



Falkirk Council

Annual Audit Plan 2015/16

Prepared for Members of Falkirk Council

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The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies (www.audit-scotland.gov.uk/about/ac/). Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General (www.audit-scotland.gov.uk/about/).

The Accounts Commission has appointed Fiona Mitchell-Knight as the external auditor of Falkirk Council for the period 2011/12 to 2015/16.

This report has been prepared for the use of Falkirk Council and no responsibility to any member or officer in their individual capacity or any third party is accepted.

This report will be published on our website after it has been considered by the council. The information in this report may be used for the Accounts Commission’s annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

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Summary

Introduction

1. Our audit is focused on the identification and assessment of the risks of material misstatement in Falkirk Council's financial statements.
2. This report summarises the key challenges and risks facing Falkirk Council and sets out the audit work that we propose to undertake in 2015/16. Our plan reflects:
 - the risks and priorities facing Falkirk Council
 - current national risks that are relevant to local circumstances
 - the impact of changing international auditing and accounting standards
 - our responsibilities under the Code of Audit Practice as approved by the Auditor General for Scotland
 - issues brought forward from previous audit reports.
3. The Charities Accounts (Scotland) Regulations 2006 specify the accounting and auditing rules for Scottish registered charities. Irrespective of the size of the charity, as a consequence of the interaction of section 106 of the Local Government (Scotland) Act 1973 with the regulations, a full audit is required of all registered charities where the local authority is the sole trustee. Falkirk Council has one trust falling into that category. Falkirk Temperance Trust with reported net assets of £0.160 million as at 31 March 2015. Accordingly, we will perform the audit of the council's charitable trust in parallel with the audit of the council's financial statements.

4. Health and social care integration: the Falkirk Integration Joint Board (FIJB) was established on 3 October 2015 although services will not transfer to the new body until 1 April 2016. The FIJB is subject to a separate audit in 2015/16. Fiona Mitchell Knight, Assistant Director, Audit Services is the appointed auditor and an annual audit plan will be issued in due course. We do not expect the FIJB to be material to the council's group accounting arrangements in 2015/16.

Summary of planned audit activity

5. Our planned work in 2015/16 includes:
 - an audit of the financial statements and provision of an opinion on whether:
 - they give a true and fair view of the state of affairs of Falkirk Council and its group as at 31 March 2016 and its income and expenditure for the year then ended
 - the accounts have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2015/16 Code of Practice on Local Authority Accounting in the United Kingdom (the Code)
 - reporting the findings of the shared risk assessment process in a Local Scrutiny Plan. This will summarise identified scrutiny risks and/or any changes to the Local Area Network's (LAN's) assessment since last year
 - a review and assessment of Falkirk Council's governance and performance arrangements in a number of key areas including:

internal controls, adequacy of internal audit and fraud prevention measures

- provision of an opinion on a number of grant claims and returns, including Whole of Government Accounts
- reporting of National Fraud Initiative arrangements and results
- collection of relevant financial and performance information to inform Audit Scotland's national reports.

Responsibilities

6. The audit of the financial statements does not relieve management or the Audit Committee as the body charged with governance, of their responsibilities.

Responsibility of the appointed auditor

7. Our responsibilities, as independent auditor, are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.
8. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements set in place by the audited body to ensure the proper conduct of its financial affairs and to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

Responsibility of the Chief Finance Officer

9. It is the responsibility of the Chief Finance Officer, as the appointed "proper officer", to prepare the financial statements in accordance with relevant legislation and the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). This means:
 - maintaining proper accounting records
 - preparing financial statements which give a true and fair view of the state of affairs of Falkirk Council and its group as at 31 March 2016 and its expenditure and income for the year then ended.
10. It is also important that the accounts are proof read before being submitted for audit to ensure a prompt start to our work and to reduce the number of presentational amendments.

Format of the accounts

11. The financial statements should be prepared in accordance with the Code, which constitutes proper accounting practice.
12. Falkirk Council prepares a Whole of Government Accounts consolidation pack annually for the Scottish Government. To enable summarisation common accounting principles and standard formats should be used.

