COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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J. TYLER McCAULEY
AUDITOR-CONTROLLER

April 12, 2007

TO: Supervisor Zev Yaroslavsky, Chairman
Supervisor Gloria Molina
Supervisor Yvonne B. Burke
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: J. Tyler McCauley
Auditor-Controller

SUBJECT: **AUDIT OF THE SHERIFF'S DEPARTMENT COMMISSARY SERVICE CONTRACT**

In September 1997, your Board approved a five-year contract (with three one-year renewal options) with Compass Group USA, Inc. (Compass or Contractor) to sell commissary items (stationery, snacks, personal care items, clothing, etc.) to Sheriff Custody Division inmates. The contract requires Compass to pay the County 31% of all net commissary sales and split all profits in excess of 6% of total net sales with the County. Compass paid the County approximately $22 million from September 29, 1997 to September 16, 2005.

We contracted with an outside Certified Public Accounting firm, Conrad and Associates, LLP (Conrad), to audit the agreement with Compass. The audit was intended to evaluate Compass' compliance with the contract provisions.

Audit Results

Conrad's report (attached) indicates that Compass generally complied with the contract. However, Conrad was unable to audit the amount Compass paid to the County for the first two years of the contract (September 1997 through September 1999), because Compass did not maintain complete documentation of their reported revenue/expense. Conrad also indicated that Compass reduced their net profit during contract years 1999 through 2005 by some expenditures which Conrad questioned. These questioned expenditures may have resulted in Compass underpaying the County approximately $640,213 ($329,719 + $310,494) in additional shared profit. The following are the specific costs questioned by Conrad.

Expenses Not Related to Compass' County Contract

Compass reduced its net profit by a total of $659,437 in expenses which Conrad concluded were not related to the County contract. Specifically, $154,476 in travel expenses, $82,948 in costs for other operating units and $422,013 in adjustments to the income statements. This equates to $329,719 in additional excess profits that Conrad indicated should be paid to the County.

Expenses Not Considered Ordinary and Necessary Under the County Contract

Compass reduced its net profit by a total of $620,989 in expenses which Conrad believes are not "ordinary and necessary" under the County contract and should not have been used to reduce Compass profit. Specifically, $304,291 in contributions to the Sheriff's Youth Foundation, $147,233 in contributions to other Sheriff activities, and $169,465 in "client hospitality".

Conrad noted that the contract does not clearly define allowable expenses and recommended that the Sheriff discuss the allowability of these expenses with County Counsel. If these costs are not allowed, it would result Compass owing the County $310,494 in additional shared profits.

Conrad also noted instances where Compass and the Sheriff could improve service level documentation, record retention policies and the Department's monitoring procedures to ensure compliance with the terms of the agreement.

Details of Conrad's findings and Compass' response are in the attached report.

Gifts To Sheriff Employees

In addition to the issues identified by Conrad, we are concerned with the $169,465 in costs identified as "client hospitality". Compass indicated in their response to Conrad's report that some of these costs were for the Compass manager to meet with Sheriff's personnel at lunch and other forums. Compass indicated that their manager would "often" pay for these meals/meetings with Sheriff's personnel.

Sheriff management indicated that their policies state that Department staff should not accept gratuities. Based on Compass' explanation that they purchased meals for Sheriff's staff, we recommend that the Sheriff reinforce the policy that staff should not accept gratuities and determine if disciplinary action is warranted for employees who violated the policy.

In addition, the California Fair Political Practices Act requires covered County employees to disclose gifts they receive that exceed $50 in value and limits gifts that may be accepted from any one source to $360 a year. Because Compass did not

provide Conrad with any documentation of the gifts to Sheriff employees, we cannot determine whether any Sheriff's staff received gifts that must be disclosed, or if they exceeded the annual limit on gifts. The Sheriff should remind Department staff that, if they accept gifts or gratuities, they must report gifts over $50 and cannot accept gifts over $360 a year.

Review of Report

Conrad discussed their report with the Sheriff and Compass management. As noted in the attached report, the Sheriff and Compass agreed with Conrad regarding the expenses that were not related to the County contract. However, Compass disagreed with the expenses that Conrad questioned as being not ordinary and necessary.

After Conrad had completed their review, Compass management indicated that they had undercharged their corporate overhead rate to the County from 2000 to 2005, and that the undercharge more than offsets the expenses that should not have been charged to the contract. As a result, Compass believes that they do not owe the County any additional profits.

Compass raised the overhead rate issue after Conrad had completed their review. To resolve this issue, we will work with the Sheriff and County Counsel to determine whether Compass owes the County any additional shared profit. The Sheriff also indicated they will restructure the vendor payment process and remove the shared profit provision in any future commissary contracts.

Please call if you have any questions, or your staff may contact Jim Schneiderman at 626-293-1101.

JTM:MMO:JLS
Attachment

c: David E. Janssen, Chief Administrative Officer
Leroy D. Baca, Sheriff
Sachi A. Hamai, Executive Officer
Public Information Office
Audit Committee

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

For the Period
September 29, 1997 through September 16, 2005

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

For the Period
September 29, 1997 through September 16, 2005

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County of Los Angeles
Inmate Welfare Commission
Los Angeles, California

INDEPENDENT AUDITORS' REPORT

We were engaged to audit the accompanying financial schedules (Schedule of Commissary Sales and Commission, and Schedule of Profit Split Incentive) for the period September 29, 1997 through September 16, 2005 reported by Compass Group USA, Inc. (doing business as Canteen Services) to the County of Los Angeles Sheriff's Department, under a contract for the operation of a concession services in the County of Los Angeles jails. These financial schedules are the responsibility of Compass Group USA, Inc. Our responsibility is to express opinions on these financial schedules based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe our audit provides a reasonable basis for our opinions.

Because of the unavailability of accounting records for the period September 29, 1997 to September 18, 1999, we were unable to form an opinion regarding the years 1998 and 1999 and have not included those years on the Schedule of Commissary Sales and Commissions and the Schedule of Profit Split Incentive.

The accompanying financial schedules were prepared to present only the sales and commissions payable by Compass Group USA, Inc. to the County of Los Angeles Sheriff's Department, for the period September 29, 1997 through September 16, 2005 under a contract with the County of Los Angeles Sheriff's Department, for the operation of a concession services in the County of Los Angeles jails as described in Note 1, and is not intended to be a complete presentation of their financial position in conformity with accounting principles generally accepted in the United States of America.

