



For Action

KPMG LLP Audit Findings Report on the Toronto Transit Commission Consolidated Financial Statements for the Year Ended December 31, 2021

Date: June 23, 2022

To: TTC Board

Summary

The subject report was reviewed by the TTC Audit & Risk Management Committee on June 9, 2022 and is forwarded to the TTC Board for its consideration.

Recommendations

It is recommended that the TTC Board:

1. Receive the KPMG LLP Audit Findings Report on the Toronto Transit Commission Consolidated Financial Statements for the Year Ended December 31, 2021; and
2. Forward a copy of this report to the City Clerk for submission to the City of Toronto Audit Committee.

Attachments

Attachment 1 – KPMG LLP Audit Findings Report on the Toronto Transit Commission Consolidated Financial Statements for the Year Ended December 31, 2021



KPMG LLP Audit Findings Report on the Toronto Transit Commission Consolidated Financial Statements for the Year Ended December 31, 2021

Date: June 9, 2022
To: TTC Audit and Risk Management Committee
From: Chief Financial Officer

Summary

This report from the TTC's external auditors, KPMG LLP (KPMG), outlines the results from the audit of the TTC's consolidated financial statements for the year ended December 31, 2021.

Recommendations

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

1. Approve this report; and
2. Forward a copy of this report to the TTC Board for its meeting of June 23, 2022 and subsequently to the City Clerk for appropriate handling to the next City Audit Committee meeting.

Implementation Points

This report requires approval at the June 9, 2022 TTC Audit and Risk Management Committee meeting to ensure timely submission to the June 23, 2022 TTC Board meeting and then to the Audit Committee meeting of the City of Toronto.

Financial Summary

There are no financial implications resulting from the adoption of this report. The attachment summarizes KPMG's findings from the audit of TTC's 2021 consolidated financial statements.

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 (KPMG) 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 and Risk Management Committee approved that the terms of reference of the Audit and Risk Management Committee include a requirement to “review with management and the external auditors the results of the audit, including any difficulties encountered.” The Audit and Risk Management Committee’s terms of reference can be accessed by the following link:

https://ttc-cdn.azureedge.net/-/media/Project/TTC/DevProto/Documents/Home/Public-Meetings/Audit-and-Risk-Management/2017/Feb-9/2_TTC_Audit_and_Risk_Management_Committee_Terms_Of_Referenc.pdf?rev=40d4ed703a344b1e8d1816787cd3cabc&hash=F50FB7E52C62C3CFEE7A8D3A1AEB2758

Issue Background

This report presents the financial audit results of the consolidated financial statements of the TTC for the fiscal year ended December 31, 2021.

Comments

The consolidated financial statements of the TTC for the year ended December 31, 2021 were prepared by management. They were audited by KPMG in accordance with the plan approved by the Audit and Risk Management Committee at its December 2, 2021 meeting.

<https://ttc-cdn.azureedge.net/-/media/Project/TTC/DevProto/Documents/Home/Public-Meetings/Audit-and-Risk-Management/2021/December-02/1KPMGLLPsAuditPlanforYearEnde-December-31-2021.pdf?rev=9b508007eb744659a847a9c927807645&hash=75938F65FCD7A4A0ED93825A59C064AA>

The attached report was prepared by KPMG and it includes the auditors’ comments on significant accounting, auditing and reporting matters.

KPMG proposes to issue an unqualified Independent Auditor’s Report on the 2021 consolidated financial statements (see Appendix 6 within Attachment 1) once the outstanding items noted on page 4 have been completed.

Kevin Travers, the Audit Partner from KPMG, will be at the TTC Audit and Risk Management Committee meeting to present this report. Committee members may wish to request the auditors to address any specific areas related to the audit.

Contact

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Signature

Josie La Vita
Chief Financial Officer

Attachments

Attachment 1 – Toronto Transit Commission Audit Findings Report for the year ended December 31, 2021

Toronto Transit Commission

Audit Findings Report
for the year ended December 31, 2021

KPMG LLP

Licensed Public Accountants

Prepared May 3, 2022 for presentation to the Audit
and Risk Management Committee on June 9, 2022

kpmg.ca/audit

KPMG



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Our refreshed Values

What we believe



We do what is right.



We never stop learning
and improving.



We think and act boldly.



We respect each other
and draw strength from
our differences.



We do what matters.



Audit Quality: How do we deliver audit quality?

Quality essentially means doing the right thing and remains our highest priority. Our **Global Quality Framework** outlines how we deliver quality and how every partner and staff member contributes to its delivery.

‘**Perform quality engagements**’ sits at the core along with our commitment to continually monitor and remediate to fulfil on our quality drivers.

Our **quality value drivers** are the cornerstones to our approach underpinned by the **supporting drivers** and give clear direction to encourage the right behaviours in delivering audit quality.

We define ‘**audit quality**’ as being the outcome when:

- audits are **executed consistently**, in line with the requirements and intent of **applicable professional standards** within a strong **system of quality controls**; and
- all of our related activities are undertaken in an environment of the utmost level of **objectivity, independence, ethics, and integrity**.



Visit our [Resources](#) page for more information.

Doing the right thing. Always.

Executive summary

Purpose of this report¹

The purpose of this report is to assist you, as a member of the Audit and Risk Management Committee, in your review of the results of our audit of the consolidated financial statements (“financial statements”) of the Toronto Transit Commission (“the Entity”) as at and for the period ended December 31, 2021.

Status of the audit

As of the date of this report, we have completed the audit of the financial statements, with the exception of certain remaining procedures, which include:

- Completing our discussions with the Audit and Risk Management Committee;
- Obtaining evidence of the Board’s approval of the financial statements;
- Subsequent event procedures up to the financial statement approval date; and
- Receipt of the signed management representation letter (to be signed upon approval of the financial statements).

We will update you on significant matters, if any, arising from the completion of the audit, including the completion of the above procedures.

Our auditors’ report, a draft of which is provided in Appendix 6: Draft Auditors’ Report, will be dated upon the completion of any remaining procedures.

Significant changes from the audit plan

There were no significant changes to our audit plan which was originally communicated to you in the audit planning report. Included in this report are the more significant findings from the audit, that we have determined appropriate to communicate to you.

Significant risks and other significant matters

There are no significant findings to communicate related to significant risks or other significant matters.

Uncorrected and corrected audit differences

Refer to page 13 of this report for uncorrected and corrected audit differences.

