For Action

PricewaterhouseCoopers LLP Audit Results Report on the Toronto Transit Commission Consolidated Financial Statements for the Year Ended December 31, 2017

Date: May 29, 2018
To: TTC Audit & Risk Management Committee
From: Chief Financial Officer

Summary

This report from the TTC's external auditors, PricewaterhouseCoopers LLP (PwC) outlines the results from the audit of the TTC's consolidated financial statements for the year ended December 31, 2017.

Recommendations

It is recommended that the TTC Audit and Risk Management Committee:

1. Approve the report; and

2. Approve forwarding a copy of the approved consolidated financial statements of the TTC to the TTC Board and then to the City Clerk for appropriate handling.

Implementation Points

This report requires approval at the May 29, 2018 TTC Audit & Risk Management Committee Meeting to ensure timely submission to the June 12, 2018 TTC Board Meeting and then to the July 13, 2018 Audit Committee Meeting of the City of Toronto.

Financial Summary

There are no financial implications resulting from the adoption of this report.

Equity/Accessibility Matters

This report and its recommendations have no accessibility or equity issues or impacts.

Decision History

The City of Toronto Act requires the city auditor (PwC) to annually audit the accounts and transactions of the City and its local boards and to express an opinion on their financial statements.

At its meeting on February 9, 2017, the TTC Audit & Risk Management Committee approved that the terms of reference of the Audit & Risk Management Committee include a requirement to “review with management and the external auditors the results of the audit, including any difficulties encountered”.

https://www.ttc.ca/About_the_TTC/Commission_reports_and_information/Committee_meetings/Audit_Risk_Management/2017/February_9/Reports/2_TTC_Audit_%20and_Risk_Management_Committee_Terms_Of_Referenc.pdf

Issue Background

The report presents the financial audit results of the consolidated financial statements of the TTC for the fiscal year December 31, 2017.

Comments

The consolidated financial statements of the TTC for the year ended December 31, 2017 were prepared by management. They were audited by PwC in accordance with the plan approved by the Audit & Risk Management Committee at its December 13, 2017 meeting.

http://www.ttc.ca/About_the_TTC/Commission_reports_and_information/Committee_meetings/Audit_Risk_Management/2016/October19/Reports/1_PWC_Consolidated_Financial_Statements_Audit_Plan_for_Year_.pdf

The attached report was prepared by PwC and it includes their comments on the significant accounting, auditing and reporting matters.

PwC proposes to issue an unqualified Independent Auditor’s Report on the 2017 consolidated financial statements (see Appendix A) once the outstanding items noted on page 1 have been completed.

Cathy Russell, Partner, Assurance of PwC will be at the Audit & Risk Management Committee meeting to present this report. You may wish to direct the auditors to address any specific areas.

Contact

Stephen Conforti, Head of Finance & Treasurer
(416) 393-3654
Stephen.Conforti@ttc.ca

Signature

Dan Wright
Chief Financial Officer

Attachments

Attachment 1 – 2017 year-end report to the Audit and Risk Management Committee www.pwc.com/ca

Toronto Transit Commission

2017 year-end report to the Audit and Risk Management Committee

Prepared as of May 17, 2018

pwc

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May 17, 2018

Members of the Audit and Risk Management Committee
of the Toronto Transit Commission
1900 Yonge Street
Toronto ON M4S 1Z2

Dear Members of the Audit and Risk Management Committee:

We have substantially completed our audit of the consolidated financial statements of the Toronto Transit Commission (TTC) prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP) established by the Public Sector Accounting Board (PSAB) of The Chartered Professional Accountants of Canada (CPA Canada) for the year ended December 31, 2017. We propose to issue an unqualified report on those financial statements, pending resolution of outstanding items outlined on page 2. Our draft auditor's report is included as Appendix A.

We prepared the accompanying report to assist you in your review of the financial statements. It includes an update on the status of our work, as well as a discussion on the significant accounting and financial reporting matters dealt with during the audit process. We will review the key elements of this report at the upcoming meeting and discuss our findings with you.

We would like to express our sincere thanks to the management and staff who have assisted us in carrying out our work, and we look forward to our meeting on May 29, 2018. If you have any questions or concerns prior to the meeting, please do not hesitate to contact me in advance.