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MEMBER OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS PRIVATE COMPANIES PRACTICE SECTION

As more fully described in Note 2, the accounting practices used to prepare the financial schedules may differ in some respects from accounting principles generally accepted in the United States of America. Accordingly, the accompanying financial schedules are not intended to present the financial position and results of operations of Compass Group USA, Inc. in conformity with accounting principles generally accepted in the United States of America.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had records relating to commissary sales and commissions for the period September 29, 1997 through September 18, 1999 been adequate, the financial schedules present fairly, in all material respects, the sales and commissions payable paid by Compass Group USA, Inc. to the County of Los Angeles Sheriff's Department, for the period September 29, 1997 through September 16, 2005 under a contract with the County of Los Angeles Sheriff's Department in conformity with the basis of accounting described in Note 2.

Our audit was conducted for the purpose of forming opinions on the financial schedules (Schedule of Commissary Sales and Commission, and Schedule of Profit Split Incentive). The Schedules of Profit Split Calculation for the years 2000 to 2005 are presented for the purpose of additional analysis. The Schedules of Profit Split Calculation have been subjected to the auditing procedures applied in the audit of the financial schedules, and in our opinion , are fairly stated in all material respects in relation to the financial schedules taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 12, 2005 on our consideration of Compass Group USA, Inc.'s internal control over financial reporting and on our tests of its compliance with provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

This report is intended solely for the information of the management of the County of Los Angeles Department of Auditor-Controller, Sheriff's Department and Compass Group USA, Inc. and is not intended to be and should not be used by anyone other than those specified parties.

Conrad and Associates, L.L.P.

December 12, 2005

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Schedule of Commissary Sales and Commissions Paid

For the Period September 29, 1997 through September 16, 2005

	Period						
	2000	2001	2002	2003	2004	2005	Total
Gross commissary sales	$ 10,506,499	$ 13,089,767	$ 13,183,013	$ 12,837,739	$ 13,265,824	$ 15,185,192	$ 78,068,034
Net deductions (Notes 4 and 5)	(558,082)	(1,758,620)	(1,735,915)	(1,217,043)	(2,154,972)	(2,732,914)	(10,157,546)
Net sales subject to commission (Note 4)	9,948,417	11,331,147	11,447,098	11,620,696	11,110,852	12,452,278	67,910,488
Gross commission (Note 4)	3,084,009	3,512,656	3,548,600	3,602,416	3,444,364	3,860,206	21,052,251
Indigent packs (Note 5)	(497,990)	(704,037)	(707,731)	(603,967)	(279,951)	(241,888)	(3,035,564)
Commission on gift bags	-	-	-	-	1,595	20,491	22,086
Net commission payable to the County (Note 4)	2,586,019	2,808,619	2,840,869	2,998,449	3,166,008	3,638,809	18,038,773
Commission paid to the County	2,586,019	2,808,619	2,840,869	2,998,449	3,166,008	3,638,809	18,038,773
Amount due to (from) the County	$ -	$ -	$ -	$ -	$ -	$ -	$ -

Note: Records were only available for the period September 19, 1999 through September 16, 2005

See accompanying notes to financial schedules

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Schedule of Profit Incentive Split

For the Period September 29, 1997 through September 16, 2005

	Period						
	2000	2001	2002	2003	2004	2005	Total
Sales (Note 6)	$ 10,633,128	$ 11,962,227	$ 12,274,742	$ 12,367,028	$ 12,610,093	$ 14,791,406	$ 74,638,624
Operating expenses (Note 7)	(9,675,481)	(10,894,770)	(11,192,946)	(11,001,376)	(11,365,633)	(13,248,845)	(67,379,051)
Gross profit	957,647	1,067,457	1,081,796	1,365,652	1,244,460	1,542,561	7,259,573
Profit split incentive calculation (Note 6):							
6% profit on Sales (Profit Objective)	637,988	717,734	736,485	742,022	756,606	887,484	4,478,319
Gross profit less Profit Objective	$ 319,659	$ 349,723	$ 345,311	$ 623,630	$ 487,854	$ 655,077	$ 2,781,254
Commission payable to the County (50% of amounts over Profit Objective)	$ 159,830	$ 174,862	$ 172,656	$ 311,815	$ 243,927	$ 327,539	$ 1,390,629
Commission paid to the County	-	193,645	169,015	122,422	110,277	155,057	750,416
Amount due to (from) the County	$ 159,830	$ (18,783)	$ 3,641	$ 189,393	$ 133,650	$ 172,482	$ 640,213

Note: Records were only available for the period September 19, 1999 through September 16, 2005

See accompanying notes to financial schedules

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Notes to Financial Schedules

For the Period September 29, 1997 through September 16, 2005

(1) General Information

On July 29, 1997, an agreement was entered into between the County of Los Angeles Sheriff's Department (County) and Compass Group USA, Inc., doing business as Canteen Services (Canteen) to provide commissary services for inmates housed at County operated jails. This agreement has been amended six times as follows.

- Amendment Number 1, dated January 5, 1998, allowed for the distribution of indigent inmate kits.
- Amendment Number 2, dated August 20, 1998, amended the Statement of Work regarding indigent inmate kits.
- Amendment Number 3, dated March 26, 1999, amended the Statement of Work regarding haircuts and indigent inmate kits.
- Amendment Number 4, dated September 1, 1999 amended the Statement of Work to allow for cash-based commissary vending.
- Amendment Number 5, dated January 23, 2002 amended the Statement of Work to allow for the sale of telephone calling cards.
- Amendment Number 6, dated September 19, 2002 exercised the first annual contract extension.

Additionally, there have been 10 Change Order/Notices issued for this Contract as follows:

- Change Order Number 1, dated May 1, 2000, allowed price changes for indigent kits.
- Change Order Number 2, dated January 1, 2002, allowed price changes to certain goods.
- Change Notice Number 3, dated December 5, 2002, allowed for the supply and delivery of Gift (Holiday) and Emergency packages.
- Change Notice Number 4, dated October 8, 2003, exercised the 2nd annual extension option.

(1) General Information (Continued)

- Change Notice Number 5, dated October 31, 2003, allowed Canteen to install 16 kiosks.
- Change Notice Number 6, dated September 29, 2004, exercised the 3rd and final annual extension option.
- Change Notice Number 7, dated March 3, 2005, covered the following items:
  - Price changes on certain goods and indigent kits;
  - The addition of items to the medication list;
  - Sale of phone cards;
  - Items only to be sold to "Pro-Per" inmates;
  - Sale of special "commissary packs"; and
  - County shall incur no costs associated with the removal of kiosks.
- Change Notice Number 8, dated August 4, 2005, allowed price changes of certain goods.
- Change Notice Number 9, dated March 3, 2005, approved a rate change in the administration fee for phone cards.
- Change Notice Number 10, dated November 7 , 2005, served as notification for a personnel change in the Inmate Service Unit.

