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# *Eastern Shires Purchasing Organisation*

External Audit Plan 2015/16

February 2016



Members of the Management Committee  
Eastern Shires Purchasing Organisation  
Barnsdale Way  
Grove Park  
Enderby  
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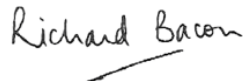
Ladies and Gentlemen,

We are pleased to present our Audit Plan, which shows how your key risks and issues drive our audit and summarises how we will deliver. We look forward to discussing it with you so that we can ensure we provide the highest level of service quality.

We would like to thank Members and Officers of the Organisation for their help in putting together this Plan.

If you would like to discuss any aspect of our Audit Plan please do not hesitate to contact Richard Bacon or Steve Hallam.

Yours faithfully,

A handwritten signature in black ink that reads "Richard Bacon". The signature is written in a cursive style and is underlined with a single horizontal stroke.

PricewaterhouseCoopers LLP

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# Introduction

## *The purpose of this plan*

This plan:

- is required by International Standards on Auditing (ISAs);
- sets out our responsibilities as external auditor under the terms of our engagement letter signed on 14<sup>th</sup> December 2015;
- gives you the opportunity to comment on our proposed audit approach and scope for the 2015/16 audit;
- records our assessment of audit risks, including fraud, and how we intend to respond to them;
- tells you about our team; and
- provides an estimate of our fees.

We ask the Management Committee to:

- consider our proposed scope and confirm that you are comfortable with the audit risks and approach;
- consider and respond to the matters relating to fraud; and
- approve our proposed audit fees for the year.

## *Our work in 2015/16*

We will:

- undertake a non-statutory audit of the accounts, assessing whether they provide a true and fair view;
- check compliance with International Financial Reporting Standards (IFRS);
- see whether the other information in the accounts is consistent with the financial statements;
- tell you promptly when we find anything significant during the audit, directly to management and as soon as practicable to the Management Committee throughout the year.

## **Risk assessment**

We considered the Organisation's operations and assessed:

- business and audit risks that need to be addressed by our audit;
- how your control procedures mitigate these risks; and
- the extent of our work on the financial statements as a result.

Our risk assessment shows:

- those risks which are significant, and which therefore require special audit attention under auditing standards; and
- our response to significant and other risks, including reliance on internal and other auditors, and review agencies.

## **Responsibilities**

*It is your responsibility to identify and address your operational and financial risks, and to develop and implement proper arrangements to manage them, including adequate and effective systems of internal control. In planning our audit work, we assess the significant operational and financial risks that are relevant to our responsibilities under the terms of our engagement letter. This exercise is only performed to the extent required to prepare our plan so that it properly tailors the nature and conduct of audit work to your circumstances. It is not designed to identify all risks affecting your operations nor all internal control weaknesses.*

# Risk Assessment

## Risk Assessment Results

Eastern Shires Purchasing Organisation continues to face a period of financial change. Your customers face extremely challenging spending cuts and changes in policy which you must adapt to as an Organisation. We have undertaken an audit risk assessment which guides our audit activities. It allows us to determine where our audit effort should be focused and whether we can place reliance on the effective operation of your controls. Risks to the accounts and our true and fair audit opinion are categorised as follows:

|   |             |                                                                                                                                                                    |
|---|-------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| ● | Significant | Risk of material misstatement in the accounts due to the likelihood, nature and magnitude of the balance or transaction. These require specific focus in the year. |
| ● | Other       | We perform standard audit procedures to address other risks in any material financial statement line items.                                                        |

Auditing Standards require us to include two fraud risks as Significant:

- Management override of controls:

*“Management is in a unique position to perpetrate fraud because of management’s ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk.”* ISA 240 paragraph 31; and

- Income recognition:

*“When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks.”* ISA 240 paragraph 26.

This is extended to include expenditure recognition in public sector bodies.

Both are included in our risk assessment.

