Toronto Transit Commission

Audit Results – Year Ended 31 December 2008

Report to the Chair and Members of the Toronto Transit Commission

Ernst & Young
Quality In Everything We Do

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9 April 2009

To the Chair and Members of the Toronto Transit Commission

We are pleased to present the results of our audit of the financial statements of the Toronto Transit Commission (the "TTC" or the "organization").

This report to the Chair and Members of the Toronto Transit Commission summarizes the terms of our engagement, the issues of audit significance discussed with management and provides the communications required by our professional standards.

Our audit was designed to express an opinion on the 31 December 2008 financial statements of the TTC. In planning the audit, we held discussions with management, considered current and emerging business risk, performed an assessment of risks that could materially affect the financial statements, and aligned our audit procedures accordingly. We received the full support and assistance of the organization's personnel in conducting our audit.

This report is intended solely for the use of the Audit Committee, the Commission, the Council of the City of Toronto and management, and is not intended to be and should not be used by anyone other than these specified parties. We disclaim any responsibility to any third party who may rely on it. Further, this report is a by-product of our audit of the 2008 financial statements and indicates matters identified during the course of our audit. Our audit did not necessarily identify all matters that may be of interest to the Audit Committee in fulfilling its responsibilities.

We appreciate this opportunity to meet with you to discuss the contents of this report and answer any questions you may have about these or any other audit-related matters.

Very truly yours,

Ernst & Young LLP

Chartered Accountants
Licensed Public Accountants

Items of Audit Significance Discussed with Management

During the course of planning and executing our audit, the following items/matters of audit significance were discussed with management:

Item	Description	Audit Results and Comments
Employee Future Benefit Plans	• In order to estimate the accrued benefit obligation, management must make estimates about a number of matters including the discount rate and future increases in benefit costs and salaries. As set out in note 10, changes in these assumptions can have a significant impact on the amounts recorded in the financial statements. Because the impact of changes is recorded over a number of years, the impact on any individual year is moderated. • In the current year, the discount rate was increased from 5.5% to 7.4% which created actuarial gains.	• We have reviewed management's estimates and believe they are within a zone of reasonableness.
Employee Benefit Provision	• The Commission is currently negotiating an employee benefit provision. Management believes that the ultimate disposition of this matter will not exceed the amount recorded in the accounts. Any additional costs will be recorded when they are known.	• We have reviewed the support related to the amount recorded in the accounts and we concur with the accounting for this matter.
Legal Matters	• There are a large number of claims outstanding against the TTC at any point in time in connection with its operations and capital program. • During the year, the class action suit against the TTC claiming $500 million plus interest and costs in connection with the alleged exposure by workers to asbestos during the construction work at the Sheppard Subway Station was dismissed. As a result, the reference to this claim has been removed from the notes to the financial statements. • Management believes that other outstanding claims are adequately covered by the general comment in note 15[a] that the TTC is subject to various arbitrations, litigations and claims related to its operations, labour relations and completion of capital projects and that the ultimate disposition of these matters will not materially exceed the amounts recorded in the accounts.	• We agree that the disclosures in the financial statements with respect to outstanding legal matters are adequate.
Deferred Revenue	• Last year we noted that there was a balance in deferred revenue of $3,517K related to the old tickets replaced in November, 2007 with the increase in fares. • We estimated that the balance of deferred revenue related to the old tickets was approximately $2 million overstated. We have included this amount on the Summary of Audit Differences as a judgmental difference. • Based on actual experience, the deferred revenue related to old tickets replaced in November, 2007 was $2.5 million overstated.	• We have included $2.5 million on last year's Summary of Audit Differences related to the overstatement of deferred revenue.

Items of Audit Significance Discussed with Management (continued)

