The Regional Municipality of York

Audit Findings Report

For the year ended December 31, 2016

KPMG LLP

May 16, 2017

kpmg.ca/audit

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Executive summary

Purpose of this report

The purpose of this Audit Findings Report is to assist you, as a member of the Audit Committee, in your review of the results of our audit of the consolidated financial statements (the "financial statements") of the Regional Municipality of York ("the Region") as at and for the year ended December 31, 2016.

Audit risks and results

Prior to the audit, we discussed a number of significant financial reporting risks. These included fraud risk over revenue recognition and management override of controls.

We also discussed some other areas of audit focus. We are satisfied that our audit work has appropriately dealt with these risks and other areas of focus. We have no significant matters to report to the Audit Committee with respect to them.

Changes from the Audit Plan

The preliminary materiality in the Audit Planning Report has been updated to reflect the Region's actual operating expenditures of approximately $1,845M. The materiality for the year-end audit was $56M, which was decreased from the Audit Planning Report materiality of $66.4M. The year-end performance materiality was $42M and the audit posting threshold was $2.8M.

There have been no other changes from the Audit Planning Report previously issued.

Significant accounting estimates

The critical areas of estimates relate to the depreciation of capital assets, employee future benefits and contingent liabilities. We are satisfied with the reasonability of accounting estimates.

Finalizing the audit

As of May 16, 2017, we have completed the audit of the consolidated financial statements and received evidence of approval of the consolidated financial statements from the Region's Commissioner of Finance (individual delegated authority to approve the financial statements). We have also extended our subsequent event procedures up to our auditor's report date.

Our audit report is dated the same as the date of approval of the consolidated financial statements by the Region's Commissioner of Finance on May 16, 2017.

Adjustments and differences

We did not identify any adjustments during the course of the audit.

Audit risks and results

Inherent risk of material misstatement is the susceptibility of a balance or assertion to misstatement which could be material, individually or when aggregated with other misstatements, assuming that there are no related controls.

Significant financial reporting risks	Our response and significant findings
Fraud risk from revenue recognition	• Our audit approach consisted of substantive procedures to address the relevant assertions associated with this significant risk. • We did not identify any issues related to fraud risk associated with revenue recognition.
Risk of management override of controls	• We performed procedures consistent with professional standards including testing of journal entries, performing a retrospective review of estimates and evaluating the business rationale of significant transactions. • We did not identify any issues or concerns regarding management override of controls.

Audit risks and results

Significant findings from the audit regarding other areas of focus are as follows:

Other areas of focus	Our response and significant findings
Development charges	• During the audit, we noted the development charge collections were $338.5M (2015 – $258.3M) and the amounts recognized as revenue were $283.4M (2015 - $281M). • We reviewed on a sample basis both development charge collections and transfers into income. We also agreed the total development charge transfers to the amount recognized into revenue. We noted that the development charge collections and transfers were appropriate, and the transfers had appropriately been recognized into revenue.
Deferred Metrolinx revenue	• During our substantive testing, we noted that the Region recognized $227.6M (2015 - $274M) of deferred revenue earned for the Metrolinx projects. The Region also received cash advances from Metrolinx of $255.9M (2015 - $87.9M). • We obtained the deferred revenue continuity schedule and selected samples for testing to determine if the selected amounts had been recognized appropriately as revenue in the current period. We also tested the cash advances by agreeing to cash payments. • Based on our testing, we concluded that the Metrolinx deferred revenue was recognized appropriately.
Expropriation accruals	• During our substantive audit of accruals we noted the expropriation accruals balance for non-Metrolinx projects was $10.9M (2015 – $16.3M) and the amount accrued for the expropriation related to Metrolinx projects was $47.8M (2015 - $54.6M). • We obtained a listing of expropriation accruals and selected significant additions and disposals for testing to determine if the year-end balance was appropriate. We also obtained detailed schedules of the expropriation accruals by project, and selected samples for testing to ensure the liability existed as of year-end and the amount accrued was appropriate. • We noted that expropriation accruals were recognized appropriately.