Yours very truly,

PricewaterhouseCoopers LLP

Cathy Russell
Partner
Assurance

c.c.: Mr. D. Wright, Chief Financial Officer
Ms. T. Bal, Office of the Chief Financial Officer
Mr. S. Conforti, Head of Finance and Treasurer

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Communication to the Audit and Risk Management Committee

Key matters for discussion	*Comments*
Status of the audit	PricewaterhouseCoopers LLP (PwC or we) has substantially completed our audit of the consolidated financial statements (the financial statements). Significant outstanding items at time of mailing include the following: • receipt of City of Toronto confirmation for capital and operating subsidy revenue and receivables; • receipt of signed management representation letter; • receipt of response to legal confirmation letters from external and internal legal counsel; • the Board's approval of the financial statements; and • subsequent events procedures to the date of our auditor's report.
Significant accounting, auditing and reporting matters discussed with management	

Significant accounting estimates	In preparing the financial statements, there were a number of significant accounting estimates that required management judgment:
	• Assets in the Pension Fund Society
	  - The fair value measurement of certain complex investments, which are disclosed.
	• Property and liability claims (self-insured and insured liabilities)
	  - The measurement of the unsettled accident claims liability uses a number of estimates and actuarial assumptions.
	• Other significant accruals
	  - The financial statements include various other significant provisions, which are based on management judgement and historical experience.
	
	PwC work performed:
	• Pension plan complex investments
	  - We tested acquisitions of investments that occurred throughout the year, as well as reviewed the investments from date of acquisition to year-end for any indication of significant change in fair values. For investments held at fair value, we confirmed with investment managers and reviewed audited financial statements for the respective investment managers. For investments, where audited financial statements are not available, we assessed historical accuracy of net asset value provided by the investment managers. There were no issues identified as a result of our testing.
	• Property and liability claims (self-insured and insured liabilities)
	  - We utilized our PwC actuarial specialists in order to assess the reasonableness of the assumptions and methodology used by the TTC in recording the unsettled accident claims liability.

Key matters for discussion	*Comments*
	We further tested the accuracy and completeness of the data used in the calculation and our specialists independently projected a reserve estimate, which was compared to the estimate recorded by the TTC. No significant differences were noted. • Other significant accruals - We tested significant provisions by inquiring with management regarding estimates and methods used, reviewing supporting documentation and, where applicable, reviewing settlements after year-end. We also engaged our PwC internal specialists as required to assess the reasonability of the assumptions and methodology used by the TTC in recording certain other provisions. There were no issues identified as a result of our testing. **Conclusion:** Based on our audit work performed, we have concluded that the significant accounting estimates included in the financial statements are supportable within an acceptable range.
Management override of controls Canadian Auditing Standards require that the risk of material misstatement due to management override of controls be considered a significant risk on every audit engagement.	Management has implemented internal controls to ensure that appropriate segregation of duties have been established at the TTC in order to mitigate the risk of management override of controls. The TTC has policies and procedures in place to prevent and detect fraud, including a code-of-conduct, an internal audit department, an integrity hotline for employees and a process to review and approve journal entries. **PwC work performed:** In completing our audit, we are responsible for maintaining professional scepticism throughout our audit engagement, considering the potential for management override of controls. • We assessed the control environment to ensure there is appropriate segregation of duties and assessed manual controls established to mitigate this risk. • We reviewed the quarterly fraud investigation reports and the call log of the City Whistle-blower hotline and TTC integrity hotline. Further, we held discussions with management, internal legal counsel and the Staff Sergeant of Special Investigations. No significant items were noted in this review other than previously communicated. • We performed audit work over non-standard journal entries made during the year. • We reviewed assumptions used by management in making significant estimates for indicators of bias. • We incorporated unpredictable procedures into our audit approach. **Conclusion:** Based on our work performed, we found no circumstances that evidenced inappropriate management override of controls.

Key matters for discussion	***Comments***
Risk of fraud in revenue recognition Canadian Auditing Standards assume a rebuttable presumption, that there is a significant risk of fraud in revenue recognition in all businesses.	The TTC has processes, controls and other procedures in place to ensure that revenue is appropriately measured and recognized. As revenue derived from PRESTO devices has increased significantly in 2017, the reliability of controls in place at PRESTO is critical to ensuring the accuracy and completeness of PRESTO revenues. **PwC work performed:** • We updated our understanding of management's processes and internal controls surrounding revenue recognition and tested certain controls on which we take reliance for operating effectiveness. • We obtained the service auditor's report for the operating effectiveness of controls in place at PRESTO and performed testing on relevant user complementary controls in place at the TTC. • We obtained confirmation for PRESTO revenues and reconciled confirmed amounts to revenue amounts recorded. • We obtained confirmations from the City of Toronto for capital and operating subsidies received during the year and traced amounts to additional supporting documentation. • We tested significant revenue streams through substantive analytical procedures and tests of detail. **Conclusion:** Based on the results of our testing to date, we noted no issues with regard to revenue recognition.
SAP implementation	We would like to provide the Audit and Risk Management Committee with an update on the current status of our audit procedures with regard to the SAP implementation. The following are the activities carried out to date: **Critical configuration and security (IT general controls)** We have completed preliminary technical reviews on both the SAP HR environments and the SAP S/4 Hana environments. The results of the testing have been shared with management, and the project team is currently validating the results and determining appropriate action plans, where remediation may be required, or determining if mitigating controls exist. **Business process automated controls (calculations) and security testing** We are currently working with the project team to set up technical walkthroughs (designed to identify key automated controls, segregation of duties controls, interfaces and reports). Walkthroughs will be performed for processes where management deems that there is sufficient system stability. This will ensure that rework is kept to a minimum. Design and operational effectiveness testing will be performed upon the final scoping of key controls for financial audit purposes.