¹ This Audit Findings Report should not be used for any other purpose or by anyone other than the Audit and Risk Management Committee, TTC Board of Directors and City of Toronto Audit Committee. KPMG shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this Audit Findings Report has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

Executive summary (continued)

Control deficiencies

We did not identify any control deficiencies that we determined to be significant deficiencies in internal control over financial reporting. A significant deficiency in internal control is a deficiency, or combination of deficiencies, in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance.

Significant accounting policies and practices

There have been no initial selections of, or changes to, significant accounting policies and practices to bring to your attention.

Independence

We are independent with respect to the Toronto Transit Commission, within the meaning of the relevant rules and related interpretations prescribed by the relevant professional bodies in Canada and any other standards or applicable legislation or regulation.

Accounting estimates

Overall, we are satisfied with the reasonability of accounting estimates. The main areas of estimates relate to: unsettled accident claims, valuation of employee future benefits and contingent liabilities.

Audit risks and results

We highlight our significant findings in respect of **significant financial reporting risks** as identified in our discussion with you in the Audit Plan, as well as any additional significant financial reporting risks identified.

Significant financial reporting risk	Estimate?
Risk of material misstatement due to fraud resulting from management override of controls.	No
Our response	
<p>As this presumed risk of material misstatement due to fraud is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk.</p> <p>Our procedures included:</p> <ul style="list-style-type: none">– Testing of journal entries and other adjustments.– Performing a retrospective review of estimates.– Evaluating the business rationale of significant unusual transactions.	
Significant findings	
<ul style="list-style-type: none">– We did not identify any issues or concerns regarding management override of controls.	

Audit risks and results (continued)

Significant financial reporting risk	Estimate?
Risk of material misstatement due to fraud resulting from fraudulent revenue recognition.	No
Our response	
<p>This is a presumed risk of material misstatement due to fraud. Audit standards require us to assume there are generally pressures/incentives on management to commit fraudulent financial reporting through inappropriate revenue recognition. This can be perpetrated through revenue cut-off or manual journal entries and other adjustments related to revenue recognition.</p> <p>Our procedures included:</p> <ul style="list-style-type: none"> – Evaluating the design and implementation of selected relevant controls. – We tested journal entries over accounts that are susceptible to manipulation through management override. We also designed search filters that allowed us to identify any unusual journal entries. – To address the inherent risk of error in revenue recognition, we substantively tested revenues and deferred revenue, including cut-off procedures. 	
Significant findings	
<ul style="list-style-type: none"> – We did not identify any issues related to fraud risk associated with revenue recognition. 	

Audit risks and results (continued)

We summarize our audit approach and findings in respect of **areas of focus** as identified in our discussion with you in the Audit Plan.

Area of Focus	Estimate?
Passenger Services Revenue	No
Our response	
<p>Total passenger services revenue for the year was \$456M (2020 - \$516M). Of this amount, passenger services revenue earned related to PRESTO was \$408M (2020 - \$474M). Additionally, there was unearned revenue from PRESTO of \$5M (2020 - \$7M), which is recorded as deferred revenue as at December 31, 2021, and will be recognized as revenue in fiscal 2022. As passenger services revenue is significant, in our testing, we took a combined approach to test the operating effectiveness of controls, and substantively test the account balance.</p> <p>Our procedures included:</p> <ul style="list-style-type: none"> – We obtained an understanding of management’s processes surrounding passenger services revenue, including PRESTO revenue, and analyzed the revenue recognition policy in the context of the Public Sector Accounting Standards (“PSAS”) on revenue recognition. – We obtained direct third-party confirmation of passenger revenue from Metrolinx and reconciled the amounts from the confirmation to the total revenue amounts reflected in the TTC financial reporting records, as well as deferred revenue amounts. Additionally, we reviewed the relevant service agreements between Metrolinx and the Toronto Transit Commission. – We reviewed a sample of monthly reconciliations performed by management, which reconciles TTC records to Metrolinx data to bank payment. – We performed control testing over the cash and ticket collection process. – We vouched cash deposits to supporting documentation and reconciled bank deposits to the general ledger. – We obtained and reviewed the service auditor’s report for the operating effectiveness of controls in place at PRESTO (CSAE 3416). 	
Significant findings	
<ul style="list-style-type: none"> – No exceptions were noted during testing. 	

Audit risks and results (continued)

Area of Focus	Estimate?
<p>Unsettled Accident Claims</p>	<p>Yes – Unsettled accident claims is a calculation as determined by actuarial experts. This calculation involves numerous inputs and assumptions.</p>
<p>Our response</p>	
<p>Unsettled accident claims represent a liability computed by management’s actuarial expert, based on an actuarial assessment of the claims liability on the basis mandated by the Financial Services Regulatory Authority of Ontario. As the unsettled accident claims is a significant and complex estimate, KPMG actuarial specialists were involved in completing the audit procedures.</p> <p>Our procedures included:</p> <ul style="list-style-type: none"> – Review of the actuarial reports prepared by management actuarial expert for determining unsettled accident claims. – Assess the competence, capability and objectivity of the actuary and evaluate adequacy of their work. – Review the methodology and underlying assumptions used to formulate management’s estimate. – Perform testing of underlying data contained in valuation to source data. – Perform testing over claims reserve set-up process and claim payment process. 	
<p>Significant findings</p>	
<ul style="list-style-type: none"> – No significant differences were identified during our audit testing. – We found management’s estimate to be reasonable overall in the context of our materiality. 	

Audit risks and results (continued)

Area of Focus	Estimate?
<p>Employee Future Benefits Liabilities</p>	<p>Yes – Employee future benefits is a calculation as determined by actuarial experts. This involves numerous inputs and assumptions</p>
<p>Our response</p>	
<p>The TTC’s employee benefit plans include post-employment plans, post-retirement plans, and pension plans. As at December 31, 2021, the liability amount was \$850M (2020 - \$784M). Employee future benefits represent a liability computed by management’s actuarial experts. As the employee future benefits liabilities are significant and complex estimates, KPMG actuarial specialists were involved in completing the audit procedures.</p> <p>Our procedures included:</p> <ul style="list-style-type: none"> – Review of the actuarial reports prepared by management actuarial experts for determining employee future benefits liabilities. – We obtained assistance from KPMG actuarial specialists to review the methodology and assumptions used by management experts for the determination of the employee future benefit liabilities. – Assess the competence, capability and objectivity of management’s actuary and evaluate adequacy of their work. – Review the methodology and underlying assumptions used to formulate management’s estimate. – Perform testing of underlying data contained in valuation to source documentation. 	
<p>Significant findings</p>	
<ul style="list-style-type: none"> – No significant differences were identified during our audit testing. – We found management’s estimate to be reasonable overall in the context of our materiality. 	

