

AUDIT

# Corporation of the City of London

**Audit Planning Report**

For the year ending December 31, 2013

**KPMG LLP**, Chartered Accountants, Licensed Public  
Accountants

January 20, 2014

[kpmg.ca](http://kpmg.ca)

# Contents

<b>Considerations in developing our Audit Plan</b> .....	<b>1</b>
<b>Our timetable</b> .....	<b>2</b>
<b>Areas of audit emphasis</b> .....	<b>3</b>
<b>Materiality</b> .....	<b>3</b>
<b>Identification of significant risks</b> .....	<b>3</b>
<b>Use of the work of others</b> .....	<b>4</b>
<b>Fees and timing</b> .....	<b>5</b>
<b>Recommended improvements</b> .....	<b>6</b>
<b>Appendices</b> .....	<b>7</b>
Highlights.....	14

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# Considerations in developing our Audit Plan

We have prepared this Audit Plan to inform you of the planned scope and timing of the audit for the purpose of carrying out and discharging your responsibilities and exercising oversight over our audit of the consolidated financial statements.

We have set out below a summary of changes that have been taken into consideration in planning the audit for the current period:

## Your organization

- Debentures in the amount of \$50M were issued in September 2013. KPMG will review the accounting for this transaction in detail during the audit.
- Eldon House commenced operations as a stand-alone entity effective January 1, 2013. Previously, Eldon House was operated through Museum London. KPMG will be performing an audit of the Eldon House beginning with the year ending December 31, 2013.
- Significant amount of roadwork done during the year
- No major facilities work
- Internal audit continues to perform testing and recommend process improvements

## Accounting standards

- Upcoming Public Sector Accounting (PSAB) changes with effective dates ranging from 2013 to 2016 include:
  - PS 1201 – Financial Statement Presentation
  - PS 3041 – Portfolio Investments
  - **PS 3410 – Government Transfers**
  - PS 3450 – Financial Instruments
  - PS 2601 – Foreign Currency Translation
  - PS 3260 – Liability for Contaminated Sites
  - PS 3510 – Tax Revenue
- Refer to the Appendices for further discussion on this matter.

## Auditing and other professional standards

- No changes to audit standards during the year.
- Refer to the Appendices for updates on the audit profession.

## Our timetable

To assist with your responsibilities as an Audit Committee member, we have planned the following interactions with you during the regular and in-camera sessions of your committee meetings:

<b>Audit Committee Interactions</b>	<b>Date</b>
Present the Audit Planning Report and obtain comments	February 13, 2014
Make annual inquiries of the Audit Committee (see below)	February 13, 2014
Present our year-end Audit Findings Report, including independence communications	June 26, 2014

Refer to the Appendices for KPMG's and management's responsibilities.

### **Annual inquiries of the Audit Committee**

Professional standards require that during the planning of our audit we obtain your views on the risk of fraud. We make similar inquiries to management as part of our planning process; responses to these questions will assist us in planning our overall audit strategy and audit approach accordingly.

- Are you aware of, or have you identified any instances of, actual, suspected, possible, or alleged non-compliance of laws and regulations or fraud, including misconduct or unethical behaviour related to financial reporting or misappropriation of assets? If so, have the instances been appropriately addressed and how have they been addressed?
- What are your views about fraud risks in the entity?
- How do you provide effective oversight of programs and controls to prevent, detect and deter fraud, including oversight over internal controls management has established to mitigate fraud risks?

# Areas of audit emphasis

We design an overall audit strategy and an audit approach to address the significant risks identified during the planning process.

## Materiality

We determine materiality in order to plan and perform the audit and to evaluate the effects of identified misstatements on the audit and of any uncorrected misstatements on the financial statements. The determination of materiality requires judgment and is based on a combination of quantitative and qualitative assessments, including the nature of account balances and financial statement disclosures.

We determine performance materiality (from materiality) in order to assess risks of material misstatement and to determine the nature, timing and extent of audit procedures.

We determine an audit misstatement posting threshold (from materiality) in order to accumulate misstatements identified during the audit.