Item	Description	Audit Results and Comments
Subsidies	• The funding of the TTC is complex and the notes to the financial statements provide significant detail about capital and operating subsidies in prior years and the current year. In order to ensure that the disclosures are consistent with the City's understanding of funding programs and the accounting for subsidies in the statements of the City, the draft disclosures in notes 12 and 13 were provided to City staff and any suggested changes were reflected in the financial statements provided to the Committee. • Note 14 to the financial statements provides details of transactions in City Reserve Funds. These details reflect information provided to the Commission by City Staff. • In order to obtain assurance about the amounts due to and from the City, TTC provides City staff with a copy of the reconciliation between the amount included in the City's records and the amount recorded in TTC's accounts. There are a number of reconciling items created primarily by timing differences.	• The City has reviewed notes 12, 13 and 14 of the financial statements for accuracy. No issues were noted. • The City has responded to the intercompany balance confirmation and no differences were noted.
Changes in Accounting Policies	• Note 2 refers to accounting policy changes implemented this year. • Additional details have been added to note 3 in order to comply with additional disclosures required to comply with CICA 3862: *Financial Instruments - Disclosures.* • Note 4 has been added to provide information on capital management required to comply with CICA 1535:*Capital Disclosures.* • Note 2 has also been revised to include the required disclosure on future changes in accounting policies.	• We concur with the disclosures in the financial statements as a result of the changes in accounting policies.
Accounting for Spare Parts	• Management reviewed the accounting for spare parts, which consist primarily of items used to repair capital assets. It was determined that these assets meet the definition of items that should be accounted for based on the guidance in CICA 3061: *Property, Plant and Equipment* rather than CICA 3031: *Inventories*. As a result, the line item description has been revised to remove the reference to inventory and the balance has been classified as a long-term rather than current assets.	• We concur with the approach to accounting for spare parts.

Item	Description	Audit Results and Comments
Accounting Standards in Canada: New Directions	• In our audit planning package previously presented to the Audit Committee, under "New Developments in Accounting and Auditing Standards", we informed you of the strategic direction for financial reporting adopted by the Accounting Standards Board ("AcSB") in Canada. • For publicly accountable entities, Canadian GAAP will be replaced by International Financial Reporting Standards ("IFRS") and cease to exist as a separate, distinct basis of financial reporting for publicly accountable enterprises. • The TTC is a government business-type organization ("GBTO") as defined by the Public Sector Accounting Board ("PSAB"). For purposes of financial reporting, government business enterprises ("GBE's") and GBTO's are deemed to be publicly accountable enterprises and are currently required to adhere to the standards applicable to publicly accountable enterprises in the CICA Handbook – Accounting. • As a result, the TTC will be required to apply IFRS under the current direction. Adoption of IFRS is required for years beginning January 1, 2011 (including comparatives for 2010). • Because of feedback suggesting that government organizations should not be required to adopt IFRS, PSAB has issued an Invitation to Comment ("ITC") that sets out alternatives for financial reporting by these organizations. Alternatives presented in the ITC include: – Applying IFRS to those government organizations that meet the definition of 'publicly accountable enterprises' as proposed by the AcSB. GBE's and GBTO's that do not meet the definition would be able to select IFRS or the PSA Handbook, depending on their objectives and circumstances. – Applying IFRS to GBE's as defined by PSAB. GBTO's would be reclassified as "Other Government Organizations" and would be able to select IFRS or the PSA Handbook, depending on their objectives and circumstances. – Applying IFRS to all GBE's, as defined by PSAB, and self-sustaining GBTO's. GBTO's that are not self-sustaining would be able to select IFRS or the PSA Handbook, depending on their objectives and circumstances. – Applying IFRS to all GBE's and only those GBTO's as defined by PSAB that are competing with similar entities outside of the public sector that also follow IFRS.	• The results of the ITC will determine whether amendments to the existing Introduction to Public Sector Accounting Standards are required. Any amendments may change the appropriate source of generally accepted accounting principles used by government organizations, including the TTC. • TTC management reviewed the alternatives proposed by PSAB and responded to the ITC by the deadline of April 17, 2009.

Items of Audit Significance Discussed with Management (continued)

Item	Description	Audit Results and Comments
Cost of Tokens	• In 2006 and 2007, new tokens with a total cost of approximately $1.9 million were purchased and expensed. • In prior years, we included the amounts expensed in the Summary of Audit Differences since we concluded they should be capitalized since they are expected to be used until the new fare card system is implemented. • Management has adjusted the accounts to set up as an asset the tokens expensed in prior years.	• We concur that the tokens should be capitalized. • The impact of adjusting the amount that should not have been expensed in prior years of $1.5 million is picked up in the turnaround impact on the Summary of Audit Differences.
Audit Opinion	• The audit opinion has been revised to include a 4th paragraph referring to the supplementary schedule. In prior years, a separate opinion was provided in front of the schedule.	• The comments in the 4th paragraph are consistent with the comments in the separate opinion provided in prior years.
Inventory Process	• In completing a special audit, we noted that there was no formal process related to the requisition of spare parts used in certain capital projects. • We understand that management has established a more formal process to document the requisition and use of parts in capital projects.	• We suggest that management have Internal Audit check that this new process is working as designed at some point during the year.