Audit risks and results (continued)

Area of Focus	Estimate?
<p>Tangible Capital Assets</p>	<p>Yes - Estimate is involved in determining useful lives of assets. Useful lives of assets are determined based on asset categories and are consistent year over year.</p>
<p>Our response</p>	
<p>The net book value of tangible capital assets (“TCA”) as at December 31, 2021 was \$12.4 billion (2020 – \$12.3 billion). During the year, the TTC recognized \$865M (2020 - \$829M) in additions to TCA. During the year, TTC incurred an amortization expense of \$723M (2020 - \$659M).</p> <p>Our procedures included:</p> <ul style="list-style-type: none"> – We obtained an understanding of management’s processes for accounting for tangible capital assets. – We reviewed on a sample basis, the additions to tangible capital assets and noted that management has appropriately capitalized the additions from construction in progress to capital assets. We vouched a sample of capital additions to supporting documentation which included non-labour, labour, and overhead costs. – For non-labour costs capitalized as TCA, KPMG obtained invoices and Certificates of Progress to verify accuracy and existence of these costs. – For labour costs capitalized as TCA, KPMG obtained and vouched a sample of labour costs to approved timesheets to verify accuracy and existence of these costs. KPMG also evaluated the nature of work performed per timesheets to determine if these costs meet the capitalization criteria as per the requirements in the financial reporting framework. – For overhead allocation, KPMG obtained an understanding of and reviewed management’s allocation process and performed recalculation. – KPMG reviewed that amortization expense is consistent with the TTC significant accounting policies, and recalculated amortization during the year based on the useful lives. 	
<p>Significant findings</p>	
<ul style="list-style-type: none"> – No exceptions were noted during testing. 	

Financial statement presentation and disclosure

Misstatements, including omissions, if any, related to presentation and disclosure items are in the management representation letter.

We also highlight the following:

Financial statement presentation - form, arrangement, and content

The form, arrangement and content of the financial statements is adequate.

Significant qualitative aspects of financial statement presentation and disclosure

We did not note any material disclosure omissions in the financial statements.

Uncorrected and corrected audit differences

Differences and adjustments include disclosure and presentation differences and adjustments.

Professional standards require that we request of management and the Audit and Risk Management Committee that all identified differences be corrected.

Uncorrected audit differences

Refer to the management representation letter in Appendix 7, which discloses the impact of all uncorrected differences considered to be other than clearly trivial.

We did not identify any factual differences. We concur with management's representation that the judgmental uncorrected difference noted is not material to the financial statements. Accordingly, the uncorrected difference has no effect on our auditors' report.

Corrected audit differences

We did not identify any misstatements that were communicated to management and subsequently corrected in the financial statements.

Appendices

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Appendix 1: Other required communications

Appendix 2: Current developments

Appendix 3: Upcoming changes to auditing standards

Appendix 4: KPMG's system of quality control

Appendix 5: Audit and assurance insights

Appendix 6: Draft auditors' report

Appendix 7: Management representation letter

**Appendix 8: Why Audit Committees should know about
Asset Retirement Obligations**



Appendix 1: Other required communications

Audit findings report

This document.

Engagement terms

A copy of the engagement letter has been provided to the Board and the Audit and Risk Management Committee.

Audit planning report

We have provided our audit planning report to the Board and Audit and Risk Management Committee.

Representations of management

A copy of the management representation letter is attached.

Matters pertaining to independence

All matters related to independence are dealt with directly by the group audit team. We confirm that we are independent of the Entity in accordance with the requirements under the external auditing standards.

Management letter

From time to time, we may identify improvement observations as we conduct our audit procedures. These recommendations will be communicated to management through a management letter.

Appendix 2: Current developments

Title	Details	Link
Public Sector Update – connection series	Public Sector Accounting Standards are evolving – Get a comprehensive update on the latest developments from our PSAB professionals. Learn about current changes to the standards, active projects and exposure drafts, and other items.	Contact your KPMG team representative to sign up for these webinars. Public Sector Minute Link

The following are upcoming changes that will be effective in future periods as they pertain to Public Sector Accounting Standards. We have provided an overview of what these standards are and what they mean to your financial reporting so that you may evaluate any impact to your future financial statements.

Standards	Summary and implications
Asset Retirement Obligations	<ul style="list-style-type: none"> – The new standard is effective for fiscal years beginning on or after April 1, 2022. – The new standard addresses the recognition, measurement, presentation and disclosure of legal obligations associated with retirement of tangible capital assets in productive use. Retirement costs will be recognized as an integral cost of owning and operating tangible capital assets. PSAB currently contains no specific guidance in this area. – The ARO standard will require the public sector entity to record a liability related to future costs of any legal obligations to be incurred upon retirement of any controlled tangible capital assets (“TCA”). The amount of the initial liability will be added to the historical cost of the asset and amortized over its useful life. – As a result of the new standard, the public sector entity will have to: <ul style="list-style-type: none"> • Consider how the additional liability will impact net debt, as a new liability will be recognized with no corresponding increase in a financial asset; • Carefully review legal agreements, senior government directives and legislation in relation to all controlled TCA to determine if any legal obligations exist with respect to asset retirements; • Begin considering the potential effects on the organization as soon as possible to coordinate with resources outside the finance department to identify AROs and obtain information to estimate the value of potential AROs to avoid unexpected issues.
Revenue	<ul style="list-style-type: none"> – The new standard is effective for fiscal years beginning on or after April 1, 2023. – The new standard establishes a single framework to categorize revenues to enhance the consistency of revenue recognition and its measurement. – The standard notes that in the case of revenues arising from an exchange transaction, a public sector entity must ensure the recognition of revenue aligns with the satisfaction of related performance obligations. – The standard notes that unilateral revenues arise when no performance obligations are present, and recognition occurs when there is authority to record the revenue and an event has happened that gives the public sector entity the right to the revenue.