For the current period consolidated financial statements, the following amounts have been determined:

Materiality	Performance Materiality	Audit Misstatement Posting Threshold
\$ 13,816,000	\$ 10,362,000, which has been set at 75% of materiality	\$ 691,000, which has been set at 5% of materiality  \$ 3,110,000 for reclassifications

We will reassess materiality based on period-end results or new information to confirm whether it remains appropriate for evaluating the effects of uncorrected misstatements on the financial statements.

## Identification of significant risks

As part of our audit planning, we identify the significant financial reporting risks that, by their nature, require special audit consideration. By focusing on these risks, we establish an overall audit strategy and effectively target our audit procedures.

The *significant* financial reporting risks identified during our audit planning are listed below:

### Significant account(s)/disclosures(s)

<b>Landfill Liability</b>
<b>Risk of material misstatement prior to consideration of internal controls</b>
CEA of landfill liability – Risk of error  Significant risk: Due to management judgments and assumptions
<b>Summary of planned audit approach</b>
<ul style="list-style-type: none"> <li>- Obtain an understanding of the calculation through discussion with the City’s engineers.</li> <li>- Audit the analyses prepared by management and obtain corroborative evidence to support management’s assumptions.</li> </ul>

<b>Claims and Legal Accruals included in Accrued Liabilities</b>
<b>Risk of material misstatement prior to consideration of internal controls</b>
CEA of claims and legal accruals – Risk of error Significant risk: Due to management judgments and assumptions
<b>Summary of planned audit approach</b>
<ul style="list-style-type: none"> <li>- Obtain an understanding of the process for recoding the legal accruals through discussion with management.</li> <li>- Review management’s assessment of the likelihood of incurring the liability for each claim and the range of possible outcomes.</li> <li>- Obtain legal letters and examine for any potentially unrecorded claim liabilities.</li> <li>- Where possible, review subsequent payments to determine whether the liabilities at year end are reasonably stated.</li> </ul>

### Risk of management override of controls

Although the level of risk of management override of controls will vary from entity to entity, professional standards presume the risk of management override of controls is nevertheless present in all entities and requires the performance of specific procedures to address this presumed risk.

<b>Identified risk</b>
Presumed risk of management override of control – Risk of fraud Significant risk: Required to be identified as a significant risk per professional standards
<b>Summary of planned audit approach</b>
We plan on performing the required procedures under professional standards.

### Use of the work of others

Our planned audit approach includes the use of the following:

- Use of management’s expert – Wes Abbott, Divisional Manager, Solid Waste Engineering
- Use of management’s expert – Mercer Human Resource Consulting
- Use of management’s expert – James P. Barber, City Solicitor

# Fees and timing

## Fees and assumptions

In determining the fees for our services, we have considered the nature, extent and timing of our planned audit procedures as described above. Our fee analysis has been reviewed with and agreed upon by management.

Our fees are estimated as follows:

	<b>Current Period Budget</b>	<b>Prior Period Actual</b>
Audit of the annual financial statements	\$87,300	\$85,900

These fees are based on the assumptions described in the engagement letter dated December 1, 2010. There have been no changes in the terms and conditions of our engagement since the date of our last letter.

## Timing of the audit

We have discussed the key audit deliverables with management and the expected dates indicated below have been agreed upon:

<b>Key deliverables and expected dates</b>	
<b>Deliverables</b>	<b>Expected dates</b>
Conduct interim audit field work	November 11, 2013 – November 15, 2013
Conduct year-end audit field work	April 2014 – June 2014
Provide audit opinion on financial statements	July 2014

## Recommended improvements

During the course of our audit, we may become aware of opportunities for improvements in financial or operational processes or controls. We will discuss any such opportunities with management and provide our recommendations for performance improvement. We will also include a synopsis of these issues and our recommendations in our discussions with you at the completion of the audit.



