



WALES AUDIT OFFICE
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Archwilydd Cyffredinol Cymru
Auditor General for Wales

Audit of Financial Statements Report Monmouthshire County Council

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infoofficer@audit.wales.

We welcome correspondence and telephone calls in Welsh and English. Corresponding in Welsh will not lead to delay.

The team who delivered the work comprised of Ann-Marie Harkin, Terry Lewis, Rhodri Davies, Peter Darlington, Martin Hall, Jane Davies, Christine Nash, Ellis Williams and Benjamin Buckley.

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Summary report

Introduction

- 1 The purpose of this report is twofold:
 - to set out for consideration the matters arising from the audit of the financial statements of Monmouthshire County Council, for 2016-17, that require reporting to those charged with governance, in time to enable appropriate action; and
 - to formally communicate the completion of our audit and capture the recommendations arising from our audit work for the year.
- 2 The Auditor General's responsibilities were set out in our **Audit Plan** along with your responsibilities as those charged with governance; we do not repeat them in detail again here.
- 3 We are grateful to the Council and its staff for their assistance, good quality working papers and draft accounts provided during the course of our audit.
- 4 The Auditor General is responsible for providing an opinion on whether the financial statements give a true and fair view of the financial position of Monmouthshire County Council at 31 March 2017 and its income and expenditure for the year then ended.
- 5 We do not try to obtain absolute assurance that the financial statements are correctly stated, but adopt the concept of materiality. In planning and conducting the audit, we seek to identify material misstatements in your financial statements, namely, those that might result in a reader of the accounts being misled.
- 6 The quantitative levels at which we judge such misstatements to be material for Monmouthshire County Council are £2,868,000. Whether an item is judged to be material can also be affected by certain qualitative issues such as legal and regulatory requirements and political sensitivity.

Status of the audit

- 7 We received the draft financial statements for the year ended 31 March 2017 on 9 June 2017, 21 days prior to the agreed deadline of 30 June 2017, and have now substantially completed our audit work.
- 8 We are reporting to you the more significant issues arising from the audit, which we believe you must consider prior to approval of the financial statements. The audit team has already discussed these issues with Head of Finance and Assistant Head of Finance.

Proposed audit report

- 9 It is the Auditor General's intention to issue an unqualified audit report on the financial statements once you have provided us with a Letter of Representation based on that set out in [Appendix 1](#).
- 10 The proposed audit report is set out in [Appendix 2](#).

Significant issues arising from the audit

Uncorrected misstatements

- 11 We set out below the misstatements we identified in the financial statements, which have been discussed with management but remain uncorrected. Explanations for not correcting these misstatements are provided (by management) in the Letter of Representation [Appendix 1](#).

a. Vehicle additions not reflected in Property, Plant and Equipment

When vehicles are purchased they are not recognised in Fixed Assets until a funding decision is made, either via borrowing (retaining ownership) or leasing. Where the decision is made in a different financial year then a cut-off error arises. The impact on the 2016-17 financial statements is that Fixed Assets are understated (Debit) by £199,224 and Accrued Income overstated (Credit) by £199,224.

b. Reversal of impairments credited to CIES instead of the Revaluation Reserve

During revaluation testing of Property, Plant and Equipment (PPE) we identified 8 assets where the reversal of impairment had been incorrectly credited to the Comprehensive Income and Expenditure Statement (CIES) instead of the Revaluation Reserve. These impairment losses had been reversed in a prior period (i.e. credited to the CIES), but this was not recognised on the Logotech asset management system. Therefore, instead of posting the upwards revaluation to the revaluation reserve, it was again credited to the CIES. The impact on the financial statements is that Surplus on revaluation of PPE in the CIES is overstated (Debit) by £735,034 and the Revaluation Reserve is understated (Credit) by £735,034.