Public Private Partnerships (“P3”)

- PSAB has introduced Section PS3160, which includes new requirements for the recognition, measurement and classification of infrastructure procured through a public private partnership. The standard has an effective date of April 1, 2023, and may be applied retroactively or prospectively.
- The standard notes that recognition of infrastructure by the public sector entity would occur when it controls the purpose and use of the infrastructure, when it controls access and the price, if any, charged for use, and it controls any significant interest accumulated in the infrastructure when the P3 ends.
- The public sector entity recognizes a liability when it needs to pay cash or non-cash consideration to the private sector partner for the infrastructure.
- The infrastructure would be valued at cost, which represents fair value at the date of recognition with a liability of the same amount if one exists. Cost would be measured in reference to the public private partnership process and agreement, or by discounting the expected cash flows by a discount rate that reflects the time value of money and risks specific to the project.

Purchased Intangibles

- In October 2019, PSAB approved a proposal to allow public sector entities to recognize intangibles purchased through an exchange transaction. Practitioners are expected to use the definition of an asset, the general recognition criteria and the GAAP hierarchy to account for purchased intangibles.
 - PSAB has approved Public Sector Guideline 8 which allows recognition of intangibles purchased through an exchange transaction. Narrow-scope amendments were made to Section PS 1000 Financial statement concepts to remove prohibition on recognition of intangibles purchased through exchange transactions and PS 1201 Financial statement presentation to remove the requirement to disclose that purchased intangibles are not recognized.
 - The effective date is April 1, 2023 with early adoption permitted. Application may be retroactive or prospective.
-

Appendix 3: Upcoming changes to auditing standards

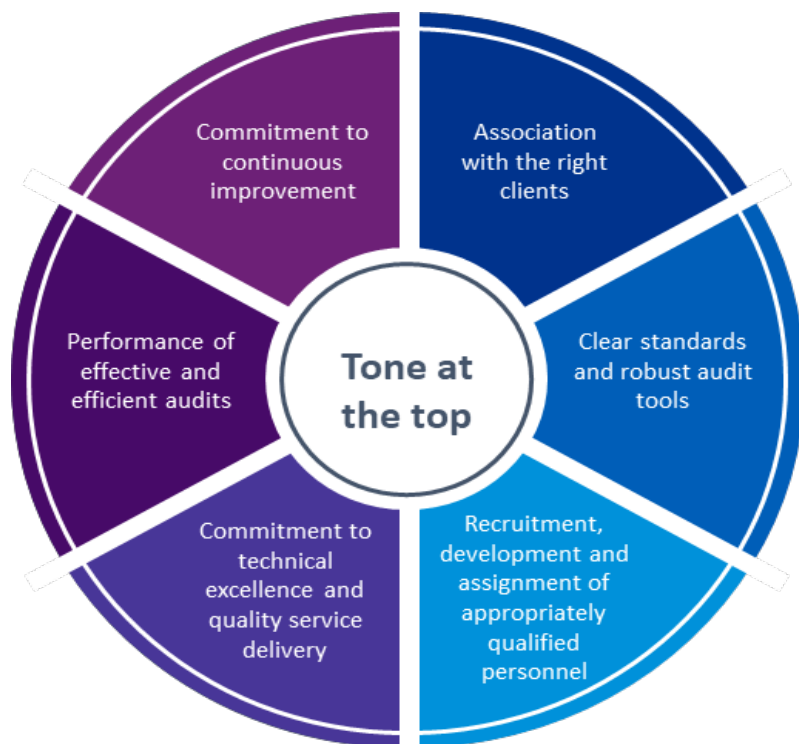
The following changes to auditing standards applicable to our 2022 audit are listed below.

Standard	Key observations
Revised CAS 315, <i>Identifying and Assessing the Risks of Material Misstatement</i>	<p>Revised CAS 315, <i>Identifying and Assessing the Risks of Material Misstatement</i> has been released and is effective for audits of financial statements for periods beginning on or after December 15, 2021.</p> <p>The standard has been significantly revised, reorganized and enhanced to require a more robust risk identification and assessment in order to promote better responses to the identified risks. Key changes include:</p> <ul style="list-style-type: none">– Enhanced requirements relating to exercising professional skepticism– Distinguishing the nature of, and clarifying the extent of, work needed for indirect and direct controls– Clarification of which controls need to be identified for the purpose of evaluating the design and implementation of controls– Introduction of scalability– Incorporation of considerations for using automated tools and techniques– New and revised concepts and definitions related to identification and assessment of risk– Strengthened documentation requirements

CPA Canada plans to publish a Client Briefing document in early 2022 to help you better understand the changes you can expect on your 2022 audit.

Appendix 4: KPMG's System of Quality Control

Quality control is fundamental to our business and is the responsibility of every partner and employee. To help all audit professionals concentrate on the fundamental skills and behaviors required to deliver a quality audit, KPMG has developed the Audit Quality Framework shown below. These are the cornerstones of how we execute our responsibilities.



What do we mean by audit quality?

Audit Quality (AQ) is at the core of everything we do at KPMG.

We believe that it is not just about reaching the right opinion, but how we reach that opinion.

We define 'audit quality' as being the outcome when audits are executed consistently, in line with the requirements and intent of applicable professional standards within a strong system of quality controls.

All of our related activities are undertaken in an environment of the utmost level of **objectivity, independence, ethics, and integrity**.

Visit our [Audit Quality Resources page](#) for more information including access to our [Transparency report](#).

Appendix 5: Audit and assurance insights

Our latest thinking on the issues that matter most to audit committees, Boards and Management.