(2) Summary of Significant Accounting Policies

Canteen uses the cash basis of accounting, which differs from generally accepted accounting principles (as required in Section 40 of the commissary agreement), in the preparation of the financial schedules. Under the cash basis, expenses are recorded at time of payment and receipts are recorded at time of receipt, which could allow for some income and expenses to be excluded from a particular fiscal period. As a result, the calculation of any profit split could be skewed, which could cause a reduction in the revenue to which the County is contractually entitled.

(3) Inmate Cashiering System

Each inmate at a County jail has an account. Monies can be placed in an account at the time of booking or at a later time at the Cashier Services window. Inmates can order an array of items from the commissary service provider. Canteen provides the County, on a daily basis, amounts to deduct from each inmate's account based upon items ordered by the inmates. Canteen must submit an invoice to the County in order to be reimbursed for products sold to inmates that the County deducted from the inmates account.

(4) Net Sales Subject to Commission

In accordance with Exhibit B of the agreement, Canteen pays the County 31% of all net sales from the sale of commissary items such as stationery items, snack items, personal care products, over-the-counter medications, beverages, cosmetics and clothing. Net sales are defined as total gross sales less sales tax and stamp sales. Additional items excluded from net sales include sales of vending machine cards and the related service fee, sales of phone cards and related service fee, sales of haircut vouchers and indigent packs, all of which are classified as net deductions. The commission is paid to the County on a biweekly basis. The commission check is net of the amount due Canteen for indigent packs that are ordered by inmates. Checks are deposited into the Inmate Welfare Fund.

(5) Non-Commission Items/Net Deductions

The commission check is net of the amount due to Canteen for indigent packs that are ordered by inmates. The cost of the indigent pack is borne by the County. Commission on vending machine cards and phone cards are assessed at the time a card is used by an inmate, not at the time a card is sold to an inmate.

(6) Profit Split Incentive

Canteen's objective is to achieve a profit return of 6% of sales at the end of each year. If Canteen achieves more than its 6% profit objective, then Canteen and the County shall split all profits in excess of the 6% profit objective on an equal basis. Sales for the purposes of the profit split

(6) Profit Split Incentive (Continued)

incentive calculation is net sales plus the value of indigent and gift packs, less sales tax collected on all items.

(7) Expenses Taken in Determining Profit

Canteen recognizes all expenses of the business unit in determining the profit subject to the profit split. Total business unit expenses include such items as contributions to other organizations, including the Sheriff's Youth Foundation, travel expenses for corporate meetings, sponsorships of Sheriff events, and overhead charged to the business unit by its corporate headquarters. Although the profit subject to the profit split is not defined in the agreement, the only expenses that should be included in the calculation are those reasonable and necessary expenses for the administration of the agreement. It is generally accepted by the County that, in the absence of specific inclusions or exclusions of allowable contract expenses, the only expenses allowable are those considered to be reasonable and necessary in the course of provided the services required by the contract.

(8) Summary of Amount Due to/From the County

The following table documents the amount due to the County for the period September 19, 1999 through September 16, 2005 as a result of our audit. Records for the period September 29, 1997 through September 18, 1999 were not available for audit. The amounts due to the County are more fully described in Finding Number 1 in the Findings and Recommendations section of this Report.

	Commission		Amount Due
	Payable	Paid	To County
Commissary services	$18,038,773	$18,038,773	$ --
Profit split incentive	1,390,629	750,416	640,213
Totals	$19,429,402	$18,789,019	$640,213

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County of Los Angeles
Inmate Welfare Commission
Los Angeles, California

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL SCHEDULES PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

We have audited the financial schedules (Schedule of Commissary Sales and Commission Paid, and Schedule of Profit Split Incentive), which summarize the amounts payable and paid to the County of Los Angeles Sheriff's Department for the period September 29, 1997 through September 16, 2005 reported by Compass Group USA, Inc. to the County of Los Angeles Sheriff's Department, under an agreement for the operation of a concession and vending machine services in the County of Los Angeles jails, and have issued our report thereon dated December 12, 2005. In our report, our opinion was qualified for the period of September 29, 1997 to September 18, 1999 due to the unavailability of accounting records. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Compass Group USA, Inc.'s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial schedules, and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Compass Group USA, Inc.'s ability to record, process, summarize and report financial data consistent with the assertions of management in the financial schedules. The reportable conditions are described in the accompanying Findings and Recommendations as Item 1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules being audited

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may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Compass Group USA, Inc.'s financial schedules are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Findings and Recommendations as items 1 through 6.

This report is intended solely for the information of the management of the County of Los Angeles Department of Auditor-Controller, Sheriff's Department and Compass Group USA, Inc. and is not intended to be and should not be used by anyone other than those specified parties.

Conrad and Associates, L.L.P.

December 12, 2005

(1) Only Expenses Related to the Agreement Should be Included in the Profit Split Calculation

During our review of the expenses included in the profit split calculation, we noted that Compass Group USA, Inc. (Canteen) included all business unit expenses in the calculation, as well as some expenses relating to business units not associated with the Agreement. Some of the expenses included were not ordinary and necessary for providing services as required by the Agreement. Specifically, we noted the following questionable expenses which were included in the profit split incentive calculation:

Expenses relating to business units not associated with the Agreement:

- Travel, lodging, airfare, meals and entertainment expenses in the amount of $154,476 to attend corporate management meetings;
- Expenses totaling $82,948 which should have been charged to business units other than the unit responsible for managing the Agreement; and
- Revisions to Field Operating Statements made by Compass Group USA during the audit process resulted in a decrease of total operating expenses in the amount of $422,013.

Expenses not considered to be ordinary and necessary for providing services as required by the Agreement:

- Contribution to the Sheriff's Youth Foundation in the amount of $304,291;
- Sponsorships in the amount of $147,233 paid to the Sheriff's Department for various events; and
- Client hospitality in the amount of $169,465.

Although the Agreement does not specifically define what constitutes allowable expenses to be deducted for profit split purposes, it is the general practice of the County that only ordinary and necessary expenses should be charged to a contract. Failure to deduct costs that are not ordinary and necessary in the administration of the Agreement and costs not associated with the agreement has resulted in a loss to the County in the amount of $640,213.