Key matters for discussion	*Comments*
	Program development controls We are currently in the process of completing the review of the system development controls (migration/testing/go-live approval, etc), and will provide an update to the Audit and Risk Management Committee should any significant issues arise. To date, we have not experienced any significant delays in completing our work. All work is in support of the 2018 audit. This did not have an impact on our 2017 audit.
Fraud and illegal acts	No fraud involving senior management, or employees with a significant role in internal control or that would cause a material misstatement of the financial statements and no illegal acts came to our attention as a result of our audit procedures. We wish to reconfirm that the Audit and Risk Management Committee is not aware of any known, suspected or alleged incidents of fraud or illegal acts not previously discussed with us.
Any matters involving known or suspected non-compliance with laws or regulations	No instances of known or suspected non-compliance with laws or regulations came to our attention as a result of our audit procedures. We wish to reconfirm whether the Audit and Risk Management Committee is aware of any known or suspected incidents of non-compliance with laws or regulations.
Summary of unadjusted items	Our final materiality was $38.0 million, which is consistent with the planning materiality previously communicated to the Audit and Risk Management Committee. As a result of our audit, we identified unadjusted items with an effect of a $5.2 million overstatement of surplus of revenue over expenses for the TTC. As a result of our audit, we conclude that the above unadjusted items are immaterial to the consolidated financial statements taken as a whole. Please see Appendix B for details of the unadjusted misstatements.
Internal controls recommendations	We have no significant internal control recommendations to report. We have noted one internal control recommendation as reported in Appendix C.
Independence	We confirm our independence with respect to the TTC in our annual independence letter, which is attached as Appendix E to this report.
Other information in documents containing audited financial information	Once it is completed, we will read the TTC Annual Report and consider whether the content or manner of presentation is materially consistent with the financial information covered by our auditor's report.

Key matters for discussion	*Comments*
Subsequent events	We have not been made aware of any subsequent events, which would impact the financial statements other than those disclosed. We will complete our subsequent events procedures to the date of our audit opinion. We wish to confirm whether the Audit and Risk Management Committee is aware of any subsequent events, which would impact the financial statements other than those disclosed.

Appendix A: Draft auditor's report

pwc

June @@, 2018

Independent Auditor's Report

To the Members of the Board of
the Toronto Transit Commission

We have audited the accompanying consolidated financial statements of the Toronto Transit Commission, which comprise the consolidated statement of financial position as at December 31, 2017 and the consolidated statements of operations and accumulated surplus, remeasurement gains and losses, net debt and cash flows for the year then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian public sector accounting standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audit is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Toronto Transit Commission as at December 31, 2017 and the results of its operations, remeasurement gains and losses, net debt and cash flows for the year then ended in accordance with Canadian public sector accounting standards.

Other matter

The accompanying consolidated financial statements schedule as at and for the year ended December 31, 2017 is presented as supplementary information only and is not a required part of the basic consolidated financial statements. The information in this schedule has been subject to audit procedures only to the extent necessary to express an opinion on the consolidated financial statements of the Toronto Transit Commission.

Chartered Professional Accountants, Licensed Public Accountants

Appendix B: Summary of unadjusted items

a. Unadjusted items

As a result of our audit, we noted the following item with an impact on the consolidated statement of financial position and consolidated statement of operations and accumulated surplus:

Description	*Current year surplus over/ (under) stated*	*Financial assets (over)/ under stated*	*Liabilities over/ (under) stated*	*Non-financial assets (over)/ under stated*	*Opening accumulated surplus over/ (under) stated*
#1 - Understatement of amortization expense for tangible capital assets retired during the year and revision to asset useful lives					
Dr. Amortization expense	$8,275,000				
Cr. Loss on disposal	($3,028,000)				
Cr. Tangible capital assets		($5,247,000)			
Total	**$5,247,000**	**($5,247,000)**	**$-**	**$-**	**$-**

Appendix C: Internal control recommendation

Inventory cycle counts not performed for certain inventory parts in the current year

Observation
Out of the 16 inventory items selected from the parts-not-counted report, it was noted that five items were erroneously omitted from the inventory counts in 2017. It was noted that these parts were active but that cycle counting, which is configured to ensure that each part is subject to an inventory count based on the inventory category, was not activated, resulting in these items being omitted for inventory cycle counting procedures.