c. Vehicles included in Property, Plant and Equipment that have been disposed of

During our review of the Fixed Asset Register (FAR) we noted numerous vehicles with a low or nil Net Book Value (NBV). Further work identified that 45 assets had been disposed of, but not removed from the FAR and they were

therefore were included in PPE. The Gross Book Value (cost/valuation) of these assets is £1,041,703.70, but the NBV is only £35,059 as most have been fully depreciated. The impact on the financial statements is that Cost/valuation of PPE is overstated (Credit) by £1,041,704, Accumulated Depreciation of PPE is overstated (Debit) by £1,006,645 and the Gain on disposal of non-current assets in the CIES is overstated (Debit) by £35,059.

d. Capital additions for Voluntary Controlled Schools incorrectly included in Property, Plant and Equipment

During review of the Fixed Asset Register there was £265,079 of capital additions regarding Voluntary Controlled Schools. As per CIPFA guidance and section E1 of the Code, these schools are to be held off-Balance Sheet. Therefore any capital expenditure should have been treated as Revenue Expenditure Funded from Capital under Statute (REFCUS). The impact on the financial statements for the year ended 31.03.17 is that Cash and Cash Equivalents is understated (Debit) by £265,079 and Short Term Debtors is overstated (Credit) by £265,079.

e. Cash received before year end but not included in Cash and Cash equivalents

A review of the bank reconciliations identified there was £451,999 of unreconciled bank receipts. This represented cash that was received prior to year end, but had not been recognised in the financial statements. The impact on the financial statements is that Cash and Cash Equivalents is understated (Debit) by £451,999 and Short Term Debtors is overstated (Credit) by £451,999.

f. Impact of not discounting the future cash flows on the Morrison's lease agreement

Under the lease agreement for Abergavenny Cattle Market to Morrison's, the Council is due to receive £4m in rental income over the next 25 years (£160,000 per annum). The impact on the financial statements of not discounting the future cash flows is that Long Term Debtors is overstated (Credit) by £1,000,000 and Deferred Capital Receipts Reserve is overstated (Debit) by £1,000,000.

g. Expenditure overstated as prepayment journal not posted at year-end

During interim expenditure testing we identified 6 transactions requiring prepayment adjustments at year end. Further work at final audit, identified that only 3 of these transactions had been adjusted in the financial statements. Further testing was undertaken focusing on types of expenditure that require prepayment adjustments, for example licences, subscriptions (i.e. expenditure likely to span the year-end). Additional errors were identified and therefore we projected these errors across the classes of expenditure where we had identified the errors resulted in an £177,000 overstatement of expenditure. The impact on the financial statements is

that Prepayments is understated (Debit) by £177,000 and Expenditure is overstated (Credit) by £177,000.

h. Re-charges incorrectly classified in the Expenditure and Funding Analysis and the CIES

Re-charges of central overhead costs are not shown on the report to management (report to Cabinet). They are shown in the original place they are debited. There is an adjustment in column II of the EFA to allocate recharges (overheads and support costs) to the various segments in the CIES. Under the Code 2016-17 (section 3.4.2.39) and per CIPFA guidance on the reporting of corporate expenditure in the CIES "Expenditure will be reported where it was originally debited". Therefore, as re-charges are not included on the report to management, these adjustments should not be reflected in the CIES. The impact on the financial statements is:

- Children & young People Net Expenditure is understated by circa £365,000
- Social Care & Health Net Expenditure is understated by circa £533,000
- Enterprise Net Expenditure is understated by circa £347,000
- Chief Executive Unit Net Expenditure is overstated by circa £1,368,000
- Resources Net Expenditure is overstated by circa £281,000
- Corporate Net Expenditure is understated by circa £404,000

However, it must be noted that the impact on the Net Cost of Services is £nil and the above adjustments are purely presentational in the CIES.

The uncorrected misstatements (above) are immaterial individually and in total. The total impact on the CIES is an £858,172 understatement of Net Expenditure.