(1) Only Expenses Related to the Contract Should be Included in the Profit Split Calculation (Continued)

Recommendation

We recommend that the County of Los Angeles recover $329,719 from Compass Group USA, Inc. as additional profit split incentive. In addition, we recommend that the County of Los Angeles seek the advice of legal council regarding the recovery of the profit split incentive in the amount of $310,494, related to expenses not considered ordinary and necessary for providing services as required by the Agreement.

Compass Response

Travel, lodging, airfare, meals and entertainment expenses in the amount of $154,000 to attend corporate management meetings:

Upon further review, Compass agrees that $154,000 in travel expenses were charged against the Los Angeles County Sheriff's Department Commissary Profit & Loss statement that belonged as expenses against other Commissary branches in the Western United States. As such, Compass is in agreement that these costs **should have been** transferred to the appropriate cost centers outside of the contractual Profit & Loss statement. In error, they were not transferred according to Compass Accounting practices.

Expenses which should have been charged to other business units:

In reviewing the source documents that the auditors requested, Compass is in agreement that $83,000 in vendor invoices were erroneously charged to the Los Angeles County Sheriff's Department Commissary Profit and Loss Statement.

Contributions to the Sheriff's Youth Foundation:

As a direct result of our agreement Canteen Correctional Services has been made aware of and has contributed to the Sheriff's Youth Foundation. In our view, all of these contributions help to reduce recidivism in the community, as well as creating hope and opportunities for socially and economically disadvantaged individuals. In compliance with Generally Accepted Accounting Practices, Compass has allocated these expenses to the profit and loss statement. These deductions in no way violate the terms and conditions outlined in the existing contractual agreement.

(1) Only Expenses Related to the Agreement Should be Included in the Profit Split Calculation (Continued)

Compass Response (Continued)

Sponsorships paid to the Sheriff's Department for various events:

Compass acknowledges that as a responsible contractor in the community, we have made various sponsorships over the course of the contract term to support our customer. We view this contract as a partnership arrangement between the County and Compass Group, and are passionate about supporting the various charitable organizations and events that are important to the community. We have supported many retirement events, charitable golf tournaments, Board of Supervisor events and the Baker to Vegas relay events. We share in the Sheriff's Department's view that these are important events worthy of Compass' support. In compliance with Generally Accepted Accounting Practices, Compass has allocated these expenses to the profit and loss statement. These deductions in no way violate the terms and conditions outlined in the existing contractual agreement.

Client Hospitality in the amount of $169,000

Senior Management at the Canoga Park facility regularly meets with several members of the Sheriff's Department to discuss business matters surrounding the Commissary and Vending Contracts. Generally, these meetings will take place over lunch or some other forum that will still allow the participants to discuss the business matters at hand. Often times, Compass will pay for the expenses associated with these meetings. In addition to these meetings, our General Manager attends regional and national trade shows on a regular basis. These events provide us with the opportunity to keep abreast of the latest trends in the Corrections Industry and to offer suggestions to improve on the Commissary Services program for Los Angeles County Sheriff's Department. Some examples of the trends that we have learned about in attending these industry trade shows is the inmate kiosk program that we installed in 2003. The recent creation of Mycarepack.com gift package offering to family and friends was learned as a result of attending an American Corrections Association trade show. Additionally, many of the secure products that are now available on the inmate menus, such as clear packaging products, were learned about at these trade events. All of the costs associated with attending the trade shows were directly related to supporting the Los Angeles County Sheriff's Department, and in keeping abreast of the latest trends in the industry; this benefit is ultimately passed on to the inmates that we service in the Los Angeles County jails.

(1) Only Expenses Related to the Contract Should be Included in the Profit Split Calculation (Continued)

Compass Response (Continued)

These events were attended only in conjunction with staff from the Los Angeles County Sheriff's Department. In compliance with Generally Accepted Accounting Practices, Compass has allocated these expenses to the profit and loss statement. These deductions in no way violate the terms and conditions outlined in the existing contractual agreement.

Other matters

In addition to the above outlined points, we did provide documentation to the audit team that supported Compass Group's position that we erroneously underestimated the allocation of Overhead Costs in the audited years 2000 through 2005. In reviewing the allocation charged against the profit split, we have identified that we should have charged $5,341,436 over the 2000 – 2005 timeframe. In reality, Compass charged $3,751,852. This represents a benefit to the Sheriff's Department of $1,589,554. For instance, in 2005, we provided supporting documents on overhead allocation cost for operating all business within the Canteen Correctional Services Division of Compass Group is at 6.7% of Gross Revenue. Included in this percentage allocation are overhead support functions provided at the Corporate, Sector and Divisional level. These overhead expenses provide the Canoga Park branch with most of the business functions necessary to operate a business. An excerpt of our proposal to the RFP is attached for review. This document outlines the levels of support and infrastructure that the Compass Corporate business functions provide to all of our businesses. These functions include, but are not limited to:

- **Accounting**
  - General Ledger Accounting and reports
  - Field accounting support, including
    - accounts payable
    - accounts receivable
    - financial planning
    - audit staff
    - financial closing cycle of profit & loss statements.

(1) Only Expenses Related to the Contract Should be Included in the Profit Split Calculation (Continued)

Compass Response (Continued)

- **Tax Department**
  - Ensure that appropriate Federal, State and County tax code is adhered to regarding Sales and Use tax, FICA, FUTA, SUTA payroll tax filing, ensuring appropriate permits are in place, and property taxes are paid.
- **Human Resources**
  - Workers Compensation management, Employee recognition programs, On the job training such as Sexual Harassment, Diversity, Hiring and Termination practices, Management skills training, customer service training. Support in dealing with sensitive associate circumstances such as hiring, termination, counseling and review process.
- **Benefits**
  - Support in rolling out annual medical, dental, 401(k), disability and life insurance plans. Provide support in administering employee recognition programs such as Be-A-Star and monthly CHAT (Communications, Help, and Training) programs. Provision of a toll free employee hotline for personal crisis counseling.
- **Training**
  - Support mechanism for training our associates on Compass policies and procedures. Additional dedicated training function in place for Corrections Division specific training, geared towards associates working in a correctional facility environment.
- **Information Technology**
  - Dedicated business function for the development of communications systems such as email, corporate purchasing of hardware such as computer workstations, printers, file servers and networks. Support of all equipment purchased to ensure minimum downtime.
- **Legal**
  - Internal team of attorneys responsible for drafting contracts, responding to inmate grievances and associate filings. Respond to client contract negotiations and addendum requests.

(1) Only Expenses Related to the Contract Should be Included in the Profit Split Calculation (Continued)

Compass Response (Continued)

- **Sales and Marketing**
  - Function as a liaison between the clients of Compass Group and the operations staff. Perform periodic customer service reviews through our Strategic Alliance Group, and offer an open line of communication for sharing client thoughts and concerns on how we are performing in the contract. Offer suggestions on improving the program through added customer service, therefore driving revenue. Provide marketing material such as quarterly newsletters and brochures on the latest developments that the company has to offer.