# Appendices

**KPMG's Audit Quality Framework**

**Other current developments**

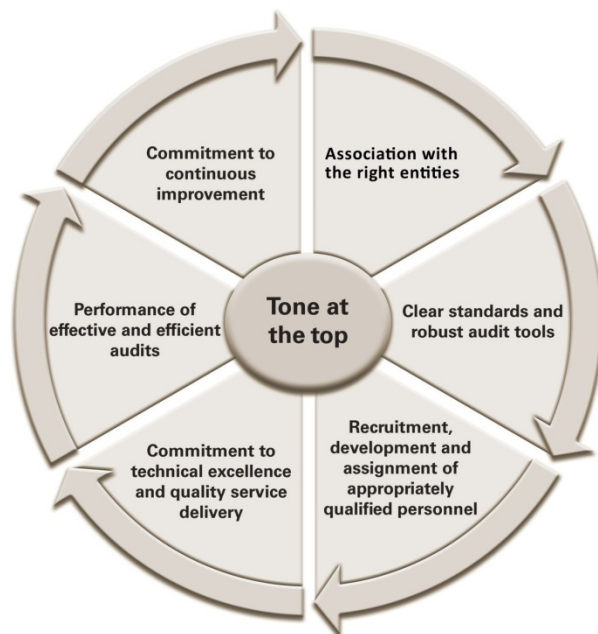
# KPMG's Audit Quality Framework

Audit quality, and the respective roles of the auditor and audit committee, is fundamental to the integrity of financial reporting in our capital markets.

This is why audit quality is at the core of everything we do at KPMG. And we believe that it is not just about reaching the right opinion, but how we reach that opinion.

To help ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.

The framework comprises seven key drivers of audit quality.



## The seven key drivers of audit quality

Driver	What it does	What it means to you
<b>Tone at the top</b>	<p><b>Audit quality is part of our culture and our values and therefore non-negotiable</b></p> <p>Allows the right behaviours to permeate across our entire organization and each of our engagements</p>	<p><b>Assures you that:</b></p> <ul style="list-style-type: none"> <li>Our culture supports our promise to you of excellent service and a high quality audit—consistently</li> <li>You're receiving an independent, transparent, audit opinion</li> <li>You're receiving an effective and high quality audit that will help you maintain investor confidence in your financial statements.</li> </ul> <p><b>Provides you with:</b></p> <ul style="list-style-type: none"> <li>An engagement team handpicked for your business needs – a team with relevant professional and industry experience</li> <li>An audit engagement team whose qualifications evolve as your business grows and changes</li> <li>An audit opinion that continues to meet your needs as a participant in the</li> </ul>
<b>Association with the right entities</b>	<p><b>Ethics above all</b></p> <p>Eliminates any potential independence and conflict-of-interest issues</p>	
<b>Clear standards and robust audit tools</b>	<p><b>A solid rule book</b></p> <p>Rigorous internal policies and guidance that help ensure our work meets applicable professional standards, regulatory requirements, and KPMG's standards of quality</p>	
<b>Recruitment, development and assignment of appropriately qualified personnel</b>	<p><b>People who add value</b></p> <p>Helps us attract and retain the best people and reinforces the importance of developing their talents</p> <p>Assigns Partners' portfolios based on their specific skill sets</p>	
<b>Commitment to technical</b>	<p><b>The right tools for the right job</b></p>	

Driver	What it does	What it means to you
<p><b>excellence and quality service delivery</b></p>	<p>Promotes technical excellence and quality service delivery through training and accreditation, developing business understanding and industry knowledge, investment in technical support, development of specialist networks, and effective consultation processes</p>	<p>capital markets</p> <p><b>Assists you with:</b></p> <ul style="list-style-type: none"> <li>Assessing the effectiveness and efficiency of the audit</li> <li>Performing your governance role with confidence.</li> </ul>
<p><b>Performance of effective audits</b></p>	<p><b>We understand that how an audit is conducted is as important as the final result.</b></p> <p>A code of conduct, audit delivery tools, and internal policies and procedures that help ensure the work performed by engagement personnel meets applicable professional standards, regulatory requirements, and our standards of quality</p>	
<p><b>Commitment to continuous improvement</b></p>	<p><b>Comprehensive and effective monitoring</b></p> <p>We regularly solicit feedback from the audit committees of the entities we audit. Our robust internal quality review program ensures the work of each partner is reviewed every three years. Additionally, our procedures and a sample of our audits of listed entities are reviewed by the Canadian Public Accountability Board (CPAB), the independent regulator of the accountancy profession in Canada. The Public Company Accounting Oversight Board (PCAOB) in the US also conducts an annual inspection of a sample of our audits of SEC registrants. Finally, a sample of other audits and reviews is undertaken annually by the various provincial institutes in Canada. We consider the recommendations that come from these reviews and implement actions to strengthen our policies and procedures, as appropriate.</p>	