Corrected misstatements

- 12 There are misstatements that have been corrected by management, but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process. They are set out with explanations in [Appendix 3](#)

Other significant issues arising from the audit

- 13 In the course of the audit, we consider a number of matters both qualitative and quantitative relating to the accounts and report any significant issues arising to you. There were some issues arising in these areas this year:
- **We have some concerns about the qualitative aspects of your accounting practices and financial reporting as follows:**
 - a. We identified numerous rounding errors in the draft financial statements and have recommended that these are adjusted for. Management has

decided not to adjust for 2016-17 but has agreed that rounding formulas will be used in the preparation of next year's accounts..

- b. Some disclosures did not comply with the Code of Practice for Local Authority Accounting. For example, additional disclosure was required for the Fair Value of Investment Properties, the 2016/17 Action Plan in the Annual Governance Statement and a Nature of Expenses note was omitted from the draft financial statements. The Council do not use the CIPFA Disclosure checklist to ensure compliance with the Code. Use of this checklist could have identified the disclosure errors detailed above so that they could have been corrected.
- **We did not encounter any significant difficulties during the audit.** We received information in a timely and helpful manner and were not restricted in our work. There are some areas where we have identified that improvements could be made to make our audit more efficient. We have had some discussions with officers about these during the course of the audit and will undertake a 'post project learning' exercise to formalise agreement for future improvement.
 - **There were no significant matters discussed and corresponded upon with management which we need to report to you.**
 - **There are no other matters significant to the oversight of the financial reporting process that we need to report to you.**
 - **We did not identify any material weaknesses in your internal controls.**
 - **There are not any other matters specifically required by auditing standards to be communicated to those charged with governance.**

Independence and objectivity

- 14 As part of the finalisation process, we are required to provide you with representations concerning our independence.
- 15 We have complied with ethical standards and in our professional judgment, we are independent and our objectivity is not compromised. There are no relationships between the Wales Audit Office and the Council that we consider to bear on our objectivity and independence.

Appendix 1

Final Letter of Representation

[Insert proposed Letter of Representation]

Auditor General for Wales
Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

[Insert Date]

Representations regarding the 2016-17 financial statements

This letter is provided in connection with your audit of the financial statements of Monmouthshire County Council for the year ended 31 March 2017 for the purpose of expressing an opinion on their truth and fairness.

We confirm that to the best of our knowledge and belief, having made enquiries as we consider sufficient, we can make the following representations to you.

Management representations

Responsibilities

We have fulfilled our responsibilities for:

The preparation of the financial statements in accordance with legislative requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17; in particular the financial statements give a true and fair view in accordance therewith.

- The design, implementation, maintenance and review of internal control to prevent and detect fraud and error.

Information provided

We have provided you with:

- Full access to:
 - all information of which we are aware that is relevant to the preparation of the financial statements such as books of account and supporting documentation, minutes of meetings and other matters;

- additional information that you have requested from us for the purpose of the audit; and
- unrestricted access to staff from whom you determined it necessary to obtain audit evidence.
- The results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- Our knowledge of fraud or suspected fraud that we are aware of and that affects Monmouthshire County Council and involves:
 - management;
 - employees who have significant roles in internal control; or
 - others where the fraud could have a material effect on the financial statements.
- Our knowledge of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others.
- Our knowledge of all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
- The identity of all related parties and all the related party relationships and transactions of which we are aware.

Financial statement representations

- All transactions, assets and liabilities have been recorded in the accounting records and are reflected in the financial statements.
- Significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable.
- Related party relationships and transactions have been appropriately accounted for and disclosed.
- All events occurring subsequent to the reporting date which require adjustment or disclosure have been adjusted for or disclosed.
- All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.
- The financial statements are free of material misstatements, including omissions. The effects of uncorrected misstatements identified during the audit are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. A summary of these items is set out below:

a. Vehicle additions not reflected in Property, Plant and Equipment

The value of such is anticipated at circa £200k. Traditionally assets are only added to the fixed asset register once the financing decision has been resolved, and where borrowing our outright purchase has proved the result. The Council uses an external agent to evaluate the most economic form of financing, and previously it has been more common to enter into sale and leaseback arrangements which means that vehicles wouldn't be added to the Property, Plant and Equipment balance. The financing decision had not been made at the end of 2016-17 to be explicit. The management response is to seek financing advice at an early juncture to avoid the need for matters to be transferred between financial years.