Audit Approach

Our approach

13. Our audit approach is based on an understanding of the characteristics, responsibilities, principal activities, risks and governance arrangements of Falkirk Council and its group. We also consider the key audit risks and challenges in the local government sector generally. This approach includes:
 - understanding the business of Falkirk Council and its group and the risk exposure which could impact on the financial statements
 - assessing the key systems of internal control, and considering how risks in these systems could impact on the financial statements
 - identifying major transaction streams, balances and areas of estimation and understanding how Falkirk Council will include these in the financial statements
 - assessing and addressing the risk of material misstatement in the financial statements
 - determining the nature, timing and extent of the audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements give a true and fair view.
14. We have also considered and documented the sources of assurance which will make best use of our resources and allow us to focus audit testing on higher risk areas during the audit of the financial statements. The main areas of assurance for the audit come from planned management action and reliance on systems of internal control. Planned management action being relied on for 2015/16 includes:
 - comprehensive closedown procedures for the council and group financial statements accompanied by a timetable issued to all relevant staff
 - clear responsibilities for preparation of financial statements and the provision of supporting working papers
 - delivery of unaudited financial statements to agreed timescales with a comprehensive working papers package
 - completion of the internal audit programme for 2015/16.
15. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. Internal audit services are provided by the internal audit section of the council. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carry out an early assessment of the internal audit function to determine whether it has sound documentation standards and reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS).
16. We plan to place formal reliance on aspects of the work of internal audit in the following areas, to support our audit opinion on the financial statements:
 - Investment (non-pension)
 - Integra finance system – supplier data management and payments.

17. In respect of our wider governance and performance audit work we also plan to review the findings and consider other areas of internal audit work including:
- Corporate risk management arrangements
 - Adult health and social care integration
 - Data and information security - governance and practice
 - Revenues IT systems security and management
 - Corporate purchasing and contract management
 - Financial regulations.

Materiality

18. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other reasons (for example, the failure to achieve a statutory requirement or, an item contrary to law). In the event of such an item arising, its materiality has to be viewed in a narrower context; such matters would normally fall to be covered in an explanatory paragraph in the independent auditor's report.
19. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements both individually and collectively.

20. Based on our knowledge and understanding of Falkirk Council we have set our planning materiality at £6.415 million (1% of budget gross expenditure).
21. We set a lower level, known as performance materiality, when defining our audit procedures. This is to ensure that uncorrected and undetected audit differences do not exceed our planning materiality. This level depends on professional judgement and is informed by a number of factors including:
- extent of estimation and judgement within the financial statements
 - nature and extent of prior year misstatements
 - extent of audit testing coverage.
22. For 2015/16 performance materiality has been set at £3.208 million. We will report, to those charged with governance, all misstatements identified which are greater than £64,000.

Reporting arrangements

23. The Local Authority Accounts (Scotland) Regulations 2014 require that the unaudited annual accounts are submitted to the appointed external auditor no later than 30 June each year. The authority (or a committee whose remit includes audit or governance) is required to consider the unaudited annual accounts at a meeting by 31 August.
24. Local authorities must publish the unaudited accounts on their websites and give public notice of the inspection period.
25. The 2014 regulations require the local authority (or a committee whose remit includes audit or governance) to meet by 30

September to consider whether to approve the audited annual accounts for signature. Immediately after approval, the annual accounts require to be signed and dated by specified members and officers and then provided to the auditor. The Controller of Audit requires audit completion and issue of an independent auditor's report (opinion) by 30 September each year.

26. The authority is required to publish on its website its signed audited annual accounts, and the audit certificate, by 31 October. The local authority is also required to publish a copy of the accounts of its subsidiaries. The annual audit report is required to be published on the website by 31 December.
27. A proposed timetable for the audit of the 2015/16 financial statements is included at Exhibit 1 below.

Exhibit 1: Financial statements audit timetable

Key stage	Date
Testing and review of internal control systems and transactions	January to April 2016
Meetings with officers to clarify expectations of working papers and financial system reports	Ongoing
Consideration of unaudited financial statements by those charged with governance	20 June 2016
Latest submission date of unaudited council financial statements with complete working papers package	20 June 2016
Progress meetings with lead officers on emerging issues	Ongoing

Key stage	Date
Latest date for final clearance meeting with Chief Finance Officer	12 Sep 2016
Agreement of audited unsigned financial statements, and issue of Annual Audit Report which includes the ISA 260 report to those charged with governance	26 Sep 2016
Independent auditor's report signed	26 Sep 2016
Latest date for signing of WGA return	30 Sep 2016

28. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the responsible head of service and relevant officers to confirm factual accuracy. Responses to draft reports are expected within three weeks of submission. A copy of all final agreed reports will be sent to the Chief Executive, Chief Finance Officer, and relevant senior managers, Internal Audit Manager and Audit Scotland's Performance Audit and Best Value Group.
29. We will provide an independent auditor's report to Falkirk Council and the Accounts Commission that the audit of the financial statements has been completed in accordance with applicable statutory requirements. The combined ISA 260 and Annual Audit Report will be issued by 30 September.
30. All annual audit reports produced are published on Audit Scotland's website: www.audit-scotland.gov.uk.
31. Planned outputs for 2015/16 are summarised at [Appendix 1](#).