Implication
Parts not subject to routine physical verification procedures could result in inaccurate or incomplete inventory amounts being reported, which may have an impact on the financial and operating results.

Recommendation
Monitoring over parts not counted should be performed on a periodic basis to ensure that all relevant spare parts are included in an appropriate count cycle.

Management response
Materials and Procurement is implementing a weekly review process related to this internal control recommendation. On a weekly basis, supervisors will review and compare to previous week's report from IFS detailing any active inventory parts that do not have cycle counting procedures activated. This will be in place by June 1, 2018.

Appendix D: Management representation letter

Client Letterhead

June @@, 2018

Ms. Cathy Russell, Partner
PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON M5J 0B2

We are providing this letter in connection with your audit of the consolidated financial statements of Toronto Transit Commission and its subsidiaries (together, TTC) as at December 31, 2017 and for the year then ended for the purpose of expressing an opinion as to whether such consolidated financial statements present fairly, in all material respects, the consolidated financial position, consolidated results of operations, consolidated remeasurement gains and losses, consolidated net debt and consolidated cash flows of TTC in accordance with Canadian public sector accounting standards.

A. Management's responsibilities

We have fulfilled our responsibilities, as set out in the terms of the audit engagement letter dated November 30, 2015. In particular, we confirm to you that:

- We are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with Canadian public sector accounting standards;
- We are responsible for designing, implementing and maintaining an effective system of internal control over financial reporting to enable the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error. In this regard, we are responsible for establishing policies and procedures that pertain to the maintenance of accounting systems and records, the authorization of receipts and disbursements, the safeguarding of assets and for reporting financial information;
- We have provided you with all relevant information and access, as agreed in the terms of the audit engagement; and
- All transactions have been recorded in the accounting records and are reflected in the consolidated financial statements.

We confirm the following representations:

B. Preparation of consolidated financial statements

The consolidated financial statements include all disclosures necessary for fair presentation in accordance with Canadian public sector accounting standards and disclosures otherwise required to be included therein by the laws and regulations to which TTC is subject.

We have appropriately reconciled our books and records (e.g. general ledger accounts) underlying the consolidated financial statements to their related supporting information (e.g. subledger or third party data). All related reconciling items considered to be material were identified and included on the reconciliations and were appropriately adjusted in the consolidated financial statements. There were no material unreconciled differences or material general ledger suspense account items that should have been adjusted or reclassified to another account balance. There were no material general ledger suspense account items written off to a balance sheet account, which should have been written off to a profit and loss account and vice versa. All consolidating entries have been properly recorded. All inter-governmental unit accounts have been eliminated or appropriately measured and considered for disclosure in the consolidated financial statements.

C. Accounting policies

We confirm that we have reviewed TTC's accounting policies and, having regard to the possible alternative policies, our selection and application of accounting policies and estimation techniques used for the preparation and presentation of the consolidated financial statements is appropriate in the TTC's particular circumstances to present fairly in all material respects its financial position, results of operations, remeasurement gains and losses and cash flows in accordance with Canadian public sector accounting standards.

D. Internal controls over financial reporting

We have designed disclosure controls and procedures to ensure material information relating to the TTC, including its consolidated subsidiaries is made known to us by others within those entities.

We have designed internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the consolidated financial statements for external purposes in accordance with Canadian public sector accounting standards.

We have not identified any significant deficiencies in the design or operation of disclosure controls and procedures and internal control over financial reporting as at December 31, 2016.

E. Minutes

All matters requiring disclosure to or approval of the Board of Directors or the shareholders have been brought before them at appropriate meetings and are reflected in the minutes.

F. Completeness of transactions

All contractual arrangements entered into by TTC with third parties have been properly reflected in the accounting records or/and, where material (or potentially material) to the consolidated financial statements, have been disclosed to you. We have complied with all aspects of contractual agreements that could have a material effect on the consolidated financial statements in the event of non-compliance. There are no side agreements or other arrangements (either written or oral) undisclosed to you.

G. Fraud

We have disclosed to you:

- The results of our assessment of the risk that the consolidated financial statements may be materially misstated as a result of fraud;
- All information in relation to fraud or suspected fraud of which we are aware affecting TTC involving management, employees who have significant roles in internal control or others where the fraud could have a material effect on the consolidated financial statements; and
- All information in relation to any allegations of fraud, or suspected fraud, affecting TTC's consolidated financial statements, communicated by employees, former employees, analysts, regulators or others.