Audit risks and results

Significant findings from the audit regarding other areas of focus are as follows:

Other areas of focus	Our response and significant findings
Investments and investment income	• As at year-end, the Region held $2,572.9M (2015 - $2,318.4M) in investments. The cash balances also includes $120M (2015 - $316M) of short-term investments with maturity dates less than 3 months from year-end. • We performed test of details over the additions and disposals of investments, compared the investment listing to third party confirmations, and reviewed the investments for compliance with the investment policy. • We noted the recognition of additions and de-recognition of disposals were properly executed. The accounting records were compared to third party confirmations without issue. Also the investment activity and balances were consistent with the Region's policies.
Tangible capital assets	• During our substantive testing of tangible capital asset additions, we noted that the Region recognized $648.1M (2015 -$808.5M) in total additions, which is comprised of $590.8M (2015 - $799.0M) of additions to the Region's work in progress ("WIP"), and $57.3M (2015 - $9.5M) of additions to HYI. The Region also capitalized $1,041M (2015 - $1,208M) from WIP into tangible capital assets. • The Region disposed of assets with a cost base of $53.1M (2015 - $66.3M) and accumulated amortization of $49.6M (2015 - $54.4M). The proceeds on the disposals of capital assets were $0.8M (2015 - $3.9M), which resulted in a loss on disposal of $2.6M (2015 - $8.0M). • We reviewed on a sample basis the additions to both WIP and tangible capital assets. We noted that the capital additions were appropriate and management has correctly capitalized the additions from work in progress to capital assets. We also reviewed on a sample basis the disposals of tangible capital assets, and recalculated the overall loss on disposal. We noted that the disposals were recorded appropriately.

Critical accounting estimates

Management is required to disclose information in the consolidated financial statements about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to carrying amounts of assets and liabilities within the next financial year. Generally, these are considered to be "critical accounting estimates."

We have summarized our assessment of the subjective areas.

Critical accounting estimates

Item	KPMG comment
Contingent liabilities	• The CPA Handbook PS 3300 Contingent Liabilities requires that the Region recognize a liability when *"…it is likely that a future event will confirm that a liability has been incurred at the date of the financial statements; and the amount can be reasonably estimated."* • At any point in time, the Region is subject to a number of matters which could potentially result in the determination of a contingent liability as defined above, including, but not limited to matters such as legal claims, contract settlement accruals etc. • We reviewed the Region's assessments of contingent liabilities and the process employed to develop and record the estimated liabilities. Where applicable, we met with the individuals responsible for the process and are satisfied that the methodology used is consistent with the approach taken in prior years and has been appropriately reviewed. • As these items are resolved, it is possible that the final amounts recorded for these liabilities may change, however the amounts currently recorded represent management's best estimates of exposure given the information presently available.
Amortization expense	• We have also reviewed the estimated useful lives of the various additions from work in progress to tangible capital assets and conclude that they are reasonable. • Fiscal 2016 amortization expense was recalculated and it was determined that management's calculation of the amortization expense was appropriate.
Employee future benefits	• We reviewed actuarial reports regarding estimates related to Employee Future Benefits, and conducted tests of detail to assess the reliability of the information used within the reports. • We recalculated the accruals based on the information noted above, and did not identify any discrepancies.

Critical accounting estimates (continued)

Management is required to disclose information in the consolidated financial statements about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to carrying amounts of assets and liabilities within the next financial year. Generally, these are considered to be "critical accounting estimates."

We have summarized our assessment of the subjective areas.

Item	KPMG Comment
Accounting treatment with Housing York Inc. ("HYI")	• HYI owns several buildings under the Affordable Housing Program ("AHP"). In prior years, HYI recorded the amortization expense for the buildings based on the terms of the mortgages secured to finance such assets and the annual charges of the mortgage as an amortization expense. This practice is in compliance with the Contribution Agreement between HYI and the Region and Section 80(2) of the Housing Services Act, 2011 (the "Act"). The treatment resulted in a non-cash deficiency of revenue over expenditures and ultimately a deficit, which was disallowed under the AHP rules. In 2012 the Contribution Agreement was amended to allow for cessation of amortization on AHP buildings. The amendment was applied in 2012 and future years. • Although amortization has not been recorded on the AHP projects since 2012 in HYI financial statements, the Region continues to record amortization in the consolidated financial statements. We performed a reasonability test to ensure that the amortization expense on the HYI buildings is adequately recorded within the Region's consolidated financial statements.

Adjustments and differences

Based on both qualitative and quantitative considerations, management have decided not to correct certain differences, and represented to us that the uncorrected differences—individually and in the aggregate—are, in their judgment, not material to the financial statements.

Corrected adjustments

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

Uncorrected differences

We did not identify differences that remain uncorrected.

