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# *Eastern Shires Purchasing Organisation*

External Audit Plan 2011/12

Government and Public  
Sector

February 2012



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Members of the Management Committee  
Eastern Shires Purchasing Organisation  
Barnsdale Way  
Grove Park  
Enderby  
Leicester  
LE19 1ES

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 either Richard Bacon or Charlotte Kennedy.

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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*In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and of audited bodies'. It is available from the Chief Executive of each audited body and on the Audit Commission's website. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas. Our reports are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to directors or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any director or officer in their individual capacity or to any third party.*



# 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 Audit Commission's requirements;
- gives you the opportunity to comment on our proposed audit approach and scope;
- 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 2011/12*

We will:

- audit the statutory accounts, assessing whether they provide a true and fair view;
- check compliance with International Financial Reporting Standards (IFRS);
- check compliance with the code of practice on local authority accounting;
- consider whether the disclosures in the Annual Governance Statement (AGS) are complete;
- see whether the other information in the accounts is consistent with the financial statements;
- report on your arrangements for securing economy, efficiency and effectiveness in the use of resources; and
- 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 financial statements and value for money work 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**

Officers and members of each local government body are accountable for the stewardship of public funds. It is our responsibility to carry out an audit in accordance with the Audit Commission's Code of Audit Practice (the Code), supplemented by the Statement of Responsibilities of Auditors and of Audited Bodies. Both documents are available from the Chief Executive or the Audit Commission's website.

*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 Code and the Audit Commission's Standing Guidance. 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 faces a range of challenges. You continue to face external scrutiny on your services and have significant savings targets in current and future years. The environment is extremely challenging. 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.
●	Elevated	Although not considered significant, the nature of the balance/area requires specific consideration.
●	Normal	We perform standard audit procedures to address normal 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 2011/12 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>	<i>Value for money conclusion</i>	
Management override of controls	◆		● Significant
Income and expenditure recognition	◆		● Significant
Financial Standing	◆	◆	● Elevated
Oracle payroll	◆		● Normal
Changes in key personnel	◆	◆	● Normal

Risks	Risk Level	Audit approach
<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 savings increases, so does the risk of management override.</p>	<p>●</p>	<p>We will review your internal control structure, taking into account any changes as a result of the review of ESPO.</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 carry out unpredictable procedures – these are tests we have not carried out before to test the robustness of controls.</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 reported revenue and expenditure position.</p>	<p>●</p>	<p>We will review your internal control structure.</p> <p>We will:</p> <ul style="list-style-type: none"> <li>● seek to place reliance on internal audit work on key income and expenditure controls;</li> <li>● test key income and expenditure controls to confirm if they are operating effectively;</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, provisions; and</li> <li>● perform analytical review on income and expenditure at year end and reconcile your management information to the information presented in the accounts on a gross basis.</li> </ul>
<p><b>Financial Standing</b></p> <p>The Public Sector is experiencing increased pressures on many of its budgets as economic conditions have worsened. The Committee may therefore experience decreased demand for its products and services.</p>	<p>●</p>	<p>We will consider the Committee's budget monitoring processes to identify any unexplained material anomalies in the budgetary position. We will bear these risks in mind when carrying out our substantive testing at our final audit. Our work in this area will also be used to inform our Value for Money Conclusion on the Committee's Use of Resources.</p>

Risks	Risk Level	Audit approach
<p><b>Change in key personnel</b></p> <p>The Committee is undergoing a period of extensive change with a new Assistant Director – Finance to be appointed in year.</p> <p>This change may expose the Committee to additional risks</p>	<p>●</p>	<p>We will liaise with the existing and new officers to ensure that the handover is effective from the current Assistant Director – Finance. We will invest time in getting to know the new AD and ensure that they are fully briefed with our audit approach and ways of working.</p>
<p><b>Oracle Payroll Implementation</b></p> <p>Leicestershire County Council (LCC) currently provides the Organisation’s payroll services. LCC are planning to change payroll systems from Trent to Oracle in 2011/12. This will change the nature of payroll information provided.</p>	<p>●</p>	<p>We will review the arrangements in place for the implementation of Oracle payroll and perform detailed testing of the IT general controls, application controls and data migration in conjunction with Internal Audit.</p>

# ***Audit approach***

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

Under the Audit Commission's Code there are two aspects to our work:

- Accounts, including a review of the Annual Governance Statement; and
- Use of Resources.

We are required to issue a two-part audit report covering both of these elements.

