potential acquisitions of complementary businesses and other assets.

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 Management s Discussion and Analysis of Financial Condition and Results of Operations Guarantees for a discussion of our guarantees related to SACS. Separately, SACS entered into a long term operating contract with South African Custodial Management (Pty) Limited, which we refer to as SACM, to provide security and other management services and with SACS s joint venture partner to provide purchasing, programs and maintenance services upon completion of the construction phase, which concluded in February 2002. Our maximum exposure for loss under this contract is $15.6 million, which represents our initial investment and the guarantees discussed in Management s Discussion and Analysis of Financial Condition and Results of Operations.

In February 2004, Correctional Services Corporation, now our wholly-owned subsidiary which we refer to as 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 March 13, 2007, we filed a universal shelf registration statement with the SEC, which became effective immediately upon filing. The universal shelf registration statement provides for the offer and sale by us, from time to time, on a delayed basis, of an indeterminate 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 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.

CRITICAL ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. We routinely evaluate our estimates based on historical experience and on various other assumptions that management believes are reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. A summary of our significant accounting policies is contained in Note 1 to our financial statements on Form 10-K for the year ended December 31, 2006.

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

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

We currently maintain a general liability policy for all U.S. corrections operations with $52.0 million per occurrence and in the aggregate. On October 1, 2004, we increased our deductible on this general liability policy from $1.0 million to $3.0 million for each claim which occurs after October 1, 2004. Geo Care, Inc. is separately insured for general and professional liability. Coverage is maintained with limits of $10.0 million per occurrence and in the aggregate subject to a $3.0 million self-insured retention. We also maintain insurance to cover property and casualty risks, workers compensation, medical malpractice, environmental liability and automobile liability. Our Australian subsidiary is required to carry tail insurance on a general liability policy providing an extended reporting period through 2011 related to a discontinued contract. We also carry various types of insurance with respect to our

operations in South Africa, United Kingdom and Australia. There can be no assurance that our insurance coverage will be adequate to cover all claims to which we may be exposed.
Since our insurance policies generally have high deductible amounts (including a $3.0 million per claim deductible under our general liability and auto liability policies and $2.0 million per claim deductible under our workers compensation policy), losses are recorded when reported and a further provision is made to cover losses incurred but not reported. Loss reserves are undiscounted and are computed based on independent actuarial studies. If actual losses related to insurance claims significantly differ from our estimates, our financial condition and results of operations could be materially impacted.
Certain of our facilities located in Florida and determined by insurers to be in high-risk hurricane areas carry substantial windstorm deductibles of up to $4.8 million. Since hurricanes are considered unpredictable future events, no reserves have been established to pre-fund for potential windstorm damage. Limited commercial availability of certain types of insurance relating to windstorm exposure in coastal areas and earthquake exposure mainly in California may prevent us from insuring our>32.9% in 2012. The decline in 2013 was due primarily to increased competition in the marketplace, a slight decline in rig utilization as a result of unfavorable weather conditions, increased rig staffing costs, fewer rigs operating around the clock that resulted in higher costs for generating comparable revenues, a decline in higher-margin services in 2013 resulting from a change in the overall mix of services provided, increased workers compensation insurance costs, and settlement of a customer claim. Such decline in the Energy segment was partially offset by the gross profit generated by Black Hawk in 2013 subsequent to the acquisition. Gross profit in the Sports segment increased by $3.0 million primarily as a result of the acquisition of UK Elite in June 2013 and the acquisition of the CrossFit® entities in November 2012 being included for the entire 2013 period.

Selling, general and administrative ("SG&A") expenses in 2013 increased by $3.0 million as compared to 2012 primarily as a result of the acquisitions in the Sports segment and Sun Well being included for the entire 2013 period, partially offset by the reversal of the contingent consideration liability of $0.5 million associated with the acquisition of Rogue.

Amortization of intangibles in 2013 increased by $1.1 million as compared to 2012 as a result of intangible assets recognized in connection with the acquisitions of Sun Well in May 2012 and UK Elite in June 2013.

Net interest income of $3.1 million in 2013 increased by $1.6 million as compared to 2012 primarily as a result of increased interest income of $2.9 million from the Company investing in higher yield money market funds and corporate obligations in 2013. Such increase was partially offset by increased interest expense of $1.3 million primarily associated with the borrowings under the Steel Energy Credit Agreement.

Other income of $1.4 million in 2013 primarily represented realized gains on the sale of marketable securities of $2.6 million, partially offset by $0.9 million of losses recognized for equity-method investees and a loss on extinguishment of debt of $0.5 million from the write off of unamortized deferred financing costs upon terminating the Sun Well Credit Agreement.

The Company recognized a benefit from income taxes of $9.3 million for the year ended December 31, 2013, primarily as a result of a reversal of $7.2 million of reserves for foreign taxes upon the expiration of the statute of limitations. In addition, in 2013 the Company reversed a portion of its valuation allowance for deferred tax assets as a result of deferred tax liabilities recognized in connection with unrealized gains on marketable securities included as a component of other comprehensive income. The Company recognized a benefit from income taxes of $15.7 million for the year ended December 31, 2012, primarily from a reversal of a portion of its valuation allowance for deferred tax assets as a result of deferred tax liabilities recognized on the identifiable intangible assets acquired in connection with the acquisition of Sun Well.

The results of operations for the year ended December 31, 2013, included a loss from discontinued operations of $5.5 million related to Ruckus, of which approximately $3.6 million related to the impairment of goodwill. The results of operations for the year ended December 31, 2012, included a loss from discontinued operations of $1.9 million related to The Show.

Year ended December 31, 2012, compared with 2011

Net revenues for the year ended December 31, 2012, increased by $97.6 million as compared to 2011 as a result of the Company expanding its Energy business through acquisitions. Net revenues from the Company's Energy segment increased by $95.8 million as a result of the acquisitions of Rogue in December 2011, Eagle Well in February 2012, and Sun Well in May 2012. Net revenues from the Company's Sports segment increased $1.8 million as a result of the acquisition of Baseball Heaven in June 2011 being included for the entire 2012 period.

Gross profit for the year ended December 31, 2012, increased by $33.0 million as compared to 2011 as a result of the Company expanding its Energy business through acquisitions. Gross profit in the Energy segment increased by $31.7 million as a result of the acquisitions of Rogue, Eagle Well, and Sun Well. Gross profit in the Sports segment increased by $1.3 million as a result of the acquisition of Baseball Heaven in June 2011 being included for the entire 2012 period.

Selling, general and administrative ("SG&A") expenses in 2012 increased by $10.9 million as compared to 2011 primarily as a result of the acquisitions in the Energy segment and the acquisition of Baseball Heaven in June 2011 being included for the entire 2012 period.

Amortization of intangibles in 2012 increased by $7.6 million as compared to 2011 as a result of intangible assets recognized in connection with the acquisitions in the Energy segment.

Net interest income of $1.5 million in 2012 decreased by $2.6 million as compared to 2011 primarily as a result of a the Company selling its positions in diversified bonds in 2011 with the proceeds invested in short-term United States Treasury securities, which had a lower yield.

Other losses for the year ended December 31, 2012, was $0.8 million. Other income for the year ended December 31, 2011, was $4.3 million, which primarily represented gains recognized on the sale of the Company's diversified bond portfolio.

The Company recognized a benefit for income taxes of $15.7 million for the year ended December 31, 2012, primarily from a reversal of a portion of its valuation allowance for deferred tax assets as a result of deferred tax liabilities recognized on the identifiable intangible assets acquired in connection with the acquisition of Sun Well.

The results of operations for the year ended December 31, 2012, included a loss from discontinued operations of $1.9 million related to The Show. The results of operations for the year ended December 31, 2011, included income from discontinued operations of $6.6 million related to the Predecessor Business.

Liquidity and Capital Resources

The Energy Credit Agreement entered into in July 2013 and amended in December 2013 provides for a borrowing capacity of $105.0 million consisting of a $95.0 million secured term loan (the “Term Loan”) and up to $10.0 million in revolving loans (the “Revolving Loans”) subject to a borrowing base of 85% of the eligible accounts receivable. Steel Energy borrowed $70.0 million under the Term Loan in July 2013, the proceeds of which were combined with $10.0 million in intercompany loans from Sun Well and Rogue and used to pay the Company a dividend of $80.0 million. Steel Energy borrowed an additional $25.0 million under the Term Loan in December 2013, the proceeds of which were combined with cash provided by the Company and Steel Energy and used to fund the acquisition of Black Hawk. At December 31, 2013, the Company had $10.0 million of borrowing capacity under the Revolving Loans, all of which was available as no Revolving Loans were outstanding. As of December 31, 2013, the Company had $92.5 million outstanding under the Term Loan.

Borrowings under the Energy Credit Agreement are collateralized by substantially all the assets of Steel Energy and its wholly-owned subsidiaries Sun Well, Rogue, and Black Hawk, and a pledge of all of the issued and outstanding shares of capital stock of Sun Well, Rogue, and Black Hawk. Borrowings under the Energy Credit Agreement are fully guaranteed by Sun Well, Rogue, and Black Hawk.

The Energy Credit Agreement runs through July 2018, with the Term Loan amortizing in quarterly installments of $3.3 million and a balloon payment due on the maturity date. Borrowings under the Energy Credit Agreement bear interest at annual rates of either (i) the Base Rate plus an applicable margin of 1.50% to 2.25% or (ii) LIBOR plus an applicable margin of 2.50% to 3.25%. The “Base Rate” is the greatest of (i) the prime lending rate, (ii) the Federal Funds Rate plus 0.5%, and (iii) the one-month LIBOR plus 1.0%. The applicable margin for both Base Rate and LIBOR is determined based on the leverage ratio calculated in accordance with the Energy Credit Agreement. LIBOR-based borrowings are available for interest periods of one, three, or six months. In addition, the Company is required to pay commitment fees of between 0.375% and 0.50% per annum on the daily unused amount of the Revolving Loans.

The Energy Credit Agreement contains certain financial covenants, including (i) a leverage ratio not to exceed 3.00:1 for quarterly periods through June 15, 2015, 2.75:1 for quarterly periods through June 30, 2017, and 2.5:1 thereafter and (ii) a fixed charge coverage ratio of 1.15:1 for quarterly periods through December 31, 2016, and 1.25:1 thereafter. The Company was in compliance with all financial covenants as of December 31, 2013.
The Energy Credit Agreement also contains standard representations, warranties, and non-financial covenants. The repayment of the Term Loan can be accelerated upon (i) a change in control, which would include Steel Energy owning less than 100% of the equity of Sun Well or Rogue or Steel Partners Holdings L.P. (“SPLP”) owning, directly or indirectly, less than 35% of Steel Energy or (ii) other events of default, including payment failure, false representations, covenant breaches, and bankruptcy.

The Company finances its operations and capital expenditure requirements from its existing cash and marketable securities balances, which at December 31, 2013, totaled $73.6 million and $178.5 million, respectively. Working capital in 2013 decreased by $25.3 million. The increase in working capital from the $70.0 million in proceeds from the initial borrowings under the Energy Credit Agreement in July 2013 were more than offset by investments in cost method and equity method investees of $25.0 million and $9.2 million, respectively, repurchases of the Company's common stock totaling $29.4 million, and repayments of long-term debt and an increase in the current portion of long-term debt totaling $20.7 million.

Cash flows from operating activities of continuing operations increased by $8.6 million in 2013 as compared to 2012 primarily due to the timing of collections of trade receivables.

During 2013 the Company paid $61.9 million for acquisitions net of cash acquired, invested $25.0 million and $9.2 million in cost-method and equity-method investees, respectively, paid $29.4 million to repurchase shares of its common stock, and invested $8.9 million in property and equipment. These investments and expenditures were financed with the proceeds from the Steel Energy Credit Agreement, net of debt repayments, of $79.5 million, proceeds from the sales and maturities of marketable securities, net of purchases, of $32.6 million, and the Company's cash reserves.

At December 31, 2013, the Company had $252.1 million in cash and marketable securities. Available-for-sale securities included short-term deposits, corporate debt and equity instruments, United States government securities, and securities of government agencies, and were recorded on our consolidated balance sheets at fair market value, with any related unrealized gain or loss reported as a component of “Accumulated other comprehensive income” in stockholders’ equity. We expect to realize the full value of all our marketable securities upon maturity or sale, as we have the intent and ability to hold the securities until the full value is realized. However, we cannot provide any assurance that our invested cash and marketable securities will not be impacted by adverse conditions in the financial markets, which may require us to record an impairment charge that could adversely impact our financial results. In addition, we maintain our cash and marketable securities with certain financial institutions, in which our balances exceed the limits that are insured by the Federal Deposit Insurance Corporation. If the underlying financial institutions fail or other adverse events occur in the financial markets, our cash balances may be impacted.

We believe that our cash balances will be sufficient to satisfy our anticipated cash needs for working capital and capital expenditures for at least the next twelve months. We anticipate making additional acquisitions and we may be required to use a significant portion of our available cash balances for such acquisitions or for working capital needs thereafter. The consummation of additional acquisitions, prevailing economic conditions, and financial, business and other factors beyond our control could adversely affect our estimates of our future cash requirements. As such, we could be required to fund our cash requirements by alternative financing. In these instances, we may seek to raise such additional funds through public or private equity or debt financings or from other sources. As a result, we may not be able to obtain adequate or favorable equity financing, if needed, due in part to our shares of common stock currently trading on the OTCQB Market. Any equity financing we obtain may dilute existing ownership interests, and any debt financing could contain covenants that impose limitations on the conduct of our business. There can be no assurance that additional financing, if needed, would be available on terms acceptable to us or at all.

Off-balance Sheet Arrangements
The Company does not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources that are material to investors.

Contractual Obligations
Our contractual obligations at December 31, 2013, were as follows:

	Payments Due By Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
	(in thousands)				
Long-term debt	$92,500	$13,214	$26,428	$52,858	$—
Interest on long-term debt (1)	9,421	2,845	5,959	617	—
Operating lease obligations	5,729	1,796	2,079	828	1,026
Capital lease obligations	1,061	464	597	—	—
Deferred compensation	3,809	100	3,709	—	—
Uncertain tax positions (2)	104	104	—	—	—
Short-term debt	346	346	—	—	—
Total	$112,970	$18,869	$38,772	$54,303	$1,026

(1) Interest on variable-rate long-term debt is estimated using current interest rates. Interest excludes commitment fees and non-cash amortization of deferred financing costs, which are included as components of interest expense in the consolidated statements of operations.
(2) The timing of payment for uncertain tax positions relating to foreign jurisdictions cannot be predicted.

Critical Accounting Policies
The Company’s management must make certain estimates and assumptions in preparing the financial statements. Certain of these estimates and assumptions relate to matters that are inherently uncertain as they pertain to future events. The Company’s management believes that the estimates and assumptions used in preparing the financial statements were the most appropriate at that time, although actual results could differ significantly from those estimates under different conditions.