b. Reversal of impairments credited to CIES instead of the Revaluation Reserve

The correction has no net effect on the reported bottom line position, but would introduce further volatility and reconciliation to particular lines in the Accounts. Management and auditors conclude the amount involved to be at an immaterial level in the Accounts but above trivial in terms of audit reporting.

c. Vehicles included in Property, Plant and Equipment that have been disposed

The net value of the adjustment was only £35,000. Rather than amend, management response focusses on better capture and timely sharing of disposal information from services.

d. Capital additions for Voluntary Controlled Schools incorrectly included in Property, Plant and Equipment

Management accept the error that has resulted. The conveyancing/transfer of title to the Diocese is still outstanding and Accounts colleagues have had to rely on a "substance over form" argument with auditors to exclude such costs from the Council's fixed assets. Unfortunately this entry was missed, but it is hoped the conveyance will get resolved prior to 2017-18 closure process to avoid the continued potential for human error.

e. Cash received before year end but not included in Cash and Cash equivalents

There is no effect on the bottom line of the Statement and the level of current assets overall remains the same. This issue generally

results where year-end coincides with bank holiday or weekend period. Management response is to consider whether an added process be undertaken as part of the year end practice to retrospectively allocate cash received with Debtors over the immediate year end period.

f. **Impact of not discounting the future cash flows per Morrison's lease agreement**

Auditors conclude that the deferred purchase amount being paid over 25 years through a lease for the cattle market, inherently includes the introduction of an interest payment. This isn't explicit in that document. But they suggest that instead of recording £4m as a deferred capital receipt, the Council should instead record £1m of that as interest. This isn't a situation the Council accords with as yet. There is no effect on the bottom line of the Statement of Accounts.

g. **Expenditure overstated as prepayment journal not posted at year-end**

The reality is the Accounts reasonably reflect 12 months' worth of service and expenditure, and to correct would introduce artificial variance in any comparison between years. Audit colleagues calculate the effect as being £177,000, but ignore the adjustments made in bringing forward expenditure from previous financial year such that the net effect of the adjustment is anticipated to have a trivial effect on bottom line of Accounts.

h. **Re-charges incorrectly classified in the Expenditure and Funding Analysis and the CIES**

Revised guidance received March 2017 now indicates that in respect of recharges that Statement of Accounts information should be prepared on the same basis as management information reported during the year. MCC's management information does not traditionally involve the regular recharging of central support services, as the focus is on central support managers having the same responsibility as service managers in managing their budgets, but given the timing of revised guidance it wasn't possible to alter arrangements retrospectively. The recharges exercise is commonly undertaken at the year-end as the Statement of Accounts service expenditure has historically been required to be prepared on a "Total Cost" basis. That total cost approach is still useful from a benchmarking and comparison point of view, and important in the consideration of service re-design or

outsourcing. Management advocate a period of reflection to decide the pro and cons of advocating changing the in-year management reporting or dismiss the year end recharging exercise for Statement of Accounts purposes.

In conclusion, given multiple demands on management's time, increasingly it is necessary to consider whether the additional efforts advocated by the audit process has an effect on the bottom line of the Accounts, and it is important to note that audit colleagues conclude the Accounts represent a "true and fair" despite these adjustments not being made.

Representations by Members of Monmouthshire County Council

We acknowledge that the representations made by management, above, have been discussed with us.

We acknowledge our responsibility for the preparation of true and fair financial statements in accordance with the applicable financial reporting framework. The financial statements were approved by Monmouthshire County Council on [Insert Date].

We confirm that we have taken all the steps that we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to you. We confirm that, as far as we are aware, there is no relevant audit information of which you are unaware.

