



EASTERN SHIRES
PURCHASING
ORGANISATION

A LOCAL AUTHORITY PURCHASING AND DISTRIBUTION CONSORTIUM

CONSORTIUM SECRETARY: JOHN SINNOTT, MA, Dipl. P.A.,
CHIEF EXECUTIVE, LEICESTERSHIRE COUNTY COUNCIL

Date: 2 June 2014
My Ref: BS/ESPO
Please ask for: Ben Smith
Direct Dialling: (0116) 305 6036
e-mail: ben.smith@leics.gov.uk

To: Members of the ESPO Finance and Audit Sub Committee

Dear Member,

ESPO FINANCE AND AUDIT SUBCOMMITTEE

A meeting of the Finance and Audit Sub Committee will be held on Tuesday, 10 June 2014 at 11.00 am in the Gartree Committee Room, County Hall, Glenfield, Leicestershire.

Yours faithfully,

B Smith

for Consortium Secretary

AGENDA

1. Election of Chairman for the municipal year ending May 2015.
2. Minutes of the meeting held on 17 February 2014. (Pages 3 - 6)
3. Declarations of interest in respect of items on the agenda.
4. To advise of any other items which the Chairman has decided to take as urgent elsewhere on the agenda.
5. Draft Outturn 2013/14. (Pages 7 - 14)
(Joint Report of the Consortium Treasurer and Director)
6. Progress Against the Internal Audit Annual Plan 2013/14. (Pages 15 - 26)
(Report of the Consortium Treasurer)

Democratic Services ◦ Chief Executive's Department ◦ Leicestershire County Council ◦ County Hall
Glenfield ◦ Leicestershire ◦ LE3 8RA ◦ Tel: 0116 232 3232 ◦ Email: democracy@leics.gov.uk



www.twitter.com/Espo



www.espo.org

7. Internal Audit Annual Members' Report 2013/14. (Pages 27 - 40)
(Report of the Consortium Treasurer)
8. Internal Audit Annual Plan 2014/15. (Pages 41 - 50)
(Report of the Consortium Treasurer)
9. Date of next meeting - 9 September 2014 at 10.30 am.
10. Any other items which the Chairman has decided to take as urgent.

The public are likely to be excluded during the consideration of the following items of business in accordance with Section 100(A)(4) of the Local Government Act 1972 (Exempt Information):

11. Supplementary Information Informing the Draft Outturn 2013/14. (Pages 51 - 58)
(Joint Report of the Consortium Treasurer and Director)
Exempt under paragraphs 3 and 10 of Section 100(A).

Minutes of a meeting of the ESPO Finance and Audit Subcommittee held at County Hall, Glenfield, Leicestershire on Monday, 17 February 2014.

PRESENT

Cambridgeshire County Council

Cllr. J. Reynolds (in the Chair)

Leicestershire County Council

Dr. R.K.A. Feltham CC

Lincolnshire County Council

Cllr. S. Rawlins

Peterborough City Council

Cllr. D. Seaton

26. MINUTES.

The minutes of the meeting held on 3 September 2013, having previously been circulated, were agreed as a correct record and signed.

27. DECLARATIONS OF INTEREST.

The Chairman invited members who wished to do so to declare any interest in respect of items on the agenda for the meeting.

No declarations were made.

28. URGENT ITEMS.

There were no urgent items for consideration.

29. CHANGE TO THE ORDER OF BUSINESS.

The Chairman sought and obtained the consent of the Subcommittee to vary the order of business from that set out in the agenda.

30. MANAGEMENT ACCOUNTS TO DECEMBER 2013.

The Subcommittee received a joint report of the Director and Consortium Treasurer setting out the results of the first nine months of trading, April to December 2013. A copy of the report, marked '4', is filed with these minutes.

Arising from the discussion the following points were made:

- (i) Store sales growth was strong and was approximately 10.7% after 18 months of the original four year Medium Term Business Strategy, consistent with the four year objective of 20% growth;
- (ii) ESPO's strategy to keep price increases below or at inflation meant that the benefits of its current growth, increased margin and turnover was passed on to the consumer. ESPO's focus on internal efficiencies of the business, meant it was also able to maintain the projected surplus back to Consortium Authorities;
- (iii) The Director reported that a review of transportation arrangements was currently in progress, with a report to be presented to Management Committee in due course on options arising. Savings expected to be yielded from contracting the service out were not as initially projected, so it was likely that a hybrid transport model would be recommended, with ESPO's own fleet supporting its core network, supplemented by contracted vehicles for further afield. Due to this hybrid approach it was likely that a number of new vehicles would need to be purchased to replace an ageing fleet and to balance investment and flexibility;
- (iv) ESPO was not experiencing excessive bad debts and the number of debtors was consistent with volume;
- (v) Appropriate marketing and management of slow-moving lines would make space for more popular and faster-moving stock in an effort to reduce the need for 'to follow' deliveries to customers and the inefficiencies this brought which could be up to 20% of cost of processing the order.

RESOLVED:

That the Director and Consortium Treasurer be thanked for their report.

31. EXCLUSION OF THE PRESS AND PUBLIC.

RESOLVED:

That under Section 100(A)(iv) of the Local Government Act 1972 the public be excluded from the meeting on the grounds that it will involve the likely disclosure of exempt information during consideration of the following items of business entitled:

'Supplementary Information informing the Management Accounts to December 2013' as defined in paragraphs 3 and 10 of Schedule 12A of the Act; and, in all circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

32. SUPPLEMENTARY INFORMATION INFORMING THE MANAGEMENT ACCOUNTS TO DECEMBER 2013.

The Subcommittee received an exempt report from the Director setting out further supplementary information regarding more detailed analysis of ESPO's accounts, supplementing item 4 of the agenda. The report contained details of a commercially

sensitive nature. A copy of the exempt report, marked 'item 8', is filed with these minutes.

The exempt report was not for publication by virtue of paragraphs 3 and 10 of Section 12A of the Local Government Act 1972.

RESOLVED:

That the report be noted.

[The meeting then reconvened into public session]

33. PROGRESS AGAINST INTERNAL AUDIT ANNUAL PLAN.

The Subcommittee received a report of the Consortium Treasurer summarising the Internal Audit Service, highlighting high importance recommendations and updating on the adoption of the Public Service Internal Audit Standards (2013). A copy of the report, marked '5', is filed with these minutes.

Arising from the discussion the following points were noted:

- (i) There were a number of audit jobs awaiting completion or commencement for the current financial year which meant there was a danger of some not being undertaken this year, over and above the 90% completion target;
- (ii) In order to better track progress and aid their understanding, Members suggested that Appendix 2 to the report would benefit from the addition of a column to the schedule of audits to show dates completed/projected completion dates, together with an overall percentage of audits completed against the number planned for the year. The Consortium Treasurer undertook to include this in future reports;

RESOLVED:

That the report be noted.

34. DATE OF NEXT MEETING.

It was noted that the next meeting would be held at 10.30 am on Tuesday 10 June 2014.

35. EXCLUSION OF THE PUBLIC.

RESOLVED:

That under Section 100(A)(iv) of the Local Government Act 1972 the public be excluded from the meeting on the grounds that it will involve the likely disclosure of exempt information during consideration of the following items of business entitled:

'Supplementary Information informing the Management Accounts to December 2013' and 'Forecast Outturn 2013/14 and Draft MTFS 2014/15 – 2017-18' as defined in

paragraphs 3 and 10 of Schedule 12A of the Act; and, in all circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

36. FORECAST OUTTURN 2013/14 AND DRAFT MTFS 2014/15 - 2017/18.

The Subcommittee received an exempt joint report from the Director and Consortium Treasurer, the purpose of which was to give an update on the implications of the Medium Term Financial Strategy (MTFS) document currently in preparation, presenting the draft 2014-15 budget and presenting draft outline budgets for the forthcoming three years. The report contained details of a commercially sensitive nature, a copy of which, marked 'item 9', is filed with these minutes.

The exempt report was not for publication by virtue of paragraphs 3 and 10 of Section 12A of the Local Government Act 1972.