H. Disclosure of information

We have provided you with:

- Access to all information of which we are aware that is relevant to the preparation of the consolidated financial statements, such as records, documentation and other matters including:
    - Contracts and related data;

- Information regarding significant transactions and arrangements that are outside the normal course of business;

- Minutes of the meetings of management and of the Board; including confidential minutes.

- Additional information that you have requested from us for the purpose of the audit; and

- Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

Except for the allegations of the employee benefit fraud discussed in the minutes of the November 12, 2015, meeting of the Audit and Risk Management Committee, we have no knowledge of any allegations of fraud or suspected fraud affecting the company received in communications from employees, former employees, analysts, regulators, short sellers, or others.

I. Compliance with laws and regulations

We have disclosed to you all aspects of laws, regulations and contractual agreements that may affect the consolidated financial statements, including actual or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

We are not aware of any illegal or possibly illegal acts committed by TTC's directors, officers or employees acting on TTC's behalf.

J. Accounting estimates and fair value measurements

Significant assumptions used by TTC in making accounting estimates, including fair value accounting estimates, are reasonable.

For recorded or disclosed amounts in the consolidated financial statements that incorporate fair value measurements, we confirm that:

- The measurement methods are appropriate and consistently applied;

- The significant assumptions used in determining fair value measurements represent our best estimates, are reasonable and have been consistently applied;

- No subsequent event requires adjustment to the accounting estimates and disclosures included in the consolidated financial statements; and

- The significant assumptions used in determining fair value measurements are consistent with TTC's planned courses of action. We have no plans or intentions that have not been disclosed to you, which may materially affect the recorded or disclosed fair values of assets or liabilities.

Significant estimates and measurement uncertainties known to management that are required to be disclosed in accordance with CPA Canada Public Sector Accounting Handbook Section PS 2130, *Measurement Uncertainty*, have been appropriately disclosed.

K. Related parties

We confirm that we have disclosed to you the identity of TTC's related parties as defined by Canadian Auditing Standard 550, and all the related party relationships and transactions.

The identity of, relationship, balances and transactions with related parties have been properly recorded and adequately disclosed in the consolidated financial statements, as required by CAS 550.

The list of related parties attached to this letter as Appendix A accurately and completely describes TTC's related parties and the relationships with such parties.

L. Going concern

We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the consolidated financial statements (e.g. to dispose of the business or to cease operations).

M. Assets and liabilities

We have satisfactory title or control over all assets. All liens or encumbrances on TTC's assets and assets pledged as collateral, to the extent material, have been disclosed in the notes to the consolidated financial statements.

We have recorded or disclosed, as appropriate, all liabilities, in accordance with Canadian public sector accounting standards. All liabilities and contingencies, including those associated with guarantees, whether written or oral, under which TTC is contingently liable in accordance with the CPA Canada Public Sector Accounting Handbook Section PS 3300, *Contingent Liabilities,* have been disclosed to you and are appropriately reflected in the consolidated financial statements.

N. Litigation and claims

All known actual or possible litigation and claims, which existed at the statement of financial position date or exist now, have been disclosed to you and accounted for and disclosed in accordance with Canadian public sector accounting standards, whether or not they have been discussed with legal counsel. The significant assumptions used in determining our best estimate for claims are reasonable and have been applied consistently. No subsequent event requires adjustment to any accounting estimate for claims included in the consolidated financial statements.

O. Misstatements detected during the audit

Certain representations in this letter are described as being limited to those matters that are material. Items are also considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement.

We confirm that the consolidated financial statements are free of material misstatements, including omissions.

The effects of the uncorrected misstatements in the consolidated financial statements, as summarized in the accompanying schedule (Appendix B), are immaterial, both individually and in the aggregate, to the consolidated financial statements taken as a whole. We confirm that we are not aware of any uncorrected misstatements other than those included in Appendix B.

There are no adjusted misstatements in the financial statements.

P. Events after balance sheet date

We have identified all events that occurred between the statement of financial position date and the date of this letter that may require adjustment of, or disclosure in, the consolidated financial statements, and have effected such adjustment or disclosure.

Q. Cash and banks

The books and records properly reflect and record all transactions affecting cash funds, bank accounts and bank indebtedness of TTC.

All cash balances are under the control of TTC, free from assignment or other charges, and unrestricted as to use, except as disclosed to you.

The amount shown for cash on hand or in bank accounts excludes trust or other amounts, which are not the property of TTC.

Arrangements with financial institutions involving compensating balances or other arrangements involving restrictions on cash balances, lines of credit, or similar arrangements have been properly disclosed.

All cash and bank accounts and all other properties and assets of TTC are included in the consolidated financial statements as at December 31, 2017.

R. Accounts receivable

All amounts receivable by TTC were recorded in the books and records.