Note 2, “Summary of Significant Accounting Policies,” to the Company’s consolidated financial statements included in this Annual Report on Form 10-K provides a detailed discussion of the various accounting policies of the Company. We believe that the following accounting policies are critical since they require subjective or complex judgments that could potentially affect the financial condition or results of operations of the Company.

Allowance for Doubtful Accounts: We assess the carrying value of our accounts receivable based on management's assessment of the collectibility of specific client accounts, which includes consideration of the creditworthiness and financial condition of those specific clients. We also assess the carrying value of accounts receivable balances based on other factors, including historical experience with bad debts, client concentrations, the general economic environment, and the aging of such receivables. We record an allowance for doubtful accounts to reduce the accounts receivable balance to the amount that is reasonably believed to be collectible. Based on our estimates there was no allowance for doubtful accounts at December 31, 2013 and 2012. A change in our assumptions, including the creditworthiness of clients and the default rate on receivables, would result in us recovering an amount of our accounts receivable that differs from the current carrying value. Such difference, either positive or negative, would be reflected as a component of SG&A expense in future periods.

Fair Value Measurements: Certain of our assets, primarily cash and marketable securities, are reported at their estimated fair value. We estimate the fair value of such assets based on quoted market prices (Level 1), quoted prices of similar instruments with an active market (Level 2), or prices obtained funds statements or from third-party pricing services (Level 3). We classify our marketable securities as “available for sale” securities, with changes in fair value recognized in stockholders' equity as "other comprehensive income (loss)". A change in our assumptions, including obtaining quoted market prices for specific securities valued as a Level 2 or Level 3 securities or obtaining quoted prices of similar securities with an active market for securities valued as a Level 3 security, would result in a fair value of such securities that differs from the previously estimated fair value. Such difference, either positive or negative, would be reflected as an increase or decrease in the carrying value of such securities.

Valuation of Long-Lived Assets: We review the carrying value of our property and equipment and other long-lived assets for impairment when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Recoverability is determined by comparing the carrying value of the assets to the future undiscounted cash flows the assets are expected to generate. If it is determined that the carrying amount is not recoverable, an impairment charge is recognized equal to the amount by which the carrying value of the asset exceeds its fair market value. No events or changes in circumstances have occurred that required the Company to assess the recoverability of its property and equipment, and therefore the Company has not recognized any impairment charges. A change in the Company’s business climate in future periods, including an inability to effectively integrate new businesses in which significant investments have been made or a general downturn in one of the Company’s businesses could lead to a required assessment of the recoverability of the Company’s long-lived assets, which may subsequently result in an impairment charge.

Valuation of Goodwill: We assess the carrying value of goodwill by comparing the carrying value of underlying businesses to their fair values. We are required to test its goodwill for impairment at least annually, and more frequently if an event occurs or circumstances change to indicate that an impairment may have occurred. The Company’s annual testing date is September 30. We estimated the fair value of our Energy business based on a third-party valuation, which relied on certain assumptions we made including projections of future revenues based on assumed long-term growth rates, estimated costs, and the appropriate discount rates. The estimates we used for long-term revenue growth and future costs are based on historical data, various internal estimates, and a variety of external sources, and are developed as part of our long-range planning process. The carrying value of the goodwill in the Energy business was $78.2 million at September 30, 2013. Based on the use of these assumptions in estimating the fair value of the Energy business, there was no impairment of goodwill as of September 30, 2013, the most recent annual testing date. A change in our assumptions, including lower long-term growth rates, higher operating costs, or higher discount rates could cause a change in the estimated fair value of the Energy business, and therefore could result in an impairment of goodwill, which would have an adverse effect on our results of operations.

Stock-Based Compensation: The amount of stock-based compensation expense to be recognized on stock options and restricted stock granted to employees and non-employee directors is based on their fair value on the grant date. We determine the fair value of the equity awards using the Black-Scholes pricing model. We must make certain assumptions in determining the fair value of the equity awards, including the volatility of our common stock, the future dividend yield on our common stock, and the term over which equity awards will remain outstanding. In addition, we must make certain assumptions regarding the rate at which options will be forfeited to estimate the service period that will be completed by the holders of stock options. Any deviation in the actual volatility of our common stock, the actual dividend yield, and the actual early exercise behavior of holders of stock options from that assumed in estimating the fair value of the equity awards will not result in a change in the amount of compensation expense recognized, but will result in the actual value realized by the holder of the award to be different than the amount of compensation expense recognized. Any deviation in the actual forfeitures of nonvested stock options during the service period from that assumed will result in a change to the amount of compensation expense recognized, either as additional compensation expense or a reversal of previously recognized compensation expense in the period of change.

Income Taxes: We make certain assumptions and judgments in determining income tax expense for financial reporting purposes. These include estimates of taxable income for the current and future periods, the timing of utilization of tax benefits, the amount of business we will conduct in the jurisdictions in which we operate, and the applicable tax rates. We also must make certain judgments in assessing the likelihood that certain tax positions will be sustained upon examination, including those in foreign jurisdictions. A change in these assumptions would result in a change in our tax provision for financial reporting purposes in future periods and could result in our cash payments for taxes to be more or less than originally estimated.

We assess the recoverability of our deferred tax assets based on our historical taxable income and estimates of future taxable income. In estimating its future taxable income, we have to make various assumptions about our future operating performance, including assumptions regarding the energy industry. We believe that it was more likely than not that the benefit associated with the deferred tax assets will not be fully realized in future periods. Accordingly, a valuation allowance in the amount of $69.8 million and $37.2 million at December 31, 2013 and 2012, respectively, was established to reserve against the carrying value of certain of our deferred tax assets. A change in the assumptions, including better or worse operating performance than projected, could result in a change in the amount of deferred tax assets that will be recovered, and therefore could result in a reduction or increase to the valuation allowance established at December 31, 2013. Such an adjustment would be reflected as a component of the provision for income taxes in the period of the adjustment

Contingent Liabilities: We are subject to subject to litigation or claims that arise in the normal course of business. We are also subject to multiple federal, state, and local laws and regulations pertaining to worker safety, the handling of hazardous materials, transportation standards, and the environment. We assessed our potential exposure to legal and environmental claims based on the facts and circumstances and our knowledge of any potential exposure. Based on such assessments we have not recognized a contingent liability for environmental or legal claims. A change in assumptions could result in us being deemed liable for certain such matters, which would be result in additional expense and an increased liability.

Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update (“ASU”) No. 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, which requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. This pronouncement was effective for reporting periods beginning after December 15, 2012. The Company adopted this pronouncement effective January 1, 2013. The adoption of ASU No. 2013-02 did not have a material effect on the Company's financial statements.

In March 2013, the FASB issued ASU 2013-05, Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity. The objective of this pronouncement is to resolve the diversity in practice regarding the release into net income of the cumulative translation adjustment upon derecognition of a subsidiary or group of assets within a foreign entity. ASU No. 2013-05 is effective prospectively for fiscal years beginning after December 15, 2013 and for interim reporting periods within those years, with early adoption being permitted. The Company does not expect the adoption of ASU No. 2013-05 to have a material effect on its financial statements.

In July 2013, the FASB issued ASU No. 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, which provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, similar tax loss, or tax credit carryforward exists. This pronouncement is effective for fiscal years beginning after December 15, 2013, and for interim reporting periods within those years. The Company does not expect the adoption of ASU No. 2013-11 to have a material impact on its financial statements.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

We are exposed to interest rate risk in connection with our borrowings under a credit facility that aggregated $92.5 million at December 31, 2013. Interest rates on funds borrowed under the credit facility vary based on changes to the prime rate, LIBOR, or the Federal funds rate. A change in interest rates of 1.0% would result in an annual change in income before taxes of $0.9 million based on the outstanding balance under the credit facility at December 31, 2013.

We are also exposed to interest rate risk related to certain of our investments in marketable securities. At December 31, 2013, our marketable securities aggregated $178.5 million, of which $84.1 million represented corporate obligations, commercial paper, and United States government securities that pay a fixed rate of interest and are reported at fair value. A change in interest rates would result in a change in the value of such securities in future periods. Although a change in interest rates in future periods will not affect the amount of interest income earned on the specific securities held at December 31, 2013, a change in interest rates of 1.0% would result in an annual change in income before taxes of $0.8 million in future periods if comparable amounts were invested in similar securities.

Equity Price Risk

We are exposed to equity price risk related to certain of our investments in marketable securities. At December 31, 2013, our marketable securities aggregated $178.5 million, of which $95.3 million represented mutual funds and corporate equities that are reported at fair value. A change in the equity price of these securities would result in a change in value of such securities in future periods.

Foreign Currency Exchange Risk

We hold assets and have legacy obligations in foreign countries even though we no longer have any operations outside of the United States. Changes in foreign currency exchange rates can have an impact on our results of operations since we translate foreign currencies into United States dollars for financial reporting purposes. Changes in foreign currency exchange rates would also result in changes in the value received or paid in United States dollars for the assets and obligations denominated in a foreign currency.

Item 8. Financial Statements and Supplementary Data

See financial statements beginning on page F-1 of this Form 10-K
.

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

None.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934 (the "Exchange Act"), we conducted an evaluation under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our principal executive officer and principal financial officer concluded that as of December 31, 2013, our disclosure controls and procedures are effective in ensuring that all information required to be disclosed in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission rules and forms and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, in a manner that allows timely decisions regarding required disclosure.

Management’s Report on Internal Control over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Exchange Act. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's consolidated financial statements for external reporting purposes in accordance with United States generally accepted accounting principles.

Under the supervision and with the participation of the Company's management, including our principal executive officer and principal financial officer, the Company conducted an evaluation of the effectiveness of the internal control over financial reporting of the Company as referred to above as of December 31, 2013, as required by Rule 13a-15(c) under the Exchange Act. In making this assessment, the Company used the criteria set forth in the framework in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its evaluation under the framework in Internal Control - Integrated Framework, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2013.

We acquired Black Hawk Energy Services, Inc. ("Black Hawk"), on December 16, 2013. Our management has excluded the operations of this business from our evaluation of, and conclusion on, the effectiveness of our internal control over financial reporting as of December 31, 2013. This business represents 12% of our total assets as of December 31, 2013, and 2% of revenues for the year then ended. Our management plans to fully integrate the operations of this business into its assessment of the effectiveness of our internal control over financial reporting in 2014.

BDO, the independent registered public accounting firm, who audited the Company's consolidated financial statements included in this Annual Report on Form 10-K, has issued a report on the effectiveness of the Company's internal control over financial reporting as of December 31, 2013, which is included herein.

Changes in Internal Control over Financial Reporting

No change in internal control over financial reporting occurred during the quarter ended December 31, 2013, that has materially affected, or is reasonably likely to materially affect, the Company ’s internal control over financial reporting except for the changes in internal control over financial reporting associated with integrating the acquisition of Black Hawk, which was completed on December 16, 2013.

Inherent Limitations on Effectiveness of Controls

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.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information with respect to directors, executive officers, and corporate governance required by this Item is incorporated herein by reference to our Definitive Proxy Statement to be filed with the Securities and Exchange Commission by April 30, 2014.

Item 11. Executive Compensation

The information with respect to executive compensation required by this Item is incorporated herein by reference to our Definitive Proxy Statement to be filed with the Securities and Exchange Commission by April 30, 2014.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information with respect to security ownership of certain beneficial owners and management and related stockholder matters required by this Item is incorporated herein by reference to our Definitive Proxy Statement to be filed with the Securities and Exchange Commission by April 30, 2014.

Item 13. Certain Relationships and Related Transactions and Director Independence

The information with respect to certain relationships and related transactions and director independence required by this Item is incorporated herein by reference to our Definitive Proxy Statement to be filed with the Securities and Exchange Commission by April 30, 2014.

Item 14. Principal Accounting Fees and Services

The information with respect to principal accounting fees and services required by this Item is incorporated herein by reference to our Definitive Proxy Statement to be filed with the Securities and Exchange Commission by April 30, 2014.

PART IV
Item 15. Exhibits and Financial Statement Schedules

(a) Listed below are the documents filed as part of this report.

1. Financial Statements and Reports of Independent Registered Public Accounting Firm:

Report of Independent Registered Public Accounting Firm
Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting
Consolidated Statements of Operations for the years ended December 31, 2013, 2012, and 2011
Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2013, 2012, and 2011
Consolidated Balance Sheets as of December 31, 2013 and 2012
Consolidated Statements of Stockholders' Equity for the years December 31, 2013, 2012, and 2011
Consolidated Statements of Cash Flows for the years ended December 31, 2013, 2012, and 2011
Notes to Consolidated Financial Statements

2. Financial Statement Schedule:

Schedule II - Valuation and Qualifying Accounts for the years ended December 31, 2013, 2012, and 2011

3. Exhibits:

See Exhibit Index beginning on page G-1

SIGNATURES

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

Steel Excel Inc.

By: /s/ Jack L. Howard
Jack L. Howard
Vice Chairman
Date: March 12, 2014

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

Signature	Title
By: /s/ Jack L. Howard Jack L. Howard Date: March 12, 2014	Vice Chairman (Principal executive officer)
By: /s/ James F. McCabe, Jr. James F. McCabe, Jr. Date: March 12, 2014	Chief Financial Officer (Principal financial officer)
By: /s/ Warren G. Lichtenstein Warren G. Lichtenstein Date: March 12, 2014	Chairman of the Board
By: /s/ John J. Quicke John J. Quicke Date: March 12, 2014	Director
By: /s/ John Mutch John Mutch Date: March 12, 2014	Director
By: Gary Ullman Date: March 12, 2014	Director
By: /s/ Robert Valentine Robert Valentine Date: March 12, 2014	Director

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Steel Excel Inc.
White Plains, New York

We have audited the accompanying consolidated balance sheets of Steel Excel Inc. as of December 31, 2013 and 2012 and the related consolidated statements of operations, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2013. In connection with our audits of the financial statements, we have also audited the financial statement schedule listed in the accompanying index. 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 also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements and schedule. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Steel Excel Inc. and subsidiaries at December 31, 2013 and 2012, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2013, in conformity with accounting principles generally accepted in the United States of America.

Also, in our opinion, the financial statement schedule, when considered in relation to the basic consolidated 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), Steel Excel Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 12, 2014 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP
New York, New York
March 12, 2014

Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

Board of Directors and Stockholders
Steel Excel Inc.
White Plains, New York

We have audited Steel Excel, Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Steel Excel, 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, included in the accompanying Item 9A, "Management's Report on Internal Control Over Financial Reporting." Our responsibility is to express an opinion on 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, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included 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.

As indicated in the accompanying Item 9A, "Management's Report on Internal Control over Financial Reporting", management's assessment of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Black Hawk Energy Services, Inc., which was acquired on December 16, 2013, and which is included in the consolidated balance sheet of Steel Excel, Inc. as of December 31, 2013, and the related consolidated statements of operations, comprehensive income, stockholders' equity and cash flows for the year then ended. Black Hawk Energy Services, Inc. constituted 12% of total assets as of December 31, 2013 and 2% of revenues for the year then ended. Management did not assess the effectiveness of internal control over financial reporting of Black Hawk Energy Services, Inc. because of the timing of the acquisition which was completed on December 16, 2013. Our audit of internal control over financial reporting of Steel Excel, Inc. also did not include an evaluation of the internal control over financial reporting of Black Hawk Energy Services, Inc.