As expected these support functions carry a real cost to the parent company and each of the profit and loss accounts that they serve. In general, support costs are provided to the branch level from the Corporate level (Compass Group the Americas Division), the Sector Level (Canteen Services) and the Division level (Canteen Correctional Services).

The attached table provides revenue to cost comparison at each level identified, with a corresponding percent of sales. In determining the overhead cost allocation against the Los Angeles County Sheriff's Department Commissary Services, Compass should have been using these allocations since the beginning of the contract. It should be noted that in all of the years identified, Compass did not in fact allocate overhead costs to the full extent of what was actually absorbed as a percent of sales at the Corporate, Sector and Division level. Compass' position is the discrepancy in these cost allocations directly benefited the Inmate Welfare fund in calculating the annual profit splits. Since this benefit produced a reduction in profit for Compass Group that more than offsets the identified costs for travel and billing, we are not in agreement with the audit recommendation that the County of Los Angeles recover any funds from Compass Group USA, Inc.

Corporate Structure

We look upon the corporate structure as a resource center, a library of knowledge and a storeroom of supplies for our field managers to use. Canteen believes the key to success in our industry is management strength at the local and account level. But we also know they require a support network and that is where the corporate staff becomes involved.

Our field management and clients are encouraged to call on corporate departments and personnel to solve problems and provide direction. These professionals and specialists are actively involved with the day-to-day operations of our field organization to ensure quality, service and financial performance.

In addition, the following lists some of the services provided by Canteen's corporate office:

- Human Resources
- Purchasing
- Training
- Sales and Marketing
- Management Information Systems
- Accounting
- Auditing
- Quality Controls Audit

Our *People* Philosophy. Whether you are talking about a jail, cafeteria, kitchen, or a faculty dining room, when you get right down to it, you're talking about people. After all, its *people* who fill the machines, deliver the product, service the equipment and cook the meals.

Therefore, it quickly becomes obvious that Canteen is a company of people whose product is a service . . . the purchase, preparation and delivery of food. We hire the best people and we keep them. Then we provide them with continuing training, support and proven service programs.

Canteen is proud of its people . . . from packers to delivery people; from field managers and dietitians to accountants and regional support. These are the people that offer that something extra. That extra ability and dedication; that extra effort; and that very important extra, a special smile.

When you are evaluating a correctional bag-in service company, take a look at the people, because we've found that it is our people who enable Canteen to serve best!

Regional Support

Canteen's regional concept was developed to give greater decision making capability to our field management. With Canteen's bag-in commissary production warehouse in L.A. and division office located in Dublin, our district management is strategically located to serve the commissary program for the Los Angeles County Jails.

Canteen's local regional office and the Regional Vice President, John Winter, has complete decision making authority on issues related to our clients. This will ensure that the Los Angeles County Jails will have immediate local action.

The Regional Vice President has developed Canteen's overall business plan, designed the necessary support organization, and the specific operations plan and team for the Los Angeles County Jails.

The most important people at Canteen are the on-site manager, production supervisors, production workers, and route personnel who deliver our services to our customers. In our organization, they are the true heroes whose day-to-day enthusiasm and diligence makes us or breaks us. Taking care of them and our customers are our top priorities.

Regional Management Responsibilities

These key California Executives will assist, advise and direct our own commissary management for the Los Angeles County Jails, as well as provide your staff with a ready source for necessary consultation.

Some of the areas our local senior management staff will monitor include:

- Levels of inmate satisfaction
- Quality assurance
- Menu planning
- Client relations
- National brand products
- Production and service
- Employee training
- Compliance with County standards
- Internal production controls
- Financial and accounting controls
- Purchasing controls
- MBE/WBE Development

CANTEEN CORRECTIONAL SERVICES
OVERHEAD COST ALLOCATION
BASIS FOR AUDIT - L.A. COUNTY

	2000	2001	2002	2003	2004	2005	Total
Corporate Level (Compass Group America's Division)							
Total Revenue (000's)	2,871,530	3,972,139	5,135,911	5,728,331	6,268,228	7,234,264	31,210,403
Total Overhead Costs (000's)	80,189	126,789	173,401	199,497	210,261	214,170	1,004,307
Percentage Overhead Costs	**2.8%**	**3.2%**	**3.4%**	**3.5%**	**3.4%**	**3.0%**	**3.2%**
Sector Level (Canteen Services)							
Total Revenue (000's)	827,788	809,483	810,035	823,841	849,437	891,042	5,011,636
Total Overhead Costs (000's)	4,997	5,858	4,246	4,853	5,291	6,462	31,707
Percentage Overhead Costs	**0.6%**	**0.7%**	**0.5%**	**0.6%**	**0.6%**	**0.7%**	**0.6%**
Division Level (Canteen Correctional Services)							
Total Revenue (000's)	126,925	168,601	191,685	247,198	300,830	336,789	1,372,028
Total Overhead Costs (000's)	3,124	5,554	7,307	9,440	10,490	10,183	46,098
Percentage Overhead Costs	**2.5%**	**3.3%**	**3.8%**	**3.8%**	**3.5%**	**3.0%**	**3.4%**
GRAND TOTAL PERCENT OVERHEAD TO REVENUE	**3.3%**	**4.8%**	**4.7%**	**4.4%**	**4.3%**	**3.7%**	**4.2%**
TOTAL OVERHEAD CHARGED TO L.A. SHERIFF'S COMMISSARY PROGRAM	**3.3%**	**4.5%**	**4.5%**	**3.4%**	**3.5%**	**3.1%**	**3.6%**
Total Net Revenue	$ 10,633,128	$ 11,962,227	$ 12,274,741	$ 12,367,028	$ 12,610,093	$ 14,791,405	$ 74,638,622
Grand Total Dollars Overhead to Revenue	**622,835**	**862,452**	**946,678**	**975,821**	**941,255**	**992,395**	**5,341,436**
Total Actual Overhead Charged	**414,692**	**538,300**	**552,363**	**630,718**	**743,115**	**872,693**	**3,751,882**
Variance	**208,143**	**324,152**	**394,314**	**345,103**	**197,259**	**119,702**	**1,589,554**

(1) Only Expenses Related to the Contract Should be Included in the Profit Split Calculation (Continued)

Auditor Response to Canteen Response

During a meeting with Canteen after the completion of fieldwork, Canteen had indicated that additional Corporate Charges could be charged to the County and provided schedules with their management response to support that position. No audit work was performed on the schedules other than was necessary to determine that the Corporate Charges originally reported to the County of Los Angeles were reasonable. As such, the requested increase in Corporate Charges is not reflected in the financial schedules.