Consideration	Key observations	Links
Audit & Assurance Insights	Curated thought leadership, research and insights from subject matter experts across KPMG in Canada	<u>Learn more</u>
Momentum	A quarterly Canadian newsletter which provides a snapshot of KPMG's latest thought leadership, audit and assurance insights and information on upcoming and past audit events – keeping management and board members abreast on current issues and emerging challenges within audit.	<u>Sign-up now</u>
COVID-19 Financial Reporting Resource Centre	Resource centre on the financial reporting impacts of coronavirus	<u>Learn more</u>
Return to the Workplace	As all levels of government begin to take steps toward re-opening the country and restarting our economy, planning for the return to a physical workplace is quickly becoming a top priority for many organizations. With the guidelines for the pandemic continuing to evolve daily, there are many considerations, stages and factors employers need to assess in order to properly develop a robust action plan which can ensure the health and safety of their workforce.	<u>Learn more</u>
Hybrid Workplace Guide	<p>In this eBook, you'll discover:</p> <p>The business case for building a hybrid workplace: What are the benefits of a hybrid work model? From employee attraction and retention to achieving enterprise-wide cost efficiencies.</p> <p>The flexibility imperative: How do you create a successful hybrid workplace model that balances employees and organizations' needs and wants? From remote work to safely supporting more face to face interactions.</p> <p>The building blocks of a hybrid workplace: We address human, organizational, regulatory, digital and physical considerations, and aspects such as how do you manage digital and cybersecurity when working from home in a hybrid workplace model? How can management lead by motivation and results for better employee engagement?</p> <p>Returning to the physical workplace: How do you ensure a safe workplace when employees return to the office space in a hybrid workplace model? How can you emphasize safety to instill confidence in your employees?</p>	<u>Learn more</u>

	Legal considerations of a hybrid work model: What could the tax implications be for companies if they implement a hybrid workplace model? Considerations to help you navigate the risks of hybrid work, including changing policies, approaches for new vs. existing employees, and security and privacy.	
Board Leadership Centre	Leading insights to help board members maximize boardroom opportunities.	<u>Learn more</u>
Going digital, faster in Canada	Pre-COVID-19, private and public organizations were moving towards a digital business model, travelling at varying speeds. But the pandemic forced a dramatic acceleration, both in the speed of change and the required investment to digitally transform. According to Canadian insights from KPMG's recent global survey, organizations are investing heavily in technology to address immediate concerns, ranging from falling revenue and interrupted supply chains to building longer-term competitiveness and operational resilience.	<u>Learn more</u>
The ESG journey: Lessons from the boardroom and C-suite	To build on our work in ESG, strategy and the long view, the Board Leadership Center interviewed directors and officers of major corporations, including Morgan Stanley, Tyson Foods, Ford Motor, Microsoft, Mars, and Whirlpool, among others.	<u>Learn more</u>
ESG, strategy, and the long view	To help boards understand and shape the total impact of the company's strategy and operations externally—on the environment, the company's consumers and employees, the communities in which it operates, and other stakeholders—and internally, on the company's performance, this paper presents a five-part framework.	<u>Learn more</u>
Inclusion and diversity practices	Getting started on the inclusion and diversity journey. Unique inclusion and diversity considerations for boards.	<u>Learn more</u>

Appendix 6: Draft auditors' report

(see attachment below)

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Toronto Transit Commission

Opinion

We have audited the consolidated financial statements of Toronto Transit Commission (the Entity), which comprise:

- the consolidated statement of financial position as at December 31, 2021
- the consolidated statement of operations and accumulated surplus for the year then ended
- the consolidated statement of remeasurement gains and losses for the year then ended
- the consolidated statement of changes in net debt for the year then ended
- the consolidated statement of cash flows for the year then ended
- and notes to the consolidated financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Entity as at December 31, 2021, and its consolidated results of operations and accumulated surplus, its consolidated remeasurement gains and losses, its consolidated changes in net debt and its consolidated cash flows for the year then ended in accordance with Canadian public sector accounting standards.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "***Auditors' Responsibilities for the Audit of the Financial Statements***" section of our auditors' report.

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Other Information

Management is responsible for the other information. Other information comprises:

- the information, other than the financial statements and the auditors' report thereon, included in the annual report.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit and remain alert for indications that the other information appears to be materially misstated.

We obtained the information, other than the financial statements and the auditors' report thereon, included in annual report as at the date of this auditors' report.

If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report.

We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group Entity to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

DRAFT

Chartered Professional Accountants, Licensed Public Accountants

Vaughan, Canada

Appendix 7: Management representation letter

(see attachment below)

KPMG LLP
Vaughan Metropolitan Centre
100 New Park Place
Vaughan, ON L4K 0J3
Canada

Date: June 23, 2022

Ladies and Gentlemen:

We are writing at your request to confirm our understanding that your audit was for the purpose of expressing an opinion on the consolidated financial statements (hereinafter referred to as "financial statements") of Toronto Transit Commission ("the Entity") or ("TTC") as at and for the period ended December 31, 2021.

GENERAL:

We confirm that the representations we make in this letter are in accordance with the definitions as set out in **Attachment I** to this letter.

We also confirm that, to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

RESPONSIBILITIES:

- 1) We have fulfilled our responsibilities, as set out in the terms of the engagement letter dated September 23, 2020, including for:
 - a) the preparation and fair presentation of the financial statements and believe that these financial statements have been prepared and present fairly in accordance with the relevant financial reporting framework.
 - b) providing you with all information of which we are aware that is relevant to the preparation of the financial statements ("relevant information"), such as financial records, documentation and other matters, including:
 - the names of all related parties and information regarding all relationships and transactions with related parties;
 - the complete minutes of meetings, or summaries of actions of recent meetings for which minutes have not yet been prepared, of shareholders, board of directors and committees of the board of directors that may affect the financial statements. All significant actions are included in summaries. Certain Board reports and minutes that were subject to legal privilege were not provided, however TTC Legal was available to discuss the content of those reports with KPMG and related liabilities were confirmed with external legal counsel.
 - c) providing you with unrestricted access to such relevant information.
 - d) providing you with complete responses to all enquiries made by you during the engagement.
 - e) providing you with additional information that you may request from us for the purpose of the engagement.
 - f) providing you with unrestricted access to persons within the Entity from whom you determined it necessary to obtain audit evidence.
 - g) such internal control as we determined is necessary to enable the preparation of financial

statements that are free from material misstatement, whether due to fraud or error. We also acknowledge and understand that we are responsible for the design, implementation and maintenance of internal control to prevent and detect fraud.

- h) ensuring that all transactions have been recorded in the accounting records and are reflected in the financial statements.

INTERNAL CONTROL OVER FINANCIAL REPORTING:

- 2) We have communicated to you all deficiencies in the design and implementation or maintenance of internal control over financial reporting of which we are aware.