Arising from the discussion the following general points were made:

- (i) ESPO had developed its e-ordering capabilities and an improved web interface for customers was in progress, due to go live during the first quarter of the 2014/15 financial year; this, alongside working with suppliers to be able to fulfil 'just in time' deliveries, would create further efficiencies, improve the customer experience and stock accuracy/levels over the course of the MTFS;
- (ii) There remained strong demand from customers for the ESPO catalogue. Whilst this meant fixed 12 month headlining pricing for stores products, members supported the use of marketing initiatives and promotions applied throughout the year to drive sales and manage stock levels;
- (iii) As the new Indigo Warehouse system became fully operation, ESPO's agency manpower costs was expected to fall as a proportion of the previous year's budget;
- (iv) A contractor was currently being employed by the Servicing Authority to assess major spend on energy at Leicestershire County Council buildings. Members felt this could be extended to cover ESPO's Grove Park building, acting as a form of review as to whether elements of its 40 efficiency projects should be altered to gain greater returns.

RESOLVED:

That the contents of the report be noted and the comments now made be presented to the Management Committee meeting of Thursday 6 March 2014.



ESPO FINANCE AND AUDIT SUBCOMMITTEE – 10 JUNE 2014

DRAFT OUTTURN 2013/14

REPORT OF THE CONSORTIUM TREASURER

Introduction

1. This report sets out the draft outturn for 2013/14 with explanations for the more significant variances to prior year, budget and forecast. Members should note that the outturn will be subject to external audit. A summary profit and loss statement (P&L) is presented below:

	<u>YEAR TO DATE</u>		
	ACTUAL	BUDGET	PRIOR YEAR
	£000	£000	£000
TOTAL SALES	95,605.3	94,199.8	94,019.2
TOTAL MARGIN	19,329.4	17,823.2	18,643.4
Margin %	20.2%	18.9%	19.8%
TOTAL EXPENDITURE	16,946.6	16,005.6	15,959.6
TRADING SURPLUS	2,382.8	1,817.5	2,683.8

Trading Summary

Income

	<u>YEAR TO DATE</u>		
	ACTUAL	BUDGET	PRIOR YEAR
	£000	£000	£000
<u>SALES</u>			
STORES	42,333.8	42,254.0	40,316.1
DIRECT	21,625.5	21,132.4	23,296.1
GAS	25,472.5	25,639.7	24,404.2
CATALOGUE ADVERTISING	930.5	896.3	918.5
REBATE INCOME	5,049.7	4,073.8	4,858.0
MISCELLANEOUS INCOME	193.2	203.7	226.3
TOTAL SALES	95,605.3	94,199.8	94,019.2

2. Overall the organisation's invoiced turnover for the year including rebates was £95.6m. This was 1.7% higher than the prior year which was primarily due to higher store sales, gas and rebates offset by lower directs.
3. Stores' sales value has increased this year, compared to the prior year, by £2m (5%) to £42.3m. Sales to member authorities including academies have increased by 2%, while sales to other authorities have increased by 8%.
4. The growth in store sales was thus principally achieved in non-member areas.
5. As a result of the Department of Education Phonics initiative coming to an end in October 2103 the Directs catalogue products business decreased to £21.6m from £23.3m the prior year, a fall of 7.2%. This national initiative was co-ordinated by ESPO on behalf of the Pro5 consortium.
6. Rebate income was £5.0m an increase of £0.2m on prior year. This has been achieved while continuing to reduce rebate margin from our suppliers.
7. Catalogue advertising was £0.9m and was consistent with the prior year. This is a good performance at a time when pressures on advertising income are considered strong.
8. Compared to budget overall sales are £1.4m higher driven by higher rebates £0.9m and higher directs £0.5m.
9. Compared to forecast overall sales are £4.1m lower driven by lower gas sales £4.0m as a result of the warmer winter. This also impacted sales of salt from the warehouse.

Margin

10. Stores margin (mark up) increased to 33.6% compared to 32.3% last year. This was mainly driven by the Sinclair deal on paper which resulted in a better buying price but lower rebate. The switch from rebates to margin as a result of this was approximately £200k
11. Directs margin fell to 9.7% as a percentage of sales compares to 10.8% last year. This was driven by a discount offer on Phonics in October which increased sales and market share but lowered margins. The margin is budgeted to return to over 10% for 2014-15.
12. Total margin was £19.3m against a budget of £17.8m, mainly as a result of higher rebates but also improved store sales margin.
13. Compared to forecast total margin was £0.9m higher driven once again by higher rebates and improved stores margin.

Expenditure

14. Total expenditure increased by £0.9m compared to last year. The key elements of this are as follows:

- Transport costs increased by £0.3m. This is mainly as a result of the aged fleet but also down to increased carrier costs. The issue of “to follow” orders also had an impact as stock levels fell over the summer months and stock availability suffered as a result.
 - Last year ESPO had a net credit on car lease annual rental of £0.1m as a result of a release of accruals. This year the charge is £0.1m which is the actual cost and was budgeted.
 - Higher IT Repairs and Maintenance costs as these contracts came up for renewal.
 - Higher catalogue and marketing costs as we invest and develop these areas.
15. Compared to budget total expenditure was £0.9m higher. The key elements of this are as follows:
- Higher agency costs over the key summer peak period.
 - Higher transport costs linked to the aged fleet.
 - Increased car lease balloon payments.
16. Compared to forecast total expenditure was £0.6m higher, the key elements of this are as follows:
- Higher agency costs in the final quarter
 - Higher transport costs, linked to carriers and the aged fleet.

Summary

17. The Net Surplus for the year was £2.4m which is £0.6m higher than budget and £0.3m higher than forecast. Whilst £0.3m lower than last year this is as a result of increased expenditure and lower directs offset by higher rebates and improved stores margins.
18. Further information which informs the Draft Outturn 2013/14, of a commercially sensitive nature, is contained elsewhere on the agenda for this meeting, this includes:
- a) Detailed breakdown of the year on year sales movement
 - b) Detailed breakdown of the overhead expenditure
 - c) Analysis by Service Lines
 - d) Detailed Balance Sheet
 - e) Staffing Analysis

Service Line Analysis

19. The net surplus for Stores was £1.01m against a forecast of £1.01m so broadly in line with no significant variances.
20. Framework Contracts achieved a surplus of £0.9m against a forecast of £0.2m. This was driven entirely by higher rebates achieved at year end.
21. Energy and Fuels operating surplus was £0.5m against a forecast of £0.7m. The shortfall is entirely down to reduced gas sales in the final quarter.

22. The detailed Service Line Analysis is included in the exempt part of the report elsewhere on the agenda.

Allocations from Operating Surplus

23. A continued further allocation of £0.4m is proposed to be used for the Building Capital Provision. The provision is necessary to ensure the building is maintained at the highest possible standard with funds allocated and available to meet general repairs and capital replacements/ improvements. This is consistent with the prior year and the MTFS.
24. It is proposed to deliver a return to members in excess of the forecast in March 2014. The forecast was for a surplus of £2.1m less the £0.4m for the building provision. This would leave a £1.7m forecast surplus of which members receive 80% or £1.4m. The extra surplus actually generated is proposed to be partly retained for investment in the business. It is thus proposed that a further £100k is set aside for a warehouse automation project. This will be subject to a detailed paper for consideration by the Management Committee in due course.

Distribution of Surplus:

25. The breakdown of the distribution of the surplus is thus as follows:

£m

Operating Surplus	2.4
Building Provision	0.4
Warehouse Automation	<u>0.1</u>
Net Surplus	1.9
General Fund	0.4
Dividend	1.5

26. The amount available for distribution after the above allocations to reserves is £1.90m of which 80% (£1.5million) is attributable to member authorities as a dividend. Year on year the member dividend has thus been maintained at the prior year level. Based on previous usage and subject to audit the breakdown of the dividend by member is

	<u>2013-14</u>
	<u>Proposed</u>
	<u>Distribution</u>
£	
Cambridgeshire	229,240
Leicester City	203,996
Leicestershire	207,492
Lincolnshire	230,412
Norfolk	336,190
Peterborough City	92,107
Warwickshire	206,823
Total	1,506,260

ESPO Balances

27. The General Fund balance is primarily to meet any adverse trading conditions, provide funding for stock balances and other expenditure prior to the receipt of income. Established practice is that 20% of operating surplus is added to this fund up to a maximum of 5% of turnover. For 2013/14 £0.35m has been added to the General Fund balance representing 20% of surplus. The level of General Fund balance is expected to increase annually until the agreed maximum is retained according to the approved funding formula, this is not expected to be reached during the period of the current MTFS.