County of Los Angeles' Response

Since the contract does not define what constitutes allowable expenses to be deducted for profit split purposes, as noted by the Audit, the Department will consult County Counsel as recommended.

(2) Need for Concessionaire and County to Follow the Record Retention Requirement

During our review of compliance with the terms of the Agreement, we noted that neither the Sheriff nor Canteen maintained all the records necessary to properly audit the Agreement.

Paragraph 40 of the Agreement states, in part:

> "Contractor shall maintain accurate and complete financial records of its operations as they relate to the services provided under this AGREEMENT in accordance with generally accepted accounting principals and procedures...accounting, financial records, and proprietary data shall be kept and maintained by CONTRACTOR for a period of five (5) years after completion of this AGREEMENT..."

Recommendation

We recommend that Canteen and the Sheriff's Department maintain all records as required by the terms of the Agreement.

(2) Need for Concessionaire and County to Follow the Record Retention Requirement (Continued)

Compass Response

Canteen management agrees with the auditors' recommendation and all records will be maintained as required by the terms of the Agreement

County of Los Angeles' Response

Sheriff movements and adjustments over the life of the contract have inadvertently caused records to be misplaced or discarded. A more comprehensive method of record keeping including maintaining records by a contracted vendor will enable the Department to retain and access records in the future. These provisions have already been implemented.

(3) Sales to Inmates are not Limited to $50.00 Per Week

During our review of compliance with the terms of the Agreement, we noted that sales to inmates routinely ran more than the maximum of $50 per week.

Item 7 of the Statement of Work in the Agreement states:

> "CONTRACTOR shall not allow inmates to make more than a fifty dollar ($50) commissary purchase at any one time. Said commissary dollar limit is established by COUNTY. COUNTY shall give written notice to CONTRACTOR of any change in the commissary dollar limit".

Failure to limit sales to the inmates as required results in non-compliance with the terms of the Agreement.

Recommendation

We recommend that the Sheriff closely monitor the terms of the Agreement and any alterations to the terms of the work provided by Canteen be documented and approved by the Sheriff's Department through a change order.

(3) Sales to Inmates are not Limited to $50.00 Per Week (Continued)

Recommendation (Continued)

Subsequent to the end of the audit period and prior to the date of the auditors' report, Change Notice Number 11 was issued which increased the amount of commissary purchase at any one time to $135 per week. No further action is required to be in compliance with the Agreement.

County of Los Angeles' Response

The Department's Contract Compliance Unit will be auditing the contract provisions and request changes when necessary in order to avoid potential issues.

(4) Sales to Inmates are not Made on a Twice Weekly Basis

During our interviews with Canteen and the Sheriff's Department staff, we were told that sales are only made once a week to each of the jail facilities.

Item 6 of the Statement of Work in the Contract states:

> "CONTRACTOR shall provide commissary sales to inmates at least twice weekly."

Our conversations with Sheriff's Department staff indicate that this practice of weekly deliveries has been the norm since the inception of the Agreement and that twice weekly deliveries were not feasible.

Recommendation:

We recommend that the Sheriff closely monitor the terms of the Agreement and any alterations to the terms of the work provided by Canteen be documented and approved by the Sheriff's Department through a change order.

(4) Sales to Inmates are not Made on a Twice Weekly Basis (Continued)

Recommendation (Continued)

Subsequent to the end of the audit period and prior to the date of the auditors' report, Change Notice Number 11 was issued which decreased the number of delivery trips to once a week. No further action is required to be in compliance with the Agreement.

County of Los Angeles' Response

The commissary services allow inmates to order consumable goods on a 24 hour basis. The vendor delivers such goods once a week on a set schedule. The vendor's delivery schedule determines when the inmate's final ordering period occurs.

A change order was issued to the vendor reflecting the deviation from the contract.

(5) Delivery of Products to Inmates is not Made within Twelve Hours of the Receipt of the Order

During our review of compliance with the terms of the Agreement, we noted that there is a requirement for Canteen to deliver products to the inmates within twelve hours of receipt of the inmate's order. We noted that the delivery turnaround time usually runs around twenty hours from time of receipt of the order form.

Item 8 of the Statement of Work in the Contract states:

> "CONTRACTOR shall deliver orders to inmates within twelve (12) hours from the time the order is received".

Management stated they were aware of the late times and indicated that they approved the later deliveries as most inmates are not in their dorms at the time of delivery making delivery much more difficult.

(5) Delivery of Products to Inmates is not Made within Twelve Hours of the Receipt of the Order (Continued)

Recommendation:

We recommend that the Sheriff's Department change the terms of the Agreement to allow Canteen more than the twelve hours to deliver the inmate's products in order to accommodate swift delivery to all inmates.

Compass Response

We are capable of turning orders around in a twelve hour timeframe. However, due to the reality of inmate movement within the system during the day, we have elected to deliver in the evening hours when the population is more likely to be in the housing units we are delivering the orders to. The Sheriff's Department is in support of this method of service, as it helps to drive revenue, and in turn commission rates to the Inmate Welfare Fund. Once again, Compass is in full agreement that a written amendment to the contract should be executed to account for this change in service.

County of Los Angeles' Response

The commissary services allow inmates to order consumable goods on a 24 hour basis. The vendor delivers such goods once a week on a set schedule. The vendor's delivery schedule determines when the inmate's final ordering period occurs.

(6) Need for County to Monitor Agreement for Compliance with Terms and Conditions

During our review of compliance with the terms of the Agreement, we noted several instances in which the County should have detected potential errors and did not address them with the Canteen. We were not provided with documentation that the County performed an effective review of the Canteen's profit objectives on an annual basis to ensure that significant increases of expenses year over year were justified and directly related to the fulfillment of the Contract profit split imitative.

(6) Need for County to Monitor Agreement for Compliance with Terms and Conditions (Continued)

Recommendation

We recommend that the County establish a formal review process for compliance with the terms of the Agreement no less than once a year, and that the results of the review be documented, approved by management and communicated to Canteen.

County of Los Angeles' Response

The Department's Contract Monitoring Unit is developing an evaluation instrument that will be used to monitor the new contract's operational and financial compliance with the provisions of the contract on an ongoing basis.

Supplementary Information

COMPASS GROUP USA, INC.