## Summary of audit risks

A summary of the audit risks identified for 2015/16 is set out below, with further information provided on the following pages.

| <i>Risk arising</i>                | <i>Potential impact upon PwC work</i> | <i>Categorisation for accounts risks</i> |
|------------------------------------|---------------------------------------|------------------------------------------|
|                                    | <i>Accounts true and fair opinion</i> |                                          |
| Management override of controls    | ◆                                     | ● Significant                            |
| Income and expenditure recognition | ◆                                     | ● Significant                            |

| <b>Risks</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             | <b>Risk Level</b> | <b>Audit approach</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><b>Management Override of Controls</b></p> <p>In any organisation, management may be in a position to override the financial controls that are in place. A control breach of this nature may result in a material misstatement. For all of our audits, we are required to consider this as a significant risk and adapt our audit procedures accordingly.</p> <p>In your organisation, as the pressure to deliver challenging performance targets increases to meet your Medium Term Financial Strategy, so does the risk of management override.</p> | ●                 | <p>We will review your internal control structure.</p> <p>In particular we will focus our work on testing of journals. This will provide you with assurance over the level of manual and automated journals.</p> <p>We will perform targeted testing over significant estimates within the financial statements.</p> <p>We will carry out unpredictable procedures – this will involve performing ad hoc testing that has not previously been performed over one or more controls or financial statement balances.</p> |
| <p><b>Revenue and Expenditure Recognition</b></p> <p>There is a risk that the Organisation could adopt accounting policies or treat income and expenditure transactions in such a way as to lead to material misstatement in the</p>                                                                                                                                                                                                                                                                                                                     | ●                 | <p>We will:</p> <ul style="list-style-type: none"> <li>• review the design and operating effectiveness of key income and expenditure controls;</li> <li>• evaluate the accounting policies for income and expenditure recognition;</li> <li>• test the appropriateness of journal entries and other adjustments;</li> <li>• review accounting estimates for income and expenditure, for example, rebates and provisions</li> </ul>                                                                                     |



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reported revenue and expenditure position.

Our audit last year resulted in a change to your accounting policies in relation to recognition of rebate income. It was recommended that an addition to the accounting policy was made, which stated: *“Rebates are recognised where they can be reliably measured and agreed with the supplier and are retrospective. Cash is accounted for in the period it is received.”*

Pressures to meet performance targets has placed increased reliance on rebate income as a revenue stream for ESPO. This increases the risk of manipulation of recognition of rebate income.

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- analyse trends in relation to income and expenditure during the year and seek to understand any unusual variations; and
- reconcile your management information to the information presented in the accounts on a gross basis.
- undertake testing procedures to ensure rebate income is recognised in line with the accounting policy and within the correct period to which it relates.

# ***Audit approach***

## ***Audit requirements***

Your statutory obligation to have an audit of your financial statements in accordance with the Audit Commission's Code of Audit Practice ended in the year to 31<sup>st</sup> March 2015. You informed us in September 2015 that you wish to continue to undertake a non-statutory audit of your financial statements for the year ended 31<sup>st</sup> March 2016. You have also elected to continue to prepare your financial statements under CIPFA guidance despite no longer having a statutory obligation to do so. We will therefore now conduct our audit in line with International Standards on Auditing (UK and Ireland) as outlined below and in our engagement letter dated 14<sup>th</sup> December 2015.

## ***Code of Audit Practice***

We will conduct our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK&I)") issued by the Auditing Practices Board ("APB") and ethical requirements.

## ***Accounts***

We plan and perform our audit to be able to provide reasonable assurance that the financial statements are free from material misstatement and give a true and fair view. We use professional judgement to assess what is material. This includes consideration of the amount and nature of transactions.

During the course of our audit work it is not unusual to find relatively small misstatements which do not raise significant concerns for those charged with governance. ISA (UK&I) 450 (revised) requires that we record all misstatements identified except those which are "clearly trivial". Matters which are clearly trivial are matters which we expect not to have a material effect on the financial statements even if accumulated. When there is any uncertainty about whether one or more items are clearly trivial, the matter is considered not to be clearly trivial.

## ***Materiality***

The ISA suggests a benchmark of 5 percent of our audit materiality level, which would suggest a 'clearly trivial' level of approximately £94,000 based on the 2014/15 audit. In the previous year, we agreed with you that we would report errors detected over this threshold, we intend to continue using this 5% benchmark for the 2015/16 audit. We therefore propose to discuss these smaller misstatements with management, but apply a threshold to the value of individual misstatements that we report to those charged with governance to be discussed and agreed with you.