Amounts receivable amounted to $99,402,000 and are considered to be fully collectible, except to the extent of $17,349,243 in respect of which, an appropriate allowance has been made in the accounts.

Amounts receivable are not subject to discount except for normal cash discounts which are appropriately provided for.

All receivables were free from hypothecation or assignment as security for advances to TTC, except as hereunder stated.

S. Portfolio investments and other financial assets

All securities and other financial assets that were owned by TTC were recorded in the accounts.

All income earned on the financial assets has been recorded in the accounts, and any interest income has been accrued using the effective interest rate method.

We are not aware of any objective evidence of impairment that would result in the recognition of an impairment loss on any financial asset.

There has been no activity in any dormant or inactive subsidiaries, business enterprises, partnerships, joint ventures or other participations, except as disclosed to you.

T. Inventory

Inventories classified as held for resale and held for consumption in the financial statements are stated at the lower of cost or net realizable value, cost being determined on the basis of weighted average cost, with due provision recorded to reduce all damaged, wholly or partially obsolete, or unusable inventories to their estimated selling price less estimated cost to sell. Inventory quantities at the balance sheet date were determined from physical counts or from TTC's perpetual inventory records, which have been adjusted on the basis of physical inventories taken by competent employees at year-end. Liabilities for amounts unpaid are recorded for all items included in inventories at balance sheet dates and all quantities billed to customers at those dates are excluded from the inventory balances.

A provision has been made to reduce excess or obsolete inventories held for resale to their estimated net realizable value.

There have been no events conditions or changes in circumstances that indicate inventory held for consumption will no longer be used or consumed in TTC's operations.

U. Tangible capital assets

All charges to tangible capital asset accounts represented the actual cost of additions to tangible capital assets.

No significant tangible capital asset additions were charged to repairs and maintenance or other expense accounts.

Book values of tangible capital assets sold, destroyed, abandoned or otherwise disposed of have been eliminated from the accounts.

Capital assets owned by TTC are being depreciated on a systematic basis over their estimated useful lives, and the provision for depreciation was calculated on a basis consistent with that of the previous date. During the year, we reviewed the appropriateness of the depreciation policy and estimate of useful lives for tangible capital assets, taking into account all pertinent factors. Any changes in our assessment from the prior year have been adequately disclosed and reflected in the consolidated financial statements.

All lease agreements covering assets leased by or from TTC have been disclosed to you and classified as leased tangible capital assets or operating leases.

There have been no events, conditions or changes in circumstances that indicate that a tangible capital asset no longer contributes to TTC's ability to provide goods and services or that the value of future economic benefits associated with the tangible capital asset is less than its net book value. We believe that the carrying amount of TTC's long-lived tangible capital assets is fully recoverable in accordance with CPA Canada Public Sector Accounting Handbook PS 3150.

V. Deferred revenue

All material amounts of deferred revenue and deferred contributions were appropriately recorded in the books and records.

W. Retirement benefits, post-employment benefits, compensated absences and termination benefits

All arrangements to provide retirement benefits, post-employment benefits, compensated absences and termination benefits have been identified to you and have been included in the actuarial valuation as required.

The actuarial valuations incorporate management's best estimates, as detailed in note 9 of the consolidated financial statements.

The actuarial assumptions and methods used to measure liabilities and costs for financial accounting purposes for pension and other post-retirement benefits are appropriate in the circumstances.

The TTC does not plan to make frequent amendments to the pension or other post-retirement benefit plans.

All changes to the plan and the employee group and the plan's performance since the last actuarial valuation have been reviewed and considered in determining the pension plan expense and the estimated actuarial present value of accrued pension benefits and value of pension plan assets where latest actuarial valuation for accounting purposes is not at the balance sheet date.

TTC's actuaries have been provided with all information required to complete their valuation as at January 1, 2017 and their extrapolation to December 31, 2017.

We confirm that the extrapolations are accurate and include the proper reflection of the effects of changes and events occurring subsequent to the most recent valuation that had a material effect on the extrapolation.

The employee future benefit costs, assets and obligations have been determined, accounted for and disclosed in accordance with CPA Canada Public Sector Accounting Handbook PS 3250, *Retirement Benefits* and CPA Canada Public Sector Accounting Handbook PS 3255, *Post-employment Benefits, Compensated Absences and Termination Benefits.*

The significant accounting policies that TTC has adopted in applying CPA Canada Public Sector Accounting Handbook Section PS 3250 and CPA Canada Public Sector Accounting Handbook Section PS 3255 are accurately and completely disclosed in the notes to the consolidated financial statements.

Each of the best estimate assumptions used reflects management's judgment of the most likely outcomes of future events.