Recommendation

28. The Subcommittee is asked to recommend to the Management Committee:
- (a) approval of the draft out turn for 2013/14;
 - (b) allocations from the operating surplus for 2013/14 as outlined in paragraphs 23 and 24 of this report;
 - (c) payment of the dividend, subject to approval of the accounts in September 2014, as outlined in paragraphs 25 and 26 of this report;

Officers to Contact

Mr J Doherty – Director (Tel: 0116 265 7930)

Mr C Tambini – Treasurer to the Consortium (Tel: 0116 305 7831)

List of Appendices

Appendix 1 – ESPO Management Accounts for Year End 31 March 2014

This page is intentionally left blank

COMBINED PRELIMINARY RESULTS**Mar-14****MONTH****Appendix 1****YEAR TO DATE**ACTUAL BUDGET PRIOR
YEARACTUAL BUDGET PRIOR
YEAR

£000 £000 £000

£000 £000 £000

SALES

STORES	3,290.2	2,805.8	2,536.4	42,333.8	42,254.0	40,316.1
DIRECT	1,916.9	1,765.3	2,089.8	21,625.5	21,132.4	23,296.1
GAS	3,112.9	4,928.5	3,530.6	25,472.5	25,639.7	24,404.2
CATALOGUE ADVERTISING	2.6	0.0	5.8	930.5	896.3	918.5
REBATE INCOME	1,077.2	669.6	648.0	5,049.7	4,073.8	4,858.0
MISCELLANEOUS INCOME	(1.2)	14.3	(16.1)	193.2	203.7	226.3

TOTAL SALES**9,398.6 10,183.5 8,794.5****95,605.3 94,199.8 94,019.2****Cost of Sales**

STORES	2,173.7	2,133.8	1,950.9	31,680.1	32,037.0	30,467.7
DIRECT	1,704.9	1,587.9	1,911.6	19,526.2	19,034.2	20,790.6
GAS	3,302.5	4,863.9	3,413.2	25,125.0	25,303.4	24,117.5
CATALOGUE ADVERTISING	0.0	0.0	0.0	0.0	0.0	0.0
REBATE INCOME	0.0	0.0	0.0	0.0	0.0	0.0
MISCELLANEOUS INCOME	0.0	0.0	0.0	0.0	0.0	0.0

TOTAL COST OF SALES**7,181.1 8,585.6 7,275.7****76,331.4 76,374.7 75,390.3****Margin**

STORES	1,116.5	672.0	585.5	10,653.7	10,217.0	9,848.4
DIRECT	211.9	177.4	178.2	2,099.3	2,098.2	2,505.5
GAS	(189.6)	64.6	117.3	347.5	336.3	286.7
CATALOGUE ADVERTISING	2.6	0.0	5.8	930.5	896.3	918.5
REBATE INCOME	1,077.2	669.6	648.0	5,049.7	4,073.8	4,858.0
MISCELLANEOUS INCOME	54.3	14.3	(16.1)	248.7	203.7	226.3

TOTAL MARGIN**2,273.0 1,597.8 1,533.1****19,329.4 17,823.2 18,643.4****Margin %****24.2% 15.7% 17.4%****20.2% 18.9% 19.8%****EXPENDITURE**

EMPLOYEES						
Staff	825.0	814.3	1,205.6	9,304.2	9,828.7	9,560.5
Agency/Contract	97.0	27.3	62.4	1,085.3	323.1	830.0
Total	922.0	841.6	1,268.0	10,389.5	10,151.8	10,390.4

OVERHEAD EXPENSES

Stores	452.6	306.7	229.7	4,095.4	3,684.1	3,837.5
CP	576.6	148.1	70.6	2,461.6	2,169.8	1,731.7
Total	1,029.2	454.8	300.3	6,557.0	5,853.8	5,569.2

TOTAL EXPENDITURE**1,951.2 1,296.4 1,568.3****16,946.6 16,005.6 15,959.6****TRADING SURPLUS****321.8 301.4 (35.2)****2,382.8 1,817.5 2,683.8****EMPLOYEES NUMBERS (Full-time equivalents):**

Stores	170	168	162	163	168	170
Purchasing	102	126	85	97	126	88
Indirects	81	76	82	81	76	83

TOTAL EMPLOYEES**352 371 329****341 370 340**

Income per Employee (FTE) £	6,450.0	4,312.0	4,654.0	56,723.0	48,136.0	54,767.0
Average Cost per Employee	2,341.0	2,197.0	3,660.0	27,304.0	26,545.0	28,085.0

This page is intentionally left blank



ESPO FINANCE AND AUDIT SUBCOMMITTEE – 10 JUNE 2014

INTERNAL AUDIT SERVICE - PROGRESS AGAINST THE 2013-14 INTERNAL AUDIT PLAN

REPORT OF THE CONSORTIUM TREASURER

Purpose of the Report

1. To give a summary of Leicestershire County Council's Internal Audit Service (LCCIAS) work to the Subcommittee and highlight any audits where high importance (HI) recommendations have been made and the position against implementing action.
2. To provide a brief summary of LCCIAS' performance against the ESPO Internal Audit Plan 2013-14
3. To provide a brief update on LCCIAS' implementation of the Public Sector Internal Audit Standards 2013 (the PSIAS)

Background

4. The Consortium Treasurer (the Treasurer) is responsible for the proper administration of ESPO's financial affairs. Rule 15 imposes a specific responsibility for arranging a continuous internal audit is delegated to the Treasurer. Under its terms of reference the Finance and Audit Subcommittee (the Subcommittee) should receive and review audit and governance reports. The Subcommittee also monitors the adequacy and effectiveness of the internal audit service provided to ESPO. To achieve this, the Subcommittee is provided with periodic progress reports.
5. The audits undertaken are based on the annual internal audit plan. Variations to the plan can occur but need to be considered with and agreed by the Treasurer and the Director of ESPO.

Summary of Progress

6. Progress against the 2013-14 plan up to the 27 May 2014, is shown in **Appendix 1**. The 'opinion' is what level of assurance can be given that material risks are being managed. Five jobs are shown as not finalised by 27 May, but there is confidence they will be by the date of this Subcommittee meeting.

7. There are four classifications of assurance: full; substantial; partial; and little. A report that has a high importance (HI) recommendation would not normally get a classification above partial. Exceptions would be where the controls are sound but there is a high importance efficiency recommendation.
8. **Appendix 2** summarises for completed audits the objectives, findings and conclusion/opinion and for audits in progress gives the objective and current position. At the Subcommittee meeting held on 17 February 2014, the HoIAS reported there were a considerable number of audits in train at different stages of workflow. In order to better track progress and aid their understanding, Members suggested that Appendix 2 to the report would benefit from additional information to show: -
- completed audits (now included on pages 21 to 23)
 - status of 'incomplete' audits with projected completion dates (page 24)
 - planned audits 'not started' & reasons (pages 25 and 26)
9. **Appendix 3 is not included but** would normally detail HI recommendations and provide a short summary of the issues surrounding these. However, there are not any new HI recommendations to report this quarter and in April LCCIAS received sufficient evidence to prove ESPO had taken appropriate action on the longstanding rebates HI recommendations. Nevertheless, Annual audit of rebates income should prove whether controls/improvements are fully embedded.