Quality control

- 32. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established as part of financial audit procedures. This is to provide reasonable assurance that those professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.
- 33. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice issued by Audit Scotland and approved by the Accounts Commission. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews and has been subject to a programme of external reviews by the Institute of Chartered Accountants of Scotland (ICAS).
- 34. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We do, however, welcome feedback at any time and this may be directed to the engagement lead, Fiona Mitchell Knight.

Independence and objectivity

- 35. Auditors appointed by the Accounts Commission must comply with the Code of Audit Practice. When auditing the financial statements, auditors must also comply with professional standards issued by the Auditing Practices Board (APB) and those of the professional

accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. The arrangements are overseen by the Assistant Auditor General, who serves as Audit Scotland's Ethics Partner.

- 36. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of Falkirk Council.

Audit issues and risks

Audit issues and risks

37. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for Falkirk Council. We have categorised these risks into financial risks and wider dimension risks. The financial statements issues and risks, which require specific audit testing, are summarised below and detail contained in [Appendix 2](#).

Financial statement issues and risks

38. **Income:** Auditing standards (ISA 240 *The auditor's responsibility to consider fraud in an audit of financial statements*) requires auditors to presume a risk of fraud where income streams are significant. Falkirk Council receives a significant amount of funding from the Scottish Government. Money is also received from other sources, including council tax, housing rents and service income from fees and charges. The complexity of income means there is an inherent risk that income could be materially misstated. It is our opinion that the council has mitigating controls in place to reduce this risk although risk can never be fully eliminated. We review the systems of internal control and perform substantive testing across all areas of income to obtain assurances for the purpose of our audit.
39. **Management override of controls:** ISA 240 recognises that management are in a unique position and have the ability to manipulate accounting records, and prepare fraudulent financial

statements, by overriding controls that would otherwise appear to be operating effectively. ISA 240 requires that this risk be recognised in audit plans.

40. **Equal pay claims:** The council recognised a provision in respect of equal pay in the 2014/15 financial statements and disclosed a contingent liability. There is a risk that the provision does not accurately reflect the liability to the council. This will become clearer as the legal position develops and cases are settled. We will monitor the situation throughout the year and review the equal pay provision as part of the 2015/16 financial statements audit process.
41. **Revaluation of council dwellings:** The council has used a discounted cash flow approach to the valuation of its council dwellings since 1 April 2010. The LASAAC Mandatory Guidance on the Valuation Methodology for Council Dwellings (the LASAAC Guidance), October 2010, requires Scottish local authorities to adopt the beacon approach methodology by 2015/16. Officers have obtained a valuation using the beacon approach methodology for inclusion in the 2015/16 financial statements. There will be a material increase in the value of council dwellings on the balance sheet. Officers will need to ensure that council dwellings are accounted for in line with the Code, including depreciation and recognition of capital expenditure. We have had early discussions with officers about the proposed accounting treatment and will review this in advance of the financial statements audit.

Wider dimension issues and risks

42. **Financial management:** As at 31 December 2015 the council was projecting an underspend of £2.055m in the year mainly due to

lower than anticipated costs in education, particularly early years provision. This is accompanied by a significant overspend of £2.864m in social work services (both children and adult), which has been funded by a £2m contingency included in the 2015/16 budget and offset by underspends in other services. Recurring overspends in social work services suggest that the budget does not accurately reflect the cost of providing these services. Members have received reports outlining plans to address the overspends. Good financial management will be critical to the council achieving a balanced budget going forward. We will continue to monitor and report on the council's financial position.