Signed by:

Officer who signs on behalf of management

Date:

Signed by:

Officer or Member who signs on behalf of those charged with governance (director only for companies)

Date:

Appendix 2

Proposed audit report of the Auditor General to the Members of Monmouthshire County Council

I have audited the accounting statements and related notes of Monmouthshire County Council for the year ended 31 March 2017 under the Public Audit (Wales) Act 2004.

Monmouthshire County Council's accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement and the related notes.

The financial reporting framework that has been applied in their preparation is applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17 based on International Financial Reporting Standards (IFRSs).

Respective responsibilities of the responsible financial officer and the Auditor General for Wales

As explained more fully in the Statement of Responsibilities for the statement of accounts set out on page 6, the responsible financial officer is responsible for the preparation of the statement of accounts, which gives a true and fair view.

My responsibility is to audit the accounting statements and related notes in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the accounting statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements and related notes sufficient to give reasonable assurance that the accounting statements and related notes are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to Monmouthshire County Council's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the responsible financial officer and the overall presentation of the accounting statements and related notes.

In addition, I read all the financial and non-financial information in the narrative report to identify material inconsistencies with the audited accounting statements and related notes and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies, I consider the implications for my report.

Opinion on the accounting statements of Monmouthshire County Council

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of Monmouthshire County Council at 31 March 2017 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016-17.

Opinion on other matters

In my opinion, the information contained in the narrative report for the financial year for which the accounting statements and related notes are prepared is consistent with the accounting statements and related notes.

Matters on which I report by exception

I have nothing to report in respect of the following matters, which I report to you, if, in my opinion:

- adequate accounting records have not been kept;
- the accounting statements are not in agreement with the accounting records and returns; or
- I have not received all the information and explanations I require for my audit;
- the Governance Statement contains material misstatements of fact or is inconsistent with other information I am aware of from my audit.

Certificate of completion of audit

I certify that I have completed the audit of the accounts of Monmouthshire County Council in accordance with the requirements of the Public Audit (Wales) Act 2004 and the Code of Audit Practice issued by the Auditor General for Wales.

For and on behalf of

Huw Vaughan Thomas
Auditor General for Wales

[Insert Date] September 2017

Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

Appendix 3

Summary of corrections made to the draft financial statements which should be drawn to the attention of the members of Monmouthshire County Council

During our audit we identified the following misstatements that have been corrected by management, but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process.

Value of correction	Nature of correction	Reason for correction
£336,000	Note 12.10 Authority as Lessee "Not later than 1 year" decreased by £161000. "Later than one year and not later than five years" decreased by £175000.	Figures disclosed were picking up the wrong cell on working paper.
£2,775,000	Note 12.5 Capital Commitments Capital commitments was decreased by £2,775,000.	Amended disclosure as balance did not agree to supporting documentation.
£6,777,000	Note 12.11 Leases – Authority as Lessor Future minimum lease payments 2016/17 were decreased by £6,777,000. The comparative figure 2015/16 was also decreased by £3,019,000.	Error on the lifetimes leases as the Council had calculated the future minimum lease payments to year 2099. However, these leases have a notice period of 1 year and therefore, the minimum future lease payments would only be 1 year. This is in line with section 4.2.4.2 of the CIPFA Code 2016-17.
£1,525	Note 16.8 Senior Officer Remuneration Senior Officer Remuneration increased by £1,525.	Senior Officer remuneration has been increased as it did not include the Benefits-in-kind.
Narrative	Note 16.8 Senior Officer Remuneration Median salary increased from £20,456 to £21,057, and the ratio decreased from 5.43:1 to 5.28:1.	Population from which the Median salary is calculated include a duplicated employee and hence the median salary and remuneration ration were incorrectly calculated. It was checked that this employee had only been paid for one role and no issues identified.