The best estimate assumptions used are, as a whole, internally consistent, and consistent with the asset valuation method adopted.

The discount rate used to determine the accrued benefit obligation was determined by reference to the City of Toronto's borrowing rate using assumptions that are internally consistent with other actuarial assumptions used in the calculation of the accrued benefit obligation and plan assets.

The assumptions included in the actuarial valuation are those that management instructed Mercer and Aon Hewitt to use in computing amounts to be used by management in determining pension costs and obligations and in making required disclosures in the above-named consolidated financial statements, in accordance with CPA Canada Public Sector Accounting Handbook Section PS 3250. In arriving at these assumptions, management has obtained the advice of the above mentioned consulting actuaries who assisted in reaching best estimates, but has retained the final responsibility for them.

The source data and plan provisions provided to the actuary for preparation of the actuarial valuation are accurate and complete.

The disclosure of the TTC's share of the risks and benefits under joint defined benefit plans, the total financial status of any joint plans, significant policies and a description of the unique nature and terms of any joint plans are accurate and complete.

All changes to plan provisions or events occurring subsequent to the date of the actuarial valuation and up to the date of this letter have been considered in the determination of pension costs and obligations and as such have been communicated to you as well as to the actuary.

X. Environmental matters

There are no liabilities or contingencies arising from environmental matters that have not already been disclosed to the auditor.

Liabilities or contingencies related to environmental matters have been recognized, measured and disclosed, as appropriate, in the consolidated financial statements.

We have considered the effect of environmental matters and the carrying value of the relevant assets is recognized, measured and disclosed, as appropriate, in the consolidated financial statements.

All commitments related to environmental matters have been measured and disclosed, as appropriate in the consolidated financial statements.

Y. Consolidations

We confirm that the TTC has 100% ownership of the Toronto Coach Terminal Inc., Toronto Transit Commission Insurance Company Limited, and the Toronto Transit Commission. Accordingly, they are controlled entities of the TTC. The Toronto Transit Commission Sick Benefit Association is also controlled by the TTC. We also confirm that there is insignificant activity in Toronto Transit Infrastructure Limited and the Toronto Transit Commission Sick Benefit Association.

Z. Use of a specialist

We assume responsibility for the findings of specialists in evaluating the employee benefit obligation and have adequately considered the qualifications of the specialists in determining the amounts and disclosures used in the consolidated financial statements and underlying accounting records. We did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an impact on the independence or objectivity of the specialists.

AA. Derivative financial instruments

The TTC has recognized, and recorded at fair value, all embedded derivative instruments that are required to be separated from their host contracts, in accordance with CPA Canada Public Sector Accounting Handbook Section PS 3450, *Financial Instruments.*

The TTC has recognized and recorded at fair value all non-financial derivatives that are included within the scope of CPA Canada Public Sector Accounting Handbook Section PS 3450, *Financial Instruments.*

We confirm that our objectives with respect to derivative financial instruments are for hedging purposes.

We confirm that the:

- The records reflect all transactions involving derivative financial instruments; and
- The assumptions and methodologies used in the valuation models applied to derivative financial instruments are reasonable.

All transactions involving derivative financial instruments have been conducted at arm's length and at fair values.

We have disclosed to you the terms of transactions involving derivative financial instruments.

There are no side agreements associated with any derivative financial instruments.

BB. General

There are no proposals, arrangements or actions completed, in process, or contemplated that would result in the suspension or termination of any material part of TTC's operations.

Information relative to any matters handled on behalf of TTC by any legal counsel, including all correspondence and other files, has been made available to you.

CC. Government transfers

We have disclosed all significant terms and agreements in respect of transfers received from governments.

Transfers without eligibility criteria or stipulations have been recognized as revenue once the transfer has been authorized.

Transfers with eligibility criteria but without stipulations have been recognized as revenue once the transfer has been authorized and all eligibility criteria have been met.

Transfers with or without eligibility criteria but with stipulations have been recognized as revenue in the year the transfer has been authorized and all eligibility criteria have been met, except when, and to the extent that, the transfer gives rise to an obligation that meets the definition of a liability for the recipient government in accordance with CPA Canada Public Sector Accounting Handbook PS 3200, *Liabilities*.

DD. Budgetary data

We have included budgetary data in our consolidated financial statements, which is relevant to the users of the consolidated financial statements and consistent with that originally planned and approved. Planned results were presented for the same scope of activities and on a basis consistent with that used for actual results.