Appendices

Appendix 1: Required communications

In accordance with professional standards, there are a number of communications that are required during the course of and upon completion of our audit. These include:

- **Auditors' report** – the conclusion of our audit is set out in our draft auditors' report.
- **Management representation letter** –In accordance with professional standards, copies of the management representation letter are provided to the Audit Committee. Management have provided you with a copy of the representation letter for the audit of the financial statements.

Appendix 2: Audit Quality and Risk Management

KPMG maintains a system of quality control designed to reflect our drive and determination to deliver independent, unbiased advice and opinions, and also meet the requirements of Canadian professional standards.

Quality control is fundamental to our business and is the responsibility of every partner and employee. The following diagram summarises the six key elements of our quality control systems

Visit http://www.kpmg.com/Ca/en/services/Audit/Pages/Audit-Quality-Resources.aspx for more information.

- Other controls include:
  - Before the firm issues its audit report, the Engagement Quality Control Reviewer reviews the appropriateness of key elements of publicly listed client audits.
  - Technical department and specialist resources provide real-time support to audit teams in the field.
- We conduct regular reviews of engagements and partners. Review teams are independent and the work of every audit partner is reviewed at least once every three years.
- We have policies and guidance to ensure that work performed by engagement personnel meets applicable professional standards, regulatory requirements and the firm's standards of quality.
- All KPMG partners and staff are required to act with integrity and objectivity and comply with applicable laws, regulations and professional standards at all times.

- We do not offer services that would impair our independence.
- The processes we employ to help retain and develop people include:
  - Assignment based on skills and experience;
  - Rotation of partners;
  - Performance evaluation;
  - Development and training; and
  - Appropriate supervision and coaching.
- We have policies and procedures for deciding whether to accept or continue a client relationship or to perform a specific engagement for that client.
- Existing audit relationships are reviewed annually and evaluated to identify instances where we should discontinue our professional association with the client.

Appendix 3: Background and professional standards

Internal control over financial reporting

As your auditors, we are required to obtain an understanding of internal control over financial reporting (ICFR) relevant to the preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on internal control. Accordingly, we do not express an opinion on the effectiveness of internal control.

Our understanding of ICFR was for the limited purpose described above and was not designed to identify all control deficiencies that might be significant deficiencies and therefore, there can be no assurance that all significant deficiencies and other control deficiencies have been identified. Our awareness of control deficiencies varies with each audit and is influenced by the nature, timing, and extent of audit procedures performed, as well as other factors.

The control deficiencies communicated to you are limited to those control deficiencies that we identified during the audit.

Documents containing or referring to the audited financial statements

We are required by our professional standards to read only documents containing or referring to audited financial statements and our related auditors' report that are available through to the date of our auditors' report. The objective of reading these documents through to the date of our auditors' report is to identify material inconsistencies, if any, between the audited financial statements and the other information. We also have certain responsibilities, if on reading the other information for the purpose of identifying material inconsistencies, we become aware of an apparent material misstatement of fact.

We are also required by our professional standards when the financial statements are translated into another language to consider whether each version, available through to the date of our auditors' report, contains the same information and carries the same meaning.

Appendix 4: Current Developments

The following is a summary of the accounting standard changes that are relevant to the Region

<table>
<tr><th>Topic</th><th>Summary</th></tr>
<tr><td>PS Introduction</td><td>This standard provides the standards to be followed by government partnerships. Government business partnerships (with all public sector partners) are to follow the standards applicable to publicly accountable entities in Part I of the CPA Canada Handbook Accounting. Non-business government partnerships with only government partners can chose either PSA Standards or the standards applicable to publicly accountable entities in Part I of the CPA Canada Handbook Accounting. Government partnerships that have one or more private sector partners should use the standards determined by the partners. This section also requires government organizations that meet the new definition of government components to apply the PSA Standards.

This standard is effective for fiscal periods beginning on or after January 1, 2017 (the Region’s December 31, 2017 year end).</td></tr>
<tr><td>PS 3210 Assets</td><td>This standard provides a definition of assets and further expands that definition as it relates to control.