In our opinion, Steel Excel, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, 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 Steel Excel, Inc. as of December 31, 2013 and 2012, and the related consolidated statements of operations, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2013, and our report dated March 12, 2014 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP
New York, New York
March 12, 2014

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Steel Excel Inc.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands, except per-share data)		
Net revenues	$120,028	$100,104	$2,502
Cost of revenues	85,385	66,064	1,459
Gross profit	34,643	34,040	1,043
Operating expenses:			
Selling, general and administrative expenses	23,372	20,397	9,505
Amortization of intangibles	8,709	7,634	49
Impairment of goodwill	—	192	—
Total operating expenses	32,081	28,223	9,554
Operating income	2,562	5,817	(8,511)
Interest income, net	3,079	1,486	4,083
Other income (expense), net	1,408	(836)	4,270
Income (loss) from continuing operations before income taxes	7,049	6,467	(158)
Benefit from income taxes	9,342	15,712	226
Net income from continuing operations	16,391	22,179	68
Income (loss) from discontinued operations, net of taxes	(5,540)	(1,935)	6,629
Net income	10,851	20,244	6,697
Net loss attributable to non-controlling interests in consolidated entities			
Continuing operations	156	22	—
Discontinued operations	3,188	427	72
Net income attributable to Steel Excel Inc.	$14,195	$20,693	$6,769
Basic income (loss) per share attributable to Steel Excel Inc.:			
Net income from continuing operations	$1.31	$1.83	$0.01
Income (loss) from discontinued operations, net of taxes	$(0.19)	$(0.12)	$0.62
Net income	$1.13	$1.71	$0.62
Diluted income (loss) per share attributable to Steel Excel Inc.:			
Net income from continuing operations	$1.31	$1.83	$0.01

Income (loss) from discontinued operations, net of taxes	$(0.19)	$(0.12)	$0.61
Net income	$1.13	$1.71	$0.62
Shares used in computing income (loss) per share:			
Basic	12,584	12,110	10,882
Diluted	12,602	12,133	10,897

See accompanying Notes to Consolidated Financial Statements.

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Steel Excel Inc.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Net income	$10,851	$20,244	$6,697
Other comprehensive income (loss), net of taxes			
Net foreign currency translation adjustment:			
Foreign currency translation adjustment	(63)	(100)	164
Release of foreign currency translation gains	(361)	—	(2,542)
	(424)	(100)	(2,378)
Net unrealized gain on marketable securities, net of taxes	5,994	303	260
Comprehensive income	16,421	20,447	4,579
Comprehensive loss attributable to non-controlling interest	3,344	449	72
Comprehensive income attributable to Steel Excel Inc.	$19,765	$20,896	$4,651

See accompanying Notes to Consolidated Financial Statements.

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Steel Excel Inc.
CONSOLIDATED BALANCE SHEETS

	December 31, 2013	December 31, 2012
	(in thousands. except per-share data)	
Assets		
Current assets:		
Cash and cash equivalents	$73,602	$71,556
Marketable securities	178,485	199,128
Accounts receivable, net of allowance for doubtful accounts of $0	24,904	17,257
Prepaid expenses and other current assets	4,559	3,482
Deferred income taxes	—	188
Current assets of discontinued operations	31	—
Total current assets	281,581	291,611
Property and equipment, net	106,383	77,768
Goodwill	80,354	53,093
Intangible assets, net	32,228	39,887
Other investments	25,844	1,021
Investments in equity method investees	8,339	—
Deferred income taxes	1,556	1,696
Other long-term assets	1,754	1,419
Total assets	$538,039	$466,495
Liabilities and Stockholders' Equity:		
Current liabilities:		
Accounts payable	$4,503	$4,282
Accrued expenses and other liabilities	7,359	6,103
Current portion of long-term debt	13,214	4,000
Current portion of capital lease obligations	412	413
Convertible senior subordinated notes	346	346
Deferred income taxes	3,612	—
Current liabilities of discontinued operations	987	—
Total current liabilities	30,433	15,144
Capital lease obligations, net of current portion	572	984
Long-term debt, net of current portion	79,286	9,000
Deferred income taxes	—	33
Other long-term liabilities	3,813	9,372
Total liabilities	114,104	34,533
Commitments and contingencies		
Stockholders' equity:		
Common stock ($0.001 par value, 40,000 shares authorized; 14,508 shares and 14,365 shares issued in 2013 and 2012, respectively)	14	14
Additional paid-in capital	274,826	272,786
Accumulated other comprehensive income	6,516	946
Retained earnings	213,967	199,772
Treasury stock, at cost (2013 - 2,503 shares; 2012 - 1,458 shares)	(71,001)	(41,617)
Total Steel Excel Inc. stockholders' equity	424,322	431,901

Non-controlling interest	(387)	61
Total stockholders' equity	423,935	431,962
Total liabilities and stockholders' equity	$538,039	$466,495

See accompanying Notes to Consolidated Financial Statements.

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Steel Excel Inc.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands)

	Common Stock		Treasury Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income	Retained Earnings	Non-Controlling Interest	Total
	Shares	Amount	Shares	Amount					
Balance, January 1, 2011	12,229	$12	(1,347)	$(38,841)	$209,924	$ 2,861	$172,310	$ —	$346,266
Net income attributable to Steel Excel Inc.	—	—	—	—	—	—	6,769	—	6,769
Net loss attributable to non-controlling interest	—	—	—	—	—	—	—	(72)	(72)
Other comprehensive loss	—	—	—	—	—	(2,118)	—	—	(2,118)
Sale of common stock under employee option plans	1	—	—	—	29	—	—	—	29
Net issuance of restricted shares	9	—	—	—	—	—	—	—	—
Stock-based compensation	—	—	—	—	523	—	—	—	523
Non-controlling interest of acquired entity	—	—	—	—	—	—	—	500	500
Balance, December 31, 2011	12,239	12	(1,347)	(38,841)	210,476	743	179,079	428	351,897
Net income attributable to Steel Excel Inc.	—	—	—	—	—	—	20,693	—	20,693
Net loss attributable to non-controlling interest	—	—	—	—	—	—	—	(449)	(449)
Non-controlling interest of acquired entities	—	—	—	—	—	—	—	157	157
Other comprehensive income	—	—	—	—	—	203	—	—	203
Net issuance of restricted shares	99	—	—	—	—	—	—	—	—
Stock-based compensation	—	—	—	—	1,487	—	—	—	1,487
Issuance of common stock for acquisition	2,027	2	—	—	60,823	—	—	—	60,825
	—	—	(111)	(2,776)	—	—	—	—	(2,776)

Repurchases of common stock									
Reversal of non-controlling interest upon disposition	—	—	—	—	—	—	—	(75)	(75)
Balance, December 31, 2012	14,365	14	(1,458)	(41,617)	272,786	946	199,772	61	431,962
Net income attributable to Steel Excel Inc.	—	—	—	—	—	—	14,195	—	14,195
Net loss attributable to non-controlling interest	—	—	—	—	—	—	—	(3,344)	(3,344)
Other comprehensive income	—	—	—	—	—	5,570	—	—	5,570
Net issuance of restricted shares	143	—	—	—	—	—	—	—	—
Stock-based compensation	—	—	—	—	2,040	—	—	—	2,040
Repurchases of common stock	—	—	(1,045)	(29,384)	—	—	—	—	(29,384)
Non-controlling interest of acquired entities	—	—	—	—	—	—	—	2,896	2,896
Balance, December 31, 2013	14,508	$14	(2,503)	$(71,001)	$274,826	$ 6,516	$213,967	$ (387)	$423,935

See accompanying Notes to Consolidated Financial Statements.

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Steel Excel Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Cash Flows From Operating Activities:			
Net income	$10,851	$20,244	$6,697
Adjustments to reconcile net income to net cash provided by operating activities:			
Loss (income) from discontinued operations	5,540	1,935	(6,629)
Stock-based compensation expense	2,040	1,487	523
Depreciation and amortization	19,185	15,303	369
Adjustment of deferred income taxes	(1,536)	(15,105)	1,395
Gain on sales of marketable securities	(2,608)	(282)	(1,713)
Reversal of tax reserves	(7,236)	—	—
Loss on equity-method investees	863	—	—
Loss on extinguishment of debt	463	—	—
Other	471	2,436	(102)
Changes in operating assets and liabilities, net of effects of acquisitions:			
Accounts receivable	2,653	(5,469)	(569)
Assets held for sale	—	—	6,216
Prepaid expenses and other assets	(833)	(1,102)	2,033
Accounts payable and other liabilities	(2,044)	(195)	(5,757)
Net cash provided by (used in) operating activities of discontinued operations	(2,116)	(847)	6,647
Net cash provided by operating activities	25,693	18,405	9,110
Cash Flows From Investing Activities:			
Purchases of businesses, net of cash acquired	(61,888)	(52,567)	(36,530)
Purchases of property and equipment	(8,932)	(11,818)	(65)
Proceeds from sale of property and equipment	552	—	—
Investments in cost method investee	(25,000)	—	—
Investments in equity method investees	(9,202)	—	—
Purchases of marketable securities	(189,268)	(523,443)	(537,898)
Sales of marketable securities	75,825	574,074	442,939
Maturities of marketable securities	145,994	64,253	92,321
Net cash provided by investing activities of discontinued operations	—	75	—
Net cash provided by (used in) investing activities	(71,919)	50,574	(39,233)
Cash Flows From Financing Activities:			
Proceeds from issuance of common stock	—	—	29
Repurchases of common stock	(29,384)	(2,776)	—
Proceeds from issuance of long-term debt	95,000	—	—
Payments for debt issuance costs	(1,368)		—
Repayments of capital lease obligations	(413)	(230)	—
Repayments of long-term debt	(15,500)	(3,000)	—
Net cash provided by (used in) financing activities	48,335	(6,006)	29

Net increase in cash and cash equivalents	2,109	62,973	(30,094)
Effect of foreign currency translation on cash and cash equivalents	(63)	96	305
Cash and cash equivalents at beginning of period	71,556	8,487	38,276
Cash and cash equivalents at end of period	$73,602	$71,556	$8,487

See accompanying Notes to Consolidated Financial Statements.

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Steel Excel Inc.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Basis of Presentation

Steel Excel Inc. (“Steel Excel” or the “Company”) currently operates in two reporting segments - Energy and Sports. Through its wholly-owned subsidiary Steel Energy Ltd. ("Steel Energy"), the Company’s Energy business provides drilling and production services to the oil and gas industry. Through its wholly-owned subsidiary Steel Sports Inc., the Company’s Sports business provides event-based sports services and other health-related services. The Company also continues to identify business acquisition opportunities in other unrelated industries. The Company began its Sports and Energy businesses in June 2011 and December 2011, respectively. Prior to that the Company provided enterprise-class external storage products and software to original equipment manufacturers (the "Predecessor Business"). Steel Partners Holdings L.P. (“Steel Partners”), an affiliate, beneficially owned approximately 55.1% of the Company’s outstanding common stock as of December 31, 2013.

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States, and include the accounts of the Company and all of its subsidiaries. The Company consolidates entities in which it owns greater than 50% of the voting equity of an entity or otherwise is able to exert control. All intercompany accounts and transactions have been eliminated in the consolidated financial statements.
Certain prior period amounts have been reclassified to conform to the 2013 presentation. The Company shut down the operations of The Show, LLC (“The Show”), a provider of baseball uniforms to Little League and softball players and coaches, and Ruckus Sports LLC (“Ruckus”), a provider of obstacle course and mass-participation events, in July 2012 and November 2013, respectively. Both The Show and Ruckus were part of the Company’s Sports business. The consolidated financial statements reflect The Show, Ruckus, and any residual activity of the Predecessor Business as discontinued operations in all periods.

2. Summary of Significant Accounting Policies

Cash and Cash Equivalents: Cash and cash equivalents include all cash balances and highly liquid investments having original maturities of three months or less.

Marketable Securities: Marketable securities are classified as available-for-sale and consist of corporate equities and obligations, United States government securities, mutual funds, and commercial paper. Marketable securities are reported at fair value, with unrealized gains and losses recognized in stockholders’ equity as “other comprehensive income (loss)”. Declines in fair value that are determined to be other than temporary are recognized as an impairment charge. Realized gains or losses on marketable securities are determined based on specific identification of the securities sold and are recognized as “other income (loss)” at the time of sale. The Company classifies its marketable securities as current assets based on the nature of the securities and their availability for use in current operations.

Allowance for Doubtful Accounts: The Company recognizes bad debt expense on trade receivables through an allowance account using estimates based on past experience, and writes off trade receivables against the allowance account when the Company believes it has exhausted all available means of collection. There was no allowance for doubtful accounts recognized as of December 31, 2013 and 2012.

Fair Value Measurements: The Company reports certain assets and liabilities at their fair value, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the
measurement date. Fair values of assets and liabilities are determined based on a three-level measurement input hierarchy. Level 1 inputs are quoted prices in active markets for identical assets or liabilities as of the measurement

date. Level 2 inputs are other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs can include quoted prices in active markets for similar assets or liabilities, quoted prices in a market that is not active for identical assets or liabilities, or other inputs that can be corroborated by observable market data. Level 3 inputs are unobservable for the asset or liability when there is little, if any, market activity for the asset or liability. Level 3 inputs are based on the best information available, and may include data developed by the Company.

Property and Equipment, Net: Property and equipment is stated at cost. Depreciation is computed on a straight-line basis over the estimated useful lives of the assets, which generally range from four years for vehicles and certain equipment to thirty-nine years for buildings. Leasehold improvements and assets recorded under capital leases are amortized on a straight-line basis over the shorter of their estimated useful lives or the terms of the leases.

Long-Lived Assets: The Company evaluates the recoverability of its finite-lived intangible assets and its property and equipment by comparing their carrying value to the expected future undiscounted cash flows to be generated from such assets when events or circumstances indicate that an impairment may have occurred.

Goodwill: Goodwill is tested for impairment on an annual basis, or more frequently if an event occurs or circumstances change to indicate that an impairment may have occurred. The Company performs its annual impairment test on September 30 of each year. The goodwill impairment test involves a two-step process. The first step compares the fair value of a reporting unit with its carrying amount, including goodwill. No potential impairment exists if the carrying value of the reporting unit is less than its fair value. If the carrying value of the reporting unit exceeds its fair value, then the second step is necessary to measure the impairment. The second step compares the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. Any excess of the reporting unit goodwill carrying value in excess of the implied fair value is recognized as an impairment.