Yours truly,

Toronto Transit Commission

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Mr. Rick Leary, Chief Executive Officer (Acting)

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Mr. Dan Wright, Chief Financial Officer

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Ms. Tara Bal, Office of the Chief Financial Officer

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Mr. Stephen Conforti, Head of Finance & Treasurer

____

Mr. Alex Cassar, Director – Budgets, Costing and Financial Reporting

____

Ms. Donna Florindi, Manager – Capital Accounting

____

Ms. Teresa Coelho, Manager – Financial Statements

____

Ms. Angelet Lim– Accounting Policy & Financial Reporting

Appendix A - List of related parties

- City of Toronto
- Toronto Coach Terminal Inc.
- Toronto Transit Commission Insurance Company Limited
- The TTC Sick Benefit Association
- The TTC Pension Fund Society
- Toronto Waterfront Revitalization Corporation (TWRC)
- Toronto Hydro Corporation
- Toronto Parking Authority

Appendix B: Summary of unadjusted items

As a result of the audit, the following items were noted with an impact on the consolidated statement of financial position and consolidated statement of operations and accumulated surplus.

Description	*Current Year Surplus Over/ (Under) Stated*	*Financial Assets (Over)/ Under Stated*	*Liabilities Over/ (Under) Stated*	*Non-Financial Assets (Over)/ Under Stated*	*Opening Accumulated Surplus Over/ (Under) Stated*
#1 - Understatement of amortization expense for tangible capital assets retired during the year and revision to asset useful lives					
Dr. Amortization expense	$8,275,000				
Cr. Loss on disposal	($3,028,000)				
Cr. Tangible capital assets		($5,247,000)			
Total	**$5,247,000**	**(5,247,000)**	**$-**	**$-**	**$-**

The above unadjusted items are immaterial - individually and in total - to the consolidated financial statements taken as a whole.

Appendix C: Internal control recommendations

Cyclic inventory counted not performed for certain inventory parts

Observation
Out of the 16 inventory items selected from the parts-not-counted report, it was noted that 5 items were erroneously omitted from the inventory counts in 2017. It was noted that these parts were active but that cycle counting, which is configured to ensure that each part is subject to an inventory count based on the inventory category, was not activated, resulting in these items being omitted for inventory cycle counting procedures.

Implication
Parts not subject to routine physical verification procedures could result in inaccurate or incomplete inventory amounts being reported, which may have an impact on the financial and operating results.

Recommendation
Monitoring over parts not counted should be performed on a periodic basis to ensure that all relevant spare parts are included in an appropriate count cycle.

Management response
Materials and Procurement is implementing a weekly review process related to this internal control recommendation. On a weekly basis, supervisors will review and compare to previous week's report from IFS detailing any active inventory parts that do not have cycle counting procedures activated. This will be in place by June 1, 2018.

Appendix E: Independence letter

May 17, 2018

Members of the Audit and Risk Management Committee of
the Toronto Transit Commission
1900 Yonge Street
Toronto ON M4S 1Z2

Dear Members of the Audit and Risk Management Committee:

We have been engaged to audit the consolidated financial statements of the Toronto Transit Commission (the TTC) for the year ended December 31, 2017.

Canadian generally accepted auditing standards require that we communicate at least annually with you regarding all relationships between the TTC, its management and us that may reasonably be thought to bear on our independence.

In determining which relationships to report, these standards require us to consider The Rules of Professional Conduct of the Chartered Professional Accountants of Ontario and applicable legislation covering such matters as:

a. holding a financial interest, either directly or indirectly, in a client;
b. serving as an officer or director of a client;
c. performance of management functions for an assurance client;
d. personal or business relationships of immediate family, close relatives, partners or retired partners, either directly or indirectly, with a client or its management;
e. economic dependence on a client;
f. long association of senior personnel with a listed entity audit client;
g. the Audit and Risk Management Committee's approval of services to a listed entity audit client; and
h. provision of services in addition to the audit engagement.

We have prepared the following comments to facilitate our discussion with you regarding independence matters arising since May 24, 2017, the date of our last letter.

We are not aware of any relationships between us and the company or its management that may reasonably be thought to bear on our independence that have occurred from May 24, 2017 to May 17, 2018.

The total fees charged to the company for audit services were $74,500 during the period from January 1, 2017 to December 31, 2017, which includes the audit of Toronto Transit Commission Insurance Corporation.

We hereby confirm that we are independent with respect to the TTC within the meaning of The Rules of Professional Conduct of the Chartered Professional Accountants of Ontario as of May 17, 2018.

PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto, Ontario, Canada M5J 0B2
T: +1 416 863 1133, F: +1 416 365 8215, www.pwc.com/ca

This letter is intended solely for the use of the Audit and Risk Management Committee, the Board of Directors, management and others within the TTC and should not be used for any other purpose.

We look forward to discussing with you the matters addressed in this letter at our upcoming meeting on May 29, 2018.

Yours very truly,

PricewaterhouseCoopers LLP

Chartered Professional Accountants