### ***The regulatory landscape is changing***

Uncertain economic forecasts and a changing regulatory environment define today's world; reliable financial information and high-quality audits have never been more essential.

We believe that high quality audits contribute directly to market confidence and we share your objectives of credible and transparent financial reporting.

Our Audit Quality Framework is particularly relevant to Audit Committees, and we see our role in being transparent to you as a key mechanism to support you in the execution of your responsibilities.

### ***Our commitment to quality***

The independence, judgment and professional skepticism of your auditors add value to your financial statements, and we believe it is important to be transparent about the processes we follow to develop a KPMG audit report. We want you to have absolute confidence in us and in the quality of your audit.

Our own professional standards dictate technical requirements for reaching and communicating an audit opinion. And we live and abide by these requirements. We invest heavily in our quality, and the Audit Quality Framework helps ensure these investments are the right ones—that they help us continuously drive and maximize our quality improvements. But we feel it is also important that we communicate to you how we view and implement audit quality. The seven key drivers outlined here, combined with the commitment of each individual in KPMG, are meant to do just that.

KPMG member firms across the world use this audit quality framework to describe, focus on and enhance audit quality for the benefit of the entities we audit and in support of the efficacy of our capital markets.

It is our hope that sharing our vision of what audit quality means is a significant step in building confidence in the value of our audits.

**Audit quality is fundamental to the way we work.**

# Other current developments

## **Public Sector Accounting Changes (PSAB)**

### **New Standard on Financial Statement Presentation**

#### **Highlights**

PSAB issued a new standard for accounting for Financial Statement Presentation that replaces PS 1200. This standard establishes general reporting principals and standards for the disclosure of information in government financial statements.

#### **Effective date and transition**

The standard is effective for fiscal periods when sections PS 2601 and PS 3450 are adopted. These are effective beginning on or after April 1, 2015; however, earlier adoption is encouraged.

#### **Implications**

This standard introduces the statement of remeasurement gains and losses, which arise from the requirements in PS 2601 and PS 3450.

### **New Standard on Portfolio Investments**

#### **Highlights**

PSAB issued a new standard for accounting for Portfolio Investments that replaces PS 3040. This standard establishes standards on accounting for and reporting portfolio investments in government financial statements.

#### **Effective date and transition**

The standard is effective for fiscal periods when sections PS 1201, PS 2601, and PS 3450 are adopted. These are effective beginning on or after April 1, 2015; however, earlier adoption is encouraged.

#### **Implications**

This standard revises the definition of portfolio investments, which results in simplified financial reporting and removes the difference between the PSA Handbook and the standards that apply to other Canadian entities. Changes were also made to ensure consistency with section PS 3450. The adoption of this standard will result in a withdrawal of section PS 3030.

### **Revised Standard on Government Transfers**

#### **Highlights**

PSAB issued a revised standard for accounting for Government Transfers. This standard sets out standards on how to account for and report government transfers to individuals, organizations and other governments from both a transferring government and a recipient government perspective.

#### **Effective date and transition**

The standard is effective for fiscal periods beginning on or after April 1, 2012; however, earlier adoption is encouraged. The standard may be applied retroactively or prospectively.

#### **Implications**

The standard will be applicable to the December 31, 2013 fiscal year. This standard could affect the timing of revenue recognition for certain government transfers. Retroactive application of this standard, if chosen, will be challenging since financial records and terms for government transfers received in prior years for capital purposes may not be available.

## **New Standard on Financial Instruments**

### **Highlights**

A new standard has been issued establishing a standard on accounting for and reporting all types of financial instruments including derivatives.