A brief summary of LCCIAS' performance against the ESPO Internal Audit Plan 2013-14

10. At the Subcommittee on 17 February, Members also requested information on performance against the plan. This can be easiest shown in the table below: -

Table 1 : Overall performance against 2013-14 internal audit plan

	<u>Due</u>	<u>Complete @ 27/5</u>	<u>Incomplete</u>	<u>Plan days</u>	<u>Actual days</u>	<u>Net days</u>
B/fwd from 12-13	5	5	0	0	15	+15
Follow up HI recs	2	2	0	0	2	+2
Planned 13-14	25	16	9	185	130	-55
Unplanned 13-14	0	2	1	0	7	+7
Client mgt.	1	1	0	15	21	+6
Total	33	26	10	200	175	-25

11. Because of the difficulty in closing down audits precisely at the end of the year, some resource has already been utilised in 2014-15 completing 2013-14 audits.
12. Reasons for the planned but incomplete work at 27 May are given in Appendix 2 pages 5 and 6. Explanations are a mix of untimely scheduling and having to balance against priorities for ESPO operations, key staff unavailability (especially in ICT audit at the start of the year) and 'overspends' closing off work. A number of unplanned jobs compensated for the postponements and a wide spectrum of ESPO's risks have still been covered.

A brief update on LCCIAS' adoption of the Public Service Internal Audit Standards (2013)

13. Organisations in the UK public sector have historically been governed by an array of differing internal audit standards. The Public Sector Internal Audit Standards (the PSIAS), which took effect from the 1st April 2013, provide a consolidated approach across the whole of the public sector enabling continuity, sound corporate governance and transparency. The PSIAS encompass not only the mandatory elements of the Global Institute of Internal Auditors (IIA), including a standard definition of internal auditing, a Code of Ethics and International Standards for the Professional Practice of Internal Auditing, but also further UK public sector requirements and interpretations.
14. The PSIAS mandate that the purpose, authority and responsibility of an organisation's internal audit activity must be formally defined in an internal audit charter (the Charter). The Head of Internal Audit Service (HoIAS) has provided a draft Internal Audit Charter for Leicestershire County Council which is currently being reviewed by the County Council's Chief Financial Officer and the Monitoring Officer. The draft Charter: -
 - a. recognises the mandatory nature of the PSIAS and relevant legislation;
 - b. defines the scope of internal audit activities;
 - c. establishes responsibilities, objectives & organisational independence;
 - d. establishes accountability, reporting lines and relationships;
 - e. sets out the arrangements for anti-fraud and anti-corruption policies;
 - f. establishes rights of access to all records, assets, people & premises;
 - g. define the terms 'board' & 'senior management';
 - h. covers the arrangements for appropriate resourcing;
 - i. defines the role of internal audit in any fraud-related work;
 - j. includes arrangements for avoiding conflicts of interest.
15. Once the Charter has been reviewed for the County Council, it would seem prudent for an adapted version for ESPO to be reviewed by the Consortium's Treasurer and Secretary and the Director of ESPO. Final approval of the Charter rests with 'the Board'. The PSIAS allows for a number of groups to satisfy the role of the Board but the standards define the Board as 'The highest level of governing body charged with the responsibility to direct and/or oversee the activities and management of the organisation'. and as such it is proposed that following consideration by the Finance and Audit

Subcommittee, the Management Committee should have responsibility to formally approve the ESPO Internal Audit Charter.

Recommendation

16. That the contents of the report be noted.

Equal Opportunities Implications

17. There are no discernible equal opportunities implications resulting from the audits listed.

Background Papers

Report to ESPO Management Committee on 27 September 2012 – Finance and Audit Subcommittee – Proposed terms of reference and indicative work plan

Officer to Contact

Neil Jones, Head of Internal Audit Service

Tel: 0116 305 7629

Email: neil.jones@leics.gov.uk

Appendices

- Appendix 1 - Summary of final internal audit reports issued 01.02.2014 – 27.05.2014
- Appendix 2 - Summary audit objectives, findings and conclusions

Summary of Internal Audit Service reports issued 1st February 2014 to 27th May 2014

Appendix 1

<u>Sub-Function</u>	<u>Name</u>	<u>Final Issued</u>	<u>Audit Opinion</u>	<u>HI Rec'n</u>
Governance	Risk Management	26/02/14	Substantial	No
Financial Asset	Business Forecasting	27/02/14	Substantial	No
Operational	Fleet Management - Vehicle Operating Licence	28/02/14	Full	No
Operational	Trading Performance & Distribution of Surplus	28/03/14	Full	No
Payroll	Payroll Changes	31/03/14	Substantial	No
Accounting/General Ledger	General ledger reconciliations	31/03/14	Substantial	No
Receivables	Rebates HI Recs f/up	03/04/14	Tested implemented	No
Human Resources	Attendance Management	08/04/14	Substantial	No
Governance	Budget Management	22/05/14	Substantial	No
Operational	Servicing Authority	27/05/14	Substantial	No
Governance	Anti Fraud and Corruption	Draft @ 27/5	<i>Substantial (*)</i>	No
Operational	IT General Controls	Draft @ 27/5	<i>Substantial (*)</i>	No
Operational	Stock Management	Draft @ 27/5	<i>Substantial (*)</i>	No
Receivables	Rebates Income	In progress		
Governance	Energy	In progress		

(*) There is little to doubt the draft opinions will change once the report is finalised

This page is intentionally left blank

Summary audit objectives, findings and conclusions**Audits concluded or in progress at 27th May 2014****Audits which are now 'concluded'**

<u>Audit title</u>	<u>Findings & conclusions</u>	<u>Opinion</u>	<u>Stage @ 27/5</u>	<u>Complete by</u>
Risk Management	Whilst there was evidence that some risk management activities were operating adequately, there was further scope to improve effective embedded risk management into operational activity.	Substantial	Finalised	N/A
Business forecasting	There are adequate controls in place to ensure that forecasts and annual budgets are approved correctly and are reviewed on an annual basis. Responsibilities are clearly assigned and timescales agreed for preparation of the annual budget. Information used in the annual budget process is accurate and budget holders are consulted. Minor recommendations around reporting key assumptions and improving budget working papers to include reasons for any significant changes, and clearly identifying when savings are as a result of specific projects within the Efficiencies Programme.	Substantial	Finalised	N/A
Fleet management – Vehicle Operating Licence	Evaluation of controls and testing confirmed that ESPO is compliant with the Vehicle Operating Licence 'General Conditions and Undertakings'	Full	Finalised	N/A

Audit title	Findings & conclusions	Opinion	Stage @ 27/5	Complete by
Trading performance & distribution of surplus	<p>There is an adequate audit trail from the Combined Preliminary reports presented to the Senior Management Team (SMT) for February 2014 back to the General Ledger.</p> <p>An framework for the calculation and distribution of dividends payable to members exists. Verification of the dividends distributed will be subject to a short audit in the 2014/15 financial year.</p>	Full	Finalised	N/A
Payroll changes	<p>Variations to pay are adequately supported by appropriately authorised documentation and changes have been made in accordance with instructions.</p> <p>Recommended that ESPO investigates delays by East Midlands Shared Services in issuing contracts and ESPO management is reminded on procedures in relation to new starters and the use of e-notification forms</p>	Substantial	Finalised	N/A
General ledger reconciliation	<p>This audit is required by the External Auditor in their annual assessment of the likelihood of material misstatement in the Authority's financial accounts.</p> <p>Accounting procedures are being applied to ensure the completeness and accuracy of the General Ledger.</p>	Substantial	Finalised	N/A
Rebates processes – HI rec's follow up	Received sufficient evidence to prove ESPO had taken appropriate action on the HI recommendations. Annual audit of rebates income should prove whether controls/improvements are fully embedded	Should be able to give substantial in future	Finalised	N/A

Audit title	Findings & conclusions	Opinion	Stage @ 27/5	Complete by
Attendance management	Recommended ESPO develop absence performance metrics now that there is meaningful data also recommended to ensure consistent application of the Attendance Management Policy by managers and a more efficient method of informing payroll of absences	Substantial	Finalised	N/A
Budget management	Whilst the budget position is reported accurately to SMT regularly and discussed and there have been some delegations to Assistant Directors, the audit recommended that processes could be improved by introducing a longer timeframe for reviewing budgets, producing forecasts and the introduction of commitments.	Substantial	Finalised	N/A
Servicing Authority	The draft SLA and processes were evaluated. Recommendations around including responsibilities and naming of key officers, clarifying the basis of charges both proposed and invoiced and monitoring and reporting service provision	Substantial	Finalised	N/A

Audits at 27 May 2014 where fieldwork has been concluded and a draft report either issued or is pending but not finalised