Other Investments: Investments that do not have a readily determinable market value and in which the Company does not have a controlling financial interest are accounted for as cost-method investments or, if they Company has the ability to exert significant influence, as equity-method investments. The carrying value of equity-method investments are adjusted for the Company's proportionate share of the investee's earnings, which may be reported on a lag of up to three months. Both cost-method investments and equity-method investments are monitored for indications of impairment.

Contingent Liabilities: The Company recognizes a liability for certain contingencies, including those related to litigation or claims or to certain governmental laws and regulations, when it is probable that an asset has been impaired or a liability has been incurred, and the amount of the loss can be reasonably estimated.

Business Combinations: The Company allocates the fair value of the total consideration of its acquisitions to the tangible assets, liabilities, and identifiable intangible assets acquired based on their estimated fair values. The excess of the fair value of the total consideration over the fair values of these identifiable assets and liabilities is recognized as goodwill. Acquisition-related expenses are recognized separately from the business combination and are expensed as incurred as a component of "selling, general, and administrative expenses."

Revenue Recognition: The Company recognizes revenue at the time the service is provided to the customer. Revenue is recognized in the Energy business when the services are rendered. Revenue is recognized in the Sports business when the service is rendered or the event occurs. Amounts received from customers in advance of the service or event are deferred until such time the service is rendered or the event occurs.

Stock-based Compensation: The Company recognizes compensation expense for stock options and restricted stock granted to employees and non-employee directors over the requisite service period based on the estimated fair value on the grant date. The fair value of equity awards is estimated using the Black-Scholes pricing model.

Advertising expenses: Advertising costs are expensed in the period in which the advertising appears in print or is broadcast. The Company's advertising expense for the years ended December 31, 2013, 2012, and 2011, was de minimis.

Foreign Currency Translation: Although the Company no longer has current operations in foreign jurisdictions, it consolidates certain foreign-based entities associated with the Predecessor Business. Assets and liabilities of foreign entities are translated from the functional currency into United States dollars using the exchange rate in effect at the balance sheet date. Revenues and expenses of foreign operations are translated from the functional currency into United States dollars using the average exchange rate for the period. Adjustments resulting from the translation into United States dollars are recognized in stockholders' equity as "other comprehensive income (loss)".

Income Taxes: The Company uses the asset and liability method of accounting for income taxes. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts. Valuation allowances are recorded to reduce deferred tax assets to the amount that will more likely than not be realized, with changes in valuation allowances recognized in the provision for income taxes. The Company accounts for uncertainty in income taxes using a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement. The Company classifies the liability for unrecognized tax benefits as current to the extent that the Company anticipates payment within one year. Interest and penalties related to uncertain tax positions are recognized in the provision for income taxes.

Income (Loss) per Share: Basic net income (loss) per share of common stock is computed by dividing net income (loss) by the weighted-average number of common shares outstanding during the period. Diluted net income (loss) per share gives effect to all potentially dilutive common shares outstanding during the period.

Concentration of Credit Risk: Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, marketable securities, and trade receivables. The Company maintains its cash balances and marketable securities with high credit quality financial institutions. Deposits held with banks, including those held in foreign branches of global banks, may exceed the amount of insurance provided on such deposits. These deposits may be withdrawn upon demand and therefore bear minimal risk. The Company limits the amount of credit exposure through diversification and management regularly monitors the composition of its investment portfolio.

The Company provides credit to customers on an uncollateralized basis after evaluating client creditworthiness. The Company’s clients in its Energy business are concentrated in the oil and gas industry, and are concentrated in North Dakota and Montana in the Bakken basin. The Company’s five largest customers in the Energy business provided approximately 51.3% and 48.3% of consolidated revenues for the years ended December 31, 2013 and 2012, respectively. In addition, amounts due from these clients represented 42.3% and 57.7% of trade accounts receivable at December 31, 2013 and 2012, respectively. A significant reduction in business from a significant customer or their failure to pay outstanding trade accounts receivable could have a material adverse effect on the Company’s results of operations and financial condition.

Use of Estimates: The preparation of the Company’s consolidated financial statements in conformity with generally accepted accounting principles in the United States requires management to make estimates and assumptions. These estimates affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from these estimates.

Recently Issued Accounting Standards: In February 2013, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update (“ASU”) No. 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income , which requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. This pronouncement was effective for reporting periods beginning after December 15, 2012. The Company adopted this pronouncement effective as of January 1, 2013. The adoption of ASU No. 2013-02 did not have a material effect on the Financial Statements.

In March 2013, the FASB issued ASU No. 2013-05, Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity. The objective of this pronouncement is to resolve the diversity in practice regarding the release into net income of the cumulative translation adjustment upon derecognition of a subsidiary or group of assets within a foreign entity. ASU No. 2013-05 is effective prospectively for fiscal years beginning after December 15, 2013, and for interim reporting periods within those years, with early adoption permitted. The Company does not expect the adoption of ASU No. 2013-05 to have a material effect on the Financial Statements.

In July 2013, the FASB issued ASU No. 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, which provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, similar tax loss, or tax credit carryforward exists. This pronouncement is effective for fiscal years beginning after December 15, 2013, and for interim reporting periods within those years. The Company does not expect the adoption of ASU No. 2013-11 to have a material effect on the Financial Statements.

3. Acquisitions

Energy Business

On December 16, 2013, the Company acquired the business and substantially all of the assets of Black Hawk Energy Services, Inc. (“Black Hawk”), a provider of drilling and production services to the oil and gas industry, for approximately $60.8 million in cash, subject to a post-closing working capital adjustment. The acquisition was funded with approximately $35.8 million from the Company's cash reserves and $25.0 million in proceeds from additional borrowings under an existing credit facility (see Note 9). The Company acquired Black Hawk to further solidify its presence in North Dakota in the Bakken basin and to expand its business into other regions, including Texas and New Mexico.

The estimated fair value of the assets and liabilities acquired in connection with the Black Hawk transaction was as follows:

	Amount (in thousands)
Accounts receivable	$9,663
Prepaid expenses and other current assets	208
Property and equipment	30,581
Accounts payable	(1,333)
Accrued expenses	(1,756)
Total net identifiable assets	37,363
Goodwill	23,400
Net assets acquired	$60,763

The fair values recognized in connection with the Black Hawk transaction are provisional pending the Company's continued evaluation, including assessing any identifiable intangible assets acquired, the value of which are included in goodwill as of December 31, 2013, and completing a valuation of the tangible and intangible assets. The fair value of trade accounts receivable was based on their carrying value at the date of acquisition and is expected to be fully collected. The goodwill recognized, which is expected to be fully deductible for tax purposes, arises from the growth potential the Company anticipates along with expected synergies within the Company’s Energy business. The results of operations of Black Hawk have been included in the Company's results of operations since the acquisition date. Revenues and operating income from Black Hawk included in the Company’s consolidated financial statements for the year ended December 31, 2013, totaled $2.5 million and $0.8 million respectively.

On February 9, 2012, the Company acquired the business and assets of Eagle Well Services, Inc. (“Eagle Well”), a provider of drilling and production services to the oil and gas industry, for approximately $48.1 million in cash. The Company acquired Eagle Well to expand its then nascent Energy business.

The estimated fair value of the assets and liabilities acquired in connection with the Eagle Well transaction was as follows:

	Amount (in thousands)
Property and equipment	$23,842
Identifiable intangible assets	14,300
Accrued expenses	(137)
Total net identifiable assets	38,005
Goodwill	10,126
Net assets acquired	$48,131

The goodwill recognized, which is fully deductible for tax purposes, arose from the growth potential the Company anticipated along with expected synergies within the Company’s Energy business. The intangible assets acquired represented customer relationships, which are being amortized over a ten-year period. The results of operations of Eagle Well have been included in the Company's results of operations since the acquisition date.

On May 31, 2012, the Company acquired all of the outstanding equity of Sun Well Service, Inc. (“Sun Well”), a provider of drilling and production services to the oil and gas industry. The total consideration aggregated $68.7 million, and consisted of 2,027,500 shares of the Company’s common stock valued at $60.8 million and $7.9 million of cash. The Company acquired Sun Well to further expand its Energy business. Steel Partners beneficially owned approximately 85% of Sun Well and approximately 40% of the Company at the time of the acquisition. Both the Company and Steel Partners appointed a special committee of independent directors to consider and negotiate the transaction because of the ownership interest held by Steel Partners in each entity (see Note 19 for related party information).

The estimated fair value of the assets and liabilities acquired in connection with the acquisition of Sun Well was as follows:

	Amount (in thousands)	
Cash	$3,561	
Accounts receivable	7,233	
Prepaid expenses and other current assets	782	
Property and equipment	29,787	
Identifiable intangible assets	27,300	
Other long-term assets	714	
Accounts payable	(1,036	)
Accrued expenses and other current liabilities	(2,030	)
Other long-term liabilities	(1,805	)
Long-term debt	(16,000	)
Capital lease obligations	(1,622	)
Deferred tax liabilities	(16,539	)
Total net identifiable assets	30,345	
Goodwill	38,401	
Net assets acquired	$68,746	

The goodwill recognized has been adjusted in 2013 to reflect additional acquisition-date deferred income tax liabilities and non-current deferred compensation obligations aggregating $1.8 million. The goodwill recognized, which is not deductible for tax purposes, arose from the growth potential the Company anticipates along with expected synergies within the Company’s Energy business. The intangible assets acquired represented customer relationships and a trade name, which are being amortized over ten-year and five-year periods, respectively. The fair value of trade accounts receivable was based on their carrying value at the date of acquisition and was expected to be fully collected.

Upon the acquisition of Sun Well, the business of Eagle Well was merged with the business of Sun Well and operated as a single business. The results of operations of Eagle Well and Sun Well have been included in the Company's results of operations since their respective acquisition dates. Revenues and operating income from the combined business of Eagle Well and Sun Well included in the Company’s consolidated financial statements for the year ended December 31, 2012, totaled $70.4 million and $14.6 million, respectively.

On December 7, 2011, the Company acquired the business and assets of Rogue Pressure Services, LLC (“Rogue”), a provider of drilling and production services to the oil and gas industry. The total consideration aggregated $30.2 million, and consisted of $29.0 million of cash and contingent consideration of $1.2 million. The acquisition of Rogue represented the Company’s entrance into the Energy business.

The estimated fair value of the assets and liabilities acquired in connection with the Rogue transaction was as follows:

	Amount (in thousands)
Accounts receivable	$4,031
Inventory	138
Prepaid expenses	78
Property and equipment	15,309
Identifiable intangible assets	5,600
Accrued expenses	(1,194)
Total identifiable net assets	23,962
Goodwill	6,256
Net assets acquired	$30,218

The goodwill recognized, which is fully deductible for tax purposes, arose from the growth potential the Company anticipated. The intangible assets acquired represented customer relationships and a trade name, which are being amortized over ten-year and five-year periods, respectively. The fair value of trade accounts receivable was based on their carrying value at the date of acquisition and was expected to be fully collected. The results of operations of Rogue have been included in the Company's results of operations since the acquisition date. Revenues and operating income from Rogue included in the Company’s consolidated financial statements for the year ended December 31, 2011, totaled $1.4 million and $0.2 million respectively.

The contingent consideration recognized at the acquisition date of Rogue was payable upon attaining certain operational performance levels in the ensuing three years. In 2012, the Company reversed $0.7 million of the contingent consideration liability based on the failure to achieve the operational performance levels in 2012 and projections of future years' performance. In 2013, the Company reversed the remaining $0.5 million of the contingent consideration liability based on the projections for 2013 and 2014. Such amounts were recognized as a reduction of "Selling, general, and administrative expenses" in the respective periods.

Sports Business

On January 31, 2013, the Company acquired a 20% membership interest in Ruckus with an option to acquire an additional 40% membership interest in the next two years. Pursuant to an operating agreement, the Company appointed two directors on a three-member board of directors and therefore has the ability to control the operations of Ruckus. Accordingly, the Company accounted for its acquisition of its 20% membership interest as a business combination and consolidates Ruckus. The total consideration aggregated $1.0 million, and consisted of $0.9 million of cash and the contribution of a loan of $0.1 million. The fair value of the non-controlling interest at the acquisition date was based on the amount paid by the Company for its 20% membership interest and a control premium equal to 50% of the total consideration based on a study of business combinations. The Company acquired its membership interests in Ruckus to expand the health-related and entertainment services of its Sports business. In May 2013 and July 2013 the Company acquired additional membership interests in Ruckus of 10% and 15%, respectively, for cash payments aggregating $1.3 million, thereby increasing the Company's ownership interest to 45%. Such additional investments were recorded as equity transactions since Ruckus was a consolidated at the time of the investments.

In connection with the acquisition of its membership interests in Ruckus, the Company recognized approximately $3.6 million of goodwill and a non-controlling interest of approximately $2.3 million. Ruckus had tangible net liabilities at the date of acquisition that were not material.

In November 2013, the Company shut down the operations of Ruckus after it did not meet operational and financial expectations. The Company recognized a goodwill impairment charge of $3.6 million in connection with the shutdown of the business. Ruckus is reported as a discontinued operation in the Company's consolidated financial statements and no amounts are included in revenues or operating income from continuing operations.

On June 19, 2013, the Company acquired 80% of the outstanding common stock of UK Elite Soccer, Inc. ("UK

Elite"), a provider of youth soccer programs and camps, for approximately $2.3 million in cash. The fair value of the non-controlling interest at the acquisition date was based on the amount paid by the Company for 80% of the common stock. The Company acquired UK Elite to expand its Sports business to include soccer events.

The estimated fair value of the assets and liabilities acquired in connection with the acquisition of UK Elite was as follows:

	Amount (in thousands)
Cash	$1,126
Marketable securities	194
Accounts receivable	637
Prepaid expenses and other current assets	759
Identifiable intangible assets	1,050
Other assets	53
Accrued liabilities and other current liabilities	(2,577)
Deferred income taxes	(447)
Total identifiable net assets	795
Non-controlling interest	(563)
Goodwill	2,018
Net assets acquired	$2,250

The goodwill recognized, which is not deductible for tax purposes, arose from the growth potential the Company anticipated. The intangible assets acquired represented customer relationships and a trade name, which are being amortized over four-year and five-year periods, respectively. The results of operations of UK Elite have been included in the Company's results of operations since the acquisition date. Revenues and operating income from UK Elite included in the Company's consolidated financial statements for the year ended December 31, 2013, totaled $6.2 million and $0.6 million, respectively.

On November 5, 2012, the Company acquired a 50% interest in two Crossfit® facilities in California that provide strength and conditioning services. Through the provisions of the operating agreements the Company has the ability to control the operations of the Crossfit® entities. Accordingly, the Company accounted for its investments as business combinations and consolidates both entities. The Company acquired its interests in the Crossfit® entities for approximately $0.1 million in cash and a commitment to loan one of the Crossfit® entities up to $1.1 million to fund the construction of the facility and the purchase of equipment.