43. **Best Value audit follow-up:** A targeted audit of Best Value arrangements at the council was published in August 2015. The audit identified a number of areas for improvement that relate to the scale and pace of change at the council and its approach to scrutiny, performance management and performance reporting¹. The Accounts Commission requires a report on the council's progress from the Controller of Audit by the end of 2016. It is important that the council is able to demonstrate that action has been taken to address improvement areas identified by the BV audit.
44. **Workforce planning:** In response to the constrained financial position that the council is facing members have approved plans to reduce the workforce by 348 full time equivalents over 2015/16 and 2016/17. If this cannot be achieved through voluntary means then other actions may need to be taken. Audit Scotland have previously

highlighted that councils need to ensure that staff reductions are considered within the context of comprehensive workforce strategies and plans. The council's existing workforce strategy only covers the period 2011-2014, although a revised strategy is being developed. Audit Scotland published a report on Scotland's Public Sector Workforce in November 2013². We will carry out local follow-up work this year based on the recommendations in the 2013 report. Any significant issues will be reported via our 2015/16 Annual Audit Report.

45. **Infrastructure Assets:** From 2016/17, the Code of Practice on Local Authority Accounting in the United Kingdom (the Code) requires infrastructure assets to be included in the council's financial statements at depreciated replacement cost. The Code requires an authority to disclose information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. The specific requirements are outlined at Appendix D to the Code. We will report on the council's preparation and review the disclosures in the 2015/16 accounts.

National performance audit studies

46. Audit Scotland's Performance Audit and Best Value Group undertake a programme of studies on behalf of the Auditor General and Accounts Commission. In line with Audit Scotland's strategy to support improvement through the audit process, we will carry out work to collect relevant financial and performance information to inform Audit Scotland's national reports.

¹ *Falkirk Council Best Value Audit 2014/15*, Audit Scotland, August 2015

² *Scotland's Public Sector Workforce*, Audit Scotland, November 2013

Fees and resources

Audit fee

47. Over the past four years, Audit Scotland has reduced audit fees by 24% in real terms, exceeding our 20% target. Due to further refinement of our audit approach we have been able to maintain audit fees for 2015/16 at the same level as last year. This represents an additional real term fee reduction of 1.6%.
48. In determining the audit fee we have taken account of the risk exposure of Falkirk Council, the planned management assurances in place, and the level of reliance we plan to take from the work of internal audit. We have assumed receipt of a complete set of unaudited financial statements and comprehensive working papers package by 20 June 2016.
49. The proposed audit fee for the 2015/16 audit of Falkirk Council and Falkirk Temperance Trust is £322,190. Our fee covers:
 - the costs of planning, delivering and reporting the annual audit including auditor's attendance at committees
 - your organisation's allocation of the cost of national performance studies and statutory reports by the Auditor General for Scotland
 - a contribution towards functions that support the local audit process (e.g. technical support and coordination of the National Fraud Initiative), support costs and auditors' travel and subsistence expenses.
50. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Audit team

51. Fiona Mitchell Knight, Assistant Director is your appointed auditor. The local audit team will be led by Jim Rundell who will be your primary contact. Details of the experience and skills of our team are provided in Exhibit 2.