## ***Audit Risks***

Our audit approach is based on a thorough understanding of your business and is risk-driven. It first identifies and then concentrates resources on areas of higher risk and issues of concern to you. This involves breaking down the accounts into components. We assess the risk characteristics of each component to determine the audit work required. In your organisation, as the pressure to deliver challenging performance targets increases to meet your Medium Term Financial Strategy, we have identified areas of the accounts which we deem to be of higher risk and concern to you. These are outlined on page 8.

We plan our work to have a reasonable expectation of detecting fraud where the potential effects would be material to the financial statements of the Organisation. Based on the level of management's control procedures, we consider whether there are any significant risks of fraud that may have a material impact on the financial statements and adapt our audit procedures accordingly. We also consider the risk of fraud due to management override of controls and design our audit procedures to respond to this risk.

Our audit approach is based on understanding and evaluating your internal control environment and where appropriate validating these controls, if we wish to place reliance on them. This work is supplemented with

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substantive audit procedures, which include detailed testing of transactions and balances and suitable analytical procedures.

### ***Internal Audit***

We also aim to rely on the work done by internal audit wherever this is appropriate. We will ensure that a continuous dialogue is maintained with internal audit throughout the year. We receive copies of all relevant internal audit reports, allowing us to understand the impact of their findings on our planned audit approach.

We plan to rely on the work of internal audit for key controls in the following areas:

- Bank reconciliation;
- Income (control accounts; material feeder systems);
- Payables (control accounts; material feeder systems);
- General Ledger;
- Stock check;
- Payroll; and
- IT General Controls.

# Risk of fraud

International Standards on Auditing (UK&I) state that we as auditors are responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. The respective responsibilities of auditors, management and those charged with governance are summarised below:

## Auditors’ responsibility

Our objectives are:

- to identify and assess the risks of material misstatement of the financial statements due to fraud;
- to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and
- to respond appropriately to fraud or suspected fraud identified during the audit.

## Management’s responsibility

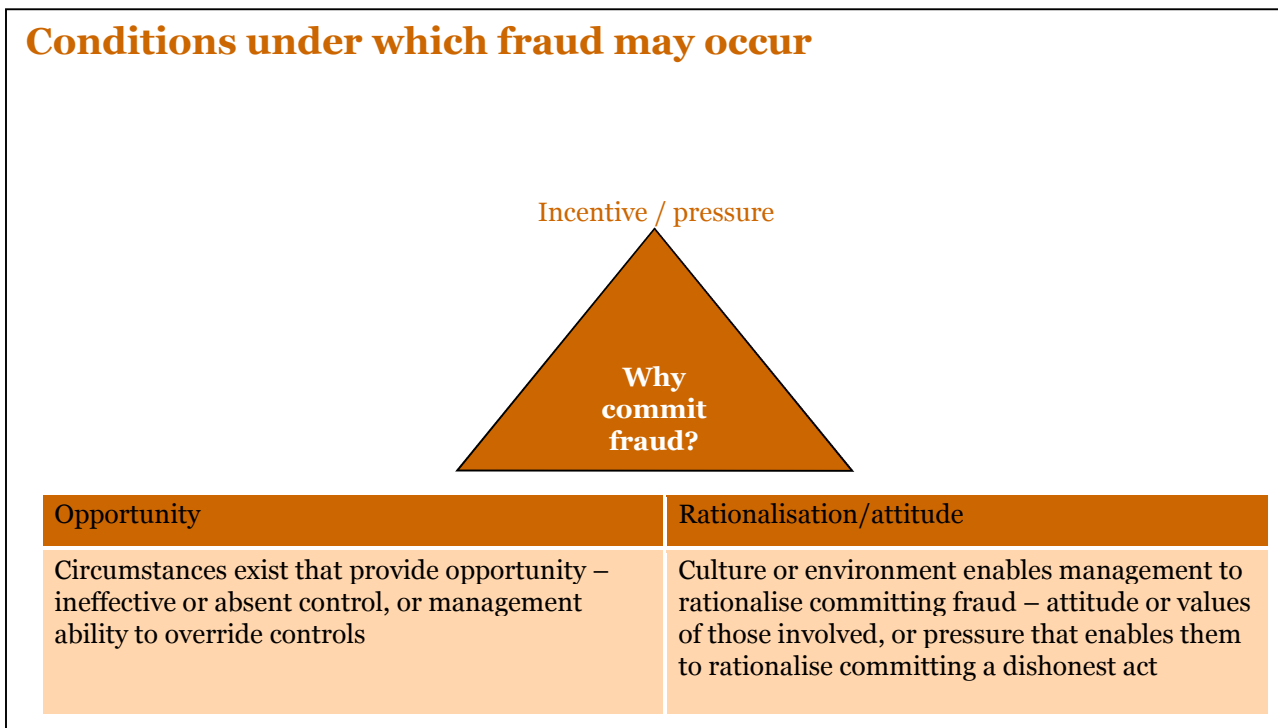
Management’s responsibilities in relation to fraud are:

- to design and implement programmes and controls to prevent, deter and detect fraud;
- to ensure that the entity’s culture and environment promote ethical behaviour; and
- to perform a risk assessment that specifically includes the risk of fraud addressing incentives and pressures, opportunities, and attitudes and rationalisation.

## Responsibility of the corporate governance committee

Your responsibility as part of your governance role is:

- to evaluate management’s identification of fraud risk, implementation of anti-fraud measures and creation of an appropriate “tone at the top”; and
- to investigate any alleged or suspected instances of fraud brought to your attention.



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## Your views on fraud

We enquire of the Management Committee:

- Whether you have knowledge of fraud, either actual, suspected or alleged, including those involving management?
- What fraud detection or prevention measures (e.g. whistleblower lines) are in place in the entity?
- What role you have in relation to fraud?
- What protocols / procedures have been established between those charged with governance and management to keep you informed of instances of fraud, either actual, suspected or alleged?

# *Our team and independence*

Your audit team has been drawn from our government and public sector team based in the Midlands. Your audit team consists of the key members listed below, but is further supported by our specialists both in the sector, and across other services:

| <b>Audit Team</b>                                                                                                                                                                 | <b>Responsibilities</b>                                                                                                                                                                                                                                                                                                                |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><b>Engagement Partner</b><br/> <b>Richard Bacon</b><br/>           5<sup>th</sup> year on the audit<br/>           0121 232 2598<br/>           richard.f.bacon@uk.pwc.com</p> | <p>Engagement Leader responsible for independently delivering the audit in line with the Code of Audit Practice, including agreeing the Audit Plan, ISA (UK&amp;I) 260 report and Annual Audit Letter, the quality of outputs and signing of opinions and conclusions. Also responsible for liaison with the Director and Members.</p> |
| <p><b>Engagement Manager</b><br/> <b>Steve Hallam</b><br/>           3<sup>rd</sup> year on the audit<br/>           07808 799145<br/>           stephen.j.hallam@uk.pwc.com</p>  | <p>Steve is the manager on the assignment responsible for overall control of the audit engagement, ensuring delivery to timetable, delivery and management of targeted work and overall review of audit outputs. Completion of the Audit Plan, ISA (UK&amp;I) 260 report and Annual Audit Letter.</p>                                  |

## *Our team members*

It is our intention that, wherever possible, staff work on the ESPO audit each year, developing effective relationships and an in depth understanding of your business. We are committed to properly controlling succession within the core team, providing and preserving continuity of team members.

We will hold periodic client service meetings with you, separately or as part of other meetings, to gather feedback, ensure satisfaction with our service and identify areas for improvement and development year on year. These reviews form a valuable overview of our service and its contribution to the business. We use the results to brief new team members and enhance the team's awareness and understanding of your requirements.

## *Independence and objectivity*

As external auditors of the Organisation we are required to be independent of you in accordance with the Ethical Standards established by the Auditing Practices Board (APB). These standards require that we disclose to those charged with governance all relationships that, in our professional judgement, may reasonably be thought to bear on our independence.

We have a demanding approach to quality assurance which is supported by a comprehensive programme of internal quality control reviews in all offices in the UK. Our quality control procedures are designed to ensure that we meet the requirements of our clients and also the regulators and the appropriate auditing standards within the markets that we operate. We also place great emphasis on obtaining regular formal and informal feedback.

We have made enquiries of all PricewaterhouseCoopers' teams providing services to you and of those responsible in the UK Firm for compliance matters. There are no matters which we perceive may impact our independence and objectivity of the audit team.