In connection with the acquisition of its interests in the Crossfit® entities, the Company recognized approximately $0.2 million of goodwill and a non-controlling interest of approximately $0.1 million. The Crossfit® entities had tangible net assets at the date of acquisition that were not material. The results of operations of the Crossfit® entities have been included in the Company's results of operations since the acquisition date. Revenues and operating income from the Crossfit® entities included in the Company's consolidated financial statements for the year ended December 31, 2012, were not material.

On June 27, 2011, the Company acquired the business and net assets of Baseball Heaven LLC and Baseball Café, Inc. (collectively, "Baseball Heaven"), a provider of baseball facility services, for approximately $6.0 million in cash. The acquisition of Baseball Heaven represented the Company’s entrance into the Sports business.

The estimated fair value of the assets and liabilities acquired in connection with the Baseball Heaven transaction was as follows:

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	Amount (in thousands)
Accounts receivable	$149
Loan receivable	15
Property and equipment	5,855
Identifiable intangible assets	235
Deferred revenue	(416)
Total identifiable net assets	5,838
Goodwill	192
Net assets acquired	$6,030

The goodwill recognized, which is fully deductible for tax purposes, arose from the growth potential the Company anticipated. The intangible assets acquired represented customer relationships and are being amortized over a five-year period. The fair value of trade accounts receivable was based on their carrying value at the date of acquisition and was expected to be fully collected. The results of operations of Baseball Heaven have been included in the Company's results of operations since the acquisition date. Revenues from Baseball Heaven included in the Company’s consolidated financial statements for the year ended December 31, 2011, totaled $1.1 million. The operating loss from Baseball Heaven included in the Company's consolidated financial statements for the year ended December 31, 2011, was not material. In December 2012, the goodwill associated with the Baseball Heaven transaction was determined to be fully impaired and the Company incurred an impairment charge of $0.2 million.

On August 15, 2011, the Company acquired a 75% membership interest in The Show, a provider of baseball uniforms to Little League and softball players and coaches, for approximately $1.5 million in cash. The fair value of the non-controlling interest at the acquisition date was based on the amount paid by the Company for the 75% membership interest. The Company acquired The Show to expand upon its then recent entry into the Sports business.

In connection with the acquisition of its membership interests in The Show, the Company recognized approximately $1.8 million of goodwill and a non-controlling interest of approximately $0.5 million. The Show had tangible net assets at the date of acquisition that were not material.

In July 2012, the Company shut down the operations of The Show after it did not meet operational and financial expectations. The Company recognized a goodwill impairment charge of $1.8 million in connection with the shutdown of The Show. The Show is reported as a discontinued operation in the Company’s consolidated financial statements and no amounts are included in revenues or operating income from continuing operations.

The following unaudited pro forma financial information combines the results of operations of the Company with the results of operations of the acquisitions consummated during the years ended December 31, 2013 and 2012, as if those acquisitions had occurred at the beginning of the year prior to the date of acquisition. The pro forma financial information does not include the results of operations of the Crossfit® entities since they were not material. The pro forma financial information also does not include the results of Ruckus and The Show, which are reported as discontinued operations in the Company's consolidated financial statements. The pro forma financial information is not necessarily indicative of what would have actually occurred had the acquisitions been consummated at the beginning of the year prior to the date of acquisition or results that may occur in the future.

	Fiscal Year Ended December 31,	
	2013	2012
	(in thousands)	
Net revenues	$182,591	$164,652
Net income from continuing operations	$27,963	$32,386
Net income	$22,423	$31,399
Net income attributable to Steel Excel Inc.	$25,767	$30,900

4. Discontinued Operations

The Company shut down the operations of Ruckus and The Show in November 2013 and July 2012, respectively, after they did not meet operational and financial expectations. Both The Show and Ruckus were part of the Company’s Sports business. In 2011 the Company sold certain patents related to the Predecessor Business and, upon the satisfaction of specified conditions, received approximately $5.0 million for amounts held in escrow in connection with the sale of a component of the Predecessor Business in 2010.

The operations of Ruckus, The Show, and the Predecessor Business are reported as discontinued operations for all periods presented in the consolidated financial statements. The results of operations of Ruckus, The Show, and the Predecessor Business and the gain (loss) on the sale or disposal are presented as discontinued operations in the accompanying consolidated financial statements follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Revenues	$1,260	$451	$91
Income (loss) from operations of discontinued operations	$(5,540)	$(1,935)	$1,624
Gain on disposal of discontinued operations	—	—	5,005
Income (loss) from discontinued operations	$(5,540)	$(1,935)	$6,629

The loss from operations for the year ended December 31, 2013, consists entirely of the loss from operations of Ruckus, and includes a goodwill impairment charge of $3.6 million. The loss from operations for the year ended December 31, 2012, consists entirely of the loss from operations of The Show, and includes a goodwill impairment charge of $1.8 million. The income from operations for the year ended December 31, 2011, includes income of $1.9 million from certain wind down activities of the Predecessor Business, partially offset by a loss from operations of $0.3 million from The Show. The gain on disposal for December 31, 2011, consists entirely of activity of the Predecessor Business. There was no tax effect on any of the activity of discontinued operations for the years ended December 31, 2013, 2012, and 2011.

5. Investments

Marketable Securities

All of the Company's marketable securities at December 31, 2013 and 2012, were classified as "available-for-sale" securities, with changes in fair value recognized in stockholders' equity as "other comprehensive income (loss)". Marketable securities at December 31, 2013, consisted of the following:

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	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
Short-term deposits	$60,909	$—	$—	$60,909
Mutual funds	15,722	5,061	—	20,783
United States government securities	50,356	23	—	50,379
Corporate securities	69,806	9,961	(5,208)	74,559
Corporate obligations	31,356	885	(276)	31,965
Commercial paper	1,799	—	—	1,799
Total available-for-sale securities	229,948	15,930	(5,484)	240,394
Amounts classified as cash equivalents	(61,909)	—	—	(61,909)
Amounts classified as marketable securities	$168,039	$15,930	$(5,484)	$178,485

Marketable securities at December 31, 2012, consisted of the following:

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
Short-term deposits	$48,596	$—	$—	$48,596
Mutual funds	10,368	1,452	—	11,820
United States government securities	99,299	178	—	99,477
Corporate securities	20,842	1,255	(1,980)	20,117
Corporate obligations	48,708	283	(277)	48,714
Commercial paper	22,275	16	—	22,291
Total available-for-sale securities	250,088	3,184	(2,257)	251,015
Amounts classified as cash equivalents	(51,887)	—	—	(51,887)
Amounts classified as marketable securities	$198,201	$3,184	$(2,257)	$199,128

Proceeds from sales of marketable securities were $75.8 million, $574.1 million, and $442.9 million for the years ended December 31, 2013, 2012, and 2011, respectively. The company determines gains and losses from sales of marketable securities based on specific identification of the securities sold. Gross realized gains and losses from sales of marketable securities, all of which are reported as a component of "Other income (expense), net" in the consolidated statements of operations for the years ended December 31, 2013, 2012, and 2011, were as follows:

	Fiscal Year Ended December 31, 2013		
	2013	2012	2011
Gross realized gains	$6,984	$628	$1,993
Gross realized losses	(4,376)	(346)	(280)
Realized gains, net	$2,608	$282	$1,713

The fair value of the Company's marketable securities with unrealized losses at December 31, 2013, and the duration of time that such losses had been unrealized, were as follows:

	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	(in thousands)					
Corporate obligations	$10,477	$(276)	$—	$—	$10,477	$(276)
Corporate securities	15,609	(4,757)	803	(451)	16,412	(5,208)
Total	$26,086	$(5,033)	$803	$(451)	$26,889	$(5,484)

The fair value of the Company's marketable securities with unrealized losses at December 31, 2012, all of which had been unrealized for a period of less than twelve months, were as follows:

	Fair Value	Gross Unrealized Losses
	(in thousands)	
Corporate securities	$6,389	$(1,980)
Corporate obligations	14,252	(277)
Total	$20,641	$(2,257)

Gross unrealized losses primarily related to losses on corporate securities. The Company has evaluated such securities, which primarily consist of investments in equity securities of publicly-traded entities, as of December 31, 2013, and has determined that there was no indication of other-than-temporary impairments. This determination was based on several factors, including the length of time and extent to which fair value has been less than the cost basis, the financial condition and near-term prospects of the entity, and the Company's intent and ability to hold the corporate securities for a period of time sufficient to allow for any anticipated recovery in market value.

The amortized cost and estimated fair value of available-for-sale securities at December 31, 2013, by contractual maturity, were as follows:

	Cost	Estimated Fair Value
	(in thousands)	
Debt securities:		
Mature in one year or less	$40,580	$40,617
Mature after one year through three years	21,097	21,251
Mature in more than three years	21,833	22,274
Total debt securities	83,510	84,142
Securities with no contractual maturities	146,438	156,252
Total	$229,948	$240,394

Equity-Method Investments

In January 2013, the Company acquired a 40% membership interest in Again Faster LLC, a fitness equipment company, for total cash consideration of $4.0 million. The Company accounts for its investment in Again Faster under the equity method as the Company owns more than 20%, providing the Company with significant influence, but does not have a controlling financial interest or other control over the operations of Again Faster. For the year ended December 31, 2013, the Company recognized a loss of $0.3 million for its proportionate share in the losses of Again Faster, which are reported as a component of "Other income (expense), net" in the consolidated statement of operations.

On August 23, 2013, the Company acquired 1,316,866 shares of the common stock of iGo, Inc. ("iGo"), in a cash tender offer for total consideration of $5.2 million. The shares of common stock of iGo acquired by the Company represent approximately 44.0% of the outstanding shares of iGo on a fully-diluted basis and approximately 44.7% of the issued and outstanding shares of iGo. Pursuant to the Stock Purchase and Sale Agreement between the Company and iGo entered into on July 11, 2013, two members of iGo’s four-member board of directors were replaced by two designees of the Company. The Company accounts for its investment in iGo under the equity method as the Company’s 44.7% voting interest and board representation provide it with significant influence, but do not provide the Company with control over iGo’s operations. For the year ended December 31, 2013, the Company recognized a loss of $0.5 million for its proportionate share in the losses of iGo, which are reported as a component of "Other income (expense), net" in the consolidated statement of operations.

Other Investments

In July 2013, the Company invested $25.0 million in a limited partnership that co-invested with other private investment funds in a public company. The Company accounts for this investment under the cost method as the limited partnership has no operations and the Company does not have significant influence over the operations of the public company investee. Such investment had an approximate fair value of $26.0 million at December 31, 2013, based on the net asset value included in the monthly statement it receives from the partnership.

6. Fair Value Measurements

Fair values of assets and liabilities are determined based on a three-level measurement input hierarchy. Level 1 inputs are quoted prices in active markets for identical assets or liabilities as of the measurement date.

Level 2 inputs are other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. Level 2 inputs can include quoted prices in active markets for similar assets or liabilities, quoted prices in a market that is not active for identical assets or liabilities, or other inputs that can be corroborated by observable market data. The Company uses quoted prices of similar instruments with an active market to determine the fair value of its Level 2 investments.

Level 3 inputs are unobservable for the asset or liability when there is little, if any, market activity for the asset or liability. Level 3 inputs are based on the best information available, and may include data developed by the Company. The Company uses the net asset value included in quarterly statements it receives in arrears from two venture capital funds to determine the fair value of such funds. The Company determines the fair vale of certain corporate securities and corporate obligations by incorporating and reviewing prices provided by third-party pricing services based on the specific features of the underlying securities. The Company uses its own forecast data and probability assessments to determine the fair value of the contingent consideration.

Assets measured at fair value on a recurring basis at December 31, 2013, summarized by measurement input category, were as follows:

	Total (in thousands)	Level 1	Level 2	Level 3
Cash, including short-term deposits(1)	$72,602	$72,602	$—	$—
Mutual funds(2)	20,783	20,783	—	—
United States government securities(2)	50,379	50,379	—	—
Corporate securities(2)	74,559	68,624	—	5,935
Commercial paper(3)	1,799	—	1,799	—
Corporate obligations(2)	31,965	—	14,535	17,430
Investments in certain funds(4)	844	—	—	844

	$252,931	$212,388	$16,334	$24,209

(1) Reported within "Cash and cash equivalents."
(2) Reported within “Marketable securities.”
(3) $1.0 million reported within "Cash and cash equivalents" and $0.8 million reported within "Marketable securities."
(4) Reported within "Other investments."

Assets and liabilities measured at fair value on a recurring basis at December 31, 2012, summarized by measurement input category, were as follows:

	Total (in thousands)	Level 1	Level 2	Level 3
Assets				
Cash, including short-term deposits[1]	$68,265	$68,265	$—	$—
Mutual funds[2]	11,820	11,820	—	—
United States government securities[2]	99,477	99,477	—	—
Corporate securities[2]	20,117	20,117	—	—
Commercial paper[3]	22,291	—	22,291	—
Corporate obligations[2]	48,714	—	46,931	1,783
Investments in certain funds[4]	1,021	—	—	1,021
	$271,705	$199,679	$69,222	$2,804
Liabilities				
Acquisition-related contingent consideration[5]	$(475)	$—	$—	$(475)

(1) $68.2 million reported within “Cash and cash equivalents” and $0.1 million reported within “Marketable securities."
(2) Reported within “Marketable securities.”
(3) $3.4 million reported within "Cash and cash equivalents" and $18.9 million reported within "Marketable securities."
(4) Reported within "Other investments".
(5) Reported within “Accrued expenses”.

There were no transfers of securities among the various measurement input levels during the year ended December 31, 2013. The liability for contingent consideration was reversed during the year ended December 31, 2013 (see Note 3).

Changes in the fair value of assets valued using Level 3 measurement inputs during the year ended December 31, 2013, were as follows:

	Amount (in thousands)
Balance, January 1, 2013	$2,804
Purchases	45,383
Sales	(23,034)
Realized gain on sale	1,556
Change in fair value	(2,500)
Balance, December 31, 2013	$24,209

In November 2012, the Company invested $6.0 million in convertible debentures of School Specialty Inc. (“School Specialty”) with a face amount of $11.9 million. On January 28, 2013, School Specialty filed for protection under Chapter 11 of the United States Bankruptcy Code, and in subsequent months the Company invested approximately $21.3 million as part of the debtor-in-possession loan to School Specialty. Upon School Specialty emerging from bankruptcy on June 11, 2013, the Company received 26,457 shares of common stock of the post-bankruptcy entity in exchange for the convertible debentures, and received $17.5 million in cash and 49,136 shares of common stock of the post-bankruptcy entity in exchange for its investment in the debtor-in-possession loan. The fair value of the common stock of the post-bankruptcy entity received was $109 per share. In connection with these transactions, the Company recognized a loss on disposal of the subordinated debentures of approximately $3.2 million and a gain on disposal of the investment in the debtor-in-possession loan of approximately $1.6 million, both of which are included as a component of “Other income (expense), net” in the consolidated statements of operations for the year ended December 31, 2013. In addition, the Company invested $9.8 million in senior secured notes of the post-bankruptcy entity in June 2013. The Company's investments in the common stock and senior secured notes of the post-bankruptcy entity are included as Level 3 corporate securities and Level 3 corporate obligations, respectively, as of December 31, 2013.