Commissary Services
Financial/Complaince Audit

Profit Split Incentive - 2000

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 10,824,937	10,824,937	-
Sales Tax	(191,809)	(191,809)	-
TOTAL SALES	10,633,128	10,633,128	-
PRODUCT COST			
Product	3,247,986	3,247,986	-
Paper and Menus	51,679	51,679	-
Rebates	-	-	-
NET PRODUCT COST	3,299,665	3,299,665	-
Gross Profit	7,333,463	7,333,463	-
PERSONNEL COST			
Direct Labor	1,393,167	1,393,167	-
Semi-Variable Labor	382,784	382,784	-
TOTAL PERSONNEL COST	1,775,951	1,775,951	-
SEMI-VARIABLE COST			
Location Commissions	3,148,225	3,148,225	-
Rent Expenses	179,035	179,035	-
Depreciation	64,384	64,384	-
Amortization	37,225	37,225	-
Sales Promotion	-	8,101	(8,101)
Travel	131,557	166,669	(35,112)
Communications	(3,393)	(3,393)	-
Fees and Services	66,772	66,772	-
Occupancy Expenses	70,094	70,094	-
Parts, Supplies and Maintenance	179,966	179,966	-
Taxes and Insurance	61,754	61,754	-
Uniforms	8,473	8,473	-
Cash Over/Short	-	-	-
Other Direct	241,081	241,631	(550)
TOTAL SEMI-VARIABLE	4,185,173	4,228,936	(43,763)
TOTAL OPERATING EXPENSES	5,961,124	6,004,887	(43,763)
(PBO) Profit Before Corporate Overhead	1,372,339	1,328,576	43,763
PBO % BREAKDOWN			
Corporate Charges	414,692	414,692	-
6% Profit Objective	637,988	637,988	-
Commission Split [profits above 6%]	319,659	275,896	43,763
LA County Amount, should be	159,830	137,948	21,882
Actual Amount Paid by Canteen	-	-	-
Variance (Under/(Over) Paid)	$ 159,830	137,948	21,882

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary
Financial/Compliance Audit

Profit Split Incentive Calculation - 2001

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 12,174,722	12,174,722	-
Sales Tax	(212,495)	(212,495)	-
TOTAL SALES	11,962,227	11,962,227	-
PRODUCT COST			
Product, net of rebates	3,532,667	3,532,667	-
Paper and Menus	108,488	108,488	-
Rebates	-	-	-
NET PRODUCT COST	3,641,155	3,641,155	-
Gross Profit	8,321,072	8,321,072	-
PERSONNEL COST			
Direct Labor	1,461,737	1,461,737	-
Semi-Variable Labor	529,473	529,473	-
TOTAL PERSONNEL COST	1,991,210	1,991,210	-
SEMI-VARIABLE COST			
Location Commissions	3,589,383	3,589,383	-
Rent Expenses	184,670	184,670	-
Depreciation	63,476	63,476	-
Amortization	37,225	37,225	-
Sales Promotion	-	28,735	(28,735)
Travel	182,915	208,218	(25,303)
Communications	106,258	106,258	-
Fees and Services	76,603	76,603	-
Occupancy Expenses	68,454	68,454	-
Parts, Supplies and Maintenance	184,658	184,658	-
Taxes and Insurance	74,576	74,576	-
Uniforms	20,637	20,637	-
Cash Over/Short	-	-	-
Other Direct	135,250	150,250	(15,000)
TOTAL SEMI-VARIABLE	4,724,105	4,793,143	(69,038)
TOTAL OPERATING EXPENSES	6,715,315	6,784,353	(69,038)
(PBO) Profit Before Corporate Overhead	1,605,757	1,536,719	69,038
PBO % BREAKDOWN			
Corporate Charges	538,300	538,300	-
6% Profit Objective	717,734	717,734	-
Commission Split [profits above 6%]	349,723	280,685	69,038
LA County Amount, should be	174,862	140,343	34,520
Actual Amount Paid by Canteen	193,645	193,645	-
Variance (Under/(Over) Paid)	$ (18,783)	(53,303)	34,520

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Profit Split Incentive Calculation - 2002

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 12,498,649	12,498,649	-
Sales Tax	(223,907)	(223,907)	-
TOTAL SALES	12,274,742	12,274,742	-
PRODUCT COST			
Product, net of rebates	3,566,815	3,557,386	9,429
Paper and Menus	137,106	137,106	-
Rebates	(9,429)	-	(9,429)
NET PRODUCT COST	3,694,492	3,694,492	-
Gross Profit	8,580,250	8,580,250	-
PERSONNEL COST			
Direct Labor	1,672,055	1,672,055	-
Semi-Variable Labor	449,894	449,894	-
TOTAL PERSONNEL COST	2,121,949	2,121,949	-
SEMI-VARIABLE COST			
Location Commissions	3,768,543	3,768,543	-
Rent Expenses	213,490	213,490	-
Depreciation	26,605	26,605	-
Amortization	30,526	30,526	-
Sales Promotion	-	38,502	(38,502)
Travel	204,728	220,128	(15,400)
Communications	70,745	70,745	-
Fees and Services	159,500	159,500	-
Occupancy Expenses	59,690	59,690	-
Parts, Supplies and Maintenance	180,829	180,829	-
Taxes and Insurance	78,549	78,549	-
Uniforms	5,339	5,339	-
Cash Over/Short	-	-	-
Other Direct	25,598	80,653	(55,055)
TOTAL SEMI-VARIABLE	4,824,142	4,933,099	(108,957)
TOTAL OPERATING EXPENSES	6,946,091	7,055,048	(108,957)
(PBO) Profit Before Corporate Overhead	1,634,159	1,525,202	108,957
PBO % BREAKDOWN			
Corporate Charges	552,363	552,363	-
6% Profit Objective	736,485	736,485	-
Commission Split [profits above 6%]	345,311	236,354	108,957
LA County Amount, should be	172,656	118,177	54,479
Actual Amount Paid by Canteen	169,014	169,014	-
Variance (Under/(Over) Paid)	$ 3,642	(50,837)	54,479

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Profit Split Incentive Calculation - 2003