FRAUD & NON-COMPLIANCE WITH LAWS AND REGULATIONS:

- 3) We have disclosed to you:
 - a) the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
 - b) all information in relation to fraud or suspected fraud which we are aware of, affecting TTC that involves:
 - management;
 - employees who have significant roles in internal control over financial reporting; or
 - otherswhere such fraud or suspected fraud could have a material effect on the financial statements.
 - c) all information in relation to allegations of fraud, or suspected fraud, affecting TTC's financial statements, communicated by employees, former employees, analysts, regulators, or others.
 - d) all known instances of non-compliance or suspected non-compliance with laws and regulations, including all aspects of contractual agreements, whose effects should be considered when preparing TTC's financial statements.
 - e) all known actual or possible litigation and claims whose effects should be considered when preparing TTC's financial statements.

SUBSEQUENT EVENTS:

- 4) All events subsequent to the date of the financial statements and for which the relevant financial reporting framework requires adjustment or disclosure in the financial statements have been adjusted or disclosed.

RELATED PARTIES:

- 5) We have disclosed to you the identity of the Entity's related parties.
- 6) We have disclosed to you all the related party relationships and transactions/balances of which we are aware.
- 7) All related party relationships and transactions/balances have been appropriately accounted for and disclosed in accordance with the relevant financial reporting framework.

ESTIMATES:

- 8) Measurement methods and significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

GOING CONCERN:

- 9) We have provided you with all information relevant to the use of the going concern assumption in the financial statements.

MISSTATEMENTS:

- 10) The effects of the uncorrected misstatement described in **Attachment II** are immaterial, both individually and in the aggregate, to the financial statements as a whole.

NON-SEC REGISTRANTS OR NON-REPORTING ISSUERS:

- 11) We confirm that the Entity is not a Canadian reporting issuer (as defined under any applicable Canadian securities act) and is not a United States Securities and Exchange Commission ("SEC") Issuer (as defined by the Sarbanes-Oxley Act of 2002).
- 12) We also confirm that the financial statements of the Entity will not be included in the group financial statements of a Canadian reporting issuer audited by KPMG or an SEC Issuer audited by any member of the KPMG organization.

Yours very truly,

Toronto Transit Commission

Richard J. Leary, Chief Executive Officer

Josie La Vita, Chief Financial Officer

Alex Cassar, Director – Budgets, Costing and Financial Reporting

Mark Del Vecchio, Capital City Projects Coordinator

Sharon Tippett, Manager – Financial Statements

Natalie Scarcello, Manager – Financial Statements

Attachment I – Definitions

MATERIALITY

Certain representations in this letter are described as being limited to matters that are material. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both.

FRAUD & ERROR

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users.

Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorization.

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Company Toronto Transit Commission
 Summary of Uncorrected Audit Misstatements
 For Year Ended

Attachment II - Uncorrected Misstatements

Amounts in CAD
 Method Used to Quantify Audit Misstate Rollover

Correcting Entry Required at Current Period End						Income Effect - Debit(Credit)	Statement of Operations Effect - Debit (Credit)				Cash Flow Effect - Increase (Decrease)		
ID	Description of misstatement	Type of misstatement	Accounts	Debit	(Credit)	Income effect according to Rollover (Income Statement) method	Accumulated Surplus	Financial Assets	Non-financial Assets	Liabilities	Operating Activities	Investing Activities	Financing Activities
				A		C-B							
FACTUAL DIFFERENCES													
No factual differences noted													
JUDGMENTAL DIFFERENCES													
1	To adjust for inter entity confirmation difference with City	Judgmental	Due from City		(4,200,000)			(4,200,000)			4,200,000		
			Net gain	4,200,000		4,200,000	4,200,000				(4,200,000)		

Attachment III: List of related parties and relationships

The TTC is on the of agencies, boards and commissions of the City of Toronto (the “City”). The TTC also operates Wheel-Trans, a paratransit service for people with disabilities (which is also subsidized by the City) and owns the Toronto Coach Terminal Inc. and its subsidiary, the TTC Insurance Company Limited. The TTC controls the TTC Sick Benefit Association which was incorporated to adjudicate benefit claims to eligible Members of Association unable to work due to illness or disability.

The following lists all related parties that had transactions and/or relationships with TTC for fiscal period 2021:

- City of Toronto (including its Agencies and Corporations as attached in Attachment IV)
- TTC Insurance Company Limited
- Toronto Coach Terminal Inc.
- TTC Sick Benefit Association
- The TTC Pension Fund Society (also referred to as the TTC Pension Plan)

Board Members as at December 2021*:

- Jaye Robinson – Chair
- Joanne De Laurentiis – Vice Chair
- Brad Bradford – Commissioner
- Shelley Carroll – Commissioner
- Fenton Jagdeo – Commissioner
- Cynthia Lai – Commissioner
- Ron Lalonde – Commissioner
- Jennifer McKelvie – Commissioner
- Denzil Minnan-Wong – Commissioner
- Julie Osborne – Commissioner

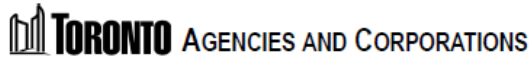
Senior Management as at December 2021*:

- Richard J. Leary – Chief Executive Officer
- Kirsten Watson – Deputy Chief Executive Officer
- Michael Atlas – Head of Legal & General Counsel
- Keisha Campbell – Chief Diversity & Culture Officer
- Gary Downie – Chief Capital Officer
- Betty Hasserjian – Chief Safety Officer (Acting)
- Josie La Vita – Chief Financial Officer
- Scott Haskill – Chief Strategy & Customer Officer (Acting)
- Mary Madigan-Lee – Chief People Officer
- Megan MacRae – Executive Director, Human Resources

- Fortunato Monaco – Chief Infrastructure & Engineering Officer
- Natalie Poole-Moffatt – Chief Corporate Affairs Officer
- James Ross – Chief Operating Officer
- Joan Taylor – Chief of Staff
- Rich Wong – Chief Vehicles Officer

*Although not explicitly listed, immediate family members are considered included as related parties by this reference.