## ***Accounts***

Our audit of your accounts is carried out in accordance with the Audit Commission's Code objective, which requires us to comply with International Standards on Auditing (ISAs) (UK & Ireland) issued by the Auditing Practices Board (APB). These standards have recently been fully updated and revised to improve their clarity and in some cases this is accompanied by additional audit requirements. We are required to comply with them for the audit of your 2011/12 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. The ISA suggests a benchmark of 5 percent of our audit materiality level, which would suggest a 'clearly trivial' level of approximately £83,000.

Last year, we agreed with you that we would report errors detected over a threshold of £1,000. The threshold set for reporting could be further increased from £1,000 up to £83,000. In order to help achieve the necessary efficiencies implicit in the reduction in fees set out later in this Audit Plan, we propose increasing the reporting thresholds for unadjusted misstatements to a level closer to that allowed by auditing standards. If you wish to retain the previous reporting thresholds, this will impact upon the number of items which will require discussion and adjustment and will have an associated impact on the audit fee. 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. We would welcome your views on these proposals.

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.

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

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.

### ***Use of Resources***

Our Use of Resources Code responsibility requires us to carry out sufficient and relevant work in order to conclude on whether you have put in place proper arrangements to secure economy, efficiency and effectiveness in the use of resources.

In accordance with recent guidance issued by the Audit Commission, in 2011/12 our conclusion will be based on two criteria:

- The organisation has proper arrangements in place for securing financial resilience; and
- The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

We will be carrying out sufficient work to allow us to reach a conclusion on your arrangements based on your circumstances.

# 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

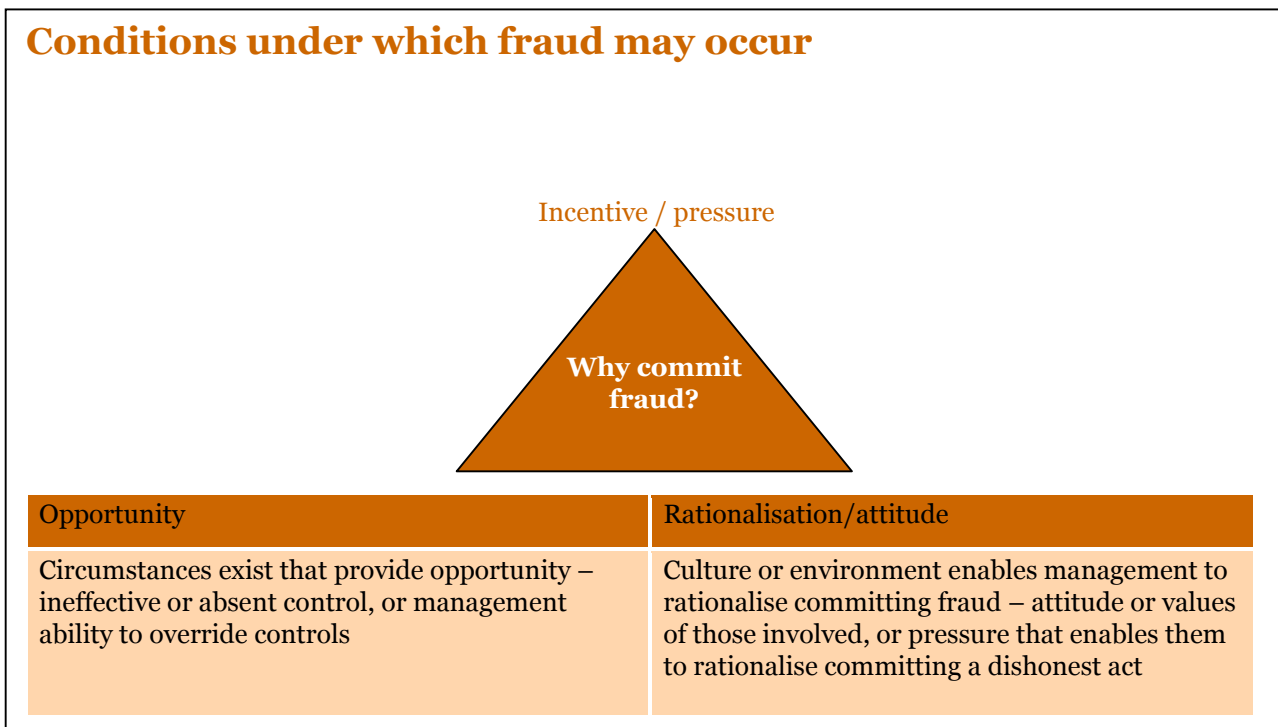
Management’s responsibilities in relation to fraud are:

- 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 antifraud measures and creation of 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 Corporate Governance 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>  <b>Richard Bacon</b>            1<sup>st</sup> year on the audit            0121 232 2598            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>Richard has taken over from Alison Breadon. Richard is also the Engagement Partner for Leicestershire County Council.</p>
<p><b>Engagement Manager</b>  <b>Charlotte Kennedy</b>            5<sup>th</sup> year on the audit            01509 604097            charlotte.kennedy@uk.pwc.com</p>	<p>Charlotte 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.