<u>Audit title</u>	<u>Findings & conclusions</u>	<u>Opinion</u>	<u>Stage @ 27/5</u>	<u>Finalise by</u>
Anti-fraud and corruption	The scope contained a review of policies and procedures, awareness and training. Minor recommendations are reliant on developments at the Servicing Authority	Substantial pending agreeing recommendations	Draft issued	Before committee
IT General controls	The External Auditor relies on this audit in their annual assessment of the likelihood of material misstatement in the Authority's financial accounts. Assurance is partly obtained through review of the integrity of the ICT infrastructure and associated applications that either directly or indirectly contributes to the production of the financial statements. Substantial assurance that the ICT infrastructure is robust and that the range of controls expected by the External Auditor are well designed and consistently applied.	Substantial pending agreeing recommendations	Draft issued	Before committee
Stock management	Evaluation of controls designed to ensure optimum stock management and warehouse operations. A few recommendations about performance indicators and mitigating risks to the optimisation model. The External Auditor may choose to place reliance on this audit.	Substantial pending agreeing recommendations	Draft issued	Before committee
Rebates income	Annual audit to validate that ESPO has received rebate in line with what was expected based on suppliers' turnover. Some disparity was found and although values are not material, ESPO will have scope to follow up with suppliers	Substantial pending agreeing recommendations	Draft pending	Before committee
Energy	The objective is to ensure that all relevant customers' records had been migrated to the new gas contract.	Still awaiting information	Draft pending	Before committee

Audits planned in 2013-14 that were not undertaken, reason, and indication of whether they'll for part of the 2014-15 plan

Audit title	Indicative scope, i.e. to ensure that...	Reason for not conducting the audit	Carry forward to 2014-15
ESPO Services	The key principles to providing the individual categories within the ESPO service menu are complied with	Scope agreed with Assistant Director but start deferred at ESPO's request due to an operational priority	Yes
Collaborative procurement	Framework and other collaborative arrangements do not jeopardise ESPO interest or risk a liability	Agreed with Director that it would be better to await the design and implementation of risk management relating to compliance and commercial activity, by way of a documented risk strategy.	Yes
Electronic transactions	P-card and other electronic transaction methods are PCI compliant	Insufficient resource at the time	Yes
Information management	Information is secure both on and off site and in transit and breaches are identified and investigated	Insufficient resource at the time	Yes
E-tendering	The security arrangements and audit trail are robust	Some advice to LCC during pilots	Yes
Applications management	Risks (e.g. continuity and resilience) to the successful operation of key business management systems within ESPO have been identified and appropriately mitigated	Insufficient ICT audit resource at the time. However, some coverage was obtained in the key IT controls audit for the External Auditor.	Yes

Audit title	Indicative scope, i.e. to ensure that...	Reason for not conducting the audit	Carry forward to 2014-15
Governance framework	The requirements of the Consortium Agreement, Constitution and appropriate schedules are embedded	No specific audit but a range of others have needed to evaluate governance arrangements and the HoIAS has experienced first-hand that due process has been applied.	Yes – specifically around governance role of the servicing authority
Fleet management	The fleet is managed effectively and efficiently (loading, routing, maintenance etc).	Full scale logistics review was prioritised over the audit.	Potential that once the fleet has been re-organised there could be scope to confirm operating as planned
Supply chain	ESPO identifies, evaluates and monitors its supply chains to ensure integrity and sustainability	Scope agreed with Assistant Director but start deferred at ESPO's request due to an operational priority	Yes



ESPO FINANCE AND AUDIT SUBCOMMITTEE – 10 JUNE 2014

INTERNAL AUDIT SERVICE – ANNUAL REPORT 2013-14

REPORT OF THE CONSORTIUM TREASURER

Purpose of Report

1. To provide the Subcommittee with an annual report on internal audit work conducted during 2013-14.

Background

2. The Consortium Treasurer (the Treasurer) is responsible for the proper administration of ESPO's financial affairs and has a specific responsibility for arranging a continuous internal audit of those affairs.
3. The Treasurer arranges for Leicestershire County Council's Internal Audit Service (LCCIAS) to provide internal audit for ESPO. LCCIAS must conform to internal audit professional standards. From April 2013 these are the Public Sector Internal Audit Standards (the PSIAS).
4. The PSIAS require the Head of Internal Audit Service (HoIAS) to provide an annual report to 'the Board' timed to support the annual governance statement. The PSIAS allow for a number of groups to satisfy the role of the Board but the standards define the Board as, 'The highest level of governing body charged with the responsibility to direct and/or oversee the activities and management of the organisation', and as such it is considered appropriate that the Management Committee approves the annual HoIAS report.
5. This report precedes the Annual Governance Statement which will be presented to the Management Committee at its meeting in September alongside the Statement of Accounts. The Statement of Accounts, accompanied by the Annual Governance Statement, will be presented to the Subcommittee at its next meeting prior to final consideration by the Management Committee.

Annual Internal Audit Service Report

6. The annual report for 2013-14 is provided in Appendix 1.
7. The HoIAS report must include an annual internal audit opinion on the overall adequacy and effectiveness of the organisation's

governance, risk and control framework (i.e. the control environment) and a summary of the audit work from which the opinion is derived (including reliance placed on work by other assurance bodies). The full HoIAS opinion and the PSIAS definition of the control environment is included at appendix 2.

8. For 2013-14, whilst recognising further improvements are required, positive opinions were given in all three areas of the framework of governance, risk management and control.

Resources Implications

9. The budget for the provision of the internal audit service is contained within ESPO' Medium Term Financial Strategy under charges by the Servicing Authority.
10. Only 175 of the planned 200 days were provided. Explanations have been given in paragraph 12 of the Internal Audit Service Quarterly Progress Report (elsewhere on the agenda for this meeting). The effect was to reduce the charge to ESPO to £49,000.

Recommendation

11. That the Subcommittee notes the Internal Audit Service annual report for 2013-14.

Equal Opportunities Implications

12. There are no specific equal opportunities implications contained within the annual summary of work undertaken.

Background Papers

Accounts and Audit Regulations (Amendment) 2011

The Public Sector Internal Audit Standards (2013)

Officer to Contact

Neil Jones	Telephone	0116 305 7629
Head of Internal Audit Service	Email	Neil.Jones@leics.gov.uk

Appendices

- Appendix 1 - Internal Audit Service Annual Report 2013-14
- Appendix 2 - The HoIAS Annual Opinion on the adequacy and effectiveness of the control environment and PSIAS definition of the control environment.

ESPO

Leicestershire County Council Internal Audit Service Annual Report 2013-14



**Neil Jones CPFA, Head of Internal Audit Service,
Leicestershire County Council**

27 May 2014

30
LEICESTERSHIRE COUNTY COUNCIL
INTERNAL AUDIT SERVICE
ANNUAL REPORT 2013-14

Overall Opinion

The Public Sector Internal Audit Standards 2013 (the PSIAS) require the Head of Internal Audit Service (HoIAS) to give an annual opinion on the overall adequacy and effectiveness of ESPO's control environment i.e. its framework of governance, risk management and control. No system of internal control can provide absolute assurance against material misstatement or loss, nor can Leicestershire County Council Internal Audit Service (LCCIAS) give absolute assurance, especially given limited resource. The work of LCCIAS is intended only to provide reasonable assurance on controls on the basis of the work undertaken.

Based on an objective assessment of the results of individual audits undertaken, actions by management thereafter, and the professional judgement of the HoIAS in evaluating other related activities, the following opinions have been drawn:-

Governance: -

Nothing of such significance, adverse nature or character has come to the HoIAS attention, and as such reasonable assurance is given that ESPO's governance arrangements are robust.

Risk management: -

ESPO has acknowledged there is scope to continue improving its risk management framework. Additionally, management has agreed to implement all internal audit recommendations which further mitigate risk, therefore reasonable assurance is given that risk is managed.

Internal financial and ICT controls: -

Reasonable assurance can be given that the operation and management of the core financial systems of ESPO are of a sufficient standard to provide for the proper administration of its financial affairs.

Full details of the HoIAS opinion for 2013-14 are found in Appendix 2

A summary of the work undertaken by Leicestershire County Council Internal Audit Service (LCCIAS) during 2013-14 is detailed below.