The Company’s 3/4% Convertible Senior Notes due December 22, 2023, had a carrying value of approximately $0.3 million as of December 31, 2013 and 2012, which was a reasonable approximation of fair value as of both dates. The Company redeemed all outstanding Convertible Senior Notes in January 2014 with a cash payment of $0.3 million.

7. Property and Equipment, Net

Property and equipment at December 31, 2013 and 2012, consisted of the following:

	December 31, 2013	December 31, 2012
	(in thousands)	
Rigs and other equipment	$100,839	$68,404
Buildings and improvements	18,716	12,019
Land	1,550	1,068
Vehicles	1,869	1,639
Furniture and fixtures	557	289
Assets in progress	1,114	2,342
	124,645	85,761
Accumulated depreciation	(18,262)	(7,993)
Property and equipment, net	$106,383	$77,768

Depreciation expense was $10.5 million, $7.8 million, and $0.3 million for the years ended December 31, 2013, 2012, and 2011, respectively, and includes the depreciation associated with assets under capital leases (see Note 10).

During the years ended December 31, 2013 and 2012, the Company wrote off property and equipment totaling $0.1 million and $0.1 million, respectively, related to the shutdown of Ruckus and The Show, respectively (see Note 4). These write-offs are included in “Income (loss) from discontinued operations" in the consolidated statements of operations.

8. Goodwill and Other Intangible Assets

The Company's intangible assets at December 31, 2013 and 2012, all of which are subject to amortization, consisted of the following:

	December 31, 2013			December 31, 2012		
	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
	(in thousands)					
Energy segment:						
Customer relationships	$43,100	$(13,700)	$29,400	$43,100	$(6,356)	$36,744
Trade names	4,100	(2,315)	1,785	4,100	(1,125)	2,975
	47,200	(16,015)	31,185	47,200	(7,481)	39,719
Sports segment:						
Customer relationships	1,163	(230)	933	235	(67)	168
Trade names	122	(12)	110	—	—	—
	1,285	(242)	1,043	235	(67)	168
Total	$48,485	$(16,257)	$32,228	$47,435	$(7,548)	$39,887

Amortization expense was $8.7 million, $7.6 million, and $49,000 for the years ended December 31, 2013, 2012, and 2011, respectively.

Estimated aggregate amortization expense related to the intangible assets for the next five years and thereafter -is as follows:

	Amount (in thousands)
For the year ended December 31:	
2014	$6,868
2015	5,537
2016	4,529
2017	3,299
2018	2,826
Thereafter	9,169
	$32,228

The changes to the Company's carrying amount of goodwill were as follows:

	Fiscal Year Ended December 31, 2013			Year Ended December 31, 2012		
	Energy (in thousands)	Sports	Total	Energy	Sports	Total
Balance at beginning of period	$52,939	$154	$53,093	$6,256	$1,988	$8,244
Acquisitions (see Note 3)	23,400	5,594	28,994	46,683	154	46,837
Adjustment to fair value	1,844	—	1,844	—	—	—
Impairments	—	(3,577)	(3,577)	—	(1,988)	(1,988)
Balance at end of period	$78,183	$2,171	$80,354	$52,939	$154	$53,093

The adjustment to fair value in 2013 represents an adjustment to reflect additional acquisition-date deferred income tax liabilities and non-current deferred compensation obligations related to Sun Well (see Note 3). During the year ended December 31, 2013, the Company recognized a goodwill impairment of $3.6 million related to the shutdown of Ruckus. During the year ended December 31, 2012, the Company recognized a goodwill impairment of $1.8 million related to the shutdown of The Show and a goodwill impairment of $0.2 million related to Baseball Heaven. The goodwill impairments related to Ruckus and The Show are included in "Income (loss) from discontinued operations" in the consolidated statements of operations. The accumulated goodwill impairment was $5.6 million and $2.0 million at December 31, 2013 and 2012, respectively.

The components of goodwill at December 31, 2013 and 2012, were as follows:

	December 31, 2013 (in thousands)	December 31, 2012
Goodwill	$85,919	$55,081
Accumulated impairment	(5,565)	(1,988)
Net goodwill	$80,354	$53,093

9. Long-term Debt

On July 3, 2013, Steel Energy entered into a credit agreement (the "Energy Credit Agreement") with Wells Fargo Bank National Association, RBS Citizens, N.A., and Comerica Bank. The Energy Credit Agreement provided for a borrowing capacity of $80.0 million consisting of a $70.0 million secured term loan (the “Term Loan”) that was fully drawn by Steel Energy on July 3, 2013, and up to $10.0 million in revolving loans (the “Revolving Loans”) subject to a borrowing base of 85% of the eligible accounts receivable. The proceeds of the Term Loan at closing, along with proceeds from intercompany loans to

Steel Energy from Sun Well and Rogue, were used to pay the Company a dividend of $80.0 million and certain fees and expenses related to the Energy Credit Agreement.

In December 2013, Steel Energy entered into an amendment to the Energy Credit Agreement (together with the Energy Credit Agreement, the "Amended Credit Agreement") pursuant to which the borrowing capacity for the Term Loan was increased by an additional $25.0 million. The additional amounts under the Term Loan were fully drawn by Steel Energy upon closing and the proceeds, together with cash provided by the Company and Steel Energy, were used to fund the acquisition of Black Hawk (see Note 3). The Company incurred fees totaling approximately $1.4 million in connection with the Amended Credit Agreement that are being amortized over the life of the arrangement as a component of interest expense.

Borrowings under the Amended Credit Agreement are collateralized by substantially all the assets of Steel Energy and its wholly-owned subsidiaries Sun Well, Rogue, and Black Hawk, and a pledge of all of the issued and outstanding shares of capital stock of Sun Well, Rogue, and Black Hawk. Borrowings under the Amended Credit Agreement are fully guaranteed by Sun Well, Rogue, and Black Hawk. The carrying values as of December 31, 2013, of the assets pledged as collateral by Steel Energy and its subsidiaries under the Amended Credit Agreement were as follows:

	Amount (in thousands)
Cash and cash equivalents	$10,164
Accounts receivable	24,350
Property and equipment, net	97,910
Intangible assets, net	31,185
Total	$163,609

The Amended Credit Agreement has a term that runs through July 2018, with the Term Loan amortizing in quarterly installments of $3.3 million and a balloon payment due on the maturity date. At December 31, 2013, $92.5 million was outstanding under the Term Loan and no amount was outstanding under the Revolving Loans. Principal payments under the Amended Credit Agreement for subsequent years are as follows:

	Amount (in thousands)
2014	$13,214
2015	13,214
2016	13,214
2017	13,214
2018	39,644
Total	92,500
Less current portion	13,214
Total long-term debt	$79,286

Borrowings under the Amended Credit Agreement bear interest at annual rates of either (i) the Base Rate plus an applicable margin of 1.50% to 2.25% or (ii) LIBOR plus an applicable margin of 2.50% to 3.25%. The “Base Rate” is the greatest of (i) the prime lending rate, (ii) the Federal Funds Rate plus 0.5%, and (iii) the one-month LIBOR plus 1.0%. The applicable margin for both Base Rate and LIBOR is determined based on the leverage ratio calculated in accordance with the Amended Credit Agreement. LIBOR-based borrowings are available for interest periods of one, three, or six months. In addition, the Company is required to pay commitment fees of between 0.375% and 0.50% per annum on the daily unused amount of the Revolving Loans. The interest rate on the borrowings under the Amended Credit Agreement was 3.0% at December 31, 2013. For the year ended December 31, 2013, the Company incurred interest expense of $1.4 million in connection with the Amended Credit Agreement, consisting of $1.1 million in interest on the Term Loans and $0.3 million of amortization of deferred financing fees.

The Amended Credit Agreement contains certain financial covenants, including (i) a leverage ratio not to exceed 3.00:1 for quarterly periods through June 15, 2015, 2.75:1 for quarterly periods through June 30, 2017, and 2.5:1

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thereafter and (ii) a fixed charge coverage ratio of 1.15:1 for quarterly periods through December 31, 2016, and 1.25:1 thereafter. The Company was in compliance with all financial covenants as of December 31, 2013.
The Amended Credit Agreement also contains representations, warranties and non-financial covenants, including, among other things, covenants relating to (i) financial reporting and notification, (ii) payment of obligations, (iii) compliance with law, (iv) maintenance of properties and (v) payment of restricted payments. The repayment of the Term Loan can be accelerated upon (i) a change in control, which would include Steel Energy owning less than 100% of the equity of Sun Well, Rogue, or Black Hawk or Steel Partners owning, directly or indirectly, less than 35% of Steel Energy or (ii) other events of default, including payment failure, false representations, covenant breaches, and bankruptcy.
Sun Well previously had a credit agreement (the "Sun Well Credit Agreement") with Wells Fargo Bank, National Association, that included a term loan of $20.0 million and a revolving line of credit for up to $5.0 million. All amounts due under the Sun Well Credit Agreement were fully repaid during 2013 and the facility was terminated as of July 3, 2013, upon closing of the Energy Credit Agreement. For the years ended December 31, 2013 and 2012, the Company incurred interest expense of $0.3 million and $0.4 million, respectively, in connection with the Sun Well Credit Agreement. Upon termination of the Sun Well Credit Agreement, the Company recognized a loss on extinguishment of $0.5 million from the write off of unamortized deferred financing costs, which was reported as a component of "Other income (expense), net" in the consolidated statements of operations for the year ended December 31, 2013.

10. Leases

The Company leases certain property and equipment used in its operations under agreements that are classified as both capital and operating leases. Such agreements generally include provisions for inflation-based rate adjustments and, in the case of leases for buildings and office space, payments of certain operating expenses and property taxes.

Future minimum rental payments required under capital leases and operating leases that have initial or remaining non-cancelable lease terms in excess of one year are as follows:

	Operating	Capital
	(in thousands)	
For the year ended December 31,		
2014	$1,796	$464
2015	1,074	464
2016	1,005	133
2017	554	—
2018	274	—
Thereafter	1,026	—
Total minimum lease payments	$5,729	1,061
Less amount representing interest		(77)
Present value of net minimum lease payments		984
Less current portion		(412)
Capital lease obligations, net of current portion		$572

Assets recorded under capital leases are included in property and equipment (see Note 7) as follows:

	December 31, 2013 (in thousands)	2012
Rigs and other equipment	$1,871	$1,871
Accumulated depreciation	(343)	(127)
Net	$1,528	$1,744

Total rental expense under operating leases was $2.2 million, $2.7 million, and $0.2 million for the years ended December 31, 2013, 2012, and 2011, respectively.

11. Other Liabilities

"Accrued expenses and other current liabilities" consisted of the following:

	December 31, 2013 (in thousands)	December 31, 2012
Tax-related	$385	$1,197
Accrued compensation and related taxes	4,033	3,424
Deferred revenue	857	299
Insurance	310	—
Professional services	608	282
Accrued fuel and rig-related charges	652	162
Interest	27	25
Other	487	714
	$7,359	$6,103

"Other long-term liabilities" consisted of the following:

	December 31, 2013 (in thousands)	December 31, 2012
Tax-related	$104	$7,340
Deferred compensation	3,709	2,032
	$3,813	$9,372

The tax-related liabilities represent uncertain tax positions relating to foreign jurisdictions in which the Predecessor Business previously operated. In 2013, the Company reversed approximately $7.2 million of reserves for foreign taxes upon the expiration of the statute of limitations (see Note 13).

12. Exit Activities

The Company initiated several restructuring plans in connection with winding down the Predecessor Business. During the year ended December 31, 2011, the Company made payments totaling $1.2 million related to the restructuring plans, of which $0.8 million related to employee termination costs and $0.4 million related to other charges. All restructuring plans were completed during 2011 and no liability remained for such plans as of December 31, 2011.

13. Income Taxes

The Company recognized a benefit for income taxes of $9.3 million for the year ended December 31, 2013, primarily as a result of a reversal in the fourth quarter of 2013 of $7.2 million of reserves for foreign taxes upon the expiration of the statute of limitations. In addition, in 2013 the Company reversed a portion of its valuation allowance for deferred tax assets as

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a result of deferred tax liabilities recognized in connection with unrealized gains on marketable securities included as a component of other comprehensive income. The Company recognized a benefit for income taxes of $15.7 million for the year ended December 31, 2012, primarily from a reversal of a portion of its valuation allowance for deferred tax assets as a result of deferred tax liabilities recognized on the identifiable intangible assets acquired in connection with the acquisition of Sun Well.

The components of the benefit from income taxes were as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Federal:			
Current	$14	$34	$(2,666)
Deferred	3,402	15,066	—
	3,416	15,100	(2,666)
Foreign:			
Current	7,281	1,373	1,979
Deferred	(1,696)	—	921
	5,585	1,373	2,900
State:			
Current	509	(979)	(8)
Deferred	(168)	218	—
	341	(761)	(8)
	$9,342	$15,712	$226

The components of income (loss) from continuing operations before income taxes were as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Domestic	$6,990	$6,326	$(2,717)
Foreign	59	141	2,559
	$7,049	$6,467	$(158)

The benefit for income taxes varied from the Federal statutory income tax rate due to the following:

	Fiscal Year Ended December 31, 2013	2012	2011
Federal statutory rate	35.0 %	35.0 %	35.0 %
State taxes, net of federal benefit	(8.1)%	15.1 %	(1.9)%
Foreign losses not benefited	(0.3)%	(0.6)%	(19.6)%
Changes in tax reserves	(78.6)%	(53.9)%	640.3 %
Change in valuation allowance	(78.7)%	(263.2)%	(654.0)%
Permanent differences	(1.8)%	24.6 %	143.2 %
	(132.5)%	(243.0)%	143.0 %

The components of the deferred tax assets and liabilities were as follows:

	December 31, 2013	2012
	(in thousands)	
Deferred tax assets		
Net operating loss carryforward	$61,212	$40,771
Research and development credits	33,484	29,659
Compensatory and other accruals	1,800	1,200
Foreign tax credits	—	7,528
Other, net	1,785	2,901
Gross deferred tax assets	98,281	82,059
Deferred tax liabilities:		
Unremitted foreign earnings	7,001	29,425
Unrealized gains on investments	3,704	321
Intangible assets	6,525	8,886
Fixed assets	13,354	4,403
Gross deferred tax liabilities	30,584	43,035
Net deferred tax asset before valuation allowance	67,697	39,024
Valuation Allowance	(69,753)	(37,173)
Net deferred tax asset (liability)	$(2,056)	$1,851

The components of the Company's deferred tax assets and deferred tax liabilities were classified in the consolidated balance sheets as follows:

	December 31,	
	2013	2012
	(in thousands)	
Deferred income tax assets - current	$—	$188
Deferred income tax assets - non-current	1,556	1,696
Total deferred income tax assets	1,556	1,884
Deferred income tax liabilities - current	3,612	—
Deferred income tax liabilities - non-current	—	33
Total deferred income tax liabilities	3,612	33
Net deferred income tax asset (liability)	$(2,056)	$1,851

At December 31, 2013, the Company had Federal net operating loss carryforwards of approximately $146.4 million that expire in 2021 through 2031, and domestic state net operating loss carryforwards of approximately $164.4 million that expire in 2014 through 2031. The Company also had Federal research and development credit carryforwards of approximately $30.3 million that expire in 2018 through 2029, and domestic state research and development credit carryforwards of approximately $17.7 million that do not expire. Of the total Federal net operating loss carryforwards, approximately $10.4 million related to deductions for stock-based compensation, the tax benefit of which will be credited to additional paid-in capital when realized. The Company's ability to utilize its net operating loss and other credit carryforwards would be subject to limitation upon a change in control. Federal income taxes and foreign withholding taxes associated with the repatriation of earnings of foreign subsidiaries have been fully provided.