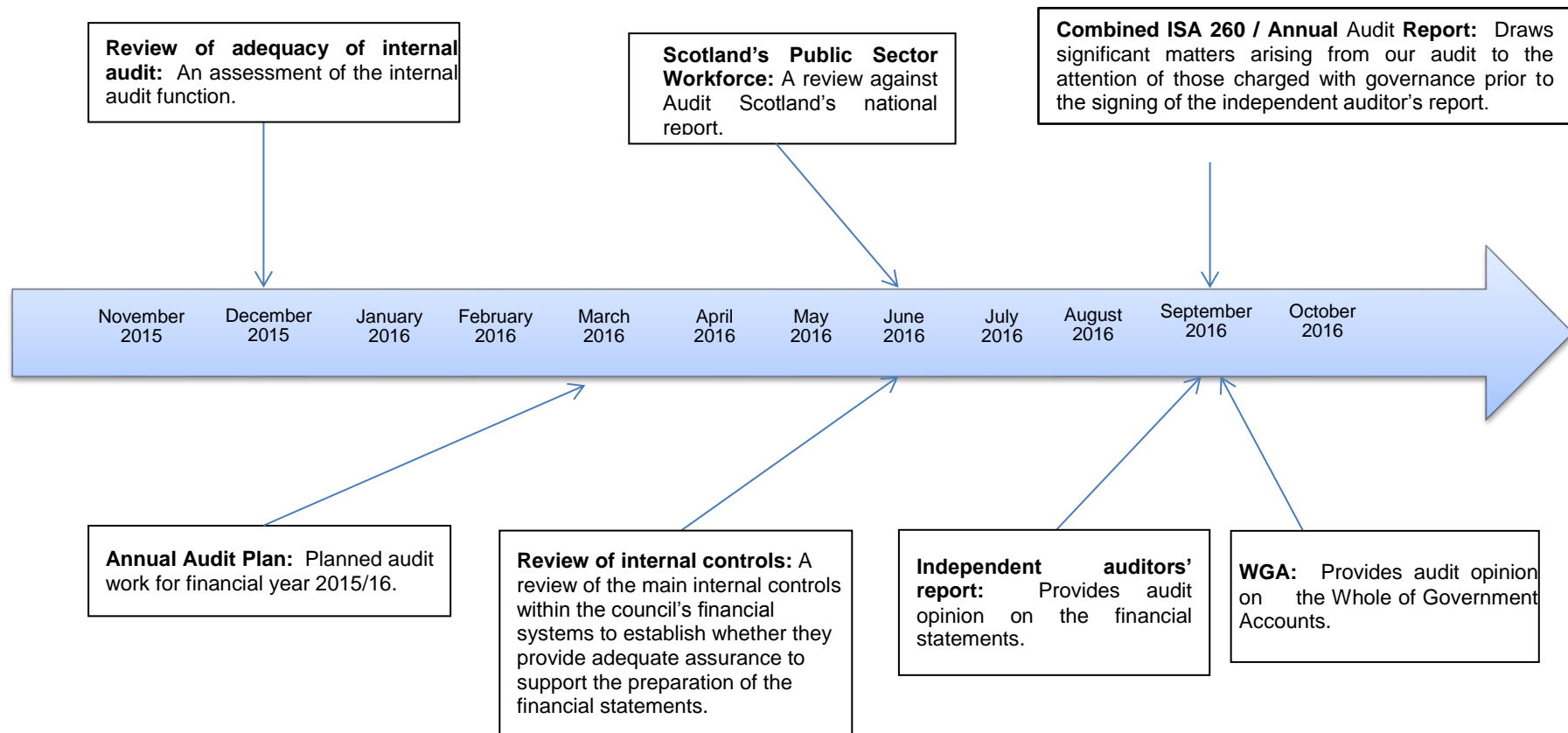
Exhibit 2: Audit team

Name	Experience
Fiona Mitchell-Knight BA (Hons) FCA <i>Assistant Director of Audit Services (and certifying auditor)</i>	Fiona took up post as Assistant Director of Audit in August 2007. Fiona has 22 years experience in public sector audit, covering local government, health and the further education sector. Fiona is also the officer who certifies the annual accounts.
Jim Rundell MA (Hons) CPFA <i>Senior Audit Manager</i>	Jim has 31 years public sector audit experience, mostly in local government and health. Recently he was responsible for revising Audit Scotland's risk management policy, strategy and assurance framework to comply with good practice, and continues to act as Risk Champion for Audit Services providing support and advice on risk. His recent audit responsibilities have included City of Edinburgh Council, NHS Greater Glasgow and Clyde and Lothian Pension Fund.
David Meechan BA CA <i>Senior Auditor</i>	David joined Audit Scotland 14 years ago, after 24 years in private sector audit, where he specialised latterly in the voluntary housing and independent schools sectors. Since joining Audit Scotland he has worked mainly on local government and health audits, most recently leading on the audit of Glasgow City Council for 2012/13 and 2013/14.
Lisa Duthie MA (Hons) CPFA <i>Senior Auditor</i>	Lisa joined Audit Scotland in 2008 and has over 7 years experience in public sector audit covering local government, health and central government.
Gerry Collins <i>Auditor</i>	Gerry has over 21 years experience working as an auditor/accountant. He has worked for the last 13 years in external and internal audit within the public sector, in both health and local government. Gerry is part ACCA qualified.
Russell Croal BAcc (Hons) <i>Professional Trainee</i>	Russell joined Audit Scotland in 2014 and is currently training for the ICAS professional accountancy qualification.

NB - The core team will call on other specialist and support staff as necessary.

Appendix 1: Planned audit outputs

The diagram below shows the key outputs planned for Falkirk Council in 2015/16.



Appendix 2: Significant audit risks

The table below sets out the key audit risks, the related sources of assurance received and the audit work we propose to undertake to address the risks during our audit work.