31 Audit Requirement

Consortium Treasurer responsible for arranging continuous audit

ESPO's Consortium Agreement schedule 3 'Functions of the Servicing Authority', directs that the Servicing Authority (Leicestershire County Council) shall be responsible for arranging the provision of support services (including internal audit).

ESPO's Financial Regulations (including the Standard Financial Instructions) further provide that the Consortium Treasurer (the Treasurer) is responsible for the proper administration of ESPO's financial affairs. Rule 15 imposes a specific responsibility for arranging a continuous internal audit is delegated to the Treasurer.

Background

Leicestershire CC internal auditors carry out the work

The Consortium Treasurer arranges for Leicestershire County Council's Internal Audit Service (LCCIAS) led by the Head of Internal Audit Service (HoIAS), to provide internal audit for ESPO. LCCIAS has adopted the principles of the Public Sector Internal Audit Standards 2013 (the PSIAS). LCCIAS works closely with the external auditor PricewaterhouseCoopers (PwC) so as to minimise duplication.

Giving assurance on ESPO's control environment

The PSIAS mandate that the HoIAS must provide an annual report to 'the Board' (Management Committee) timed to support the annual governance statement. The report must include an annual internal audit opinion on the overall adequacy and effectiveness of the organisation's governance, risk and control framework (i.e. the control environment) and a summary of the audit work from which the opinion is derived (including reliance placed on work by other assurance bodies). The PSIAS definitions of control and the control environment are found in Appendix 2.

Responsibility in respect of the control environment

It is the Director of ESPO's (the Director) responsibility to design, install and operate adequate arrangements for governance, risk management and control within appropriate constitutional frameworks; and to identify, assess and manage risks that are significant to the achievement of ESPO's objectives.

The Internal Audit Service's task is to carry out independent and objective 'assurance' type audits of the adequacy and effectiveness of these controls and, if necessary, highlight weaknesses and recommend improvements 'Consulting' type audits add value by allowing the auditor to give early commentary on management's design of controls in say a new system or process.

How Internal Audit

Much internal audit work can be planned. To this end

Service plans its work	<p>an annual plan is produced, detailing the main areas of proposed work. The plan for 2013-14 was produced from a combination of: -</p> <ul style="list-style-type: none"> • Consultation about emerging risks, planned changes and potential problems with the Director, Assistant Director (Finance), the Consortium Treasurer and Secretary, and the External Auditor • Evaluation of governance arrangements e.g. plans, committee reports, accounts, risk register and governance statements • Comparisons against risks affecting similar purchasing consortia • 'Horizon scanning' new and emerging risks from professional and industry sources. <p>A steady improvement in ESPO risk management and governance arrangements and the Director's recognition of responsibilities for internal control systems, allowed the HoIAS to utilise the information above, to devise the plan.</p>
“Joint audit” work with PwC	<p>Part of the plan requires that LCCIAS conducts annual audits on key elements of the general ledger and IT systems. These audits are undertaken in consultation with ESPO's External Auditors (PWC) to assist in their responsibility to form an opinion that ESPO's financial accounts are not materially mis-stated. PWC determines that the quality and scope of LCCIAS work is sufficient to contribute positively to ESPO's overall control environment and to allow them to place reliance on LCCIAS work.</p>
Risk based auditing	<p>LCCIAS uses a number of techniques to reach its opinions on what level of assurance can be provided that risks are being identified, evaluated and managed. Much work will be based around a “risk based” audit. With this technique key risks (based on likelihood and impact) are identified and agreed at the start of the audit. The quality of controls to mitigate these risks is then tested</p>

High importance (HI) recommendations

Following audit testing, where risk levels are considered still to be significant, (in line with ESPO's own risk scoring methodology), then recommendations are designated as High Importance (HI). Action taken to implement the recommendation is always re-tested by LCCIAS.

No new HI recommendations were made in relation to 2013-14 audits, HI recommendations carried forward from prior year audits on business continuity and rebates processes, were confirmed as implemented during 2013-14.

ESPO member involvement

The Finance & Audit Subcommittee receives audit reports i.e. annual plan, quarterly progress against the plan (including progress against implementing HI recommendations), annual report (including the HoIAS opinion) and the review of effectiveness of the system of internal audit.

Management Committee receives the annual report and shall be responsible for approving the Internal Audit Charter for ESPO as part of PSIAS.

Summary of Work**Audits undertaken in 2012-13**

Annual Governance Statement

Work undertaken during the year is listed below

The audit evaluated the arrangements to demonstrate compliance to the principles of good governance outlined in the CIPFA/SOLACE Framework. The work formed part of the HoIAS annual opinion on the adequacy and effectiveness of the internal control environment, concluding that overall, there has been a substantial strengthening of ESPO's governance arrangements and the general direction of travel for future governance arrangements is positive.

Performance Management

The audit evaluated how the performance management framework had been designed and implemented and how responsibilities had been allocated. Some recommendations around further aligning performance management against the ESPO four year business strategy, and further development and implementation of some agreed target measures.

Medium Term Financial Strategy

An audit of the processes for validating assumptions, monitoring achievements and reporting progress against efficiency projects. Recommended improvements to the framework for managing and monitoring projects contained within the Continuous Improvement Plan and reporting progress against the Plan to Finance and Audit Subcommittee

Risk Management

Whilst there was evidence that some risk

management activities were operating adequately, there was further scope to improve effective embedded risk management into operational activity.

Business forecasting	<p>There are adequate controls in place to ensure that forecasts and annual budgets are approved correctly and are reviewed on an annual basis. Responsibilities are clearly assigned and timescales agreed for preparation of the annual budget. Information used in the annual budget process is accurate and budget holders are consulted.</p> <p>Minor recommendations around reporting key assumptions and improving budget working papers to include reasons for any significant changes, and clearly identifying when savings are as a result of specific projects within the Efficiencies Programme.</p>
Fleet management – Vehicle Operating Licence	<p>Evaluation of controls and testing confirmed that ESPO is compliant with the Vehicle Operating Licence ‘General Conditions and Undertakings’</p>
Trading performance & distribution of surplus	<p>There is an adequate audit trail from the Combined Preliminary reports presented to the Senior Management Team (SMT) for February 2014 back to the General Ledger.</p> <p>A framework for the calculation and distribution of dividends payable to members exists. Verification of the dividends distributed will be subject to a short audit in the 2014/15 financial year.</p>
Payroll changes	<p>Variations to pay are adequately supported by appropriately authorised documentation and changes have been made in accordance with instructions.</p> <p>Recommended that ESPO investigates delays by East Midlands Shared Services in issuing contracts and ESPO management is reminded on procedures in relation to new starters and the use of e-notification forms</p>
General ledger reconciliation	<p>This audit is required by the External Auditor in their annual assessment of the likelihood of material misstatement in the Authority’s financial accounts.</p> <p>Concluded that accounting procedures are being applied to ensure the completeness and accuracy of the General Ledger.</p>

Attendance management	Recommended ESPO develop absence performance metrics now that there is meaningful data also recommended to ensure consistent application of the Attendance Management Policy by managers and a more efficient method of informing payroll of absences
Budget management	The budget management framework was evaluated. Whilst the budget position is reported accurately to SMT regularly and discussed and there have been some delegations to Assistant Directors, the audit recommended that processes could be improved by introducing a longer timeframe for reviewing budgets, producing forecasts and the introduction of commitments.
Servicing Authority	The draft SLA and processes were evaluated. Recommendations around including responsibilities and naming of key officers, clarifying the basis of charges both proposed and invoiced and monitoring and reporting service provision
Anti-fraud and corruption	The scope contained a review of policies and procedures, awareness and training. Minor recommendations are reliant on developments at the Servicing Authority
IT General controls	The External Auditor relies on this audit in their annual assessment of the likelihood of material misstatement in the Authority's financial accounts. Assurance is partly obtained through review of the integrity of the ICT infrastructure and associated applications that either directly or indirectly contributes to the production of the financial statements. Substantial assurance that the ICT infrastructure is robust and that the range of controls expected by the External Auditor are well designed and consistently applied.
Stock management	Evaluation of controls designed to ensure optimum stock management and warehouse operations. A few recommendations about performance indicators and mitigating risks to the optimisation model. The External Auditor may choose to place reliance on this audit.
Rebates income	Annual audit to validate that ESPO has received rebate in line with what was expected based on suppliers' turnover. Some disparity was found and although values are not material, ESPO will have scope to follow up with suppliers.