Assets are defined as follows:
• They embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows.
• The public sector entity can control the economic resource and access to the future economic benefits.
• The transaction or event giving rise to the public sector entity's control has already occurred.
The standard also includes some disclosure requirements related to economic resources that are not recorded as assets to provide the user with better information about the types of resources available to the public sector entity.
This standard is effective for fiscal periods beginning on or after April 1, 2017 (the Region’s December 31, 2018 year end).</td></tr>
<tr><td>PS 3320 Contingent Assets</td><td>This standard defines contingent assets. They have two basis characteristics:
• An existing condition or situation that is unresolved at the financial statement date.
• An expected future event that will resolve the uncertainty as to whether an asset exists.
The standard also has specific disclosure requirements for contingent assets when the occurrence of the confirming event is likely.
This standard is effective for fiscal periods beginning on or after April 1, 2017 (the Region’s December 31, 2018 year end).</td></tr>
</table>

PS 3380 Contractual Rights	This standard defines contractual rights to future assets and revenue. Information about a public sector entity's contractual rights should be disclosed in notes or schedules to the financial statements and should include descriptions about their nature and extent and the timing. The standard also indicates that the exercise of professional judgment would be required when determining contractual rights that would be disclosed. Factors to consider include, but are not limited to: (a) contractual rights to revenue that are abnormal in relation to the financial position or usual business operations; and (b) contractual rights that will govern the level of certain type of revenue for a considerable period into the future. This standard is effective for fiscal periods beginning on or after April 1, 2017 (the Region's December 31, 2018 year end.)
PS 2200 Related Party Disclosures	This standard relates to related party disclosures and defines related parties. Related parties could be either an entity or an individual. Related parties exist when one party has the ability to control or has shared control over another party. Individuals that are key management personnel or close family members may also be related parties. Disclosure is only required when the transactions or events between related parties occur at a value different from what would have been recorded if they were not related and the transactions could have a material financial impact on the financial statements. Material financial impact would be based on an assessment of the terms and conditions underlying the transaction, the financial materiality of the transaction, the relevance of the information and the need for the information to enable the users to understand the financial statements and make comparisons. This standard also specifies the information required to be disclosed including the type of transactions, amounts classified by financial statement category, the basis of measurement, and the amounts of any outstanding items, any contractual obligations and any contingent liabilities. The standard also requires disclosure of related party transactions that have occurred where no amounts has been recognized. This standard is effective for fiscal periods beginning on or after April 1, 2017 (the Region's December 31, 2018 year end).
PS 3430 Restructuring Transactions	A restructuring transaction in the public sector differs from an acquisition as they generally include either no or nominal payment. It also differs from a government transfer as the recipient would be required to assume the related program or operating responsibility. The standard requires that assets and liabilities are to be measured at their carrying amount. It also prescribes financial statement presentation and disclosure requirements. This standard is effective for fiscal periods beginning on or after April 1, 2018 (the Region's December 31, 2019 year end).
PS 3420 Inter-entity Transactions	This standard relates to the measurement of related party transactions and includes a decision tree to support the standard. Transactions are recorded a carrying amounts with the exception of the following: • In the normal course of business – use exchange amount • Fair value consideration – use exchange amount • No or nominal amount – provider to use carrying amount; recipient choice of either carrying amount or fair value.

	• Cost allocation – use exchange amount This standard is effective for fiscal periods beginning on or after April 1, 2017 (the Region's December 31, 2018 year end).
PS 3450 Financial Instruments	A standard has been issued, establishing a standard on accounting for and reporting all types of financial instruments including derivatives. The effective date of this standard has recently been deferred and it is now effective for fiscal periods beginning on or after April 1, 2019 (the Region's December 31, 2019 year end). This standard will require the Region to identify any contracts that have embedded derivatives and recognize these on the consolidated statement of financial position at fair value. Portfolio investments in equity instruments are required to be recorded at fair value. Changes in fair value will be reported in a new financial statement – statement of remeasurement gains and losses. This standard sets out a number of disclosures in the financial statements designed to give the user an understanding of the significance of financial instruments to the Region. These disclosures include classes of financial instruments and qualitative and quantitative risk disclosures describing the nature and extent of risk by type. The risks to be considered include credit, currency, interest rate, liquidity, and market risk.
Revised Standard PS 2601 Foreign Currency Translation	A revised standard has been issued establishing standards on accounting for and reporting transactions that are denominated in a foreign currency. The effective date of this standard has been deferred and is effective for fiscal periods beginning on or after April 1, 2019 (The Region's December 31, 2020 year-end). Earlier adoption is permitted. An entity early adopting this standard must also adopt the new financial instruments standard. This standard will require exchange gains and losses arising prior to settlement are recognized in a new statement of remeasurement gains and losses.

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