## *Non Audit Work*

At this stage we have not planned to undertake any work for you in addition to the work we have set out in this Plan.

***Relationships and Investments***

Senior officers should not seek or receive personal financial or tax advice from PwC. Members who receive such advice from us (perhaps in connection with employment by a client of the firm) or who also act as director for another audit or advisory client of the firm should notify us, so that we can put appropriate conflict management arrangements in place.

***Independence conclusion***

At the date of this plan we confirm that in our professional judgement, we are independent accountants with respect to the Organisation, within the meaning of UK regulatory and professional requirements and that the objectivity of the audit team is not impaired.

# Communicating with you

## Communications Plan and timetable

Our team works on the audit engagement throughout the year to provide you with a timely and responsive service. Below are the dates when we expect to provide the Management Committee with the outputs of our audit.

| Stage of the audit    | Output                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | Date                 |
|-----------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|
| <b>Audit planning</b> | <b>Audit Plan</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               | February 2016        |
| <b>Audit findings</b> | Internal control issues and recommendations for improvement (if applicable - may form part of the Audit Memorandum)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             | Throughout the audit |
|                       | <b>ISA (UK&amp;I) 260 report incorporating specific reporting requirements, including:</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      | September 2016       |
|                       | <ul style="list-style-type: none"> <li>• Any expected modifications to the audit report;</li> <li>• Uncorrected misstatements, i.e. those misstatements identified as part of the audit that management have chosen not to adjust;</li> <li>• Material weaknesses in the accounting and internal control systems identified as part of the audit;</li> <li>• Our views about significant qualitative aspects of your accounting practices including accounting policies, accounting estimates and financial statements disclosures;</li> <li>• Any significant difficulties encountered by us during the audit;</li> <li>• Any significant matters discussed, or subject to correspondence with, Management;</li> <li>• Any other significant matters relevant to the financial reporting process; and</li> <li>• Summary of findings from our use of resources audit work to support our value for money conclusion</li> </ul> |                      |
| <b>Audit reports</b>  | <b>Financial Statements and ISA 260 report.</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | September 2016       |



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# *Audit fees*

Our fees will be in line with those included in our proposal for the audit:

|              | <b>2015/16</b> |
|--------------|----------------|
| Accounts     | 25,000         |
| <b>Total</b> | <b>25,000</b>  |

We have based the fee level on the following assumptions:

- Officers meeting the timetable of deliverables, which we will agree in writing;
- We are able to place reliance, as planned, upon the work of internal audit;
- We are able to draw comfort from your management controls;
- Our use of resources conclusion and accounts opinion being unqualified.

If these prove to be unfounded, we will seek a variation order to the agreed fee, to be discussed in advance with you.

# *Other engagement information*

## **Proposed form of auditors' report**

### **INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE EASTERN SHIRES PURCHASING ORGANISATION MANAGEMENT COMMITTEE**

We have audited the non-statutory financial statements of Eastern Shires Purchasing Organisation for the year ended 31 March 2016 which comprise the Balance Sheet, the Comprehensive Income and Expenditure Statement, the Cash Flow Statement, the Movement in Reserves Statement and the related notes. The financial reporting framework that has been applied in the preparation of these non-statutory financial statements is the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

#### **Respective responsibilities of the Consortium Treasurer and auditors**

As explained more fully in the Consortium Treasurer's Responsibilities and the Eastern Shires Purchasing Organisation Consortium's Responsibilities [set out on pages..], the Consortium Treasurer is responsible for the preparation of the non-statutory financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the non-statutory financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinion, has been prepared for and only for the members for management purposes in accordance with our engagement letter dated 14 December 2015 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come including without limitation under any contractual obligations of the company, save where expressly agreed by our prior consent in writing.

#### **Scope of the audit of the non-statutory financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the non-statutory financial statements sufficient to give reasonable assurance that the non-statutory financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the organisation's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the non-statutory financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited non-statutory financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### **Opinion on non-statutory financial statements**

In our opinion the non-statutory financial statements:

- give a true and fair view of the state of the organisation's affairs as at 31 March 2016 and of its profit and cash flows for the year then ended; and

- 
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