Summary of Audit Differences

During the course of our audit, we accumulate differences between amounts recorded by your organization and amounts that we believe are required to be recorded under generally accepted accounting principles. Following is a summary of those differences we have identified through the date of this report:

	Recording/Differences Would Have Increased (Decreased) Net Assets/Excess of Revenue over Expenses	
	2008	**2007**
	$	$
Audit Differences:		
Overstatement of deferred revenues related to tickets	—	2,500
Understatement of long-term assets related to cost of new tokens	—	1,500
Total Unadjusted Audit Differences Before Turnaround Effect of Prior Year Differences	—	4,000
Turnaround Effect of Prior Year Differences in Net Assets	(4,000)	
Total Unadjusted Audit Differences in Excess of Revenue over Expenses	(4,000)	

Required Communications

Generally accepted auditing standards in Canada require the auditor to communicate certain matters to the Audit Committee that may assist them in overseeing management's financial reporting and disclosure process. Below we summarize these required communications as they apply to your organization.

Area	Comments
Auditors' Responsibilities Under Generally Accepted Auditing Standards (GAAS)	
As set out in the planning document presented to the Audit Committee, we designed our audit to express an opinion on your organization's financial statements. The financial statements are the responsibility of management. Our audit was designed in accordance with GAAS which provides for reasonable, rather than absolute, assurance that the financial statements are free from material misstatement. As a part of our audit, we obtained a sufficient understanding of the internal control structure to plan our audit and to determine the nature, timing and extent of testing performed.	We anticipate issuing an unqualified audit opinion dated March 25, 2009 upon approval of the financial statements by the Commission and completion of certain outstanding procedures. The following procedures are outstanding: • signed letter of representation; • review of Annual Report;
Changes to Audit Approach Outlined in Planning Document	
In our planning document, we indicated that we would obtain an understanding of the business and controls to provide the basis for our audit risk assessments, and the identification of audit procedures responsive to those risk assessments. This balanced approach is designed to focus comparatively more audit effort on complex, higher-risk areas than on those assessed as lower risk. We indicated that our audit would focus significant attention on the various estimates required to prepare the financial statements. We indicated that we would review the assumptions used for reasonableness and the detailed calculations. We planned to rely on systems and therefore test relevant controls over the more significant revenues and disbursements.	There were no changes to the audit approach outlined in the planning document.

Area	Comments
Adoption of, or Changes in, an Accounting Principle, Including Material Alternative Accounting Treatments Discussed with Management and Acceptability of a Particular Policy used by Management We determine that the Audit Committee is informed about the initial selection of, and any changes in, significant accounting principles or their application when the accounting principle or its application, including alternative methods of applying the accounting principle, has a material effect on the financial statements. In addition, we report to the Audit Committee all alternative accounting treatments within Canadian generally accepted accounting principles (GAAP) for policies and practices related to material items (including recognition, measurement, presentation and disclosure alternatives) that have been discussed with management during the current audit period including acceptability of the policies or methods ultimately selected by management.	Refer to “Items of Audit Significance Discussed with Management" section.
Our Judgments About the Quality of the Organization's Accounting Principles We discuss our judgments about the quality, not just acceptability, of the accounting principles as applied in the organization's financial reporting, including the consistency of the accounting policies and their application and the clarity and completeness of the financial statements and related disclosures.	Refer to “Items of Audit Significance Discussed with Management” section.
Sensitive Accounting Estimates and Disclosures The preparation of financial statements requires the use of accounting estimates. Certain estimates and disclosures are particularly sensitive due to their significance to the financial statements and the possibility that future events may differ significantly from management’s current judgments. We determine that the Audit Committee is informed about management’s process for formulating particularly sensitive accounting estimates and disclosures and about the basis for our conclusions regarding the reasonableness of those estimates.	Refer to “Items of Audit Significance Discussed with Management” section.