Presentational	<p>Note 11.7 Grant income (Revenue Grants and Contributions)</p> <p>Sustainable Waste Management grant increased by £294,000 and Other WAG grants decreased by £294,000.</p>	Classification error within Revenue Grants and Contributions Note 11.7.
£592,403	<p>Note 13.4 Nature and Extent of risk arising from financial instruments (part c Credit Risk)</p> <p>The value disclosed for the impact of a 1% change in interest rates on the fair value of financial liabilities has been increased from £9,231,000 to £9,823,403.</p>	Amended disclosure as balance did not agree to supporting documentation.
Presentational	<p>Note 11.1 Adjustments from the General Fund to arrive at the CIES amounts</p> <p>Net change for pension adjustments 2105/16 increased by £324,000 and Other differences decreased by £324,000.</p>	The "Net change for pension adjustments" 2015/16 per Note 11.1 to the Expenditure and Funding Analysis does not agree to Note 10.2 "Adjustments between accounting basis and funding basis under regulations".
Narrative	<p>Note 12.7 Investment Properties</p> <p>Additional information added regarding the fair value hierarchy (i.e. levels 1, 2 & 3) of investment properties.</p>	Additional disclosure required to comply with sections 2.10.1.1 and 2.10.4.1. of the CIPFA Code 2016-17.
Presentational	<p>Note 11.2 Nature of Expenditure</p> <p>Note added detailing the nature of the expenses in the CIES, including depreciation and amortisation expense and employee benefits expense.</p>	Under section 3.4.2.43 of the CIPFA Code 2016-17 the Council are required to disclose a "Nature of Expenses" note.
Presentational	<p>Note 14.9 Summary of the movements in assets and liabilities</p> <p>All totals for the pension scheme years 2012/13 to 2106/17 had to be shifted one column left (i.e. to the prior year) and totals entered for 2016/17 as follows:</p> <ul style="list-style-type: none"> * Deficit on LG Pension Scheme £211,819 * Deficit on Teachers Unfunded Scheme £5,417 * Total Deficit £217,236 	Figures disclosed were picking up the wrong cell on working paper.

Presentational	<p>Note 16.6 Related Business Operations</p> <p>The comparative information for Dragon Waste, Y Prentis and Gwent Crematorium was for 31.03.15. These have been updated to reflect the year ended 31.03.16.</p> <p>There was inconsistent reporting of entities figures as some entities had "gross" trading figures (e.g. Gwent Archives, Gwent Crematorium & SRS Business Solutions Ltd), and some shown as percentage of shareholding (e.g. Project Gwyrdd & Dragon Waste Ltd). These have been updated to show the "gross" trading figures for all entities and Monmouthshire County Council's shareholding/interest clearly stated.</p>	Note was not presented in a consistent manor and potentially misleading for the user of the accounts.
Presentational	<p>Supporting notes added for material Balance Sheet items as follows:</p> <ul style="list-style-type: none"> * Long Term Debtors £4,240,000 * Deferred Capital Receipts £4,000,000 	Additional disclosure required to comply with the CIPFA Code 2016-17.
Presentational	<p>Note 11.1 Expenditure and Funding Analysis</p> <p>The following three lines disclosed in the EFA have been aggregated:</p> <ul style="list-style-type: none"> * Other operating expenditure * Financing and investment income and expenditure * Taxation and non-specific grant income and expenditure. 	Disclosure adjusted to comply with section 3.4.2.97 of the CIPFA Code 2016-17.

Wales Audit Office
24 Cathedral Road
Cardiff CF11 9LJ

Tel: 029 2032 0500

Fax: 029 2032 0600

Textphone.: 029 2032 0660

E-mail: info@audit.wales

Website: www.audit.wales

Swyddfa Archwilio Cymru
24 Heol y Gadeirlan
Caerdydd CF11 9LJ

Ffôn: 029 2032 0500

Ffacs: 029 2032 0600

Ffôn testun: 029 2032 0660

E-bost: post@archwilio.cymru

Gwefan: www.archwilio.cymru