Unplanned work

Three small pieces of work were undertaken – validating the accuracy of records migrated to the new gas contract; reporting a minor whistleblowing investigation and guidance on expense claims.

Person to Contact about this Report

Neil Jones CPFA Head of Internal Audit Service
LCCIAS

neil.jones@leics.gov.uk
0116-305-7629

**The Head of Internal Audit Service's Annual Opinion
on the overall adequacy and effectiveness
of ESPO's control environment
2013-14**



**Neil Jones CPFA, Head of Internal Audit Service,
Leicestershire County Council**

27th May 2014

To the Consortium Treasurer

Background

During the financial year 2013-14, Leicestershire County Council Internal Audit Service (LCCIAS) provided internal audit to the Eastern Shires Purchasing Organisation (ESPO). LCCIAS adopts the principles of the Public Sector Internal Audit Standards 2013 (the PSIAS) which requires the Head of Internal Audit Service (HoIAS) to give an annual opinion on the overall adequacy and effectiveness of ESPO's control environment i.e. its framework of governance, risk management and control. The PSIAS definition of the control environment is to be found at the end of this document.

The HoIAS annual opinion is for a specific time interval i.e. 2013-14 and combines: -

- an objective assessment, based on the results of individual audits undertaken and actions taken by management thereafter. Individual audit opinions on what level of assurance can be given as to whether risk is being identified and adequately managed, are formed by applying systematic grading to remove any elements of subjectivity.
- the professional judgement of the HoIAS based on his evaluation of other related activities.

The results of the above, when combined, form the basis for the overall opinion on the adequacy of the ESPO control environment. No system of internal control can provide absolute assurance against material misstatement or loss, nor can LCCIAS give absolute assurance, especially given limited resource. The work of LCCIAS is intended only to provide reasonable assurance on controls on the basis of the work undertaken.

Governance related internal audit work

An opinion on whether good governance principles have been applied is based on the results of audits of AGS; elements of key ICT controls; fraud management; budget management; MTFS; attendance management; risk management and the role of the servicing authority. Recommendations were relatively minor and where they related to governance, it was to strengthen it, i.e. not to have to establish it.

The HoIAS attends Finance and Audit Subcommittee and appropriate Management Committee meetings to present audit plans and reports, which enables him to gauge ESPO Member governance at first hand. The HoIAS has regular discussions with the ESPO Director and Assistant Director (Finance), the Consortium Treasurer (and where required the Consortium Secretary) on governance issues and related aspects of audits.

HolIAS opinion: - Nothing of such significance, adverse nature or character has come to the HolIAS attention, and as such reasonable assurance is given that ESPO's governance arrangements are robust.

Risk management related internal audit work

The majority of audits planned and conducted were 'risk based' i.e. ensuring that ESPO management identifies, evaluates and manages risk to achieving its objectives i.e. ensuring controls are in place to reduce risk exposure. A specific audit of the ESPO risk management framework (corporate risk register) proved there were further improvements and good elements of risk management, although further embedding at operational level would strengthen arrangements. Recommendations have been implemented and a further follow up audit will take place before the end of the 2014-15 financial year to evaluate progress.

The HoIAS provides the External Auditor with an opinion on ESPO management of fraud risk. This was followed up with the specific audit of counter fraud arrangements with some minor recommendations.

A previous year's High Importance recommendation relating to business continuity was tested and confirmed as implemented.

HoIAS opinion: ESPO has acknowledged there is scope to continue improving its risk management framework. Additionally, management has agreed to implement all internal audit recommendations which further mitigate risk, therefore reasonable assurance is given that risk is managed.

Financial (and ICT) Controls related internal audit work

A number of financial system audits were undertaken on ESPO's general ledger activities and other operational financial systems including payroll and stock management.

No findings were of such seriousness as to suggest a fundamental weakness in a main financial system.

Previous year's High Importance recommendations relating to rebates income processes were tested and confirmed as implemented.

HoIAS opinion: Reasonable assurance can be given that the operation and management of the core financial systems of ESPO are of a sufficient standard to provide for the proper administration of its financial affairs.

Dated 27th May 2014

Signed Neil Jones CPFA
Head of Internal Audit Service
Leicestershire County Council

The control environment

The Public Sector Internal Audit Standards 2013 (the PSIAS) contain the following definitions: -

Control

Any action taken by management, the board and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved. Management plans, organises and directs the performance of sufficient actions to provide reasonable assurance that objectives and goals will be achieved.

Control Environment

The attitude and actions of the board and management, regarding the importance of control within the organisation. The control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal control. The control environment includes the following elements: -

- Integrity and ethical values.
- Management's philosophy and operating style.
- Organisational structure.
- Assignment of authority and responsibility.
- Human resource policies and practices.
- Competence of personnel.



ESPO FINANCE AND AUDIT SUBCOMMITTEE – 10 JUNE 2014

ANNUAL INTERNAL AUDIT PLAN 2014-15

REPORT OF THE CONSORTIUM TREASURER

Purpose of Report

1. The purpose of this report is to provide information on the work undertaken to create the annual internal audit plan 2014-15.

Background

2. The Consortium Treasurer (the Treasurer) is responsible for the proper administration of ESPO's financial affairs and has a specific responsibility for arranging a continuous internal audit of these affairs.
3. The Treasurer arranges for Leicestershire County Council's Internal Audit Service (LCCIAS) to provide internal audit for ESPO. LCCIAS must conform to the Public Sector Internal Audit Standards 2013 (the PSIAS).
4. The PSIAS require the Head of Internal Audit (at LCCIAS this is the Head of Internal Audit Service – HoIAS) to give an annual opinion on the overall adequacy and effectiveness of the organisation's control environment, which the PSIAS further explain is the organisation's framework of governance, risk management and control. In order to do this, the scope of internal audit work needs to be wide. The PSIAS require the HoIAS to prepare a risk based internal audit plan to determine the priorities of the internal audit activity, consistent with the organisation's goals.

Terms of Reference

5. Part of the role of the Finance & Audit Subcommittee (the Subcommittee) is to review audit reports. The Subcommittee should receive and note the annual internal audit plan; regular progress reports against the plan; an annual report on work undertaken and an assessment of the internal audit service effectiveness.

Planning methodology

6. The HoIAS takes into account ESPO's risk management framework, including using risk appetite levels set by management. The annual plan reflects changes in ESPO's business, risks, operations, programs, systems, and controls including other forms of assurance gained. An 'audit universe' (a list of entities to audit) exists along with a scoring/ranking system against those entities.

7. Given the pace across society of transformational change, new and emerging risk, organisational instability, continuing austerity and the need to make savings, new entities are added to the audit universe each year (and indeed throughout the year) whilst traditional entities remain on the list but their risk might reduce. To develop the universe the HoIAS researches and evaluates where risk might occur to ESPO using methods including: -
 - a. Consultation about emerging risks, planned changes and potential issues with the Director of ESPO (the Director) and his Senior Management Team, the Consortium Treasurer and Secretary and the External Auditor
 - b. Evaluation of governance arrangements e.g. plans, committee reports, accounts, risk register and governance statements
 - c. Identification and evaluation of the robustness of other forms of assurance received
 - d. Where possible comparisons against similar purchasing consortia audit plans
 - e. 'Horizon scanning' new and emerging risks from professional and industry sources.

7. Modern internal audit planning requires flexibility to ensure that key and emerging risks take precedence when balanced against available internal audit resource and budgets. A continuing improvement in ESPO risk management and governance arrangements and the Director of ESPO's recognition of his Senior Management Team's responsibilities for internal control systems, has allowed the HoIAS to utilise the methods in 7 (a-e) above, to devise the plan.

8. Of particular importance to internal audit planning is the detailed content of the Four Year Business Strategy that was reported by the Director to Management Committee on 6 March 2014. It is readily acknowledged there will be risks to the achievement of the Strategy's objectives that will need to be identified and evaluated by ESPO management and mitigated where required.