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 12,588,478	12,588,478	-
Sales Tax	(221,450)	(221,450)	-
TOTAL SALES	12,367,028	12,367,028	-
PRODUCT COST			
Product, net of rebates	3,613,763	3,613,763	-
Paper and Menus	144,818	144,818	-
Rebates	-	-	-
NET PRODUCT COST	3,758,581	3,758,581	-
Gross Profit	8,608,447	8,608,447	-
PERSONNEL COST			
Direct Labor	1,479,942	1,479,942	-
Semi-Variable Labor	487,419	487,419	-
TOTAL PERSONNEL COST	1,967,361	1,967,361	-
SEMI-VARIABLE COST			
Location Commissions	3,627,671	3,627,671	-
Rent Expenses	233,052	233,052	-
Depreciation	6,991	11,710	(4,719)
Amortization	-	(4,719)	4,719
Sales Promotion	-	28,595	(28,595)
Travel	226,443	279,500	(53,057)
Communications	87,242	87,242	-
Fees and Services	180,543	180,543	-
Occupancy Expenses	39,802	39,802	-
Parts, Supplies and Maintenance	131,060	131,060	-
Taxes and Insurance	81,536	81,536	-
Uniforms	13,889	13,889	-
Cash Over/Short	-	-	-
Other Direct	16,487	96,661	(80,174)
TOTAL SEMI-VARIABLE	4,644,716	4,806,542	(161,826)
TOTAL OPERATING EXPENSES	6,612,077	6,773,903	(161,826)
(PBO) Profit Before Corporate Overhead	1,996,370	1,834,544	161,826
PBO % BREAKDOWN			
Corporate Charges	630,718	630,718	-
6% Profit Objective	742,022	742,022	-
Commission Split [profits above 6%]	623,630	461,804	161,826
LA County Amount, should be	311,815	230,902	80,913
Actual Amount Paid by Canteen	122,422	122,422	-
Variance (Under/(Over) Paid)	$ 189,393	108,480	80,913

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Profit Split Incentive Calculation - 2004

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 12,836,527	12,836,527	-
Sales Tax	(226,434)	(226,434)	-
TOTAL SALES	12,610,093	12,610,093	-
PRODUCT COST			
Product	3,972,784	3,972,784	-
Paper and Menus	142,680	142,680	-
Rebates	-	-	-
NET PRODUCT COST	4,115,464	4,115,464	-
Gross Profit	8,494,629	8,494,629	-
PERSONNEL COST			
Direct Labor	1,137,568	1,137,568	-
Semi-Variable Labor	773,708	773,708	-
TOTAL PERSONNEL COST	1,911,276	1,911,276	-
SEMI-VARIABLE COST			
Location Commissions	3,499,003	3,499,003	-
Rent Expenses	233,379	233,379	-
Depreciation	35,520	35,520	-
Amortization	-	-	-
Sales Promotion	-	21,828	(21,828)
Travel	281,208	377,208	(96,000)
Communications	56,220	56,220	-
Fees and Services	164,004	175,504	(11,500)
Occupancy Expenses	58,962	58,962	-
Parts, Supplies and Maintenance	133,292	133,292	-
Taxes and Insurance	91,219	91,219	-
Uniforms	14,094	14,094	-
Cash Over/Short	-	-	-
Other Direct	28,877	96,945	(68,068)
TOTAL SEMI-VARIABLE	4,595,778	4,793,174	(197,396)
TOTAL OPERATING EXPENSES	6,507,054	6,704,450	(197,396)
(PBO) Profit Before Corporate Overhead	1,987,575	1,790,179	197,396
PBO % BREAKDOWN			
Corporate Charges	743,115	743,115	-
6% Profit Objective	756,606	756,606	-
Commission Split [profits above 6%]	487,854	290,458	197,396
LA County Amount, should be	243,927	145,229	98,698
Actual Amount Paid by Canteen	110,277	110,277	-
Variance (Under/(Over) Paid)	$ 133,650	34,952	98,698

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Profit Split Incentive Calculation - 2005

	As Audited	As Reported - *	Variance
SALES			
Commissary Sales	$ 14,981,575	14,981,575	-
Sales Tax	(190,169)	(190,169)	-
TOTAL SALES	14,791,406	14,791,406	-
PRODUCT COST			
Product	5,143,526	5,143,526	-
Paper and Menus	133,417	133,417	-
Rebates	-	-	-
NET PRODUCT COST	5,276,943	5,276,943	-
Gross Profit	9,514,463	9,514,463	-
PERSONNEL COST			
Direct Labor	1,237,434	1,237,434	-
Semi-Variable Labor	599,106	599,106	-
TOTAL PERSONNEL COST	1,836,540	1,836,540	-
SEMI-VARIABLE COST			
Location Commissions	4,033,596	4,033,596	-
Rent Expenses	214,369	214,369	-
Depreciation	88,300	88,300	-
Amortization	-	-	-
Sales Promotion	-	23,972	(23,972)
Travel	317,243	416,312	(99,069)
Communications	85,704	85,704	-
Fees and Services	79,447	162,395	(82,948)
Occupancy Expenses	81,464	81,464	-
Parts, Supplies and Maintenance	198,270	198,270	-
Taxes and Insurance	118,144	118,144	-
Uniforms	32,145	32,145	-
Cash Over/Short	-	-	-
Other Direct	13,987	85,431	(71,444)
TOTAL SEMI-VARIABLE	5,262,669	5,540,102	(277,433)
TOTAL OPERATING EXPENSES	7,099,209	7,376,642	(277,433)
(PBO) Profit Before Corporate Overhead	2,415,254	2,137,821	277,433
PBO % BREAKDOWN			
Corporate Charges	872,693	872,693	-
6% Profit Objective	887,484	887,484	-
Commission Split [profits above 6%]	655,077	377,644	277,433
LA County Amount, should be	327,538	188,823	138,715
Actual Amount Paid by Canteen	155,057	155,057	-
Variance (Under/(Over) Paid)	$ 172,481	33,766	138,715

* - The Field Operating Statements which were provided to the County of Los Angeles have been revised prior to the finalizing of this audit.

COMPASS GROUP USA, INC.

Commissary Services
Financial/Compliance Audit

Exit Conference

Date: July 18, 2006

Location: Department of Auditor-Controller, Alhambra, California

Present:

Compass Group USA, Inc.
Larry Jolly
Sean Mahoney
Craig Tramontano

Los Angeles County Sheriff's Department
Karen Anderson
Peter Burnstein
Karen Dalton
Grady Machnick
Ritu Sehgal
Paula Tokar
Amy Wang
Teri Wilhelm
Frank Williams
Henry Yee

Los Angeles County Department of Auditor-Controller
Karen Fee
Joe Nurre
Glenn Uyeda

Mayer Hoffman McCann P.C.
Marc Davis
Steven Dobrenen

Items discussed:

1) Which expenses are includable in determining the profit split calculation
2) Need to revise the record retention requiremnt
3) A change notice has been issued with respect to commissary purchase limits limits and weekly deliveries.
4) Due dates for management responses and due date for final report.