Required Communications (continued)

Area	Comments
Major Issues Discussed with Management Including Accounting for Significant Unusual Transactions and for Controversial or Emerging Areas	
We determine that the Audit Committee is informed about the methods used to account for significant unusual transactions and the effects of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.	We are not aware of any significant unusual transactions recorded by the organization or of any significant accounting policies used by the organization related to controversial or emerging areas for which there is a lack of authoritative guidance.
Significant Audit Adjustments and Unrecorded Audit Differences Considered by Management to be Immaterial	
We provide the Audit Committee with information about adjustments arising from the audit (whether recorded or not) that could in our judgment either individually or in the aggregate have a significant effect on the organization's financial statements.	There were no recorded audit adjustments related to the current year.
We inform the Audit Committee about unrecorded audit differences accumulated by us (i.e. adjustments either identified by us or brought to our attention by management) during the current audit period and pertaining to the latest period presented that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements taken as a whole.	Refer to "Summary of Audit Differences" section for details of unrecorded differences.
Disagreements with Management	None.
Serious Difficulties Encountered in Dealing with Management when Performing the Audit	None.
Significant Weaknesses in Internal Controls	
We communicate all significant weaknesses in internal control over financial reporting that may have been identified during the course of our audit.	No significant weaknesses in internal control were identified.
Fraud and Illegal Acts	
We report to the Audit Committee fraud and illegal acts involving senior management and fraud and illegal acts (whether caused by senior management or other employees) that cause a material misstatement to the financial statements.	We are not aware of any matters that require communication.
We are also required to make inquiries of the Audit Committee related to fraud, including both (1) their views about the risks of fraud, and (2) their knowledge of any actual or suspected fraud.	We would request that the Audit Committee members raise with us any areas of risk not addressed in our communications and that they inform us of their knowledge of any actual or suspected fraud.

Area	Comments
Consultation with Other Accountants	None of which we are aware.
Other Information in Documents Containing Audited Financial Statements Our financial statement audit opinion relates only to the financial statements and accompanying notes. However, we also review other information in the Annual Report, such as Management's Discussion and Analysis, for consistency with the audited financial statements.	Once completed, we will review the Annual Report for consistency between the audited financial statements and other sections of that document.
Related Party Transactions Related party transactions identified by the auditor that are not in the normal course of operations or that involve significant judgments made by management concerning measurement or disclosure must be disclosed to the Audit Committee.	None of which we are aware.
Major Issues Discussed with Management in Connection with Initial or Recurring Retention	None.
Auditors' Independence Canadian generally accepted auditing standards (GAAS) require that we communicate at least annually with you regarding all relationships between your organization and Ernst & Young that, in our professional judgment, may reasonably be thought to bear on our independence.	Refer to "Independence Letter" section.
Fees	• A summary of our fees is included below for your reference.

	2008 $	2007 $
Annual audit fees:		
Toronto Transit Commission	94,580	57,143
Toronto Coach Terminal Inc.	7,985	4,762
TTC Insurance Company Limited	19,200	9,524

All fees noted are in accordance with the contract with the City of Toronto and include all applicable expenses and taxes.

Area	Comments
Other Services	• We are in the process of completing a special audit of disbursements of $284 million related to a claim of $113 million under the CSIF program.

Independence Letter

9 April 2009

To the Chair and Members of
the Toronto Transit Commission

We have been engaged to audit the financial statements of the Toronto Transit Commission (the "TTC") for the year ended 31 December 2008.

Pursuant to Canadian generally accepted auditing standards, we communicate at least annually with you regarding all relationships between Ernst & Young and its related entities and the TTC and its related entities that, in our professional judgment, may reasonably be thought to bear on our independence.

We have prepared the following comments to facilitate our discussion with you regarding independence matters arising since 8 April 2008, the date of our last letter.

We are not aware of any relationships between Ernst & Young and the TTC that, in our professional judgment, may reasonably be thought to bear on our independence since 16 April 2008, the date of our last letter.

Canadian generally accepted auditing standards require that we confirm our independence to the Audit Committee in the context of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario. Accordingly, we hereby confirm that we are independent with respect to the TTC within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario as of 8 April 2009.

The total fees charged to the TTC during this period are set out in the Audit Results package.

We are looking forward to discussing with you the matters addressed in this package at our upcoming meeting.

This report is intended solely for the use of the Audit Committee, management, and others within the TTC and should not be used for any other purposes.

Yours truly,

Ernst & Young LLP

Chartered Accountants
Licensed Public Accountants

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