9. Throughout the four year lifecycle of the Strategy, as well as evaluating that progress and attainment of objectives is adequately governed, as new programmes and projects are planned to come on stream, LCCIAS has a role to: -
 - a. Review and advise on ESPO management's control/mitigation design, and strategies for testing robustness before systems/processes 'go live' (consulting type audit)
 - b. Once systems/processes are embedded, that the approved controls and mitigations are being applied as originally required (assurance type audit)
10. Part of the plan requires that LCCIAS conducts annual audits on key elements of the general ledger and IT systems. These audits are undertaken in consultation with ESPO's External Auditors (PWC) to assist in their responsibility to form an opinion that ESPO's financial accounts are not materially mis-stated. PWC determines that the quality and scope of LCCIAS work is sufficient to contribute positively to ESPO's overall control environment and to allow them to place reliance on LCCIAS work.

The internal audit plan 2014-15

11. The attached plan for 2014-15 (Appendix 1) contains a wide scope of audits that will allow the HoIAS to form an opinion on the overall adequacy and effectiveness of ESPO's framework of governance, risk management and control. The wide scope of LCCIAS' planned audits of ESPO is similar to that of another large scale purchasing consortium. Even though that organisation has not indicated the total days provided, its scope covers: -
 - a. Main Financial Systems – annual review and testing
 - b. New systems/initiatives being developed
 - c. Strategic risks & other risk based audits
 - d. Annual Governance Statement and Code of Corporate Governance
 - e. Anti-fraud and bribery arrangements/testing
 - f. Follow up on work undertaken and reported previously
 - g. Input to Committee function
 - h. Liaison, consultancy and advice
12. A small amount of resource has been planned to finalise 2013-14 audits. A number of audits not started in 2013-14 are deemed to be of sufficient importance to be included in 2014-15.
13. The first column indicates which part of the control environment the audit primarily matches (there is often overlap) and the third column is an attempt to match to ESPO's current Key Risk Register (again there is some overlap)
14. The indicative objective for each audit is included in the attached plan but the scope is discussed and agreed in detail at the

engagement stage. Indicative days have been assigned but these are subject to variation and change. The HoIAS would notify the Director and Consortium Treasurer where this is material.

Progressing the Audit Plan

15. Responsibility for the evaluation and management of risk and the design and consistent operation of internal controls rests with ESPO management. LCCIAS' role and responsibility is to carry out independent and objective audits and give an opinion on the extent to which risk is being managed and (where appropriate) make recommendations to improve controls.
16. On completion of each audit a report, findings will be discussed with the appropriate risk owner before issuing a report to the Director of ESPO and the Consortium Treasurer. The opinions reached, along with summary findings are reported each quarter to the Subcommittee. If any audit produces a 'high importance' recommendation, then the full report is shared with the Subcommittee, and specific re-testing is undertaken later in the year to prove that control has actually improved and is embedded.

Resources Implications

17. The budget for the provision of the internal audit service is contained within ESPO's Medium Term Financial Strategy under charges by the Servicing Authority. Plan days for 2013-14 have been reduced by 15 to 185 to reflect that constitutional change and governance arrangements are more embedded, there is a stable and complete Senior Management Team and risk management continues to improve. However, there is still significant change planned within the organisation not least with the need for new operational systems and the risks that apply to implementing the four year business strategy.
18. The 185 days (indicative cost £52,000) should enable the HoIAS to provide reasonable assurance to the Consortium Treasurer that risks are being managed.

Conclusion

19. The details of the 2014-15 internal audit plan, including a summary of the days allocated, is attached in Appendix 1 to this report. The plan has been presented to the Consortium Treasurer, Consortium Secretary and the Director of ESPO for comments and approval.

Recommendation

20. The Subcommittee is requested to:
- a) Support the methodology used as a basis for developing the internal audit plan;
 - b) Note the ESPO Internal Audit Plan for 2014-15.

Equal Opportunities Implications

21. At this stage there are no known direct implications resulting from the internal audit plan strategy, although 'human resource' elements will be audited.

Background Papers

None.

Officer to Contact

Neil Jones, Head of Internal Audit Service
Tel: 0116-305-7629
Email: neil.jones@leics.gov.uk

Appendices

Appendix 1 - Internal Audit Plan 2014-15

This page is intentionally left blank

ESPO Internal Audit Plan 2014-15**Appendix 1**

<u>Category</u>	<u>Entity</u>	<u>KRR</u>	<u>The indicative audit objective is to ensure that...</u>	<u>Days</u>
Various	Incomplete from 2013-14	Var	Key IT controls; Anti-Fraud & Corruption; Rebates income; Servicing Authority; Energy	10
Governance	Budget management	8&20	There is a sound framework for the control of the budget	4
Governance	ESPO services	8	The key principles to providing the individual categories within the ESPO service menu are complied with	7
Governance	Business Strategy	2&25	Attainment of the objectives of the Strategy is well governed	5
Governance	Governance framework	8	The requirements of the Consortium Agreement, Constitution and appropriate schedules are embedded - to include role of Servicing Authority	7
Governance	Risk management	8	The revised policy and framework is operating as intended. Lines of defence are understood and complied with.	3
Governance	Annual governance statement	8	There are adequate arrangements to demonstrate compliance to the principles of good governance outlined in the CIPFA/SOLACE Framework.	5
Governance	Information management	8	Information is secure both on and off site and in transit and breaches are identified and investigated	5

ESPO Internal Audit Plan 2014-15

Appendix 1

<u>Category</u>	<u>Entity</u>	<u>KRR</u>	<u>The indicative audit objective is to ensure that...</u>	<u>Days</u>
Risk management	Counter fraud	20	There is no pattern of fraud in large data sets - use of data matching tool	6
Risk management	GEMS replacement	1&36	The replacement energy system is well planned, risk managed and governed throughout	10
Risk management	Applications management	1&30	Risks (e.g. continuity and resilience) to the successful operation of key business management systems within ESPO have been identified and appropriately mitigated.	8
Risk management	Business Strategy	25	Control design (of specific project(s)) is adequate to mitigate risk	10
Risk management	Supply chain	12	ESPO identifies, evaluates and monitors its supply chains to ensure integrity and sustainability	8
Risk management	Procurement & Compliance risk management	26,32&35	The framework is sufficiently robust to prove effectiveness and avoid liability	10
				48

ESPO Internal Audit Plan 2014-15

Appendix 1

<u>Category</u>	<u>Entity</u>	<u>KRR</u>	<u>The indicative audit objective is to ensure that...</u>	<u>Days</u>
Internal control	Rebates income	27	Annual audit to evaluate whether rebates received conform to estimates of supplier business generated	5
Internal control	General ledger reconciliations (*)	8&20	Reconciliations are undertaken to facilitate the accuracy and completeness of the general ledger. Usual coverage of cash & treasury; receivables; payables; payroll and stock	10
Internal control	Trading performance & distribution of surplus (*)	4	The trading results provided by ESPO, both for internal use and reported to the Management Committee, are well founded in the general ledger and the distribution of surpluses process is robust.	10
Internal control	Servicing authority	8	The servicing authority is providing service in line with the agreement	6
Internal control	Electronic transactions	20	P-card and other electronic transaction methods are PCI compliant	5
Internal control	IT general controls (*)	1	The range of controls expected by the External Auditor are well designed and consistently applied.	10
Internal control	Stock management	2,28&34	Stock levels are optimised & an effective warehouse management system is operated	8
Internal control	Fleet management	2&34	The outcomes from the logistics review are embedded so that fleet is managed effectively and efficiently	8
Internal control	E-tendering	32&35	ESPO complies with its role in e-tendering arrangements	5
	Client management		Planning & research; progress meetings; servicing Committees; confirming implementation of high importance internal audit recommendations External Audit liaison; advice	20
Total days (note days are indicative & subject to change)				185

(*) Annual audits undertaken to assist the External Auditors to form an opinion that ESPO's financial accounts are not materially mis-stated

This page is intentionally left blank

Document is Restricted

This page is intentionally left blank

By virtue of paragraph(s) 3, 10 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Document is Restricted

This page is intentionally left blank