Attachment IV: City of Toronto List of Agencies and Corporations



Agencies		Corporations		Adjudicative Bodies		
<p>Service Agencies</p> <ul style="list-style-type: none"> > CreateTO > Exhibition Place Board of Governors > Heritage Toronto > TO Live > Toronto Atmospheric Fund > Toronto Board of Health and Toronto Public Health > Toronto Investment Board > Toronto Police Services Board and Toronto Police Service > Toronto Public Library Board > Toronto Transit Commission > Toronto Zoo Board of Management > Yonge-Dundas Square Board of Management 		<p>Community-Based Boards:</p> <ul style="list-style-type: none"> > 85 Business Improvement Area (BIA) Boards of Management > Arena Boards of Management: <ul style="list-style-type: none"> • George Bell Arena • Larry Grossman Forest Hill Memorial Arena • Leaside Memorial Community Gardens Arena • McCormick Playground Arena • Moss Park Arena • North Toronto Memorial Arena • Ted Reeve Community Arena • William H. Bolton Arena > Community Centre Boards of Management (AOCCs): <ul style="list-style-type: none"> • 519 Church Street Community Centre • Applegrove Community Complex • Cecil Community Centre • Central Eglinton Community Centre • Community Centre 55 • Eastview Neighbourhood Community Centre • Ralph Thornton Community Centre • Scadding Court Community Centre • Swansea Town Hall Community Centre • Waterfront Neighbourhood Centre 		<p>City Corporations</p> <ul style="list-style-type: none"> > Build Toronto Inc. > Casa Loma Corporation > Lakeshore Arena Corporation > Toronto Community Housing Corporation > Toronto Hydro Corporation > Toronto Port Lands Company (Toronto Economic Development Corporation) > Toronto Seniors Housing Corporation 	<p>Partnered Corporations</p> <ul style="list-style-type: none"> > Toronto Pan Am Sports Centre Inc. > Waterfront Toronto (Toronto Waterfront Revitalization Corporation) 	<p>Quasi-Judicial & Adjudicative Boards</p> <ul style="list-style-type: none"> > Administrative Penalty Tribunal > Committee of Adjustment > Committee of Revision > Compliance Audit Committee > Dangerous Dog Review Tribunal > Property Standards Committee > Rooming House Licensing Commissioner ¹ > Sign Variance Committee > Toronto Licensing Tribunal > Toronto Local Appeal Body
<p>Partnered Agency</p> <ul style="list-style-type: none"> > Toronto and Region Conservation Authority 		<p>Notes:</p> <p>1. Rooming House Licensing Commissioner and Deputy are Officers, rather than an agency of the City, but in all other respects function as a quasi-judicial and adjudicative board.</p> <p style="text-align: right;">Updated: April 27, 2022</p>				

Source: <https://www.toronto.ca/wp-content/uploads/2022/04/90aa-Agency-Chart-April-2022.pdf>

Appendix 8: Why Audit Committees should know about Asset Retirement Obligations

(see attachment below)



Why Audit Committees should know about Asset Retirement Obligations

home.kpmg/ca



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Municipalities have evolved significantly over the last two decades and this evolution has escalated over the last two years due to the huge push towards digital transformation. Municipalities have come to a refreshed realization about the dynamic change it needs from their citizens resulting in a push towards a citizen-centric approach to defining their goals and objectives.

With all this change, the citizens are looking for new and improved ways to obtain information from the municipalities and public sector entities generally. They are looking for information that is timely, accurate and accessible. For instance, more and more municipalities are moving towards quarterly financial reporting to provide more timely information to stakeholders.

The finance function within municipalities tend to focus a large portion of their resources on their budget-setting process each year, relative to financial reporting. This budget sets out the municipality's operating and capital spending plan for the next year, leading to the determination of the necessary tax levy to support the planned spend. It is necessarily a cash-based document, which leads to difficulty in comparing it to a municipality's financial results, which are prepared on a basis prescribed by the Chartered Professional Accountants Canada. The annual financial statements are presented on an accrual basis in accordance with Public Sector Accounting Standards (PSAS). This disconnect between the cash basis and accrual basis often makes it difficult for 'Those Charged With Governance' (TCWG) to fully understand the actual financial results since relatively more resources are deployed towards the creation of the budget than the presentation of the financial results. While there are quite a few intersections between the budget-based reporting and PSAS reporting, there are many differences that can come in the way of effective municipal financial management and oversight.

Please note that the discussion in this paper is relevant for all public sector entities that report their financial results in accordance with PSAS. While the specific examples in this paper focus on municipalities, the same implications can be applied to other entities with slight modification to incorporate the differences in operations in the various types of public sector entities.

With that in mind, let's talk about a new reporting standard which is required to be implemented by public sector entities for years ending on or after April 1, 2022 and why it is important for TCWG to understand the implications of this new standard. This standard pertains to Asset Retirement Obligations (ARO) and requires public sector entities to set up a liability related to the legal obligation for retiring a tangible capital asset. The assets that fall into this standard are the ones that are controlled by the public sector entity and includes leased assets. This standard has far-reaching impacts for municipalities and requires proper attention from TCWG, in order to exercise appropriate oversight over the financial reporting process. We have highlighted some key items here:

- (a) Completeness of liabilities
- (b) Legal obligations
- (c) Completeness of assets
- (d) Technical expertise
- (e) Financing repercussions
- (f) Environmental Social Governance (ESG) implications

Let's talk about these one by one!

a. Completeness of liabilities

In many cases, the liability associated with AROs has not been recorded within the financial records of the public sector entities which means that these entities are underreporting their obligations. It is possible that certain public sector entities might have some of these obligations included within their legal obligations however it is unclear how these are being tracked and whether the process used to determine the magnitude of these legal obligations is accurate.

Not only is it important to have accurate and complete information for the measurement and recognition of these liabilities for financial reporting purposes, but the same information is also equally important for financial planning and for effective financial management of the municipalities.

One of the tools used by municipalities in order to perform long term financial planning is through reserves and reserve funds to ensure they have sufficient funds set aside for future needs. If a municipality does not have a clear understanding of their ARO liability, it would hinder their ability to assess the adequacy of their reserve funds. Cash flow management would also be impacted due to the potential unplanned outflow in any given year.





b. Legal obligations

Next, let's talk about legal obligations. It is important to understand that the obligation related to the ARO is a legal obligation. However, unlike some of the traditional legal obligations, where there might be uncertainty around the outcome of the legal item, there is no uncertainty related to the existence of the future obligation related to an ARO. This means that the future settlement is guaranteed for an ARO and the uncertainty in this situation is limited to the quantification or the amount of the future settlement.

Not getting a good handle on the ARO liability also increases the risk of negative legal implications for the municipality in the future. As an example, if there is a contaminated site that requires a municipality to perform clean up to ensure the safety of the residents, but this contamination is not rectified in a timely and reasonable manner as required by environmental regulations. This could result in severe legal implications for the municipality due to the hazardous nature of these materials and potential negative health impact on the residents.