### **Effective date and transition**

The standard is effective for fiscal periods beginning on or after April 1, 2015 for governments; however, earlier adoption is permitted. An entity early adopting this standard must also adopt the revised Foreign Currency Translation standard.

### **Implications**

This standard will require the City to identify any contracts that have embedded derivatives and recognize these on the 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. Long term debt that has been purchased by the City (i.e. investments in own debentures) will have to be accounted for as an extinguishment of that debt. 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 City. These disclosures include classes of financial instruments and qualitative and quantitative risk disclosures describing the nature and extent of risk by type (credit, liquidity and market).

## **Revised Standard on Foreign Currency Translation**

### **Highlights**

A revised standard has been issued establishing standards on accounting for and reporting transactions that are denominated in a foreign currency.

### **Effective date and transition**

The standard is effective for fiscal periods beginning on or after April 1, 2015 for governments; however, earlier adoption is permitted. An entity early adopting this standard must also adopt the new Financial Instruments standard.

### **Implications**

Exchange gains and losses arising prior to settlement are recognized in the statement of remeasurement gains and losses.

## **New Standard on Liability for Contaminated Sites**

### **Highlights**

A new standard has been issued establishing a standard for the recognition of liabilities for contaminated sites.

### **Effective date and transition**

This standard is effective for fiscal years beginning on or after April 1, 2014; however, earlier adoption is encouraged.

### **Implications**

A liability for remediation of contaminated sites should be recognized when an environmental standard exists, the contamination exceeds the environmental standard, the government is directly responsible or accepts responsibility for the remediation, it is expected future economic benefits will be given up and a reasonable estimate of the amount can be made. The liability estimate should include those costs directly attributable to remediation activities.

## **Revised Standard on Tax Revenue**

### **Highlights**

A revised standard has been issued establishing standards on accounting for and reporting tax revenue in government financial statements.

### **Effective date and transition**

The standard is effective for fiscal periods beginning on or after April 1, 2012 for governments.

### **Implications**

This standard provides guidance on the recognition of tax revenue and expenses on a gross versus net basis.

# Recent Developments in the Audit Profession

## Highlights

- The Canadian Public Accountability Board (CPAB) and the Canadian Institute of Chartered Accountants (CICA) collaborated on the development of three papers in 2012 and 2013 related to enhancing audit quality – the auditor reporting model, auditor independence and the role of the audit committee in external auditor oversight. Comment letters have been received for each paper.
- The Independence Working Group (IWG) notes that extensive safeguards already exist in Canada to maintain auditor independence and objectivity. The IWG recommended mandatory comprehensive review by audit committees as the IWG believed it would best achieve the objective of enhancing both audit committee and auditor focus on audit quality and on the exercise of professional skepticism by auditors. The IWG does not support mandatory audit firm rotation and mandatory tendering because of the potential negative consequences to audit quality and associated corporate governance.
- The Audit Committee Working Group (ACWG) which was formed to consider ways in which audit committees can contribute to audit quality, concurred with the recommendations of the IWG. The ACWG recommended that audit committees should conduct a mandatory comprehensive review of the external audit firm at least every five years. KPMG has prepared an assessment form that may be used by audit committees to assist with their comprehensive assessment. We would be pleased to provide and discuss this assessment form with you.
- The Public Company Accounting Oversight Board (PCAOB) issued two concept releases on auditor independence and audit firm rotation for which comments have been received. The primary focus of the first release is mandatory auditor rotation. The second release discusses alternatives for changing the auditor's reporting model to provide investors with more transparency in the audit process and more insight into the company's financial statements or other information outside the financial statements.
- In June, the US House Financial Services Committee unanimously approved a bill that would prohibit mandatory rotation of auditors.
- The European Commission, in addition to other countries around the world, have proposed changes covering many of the same issues discussed above, including auditor independence and auditor rotation.
- KPMG is fully committed to the goal of enhancing audit quality, including auditor independence, objectivity and professional skepticism. We continue to be actively engaged with CPAB, PCAOB and other regulatory bodies to pursue actions aimed at improving audit quality.



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