The Company established a valuation allowance to reserve its net deferred tax assets at December 31, 2013 and 2012, based on its assessment that it is more likely than not that such benefit will not be fully realized. This assessment was based on, but not limited to, the Company’s operating results for the past three years, uncertainty in the Company’s projections of taxable income, uncertainty in general economic conditions in general and in the oil and gas industry in particular, and the effects of multiple acquisitions and the Company’s ability to effectively integrate the acquired entities.

The changes in unrecognized tax positions were as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Balance at beginning of period	$26,419	$29,903	$31,818
Tax positions related to prior year:			
Additions	—	—	951
Expiration of statute of limitations	(7,298)	—	—
Settlements	—	(3,484)	(2,866)
Balance at ending of period	$19,121	$26,419	$29,903

As of December 31, 2013, the Company’s total gross unrecognized tax benefits were $19.1 million, of which $0.1 million, if recognized, would affect the provision for income taxes. In 2013, the Company reversed approximately $7.3 million of reserves for foreign taxes upon the expiration of the statute of limitations. The Company recognizes interest and penalties related to uncertain tax positions as a component of “Benefit from income taxes” in its consolidated statements of operations. For the years ended December 31, 2013. 2012, and 2011, the amount of such interest and penalties recognized was immaterial.

The Company is subject to Federal income tax as well as income taxes in many domestic states and foreign jurisdictions in which the Company operates or formerly operated. As of December 31, 2013, fiscal years from 1999 onward remain open to examination by the United States taxing authorities and fiscal years 2009 onward remain open to examination in Singapore.

14. Stock Benefit Plans

The Company grants equity-based awards to employees under its 2004 Equity Incentive Plan, as amended (the “2004 Plan”). Stock options granted under the 2004 Plan have a term of up to seven years from the grant date, with the exception of incentive stock options granted to employees who own more than 10% of the voting power of all classes of stock of the Company, which have a term of up to five years. The exercise price and vesting period of stock options granted under the 2004 Plan is determined by the board of directors or its delegates, subject to certain provisions of the 2004 Plan. The exercise price of incentive stock options granted to employees who own more than 10% of the voting power of all classes of stock of the Company shall not be less than 110% of the fair market value of the Company’s common stock on the grant date. The exercise price of incentive stock options granted to other employees shall be no less than 100% of the fair market value of the Company’s common stock on the grant date. The exercise price of non-qualified stock options granted to employees shall no less than 100% of the fair market value of the Company’s common stock on the grant date, but in certain circumstances could be as low as 85% of the fair market value of the Company’s common stock on the grant date.

The 2004 Plan also allows for the granting of stock appreciation rights, restricted stock awards, and restricted stock units, the terms of such grants being determined by the board of directors or its delegates subject to certain provisions of the 2004 Plan. Stock appreciation rights granted under the 2004 Plan shall have a term of up to seven years and an exercise price of no less than 100% of the fair market value of the Company’s common stock on the grant date. Restricted stock awards and restricted stock units (collectively, “restricted stock”) granted under the 2004 Plan shall have a purchase price of at least $0.001 per share.

The Company grants equity-based awards to non-employee directors under its 2006 Director Plan, as amended (the "2006 Plan", and together with the “2004 Plan”, the "Equity Plans"). The terms of all stock-based awards granted under the 2006 Plan are determined by the compensation committee of the board of directors, subject to certain provisions of the 2006 Plan. All options granted under the 2006 Plan are non-qualified stock options, and shall have a term of up to ten years and an exercise price of no less than 100% of the fair market value of the Company’s common stock on the grant date. The 2006 Plan also allows for the granting of stock appreciation rights, restricted stock awards, and restricted stock units. Stock appreciation rights granted under the 2006 Plan shall have a term of up to ten years and an exercise price of no less than 100% of the fair market value of the Company’s common stock on the grant date. Restricted stock granted under the 2006 Plan shall have a purchase price equal to at least the par value of the Company’s common stock on the grant date.

There are 1,805,613 shares and 1,200,000 shares of the Company’s common stock reserved for the issuance of equity-based awards under the 2004 Plan and the 2006 Plan, respectively. Under the 2004 Plan, 1,549,776 shares remained available for the issuance of equity-based awards and 149,545 equity-based awards were outstanding at December 31, 2013. Under the 2006 Plan, 409,045 shares remained available for the issuance of equity-based awards and 56,539 equity-based awards were outstanding at December 31, 2013.

The Company recognizes stock-based compensation based on the estimated fair values of equity-based awards on the grant dates. Stock-based compensation is recognized ratably over the requisite service or vesting period of the equity-based awards and is adjusted for estimated forfeitures. Certain grants of restricted stock to non-employee directors vest in full when the individual ceases being a member of the board of directors for any reason. The fair value of such grants are recognized as stock-based compensation on the grant date. The fair value of restricted stock is based on the closing price of the Company’s common stock on the grant date. The Company uses the Black-Scholes option pricing model to estimate the fair value of stock options. No stock options were granted in 2013 and 2011. The following weighted average assumptions were used in calculating the fair value of the stock options granted in 2012 under the Equity Plans:

Expected life (in years)	1.1
Risk-free interest rate	0.2%
Expected volatility	58%
Dividend yield	—

The expected term of stock options was based on historical data used to estimate the period of time that options were expected to be outstanding. The expected volatility is based on the historical volatility of the Company’s common stock. The expected dividends are based on the historical dividends paid and the dividends the Company expects to pay in future periods.

The risk-free interest rate is based on the yields of United States Treasury Notes at the time stock options are granted.

Stock-based compensation expense by type of equity-based award, all of which was recognized as a component of "Selling, general, and administrative expenses" in the consolidated statements of operations for the years ended December 31, 2013, 2012, and 2011, was as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Stock options	$91	$92	$69
Restricted stock	1,949	1,395	454
Total stock-based compensation	$2,040	$1,487	$523

Information relating to stock option activity in the Equity Plans for the year ended December 31, 2013, is summarized in the following table. All stock option grants had exercise prices equal to or greater than the market price on the grant date.

	Shares	Weighted Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
	(in thousands)			(in thousands)
Outstanding, January 1, 2013	65	$30.93		
Options forfeited	(1)	$39.04		
Outstanding, December 31, 2013	64	$30.84	7.1	$38
Exercisable, December 31, 2013	58	$31.31	6.8	$26

Information relating to restricted stock activity in the Equity Plans for the year ended December 31, 2013, is summarized in the following table.

	Shares	Weighted Average Grant Date Fair Value
	(in thousands)	
Non-vested stock, January 1, 2013	103	$23.34
Awarded	141	$28.19
Vested	(102)	$27.32
Non-vested stock, December 31, 2013	142	$28.19

Information relating to fair value of grants of equity awards and the fair value of options exercised and restricted shares vested for the years ended December 31, 2013, 2012, and 2011 is summarized in the following table.

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands)		
Weighted average fair value on grant date:			
Options	$—	$27	$811
Restricted stock	$3,977	$2,795	$428
Intrinsic value of options exercised	$—	$—	$29
Fair value of restricted stock vested	$2,797	$415	$162

Compensation expense related to equity-based awards granted under the Equity Plans that was not recognized as of December 31, 2013, totaled $3.4 million and is expected to be recognized over a weighted average period of 0.9 years. The Company did not receive any proceeds from the exercise of equity-based awards during the years ended December 31, 2013, and 2012, and received approximately $29,000 from the exercise of stock options during the year ended December 31, 2011. The Company has a policy of issuing new shares of common stock upon the exercise of stock options.

15. Net Income (Loss) Per Share

Basic net income (loss) attributable to Steel Excel per share of common stock is computed by dividing net income (loss) attributable to Steel Excel by the weighted-average number of common shares outstanding during the period. Diluted net income (loss) per share attributable to Steel Excel gives effect to all potentially dilutive common shares outstanding during the period.

Amounts used in the calculation of basic and diluted net income (loss) per share of common stock for the years ended December 31, 2013, 2012. and 2011, were as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
	(in thousands, except per share data)		
Numerators:			
Net income from continuing operations	$16,391	$22,179	$68
Non-controlling interest	156	22	—
Net income from continuing operations attributable to Steel Excel Inc.	$16,547	$22,201	$68
Income (loss) from discontinued operations	$(5,540)	$(1,935)	$6,629
Non-controlling interest	3,188	427	72
Loss from discontinued operations attributable to Steel Excel Inc.	$(2,352)	$(1,508)	$6,701
Net income attributable to Steel Excel Inc.	$14,195	$20,693	$6,769
Denominators:			
Basic weighted average common shares outstanding	12,584	12,110	10,882
Effect of dilutive securities - stock-based awards	18	23	15
Diluted weighted average common shares outstanding	12,602	12,133	10,897
Basic income (loss) per share attributable to Steel Excel Inc.:			
Net income from continuing operations	$1.31	$1.83	$0.01
Income (loss) from discontinued operations, net of taxes	$(0.19)	$(0.12)	$0.62
Net income	$1.13	$1.71	$0.62
Diluted income (loss) per share attributable to Steel Excel Inc.:			
Net income from continuing operations	$1.31	$1.83	$0.01
Income (loss) from discontinued operations, net of taxes	$(0.19)	$(0.12)	$0.61
Net income	$1.13	$1.71	$0.62

16. Accumulated Other Comprehensive Income

Changes in the components of "Accumulated other comprehensive income" were as follows:

	Unrealized Gain on Securities (in thousands)	Cumulative Translation Adjustment	Total
Balance at December 31, 2012	$927	$19	$946
Unrealized gain (loss) - pretax	12,126	(63)	12,063
Tax effect on unrealized gain (loss)	(4,490)	—	(4,490)
Unrealized gain - net of tax	7,636	(63)	7,573
Reclassification to realized gain - pretax	(2,608)	(361)	(2,969)
Tax effect on reclassification	966	—	966
Reclassification to realized gain - net of tax	(1,642)	(361)	(2,003)
Net current period other comprehensive income (loss)	5,994	(424)	5,570
Balance at December 31, 2013	$6,921	$(405)	$6,516

Amounts reclassified for realized gains on marketable securities and cumulative translation adjustments for the year ended December 31, 2013, are reported as a component of "Other income (expense), net" in the consolidated statement of operations.

17. Supplemental Cash Flow Information

Cash paid for interest and income taxes and non-cash investing and financing activities for the years ended December 31, 2013, 2012, and 2011, were as follows:

	Fiscal Year Ended December 31, 2013 (in thousands)	2012	2011
Interest paid	$1,304	$434	$3
Income taxes paid (refunded) - net	$916	$(1,130)	$(542)
Non-cash investing and financing activities:			
Non-controlling interests recognized in connection with acquisitions	$2,896	$82	$500
Issuance of common stock for acquisition of Sun Well	$—	$60,825	$—

18. Commitments and Contingencies

From time to time we are subject to litigation or claims that arise in the normal course of business. While the results of such litigation matters and claims cannot be predicted with certainty, we believe that the final outcome of such matters will not have a material adverse impact on our financial position or results of operations. However, because of the nature and inherent uncertainties of litigation, should the outcome of these actions be unfavorable, our business, financial condition, and results of operations could be materially and adversely affected.

The Company entered into agreements in connection with the sale of portions of the Predecessor Business that included certain indemnification obligations. These indemnification obligations generally required the Company to compensate the other party for certain damages and costs incurred as a result of third party claims. The Company is not aware of any claims under the indemnification provisions and no liabilities have been recognized in connection with such contingent obligations.

19. Related Party Transactions

SPLP beneficially owned approximately 55.1% of the Company’s outstanding common stock as of December 31, 2013. The power to vote and dispose of the securities held by SPLP is controlled by Steel Partners Holdings GP Inc. (“SPH GP”). Warren G. Lichtenstein, the Chairman of the Board of Directors and President of the Company's Sports segment, is also the Executive Chairman of SPH GP. Certain other affiliates of SPH GP hold positions with the Company, including Jack Howard, as Vice Chairman and principal executive officer, James F. McCabe, Jr., as Chief Financial Officer, and Leonard J. McGill, as Vice President, General Counsel, and Secretary. Each of Warren G. Lichtenstein and Jack L. Howard is compensated with cash compensation and equity awards or equity-based awards in amounts that are consistent with the Company’s Non-employee Director Compensation Policy.

In October 2011, the Company contracted with SP Corporate Services LLC (“SP Corporate”), a SPLP affiliate, to provide financial management and administrative services, including the services of a chief financial officer. Through July 2012, the Company paid SP Corporate $35,000 per month for the provision of such services. Effective August 2012, the services SP Corporate provides were expanded to include executive and financial management services in the areas of finance, regulatory reporting, and other administrative and operational functions. The Company paid SP Corporate $300,000 per month for these expanded services through December 31, 2013. Effective January 1, 2014, the services SP Corporate provides were further expanded, and the Company will pay SP Corporate $667,000 per month for such services. The services agreement with SP Corporate and subsequent amendments were approved by a committee of the Company’s independent directors. In addition, the Company reimburses SP Corporate and other SPLP affiliates for certain expenses incurred on the Company’s behalf. During the years ended December 31, 2013, 2012, and 2011, the Company incurred expenses of $4.4 million, $2.7 million, and $0.4 million, respectively, for services provided by SP Corporate and for reimbursement of expenses incurred on its behalf by SP Corporate and its affiliates. As of December 31, 2013 and 2012, the Company owed SP Corporate $0.3 million and $0.3 million, respectively. As of December 31, 2013, the Company was owed $0.2 million from SPH GP for expenses the Company paid on its behalf.

In October 2013, iGo contracted with SP Corporate to provide certain executive, other employee, and corporate services for a fixed annual fee of $0.4 million. In addition, iGo will reimburse SP Corporate for reasonable and necessary business expenses incurred on iGo’s behalf. The services agreement was approved by the independent directors of iGo.

The Company holds $15.2 million of short-term deposits at WebBank, an affiliate of SPLP, and recorded interest income of $0.1 million and $0.1 million, for the years ended December 31, 2013 and 2012, respectively.