The new ARO reporting standard also includes the concept of promissory estoppel as part of the legal liability assessment. For your convenience, we have included the definition of promissory estoppel in the glossary at the end of this document.

The key point that is important to emphasize is that it would be important to engage a legal expert as part of the ARO implementation team as this assessment might be outside the expertise of the core finance team members.

c. Completeness of assets

When Canadian municipalities first began reporting their tangible capital assets as a component of their balance sheets back in 1999, it was apparent that many municipalities did not have good historical data on the assets that they owned at that time and consequently many still do not have a complete listing of owned assets. A comprehensive approach to asset management brings numerous benefits to local and regional governments and assists them in being able to demonstrate that taxpayers get good value from each capital asset they fund, in part or in whole.

This is a contributing factor as to why there are regulatory requirements for good asset management practices. For example, the Federal Gas Tax Agreement requires municipalities to demonstrate a strong asset management system. In absence of a well-thought-out asset management plan, local municipalities could put at risk the operational effectiveness of their assets, public health and safety and overall public confidence in the local government. A solid asset management approach helps to ensure reliability of the services offered by a local government and thus instill more confidence from the public.

Asset management itself is quite a broad topic of discussion for municipalities, perhaps the above description provides an understanding of why there is so much emphasis placed on good asset management. As important as it already was to have a complete listing of tangible capital assets in order to develop a reasonable asset management plan, it has become even more so with the implementation of financial reporting standards for AROs. This due to the fact that AROs are based on identifiable

tangible capital assets controlled by the Entity. If the asset listing is not complete or not up to date, any obligations relating to assets not being reported would also not be captured. If items are missed in the scoping and measurement of AROs, this results in a significant risk for the municipalities where the corresponding liabilities will be incomplete. There might be other consequences of missing these liabilities for municipalities depending on the nature and extent of error such as cash-flow management, environmental and social implications.

The ARO standard does not require entities to assess their overall asset management approach for reasonableness. The ARO standard also does not require entities to undertake an asset management exercise to make sure they have a complete inventory of all of their assets. However, it is quite clear that the entities who have an accurate and complete listing of their assets through a well-thought-out asset management plan are the ones who will be in the best position to ensure completeness of their AROs.





d. Technical expertise

Another matter to consider and assess is the quality of the information that the entity has regarding their assets. How well does the entity understand its assets including the nature and components of its assets? For the finance team to scope and measure the ARO associated with different assets, they would need clear guidance from subject matter experts that understand the technical aspect of this determination.

Finance teams would likely have the requisite expertise relating to the cost and fair value of these assets but may not be as aware of the legal, environmental, and / or other obligations attached to these assets. The knowledge of subject matter experts will be to assist the finance team in this area.

In addition to legal experts, other experts on which the exercise may depend upon include individuals from the operations team, mechanical and engineering teams, etc.

It would be important to have a discussion with the finance team to identify which subject matter experts are considered necessary based on their initial assessment in order to make optimal resource allocations. It would also be important to note that these needs could change as the implementation project matures.

e. Financing repercussions

Even though not directly related to ARO, financing repercussions should also be front of mind with overall asset management, particularly when planning for asset replacement / remediation / maintenance. In different provinces in Canada, there are restrictions on the amount of borrowing for local municipalities. In Ontario, for instance, long-term borrowing is restricted to capital investments and is also subject to a prescribed maximum level based on a preset formula.

Local municipalities use debt to help finance large capital projects. Local municipalities conduct long-term financial planning through the adoption of a multi-year capital plan and a long-term fiscal plan that would typically consider the amount and timing of debt necessary to support the planned expenditures over the term of Council. It also becomes important to understand the useful life of the asset in order to match the cost to the period over which the benefits are received. This provides more affordable financing by matching the repayment term to the economic useful life of the project, instead of funding the entire cost from current revenues.

In recent years, we have noted the trend of the issuance of green bonds, with the province of Ontario reaching a whopping \$10.75 billion in green bonds in 2021. Other local municipalities are following suit and this move is expected to continue. It would be important to have a good grasp on the asset management plans before these green bonds are attached to environmentally friendly infrastructure capital projects. Talking about green bonds, let's move into other ESG considerations.



f. ESG Implications

It is quite interesting that the concept of ARO touches all three aspects of the ESG spectrum i.e., environmental, social and governance. Physical contamination caused by hazardous materials such as asbestos or the toxins and leachate from landfills are all contributors towards damaging the environment.

Inappropriate or sub-optimal treatment of these hazardous materials can have significant health detriments which becomes a social responsibility issue whereby the expectation is that public sector entities, especially municipalities would ensure appropriate level of remediation for these hazardous items. The heightened fiduciary responsibility in the public sector environment especially with the elected officials with the municipalities creates a huge need for an appropriate level of governance in place.

The ESG implications for ARO have gained a lot of traction in recent years. These discussions have become more important now as public sector entities work towards the implementation of this new standard. While it is important to embrace ESG into our strategic planning, it will be critical to ensure that this planning is comprehensive and well thought out. As daunting as this task can seem, the key is to have a structured approach to map out what is relevant for the organization and to design a plan to tackle these implications.

In conclusion, while the ARO standard implementation may seem like any other accounting standard implementation, it has far reaching implications from a municipal operational and governance perspective requiring consideration and input from the organization as a whole, not just its finance team. It is therefore critical to take the time to understand these implications and design a plan to address them in a meaningful manner.

We would be more than happy to continue this discussion with you. We are currently running customized sessions for different entities to help them understand these various implications of AROs and how to best address them.

Special thanks to Kevin Travers, Partner KPMG Enterprise and Bailey Church, Partner Accounting Advisory Services for their contributions to this publication.





The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

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Glossary

Public Sector

Public sector refers to governments, government components, government organizations and partnerships. Each of these entities is a “public sector entity”. A government component is an integral part of government, such as a department, ministry or fund. It is not a separate entity with the power to contract in its own name and that can sue and be sued. A government organization is any organization controlled by a government that is a separate entity with the power to contract in its own name and that can sue and be sued. Public sector organizations have a higher accountability to the taxpayer – above and beyond the traditional fiduciary duty.

Promissory estoppel

The elements of a promissory estoppel claim are “(1) a promise clear and unambiguous in its terms; (2) reliance by the party to whom the promise is made; (3) [the] reliance must be both reasonable and foreseeable; and (4) the party asserting the estoppel must be injured by his reliance.”



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