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***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

ISA (UK&I) 260 (revised) ‘Communication of audit matters with those charged with governance’ requires auditors to plan with those charged with governance the form and timing of communications with them. We have assumed that ‘those charged with governance’ are the Management Committee. Our team works on the 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
Audit planning	Audit Fee letter	July 2011
	Audit Plan	March 2012
Audit findings	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> <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>	September 2012
Audit reports	<b>Financial Statements including Use of Resources</b>	September 2012
Other public reports	<b>Annual Audit Letter</b> A brief summary report of our work, produced for Members and to be available to the public.	November 2012

# Audit fees

The Audit Commission has provided indicative audit fee levels for Joint Committee for the 2011/12 financial year, which depend upon the level of expenditure and potential risk. Based on your expenditure, the indicative fee scale for the audit of the Committee is £23,670.

Due to our assessment of risk and your control environment, we categorise the Committee as low risk. In our audit fee letter dated 21 July 2011 we therefore agreed an audit fee of £23,670. This is the lowest fee we can charge you under the Audit Commission fee scales for 2011/12.

	2010/11	2009/10
Accounts	23,670	24,400
<b>Total</b>	<b>23,670</b>	<b>24,400</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;
- No significant changes being made by the Audit Commission to the use of resources criteria on which our conclusion will be based; and
- 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*

The Audit Commission appoint us as auditors to Eastern Shires Purchasing Organisation and the terms of our appointment are governed by:

- The Code of Audit Practice; and
- The Standing Guidance for Auditors.

There are four further matters which are not currently included within the guidance, but which our firm's practice requires that we raise with you.

## ***Electronic communication***

During the engagement we may from time to time communicate electronically with each other. However, the electronic transmission of information cannot be guaranteed to be secure, virus or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use.

PwC partners and staff may also need to access PwC electronic information and resources during the engagement. You agree that there are benefits to each of us in their being able to access the PwC network via your internet connection and that they may do this by connecting their PwC laptop computers to your network. We each understand that there are risks to each of us associated with such access, including in relation to security and the transmission of viruses.

We each recognise that systems and procedures cannot be a guarantee that transmissions, our respective networks and the devices connected to these networks will be unaffected by risks such as those identified in the previous two paragraphs. We each agree to accept the risks of and authorise (a) electronic communications between us and (b) the use of your network and internet connection as set out above. We each agree to use commercially reasonable procedures (i) to check for the then most commonly known viruses before either of us sends information electronically or we connect to your network and (ii) to prevent unauthorised access to each other's systems.

We shall each be responsible for protecting our own systems and interests and you and PwC (in each case including our respective directors, members, partners, employees, agents or servants) shall have no liability to each other on any basis, whether in contract, tort (including negligence) or otherwise, in respect of any error, damage, loss or omission arising from or in connection with the electronic communication of information between us and our reliance on such information or our use of your network and internet connection.

The exclusion of liability in the previous paragraph shall not apply to the extent that such liability cannot by law be excluded.

## ***Access to audit working papers***

We may be required to give access to our audit working papers to the Audit Commission or the National Audit Office for quality assurance purposes.

## ***Quality arrangements***

We want to provide you at all times with a high quality service to meet your needs. If at any time you would like to discuss with us how our service could be improved or if you are dissatisfied with any aspect of our services, please raise the matter immediately with the partner responsible for that aspect of our services to you. If, for any reason, you would prefer to discuss these matters with someone other than that partner, please contact Paul Woolston, our Audit Commission Lead Partner at our office at 89 Sandyford Road, Newcastle Upon Tyne, NE1 8HW, or James Chalmers, UK Head of Assurance, at our office at 7 More London, Riverside, London, SE1 2RT.

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In this way we can ensure that your concerns are dealt with carefully and promptly. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. This will not affect your right to complain to the Institute of Chartered Accountants in England and Wales or to the Audit Commission.

***Events arising between signature of accounts and their publication***

ISA (UK&I) 560 (revised) places a number of requirements on us in the event of material events arising between the signing of the accounts and their publication. You need to inform us of any such matters that arise so we can fulfil our responsibilities.

If you have any queries on the above, please let us know before approving the Audit Plan or, if arising subsequently, at any point during the year.

In the event that, pursuant to a request which Eastern Shires Purchasing Organisation has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PwC promptly and consult with PwC prior to disclosing such report. Eastern Shires Purchasing Organisation agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Eastern Shires Purchasing Organisation shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC Eastern Shires Purchasing Organisation discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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