20. Segment Information

The Company has determined that its two reportable segments are Energy and Sports. The Energy segment provides drilling and production services to the oil and gas industry. The Sports segment provides event-based sports services and other health-related services.

The Company identifies its operating segments based on the services provided by its various operations and the financial information used by its chief operating decision maker to make decisions regarding the allocation of resources to and the financial performance of the operating segments. The reporting segments represent an aggregation of individual operating segments with similar economic characteristics. The Energy segment is an aggregation of the individual operating segments represented by Sun Well, Rogue, and Black Hawk. The Sports segment is an aggregation of the individual operating segments represented by Baseball Heaven, UK Elite, and the Crossfit® entities.

The Company measures profit or loss of its segments based on operating income. The accounting policies used to measure operating income of the segments are the same as those used in preparing the Company’s consolidated financial statements (see Note 2).

Segment information relating to the Company's results of continuing operations was as follows:

	Fiscal Year Ended December 31,		
	2013	2012	2011
Revenues			
Energy	$109,624	$97,191	$1,417
Sports	10,404	2,913	1,085
Total revenues	$120,028	$100,104	$2,502
Operating income (loss)			
Energy	$12,381	$16,837	$165
Sports	(1,408)	(2,061)	(354)
Total segment operating income	10,973	14,776	(189)
Corporate and other business activities	(8,411)	(8,959)	(8,322)
Interest income, net	3,079	1,486	4,083
Other income (expense), net	1,408	(836)	4,270
Income from continuing operations before income taxes	$7,049	$6,467	$(158)
Depreciation and amortization expense:			
Energy	$18,392	$14,785	$144
Sports	$793	518	225
Total depreciation and amortization expense	$19,185	$15,303	$369

For the year ended December 31, 2013, revenues from the two largest customers in the Company's Energy segment were approximately $20.4 million and $12.7 million, representing 17.0% and 10.5%, respectively, of the Company's consolidated revenues. For the year ended December 31, 2012, revenues from the two largest customers in the Company's Energy segment were approximately $11.2 million and $11.0 million, representing 11.1% and 11.0%, respectively, of the

Company’s consolidated revenues. No single customer accounted for more than 10% of the Company’s consolidated revenues for the year ended December 31, 2011.

Segment information related to the Company's assets was as follows:

	December 31, 2013 (in thousands)	December 31, 2012
Total assets		
Energy	$243,746	$199,889
Sports	20,495	7,613
Corporate and other business activities	273,798	258,993
Total assets	$538,039	$466,495
Capital expenditures		
Energy	$5,846	$11,090
Sports	$3,086	$728
Total capital expenditures	$8,932	$11,818

Total assets of the Sports segment and Corporate and other business activities at December 31, 2013, include investments in equity-method investees of $3.7 million and $4.7 million, respectively.

21. Selected Quarterly Financial Data (Unaudited)

	Quarter Ended:			
	March 31	June 30	September 30	December 31
	(in thousands, except per-share data)			
Fiscal year ended December 31, 2013:				
Net revenues	$26,351	$28,761	$31,420	$33,496
Gross profits	$7,686	$8,705	$8,080	$10,172
Net income from continuing operations	$3,369	$1,080	$3,047	$8,895
Net income	$2,974	$886	$2,159	$4,832
Net income attributable to Steel Excel Inc.	$3,310	$1,071	$2,470	$7,344
Net income from continuing operations attributable to Steel Excel Inc.	$3,389	$1,116	$2,869	$9,173
Net income from continuing operations attributable to Steel Excel Inc. per share of common stock				
Basic	$0.26	$0.09	$0.23	$0.75
Diluted	$0.26	$0.09	$0.23	$0.75
Fiscal year ended December 31, 2012:				
Net revenues	$14,446	$24,450	$34,293	$26,915
Gross profits	$5,687	$9,481	$12,204	$6,668
Net income from continuing operations	$(120)	$17,430	$4,865	$4
Net income	$(2,468)	$17,309	$5,349	$54
Net income attributable to Steel Excel Inc.	$(1,888)	$17,309	$5,349	$(77)
Net income from continuing operations attributable to Steel Excel Inc.	$(120)	$17,430	$4,865	$26

Net income from continuing operations attributable to Steel Excel Inc. per share of common stock				
Basic	$(0.01)	$1.50	$0.37	$—
Diluted	$(0.01)	$1.50	$0.37	$—

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Exhibit Index

Exhibit #	Exhibit Description	Form	File #	Exhibit	File Date
2.1	Asset Purchase Agreement between the Company and PMC-Sierra, Inc., dated as of May 8, 2010	10-Q	000-15071	2.1	08/11/10
2.2	Amended Asset Purchase Agreement between the Company and PMC-Sierra, Inc., dated as of June 8, 2010	10-Q	000-15071	2.2	08/11/10
2.3	Second Amendment to the Asset Purchase Agreement between the Company and PMC-Sierra, Inc., dated as of September 23, 2010	10-Q	000-15071	2.1	11/05/10
2.4	Stock Purchase and Sale Agreement, dated as of July 11, 2013, between Steel Excel Inc. and iGo, Inc.	SC 13-D	005-60065	2	7/22/13
2.5	Asset Purchase Agreement, dated as of October 29, 2013 by and among Black Hawk Acquisition, Inc., Black Hawk Energy Services, Inc. and Chris Beal, Stuart Buckingham, Kenneth Stevens, Jeff Thomas and Gregory M. Tucker.	8-K	000-15071	2.1	11/4/13
3.1	Unofficial Composite Certificate of Incorporation of Steel Excel Inc. as currently in effect	10-Q	000-15071	3.1	11/08/12
3.2	Certificate of Designation of Series B Preferred Stock filed with the Delaware Secretary of State on December 20, 2011	8-K	000-15071	3.1	12/22/11
3.3	Amended and Restated Bylaws of the Company, effective October 14, 2010	8-K	000-15071	3.1	10/20/10
4.1	Specimen Common Stock Certificate	10-Q	000-15071	4.1	08/09/12
4.2	Tax Benefits Preservation Plan, dated December 21, 2011	8-K	000-15071	4.1	12/22/11
4.3	First Amendment to the Tax Benefits Preservation Plan, dated as of May 1, 2012, by and between Steel Excel Inc. and Registrar and Transfer Company, as Rights Agent	10-Q	000-15071	4.2	08/09/12
4.4	Indenture, dated as of December 22, 2003, by and between the Registrant and Wells Fargo Bank, National Association	10-Q	000-15071	4.01	02/09/04
4.5	Form of 3/4% Convertible Senior Subordinated Note	10-Q	000-15071	4.02	02/09/04
10.1†	Separation Agreement of John M. Westfield, effective November 17, 2009	10-Q	000-15071	10.3	02/03/10
10.2†	Separation Agreement of Subramanian Sundaresh, effective January 4, 2010	10-Q	000-15071	10.1	02/03/10
10.3†	Consulting Service Agreement of Subramanian Sundaresh, effective January 4, 2010‡	10-Q	000-15071	10.2	02/03/10
10.4†	Separation Agreement of John Noellert, effective February 4, 2010	10-K	000-15071	10.11	05/27/10
10.5†	Separation Agreement of Marcus Lowe, effective March 4, 2010	10-K	000-15071	10.12	05/27/10
10.6†	Separation Agreement of Mary L. Dotz, effective July 16, 2010	10-Q	000-15071	10.1	08/11/10
10.7†	Amended Separation Agreement of Mary L. Dotz, effective September 29, 2010	10-Q	000-15071	10.1	11/05/10
10.8†	Amended Separation Agreement of Mary L. Dotz, effective December 10, 2010	10-KT	000-15071	10.10	03/03/11
10.9†	Mary L. Dotz Retention Bonus Letter, effective June 15, 2010	10-KT	000-15071	10.11	03/03/11
10.10†		10-KT	000-15071	10.12	03/03/11

	Independent Contractor Agreement with John J. Quicke, effective February 2, 2010				
10.11†	Amendment No. 1 to the Independent Contractor Agreement with John J. Quicke, effective June 25, 2010	10-KT	000-15071	10.13	03/03/11
10.12†	Amendment No. 2 to the Independent Contractor Agreement with John J. Quicke, effective December 7, 2010	10-KT	000-15071	10.14	03/03/11
10.13†	Amendment No. 3 to the Independent Contractor Agreement with John J. Quicke, effective April 3, 2012	8-K	000-15071	10.1	04/04/12
10.14†	Independent Contractor Agreement with Mary L. Dotz, effective June 1, 2011	10-Q	000-15071	10.4	08/09/11
10.15†	2004 Equity Incentive Plan, as amended and restated on August 20, 2008	Def 14A	000-15071	A	09/08/08

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10.16†	Amendment No. 2 to 2004 Equity Incentive Plan, dated as of November 17, 2011	10-Q	000-15071	10.2	11/08/12
10.17†	Amendment No. 3 to 2004 Equity Incentive Plan, dated as of August 7, 2012	10-Q	000-15071	10.3	11/08/12
10.18†	Form of Restricted Stock Award Agreement for 2004 Equity Incentive Plan, as amended August 7, 2012	10-Q	000-15071	10.4	11/08/12
10.19†	Form of Stock Option Agreement under the 2004 Equity Incentive Plan	10-Q	000-15071	10.02	11/10/04
10.20†	Adaptec, Inc. 2006 Director Plan	Def 14A	000-15071	A	07/28/06
10.21†	Amendment No. 1 to 2006 Director Plan, dated November 17, 2011	10-Q	000-15071	10.1	11/08/12
10.22†	Form of Restricted Stock Award Agreement under 2006 Director Plan, as amended on August 7, 2012	10-Q	000-15071	10.5	11/08/12
10.23†	Stock Option Award Agreement under 2006 Director Plan, as amended on December 7, 2010	10-KT	000-15071	10.25	03/03/11
10.24†	Stock Appreciation Right Award Agreement under 2006 Director Plan as amended on February 7, 2008	8-K	000-15071	10.03	02/11/08
10.25†	SNAP Appliance, Inc. 2002 Stock Option and Restricted Stock Purchase Plan, effective November 14, 2002	S-8	333-118090	4.04	08/10/04
10.26†	Director Compensation Policy, dated May 25, 2011	10-Q	000-15071	10.5	08/09/11
10.27†	Fiscal 2010 Incentive Plan, effective for fiscal 2010	10-K	000-15071	10.29	05/27/10
10.28	Form of Indemnification Agreement entered into between the Company and its officers and directors	10-K	000-15071	10.47	06/06/07
10.29	Settlement Agreement, dated as of October 26, 2007, among the Registrant, Steel Partners, L.L.C. and Steel Partners II, L.P.	8-K	000-15071	10.01	10/31/07
10.30	Management Services Agreement, dated October 1, 2011, between the Company and SP Corporate Services LLC	8-K	000-15071	10.1	10/06/11
10.31	Amended and Restated Management Services Agreement, dated as of August 1, 2012, between the Company and SP Corporate Services LLC	8-K	000-15071	10.6	8/10/12
10.32	Share Acquisition Agreement, dated as of April 30, 2012, by and among the Company and BNS Holding, Inc., SWH, Inc. and SPH Group Holdings LLC	8-K	000-15071	2.1	04/30/12
10.33	Agreement of Purchase and Sale and Escrow Instructions, dated March 26, 2011, between the Company and Swift Realty Partners, LLC	10-Q	000-15071	10.1	08/09/11
10.34	First Amendment to the Agreement of Purchase and Sale and Escrow Instructions, dated May 4, 2011, between the Company and Swift Realty Partners, LLC	10-Q	000-15071	10.2	08/09/11
10.35	Second Amendment to the Agreement of Purchase and Sale and Escrow Instructions, dated May 26, 2011, between the Company and Swift Realty Partners, LLC	10-Q	000-15071	10.3	08/09/11
10.36	Amendment No. 1 to the Amended and Restated Management Services Agreement between Steel Excel Inc. and SP Corporate Services LLC, dated as of April 5, 2013	8-K	000-15071	10.1	4/5/13
10.37	Credit Agreement, dated as of July 3, 2013, among Steel Energy Ltd., and Wells Fargo Bank, National Association, as Administrative Agent, Issuing Lender, a Revolving Lender, a	8-K	000-15071	99.1	7/10/13

	Swing Line Lender and a Term Lender, RBS Citizens, N.A., as a Revolving Lender and a Term Lender and Comerica Bank, as a Revolving Lender and a Term Lender				
10.38†	Amendment No. 4 to 2004 Equity Incentive Plan, dated as of May 21, 2013	10-Q	000-15071	10.2	8/7/13
10.39†	Form of Restricted Stock Unit Agreement under the 2004 Equity Incentive Plan, as amended May 21, 2013	10-Q	000-15071	10.3	8/7/13

10.40	Commitment Increase Agreement and Amendment to Credit Documents, dated as of December 17, 2013, among Steel Energy Ltd., and Wells Fargo Bank, National Association, as Administrative Agent, Issuing Lender, a Revolving Lender, a Swing Line Lender and a Term Lender, RBS Citizens, N.A., as a Revolving Lender and a Term Lender and Comerica Bank, as a Revolving Lender and a Term Lender.	8-K	000-15071	10.1	12/20/13
10.41	Amendment No. 2 to the Amended and Restated Management Services Agreement between Steel Excel Inc. and SP Corporate Services LLC, dated as of January 1, 2014	8-K	000-15071	10.1	1/14/14
21*	Subsidiaries of Registrant				
23*	Consent of Independent Registered Public Accounting Firm, BDO USA, LLP				
31.1*	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				
31.2*	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				
32*	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				
101.INS**	XBRL Instance Document				
101.SCH**	XBRL Taxonomy Extension Schema Document				
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document				
101.DEF**	XBRL Taxonomy Extension Definition Linkbased Document				
101.LAB**	XBRL Taxonomy Extension Labels Linkbase Document				
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document				

† Management contract or compensatory plan or arrangement.
‡ Confidential treatment has been granted for portions of this agreement.
* Filed herewith.
** Furnished with this Form 10-K. In accordance with Rule 406T of Regulation S-T, the interactive data files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for the purposes of Section 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections.

Steel Excel Inc.
Schedule II - Valuation and Qualifying Accounts
For the years ended December 31, 2013, 2012, and 2011

Description	Balance at beginning of period	Additions Charged to costs and expenses	Charged to other accounts	Deductions [1]	Balance at end of period
Allowances deducted in the balance sheet from assets to which they apply:					
For the year ended December 31, 2013:					
Allowance for doubtful accounts	$—	$—	$—	$—	$—
Valuation allowance on deferred tax assets	$37,173	$32,580	$—	$—	$69,753
For the year ended December 31, 2012:					
Allowance for doubtful accounts	$80	$—	$—	$(80)	$—
Valuation allowance on deferred tax assets	$69,508	$—	$—	$(32,335)	$37,173
For the year ended December 31, 2011:					
Allowance for doubtful accounts	$—	$80	$—	$—	$80
Valuation allowance on deferred tax assets	$70,449	$—	$—	$(941)	$69,508

(1) Recognized as a reduction of expense