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Eastern Shires Purchasing Organisation

External Audit Plan 2012/13

Government and Public Sector

December 2012

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 Tom Gibbs.

Yours faithfully,

Richard Bacon

PricewaterhouseCoopers LLP

Encs

PricewaterhouseCoopers LLP, Cornwall Court, 19 Cornwall Street, Birmingham, B3 2DT
T: +44 (0) 121 265 5000, F: +44 (0) 121 232 2725, www.pwc.co.uk

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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 for the 2012/13 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 2012/13

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 the Organisation's arrangements for securing economy, efficiency and effectiveness in its 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 continues to face a period of organisational 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.
●	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 2012/13 is set out below, with further information provided on the following pages.

Risk arising	***Potential impact upon PwC work***		***Categorisation for accounts risks***
	Accounts true and fair opinion	***Value for money conclusion***	
Management override of controls	◆		● Significant
Income and expenditure recognition	◆		● Significant
Financial Standing	◆	◆	● Normal
Changes in key personnel	◆	◆	● Normal
Warehouse management system	◆		● Normal

Risks	Risk Level	Audit approach
Management Override of Controls 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. In your organisation, as the pressure to deliver savings increases, so does the risk of management override.	●	We will review your internal control structure, taking into account changes in senior management. 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. We will perform targeted testing over significant estimates within the financial statements. 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.
Revenue and Expenditure Recognition There is a risk that the Organisation could adopt accounting policies or treat income and expenditure transactions in such as way as to lead to material misstatement in the reported revenue and expenditure position.	●	We will review your internal control structure. We will: • review the design and operating effectiveness of key income and expenditure controls; • evaluate the accounting policies for income and expenditure recognition; • test the appropriateness of journal entries and other adjustments; • review accounting estimates for income and expenditure, for example, rebates and provisions; • 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.

Risks	Risk Level	Audit approach
Financial Standing The Public Sector continues to experience increased pressures on many of its budgets during the recession. Changes in Government spending and policy decisions impact upon ESPO's key customer base. As a result, the Committee may experience decreased demand for its products and services. Conversely customers may choose to use ESPO's services increasingly, to make further economies. We have not identified a significant incremental risk to the financial statements audit, but we will carry out planned procedures on going concern, value for money and on management override, as described above.	●	We will review management's processes for monitoring the financial performance of the Organisation and actions taken to address adverse performance. We will review the financial standing of the Organisation throughout the year and analyse performance trends. We will consider any risks identified from the above work 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.
Change in key personnel The Committee is undergoing a period of extensive change with a new Assistant Director – Finance appointed in 2011/12 and a new Director appointed during 2012/13. This change may expose the Committee to additional risks, although we have not at this stage identified a significant risk to the audit of the financial statements.	●	We will meet with the new Director and attend Management Committee meetings in order to understand the significant changes the organization is going as a result of this change in leadership. We will assess the impact of this on our audit approach and value for money opinion.
Warehouse Management System A new warehouse management software system is planned for implementation during 2012/13. This change represents an inherent risk in relation to data transfer and integration with your financial system. During our planning work we will consider whether our work needs to be extended in this year of system change, relying where we can on internal audit's work.	●	We will review the work of internal audit or external experts around the implementation of the new warehouse system. We will perform sufficient audit procedures in order to ensure the reliability of the data within the new system. We will perform a review of stock count controls, including attendance at at least one stock count, in order to gain assurance over the accuracy and completeness of inventory.

Audit approach

Code of Audit Practice

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

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

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 2012/13 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 £86,000 based on the 2011/12 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 2012/13 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.

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 2012/13 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:

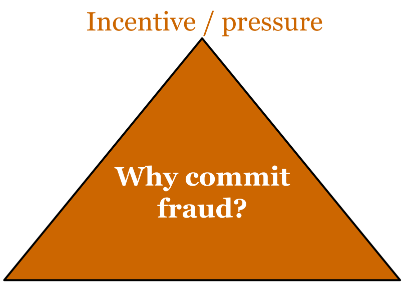
- to design and implement programmes and controls to prevent, deter and detect fraud;
- to ensure that the entity's culture and environment promote ethical behaviour; and
- to perform a risk assessment that specifically includes the risk of fraud addressing incentives and pressures, opportunities, and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

Conditions under which fraud may occur



Opportunity	Rationalisation/attitude
Circumstances exist that provide opportunity – ineffective or absent control, or management ability to override controls	Culture or environment enables management to rationalise committing fraud – attitude or values of those involved, or pressure that enables them to rationalise committing a dishonest act

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:

Audit Team	Responsibilities
Engagement Partner **Richard Bacon** 2nd year on the audit 0121 232 2598 richard.f.bacon@uk.pwc.com	Engagement Leader responsible for independently delivering the audit in line with the Code of Audit Practice, including agreeing the Audit Plan, ISA (UK&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. Richard is also the Engagement Partner for Leicestershire County Council.
Engagement Manager **Tom Gibbs** 2nd year on the audit 07850 516463 Thomas.j.gibbs@uk.pwc.com	Tom 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&I) 260 report and Annual Audit Letter.

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
Audit planning	**Audit Plan**	December 2012
Audit findings	Internal control issues and recommendations for improvement (if applicable - may form part of the Audit Memorandum)	Throughout the audit
	ISA (UK&I) 260 report incorporating specific reporting requirements, including: • Any expected modifications to the audit report; • Uncorrected misstatements, i.e. those misstatements identified as part of the audit that management have chosen not to adjust; • Material weaknesses in the accounting and internal control systems identified as part of the audit; • Our views about significant qualitative aspects of your accounting practices including accounting policies, accounting estimates and financial statements disclosures; • Any significant difficulties encountered by us during the audit; • Any significant matters discussed, or subject to correspondence with, Management; • Any other significant matters relevant to the financial reporting process; and • Summary of findings from our use of resources audit work to support our value for money conclusion	September 2013
Audit reports	**Financial Statements including Use of Resources**	September 2013
Other public reports	**Annual Audit Letter** A brief summary report of our work, produced for Members and to be available to the public. This will form part of our ISA260 audit report.	September 2013

Audit fees

The Audit Commission has provided indicative audit fee levels for Joint Committee for the 2012/13 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 £14,202, which represents a 40% reduction in fee from the previous year.

Due to our assessment of risk and your control environment, we categorise the Committee as low risk. This is the lowest fee we can charge you under the Audit Commission fee scales for 2012/13

	2012/13	2011/12
Accounts	14,202	23,670
Total	**14,202**	**23,670**

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;
- No further work is required to understand and test controls in the new warehousing system
- 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.

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.