#	Audit Risk	Source of assurance	Audit assurance procedure
Financial statement issues and risks			
1	Income Falkirk Council receives a significant amount of income in addition to SG funding. The complexity of that income means there is an inherent risk of fraud in accordance with ISA240.	<ul style="list-style-type: none"> Mitigating controls in place to reduce this risk e.g. regular reconciliations, segregation of duties. Internal audit reviews. 	<ul style="list-style-type: none"> Controls testing of accounts receivable system and transaction testing which will cover each service income area. Detailed testing of revenue transactions focusing on areas considered higher risk. Testing of significant grants received. Focussed testing on local taxation systems.
2	Management override of controls As stated in ISA 240, management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.	<ul style="list-style-type: none"> A sound system of budgetary control, including regular budget monitoring. Regular updates of Standing Orders and Financial Regulations, which require approval by the Full Council. 	<ul style="list-style-type: none"> Detailed testing of journal entries. Review of accounting estimates for bias. Evaluating significant transactions that are outside the normal course of business. Focussed testing of the regularity and cut-off assertions during the financial statements audit.
3	Equal pay claims There is still uncertainty over the legal position of outstanding equal pay claims against the council. Risk: Material misstatement of the level of provision required.	<ul style="list-style-type: none"> Finance team seek advice from the council's legal team when determining provisions to be included in the accounts. 	<ul style="list-style-type: none"> Monitor legal developments nationally; assess potential financial impact on the council. Review of calculations and assumptions supporting provision.

#	Audit Risk	Source of assurance	Audit assurance procedure
4	<p>Revaluation of council dwellings</p> <p>The council has obtained a valuation of its council dwellings under the beacon approach methodology for inclusion in the 2015/16 financial statements.</p> <p>Risk: Council dwellings are not accounted for correctly in the financial statements.</p>	<ul style="list-style-type: none"> Valuation obtained from District Valuer. Council dwellings will be accounted for in line with the Code. Early discussions with auditors to ensure consistent view on accounting treatment. 	<ul style="list-style-type: none"> Review the valuation and accounting treatment of council dwellings in advance of the financial statements audit.
Wider dimension issues and risks			
5	<p>Financial management</p> <p>Social work services (both children and adult) continue to overspend in 2015/16. The overspend of £2.864m as at 31 December 2015 has been funded by a £2m contingency and offset by underspends in other areas.</p> <p>Risk: Overspends persist and the council is unable to balance the budget in future years.</p>	<ul style="list-style-type: none"> Proposals to address the situation have been reported to the Scrutiny Committee, although the impact is yet to be seen. 	<ul style="list-style-type: none"> We will monitor the council's financial position and comment in our annual audit report.
6	<p>Best Value follow-up audit</p> <p>The Accounts Commission requires a report on the council's progress against the improvements identified in the Best Value audit report from the Controller of Audit by the end of 2016.</p> <p>Risk: The council is unable to demonstrate that action has been taken to address the improvement areas identified.</p>	<ul style="list-style-type: none"> A Best Value improvement plan has been developed and agreed by members. 	<ul style="list-style-type: none"> Best Value follow-up audit to be reported by the end of 2016.

#	Audit Risk	Source of assurance	Audit assurance procedure
7	<p>Workforce planning</p> <p>In response to the constrained financial position that the council is facing members have approved plans to reduce the workforce by 348 full time equivalents during 2015/16 and 2016/17.</p> <p>Risk: Reduced workforce and a loss of intellectual capacity has an adverse impact on service delivery and staff morale.</p>	<ul style="list-style-type: none"> The council will update its workforce strategy for approval by members by March 2016. 	<ul style="list-style-type: none"> We will carry out local follow up work this year based on the recommendations in Audit Scotland's report, <i>Scotland's Public Sector Workforce</i>.
8	<p>Infrastructure assets</p> <p>The Code requires an authority to disclose information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted.</p> <p>Risk: The council has not prepared the information needed to include the appropriate disclosures in 2015/16 and meet the change in accounting requirement for 2016/17.</p>	<ul style="list-style-type: none"> Training delivered by CIPFA to staff concerned. Utilising the Valuation Toolkit that has been provided as part of the CIPFA supporting materials. Disclosures in the 2015/16 accounts will include an estimate of the impact on the 2016/17 figures. 	<ul style="list-style-type: none"> We will review the disclosures relating this standard issued but not yet adopted in the 2015/16 accounts. We will consider the council's preparedness for the change to accounting for infrastructure assets and comment in our annual audit report.