

Mission Statement

Freedom to Discover

Strategic Priorities

*A Community Beacon Relevant and Responsive
A Creative and Changing Organization*

HAMILTON PUBLIC LIBRARY BOARD

Audit Committee Meeting

Tuesday, February 7th, 2017

Central Library, Admin Committee Room

4:00 p.m. Meeting

AGENDA

1. **Acceptance of the Agenda**
2. **Appointment of Chair**
3. **HPL Audit Planning Report** Attachment #1
4. **Auditor and Audit Committee meet without Staff**
5. **Adjournment**



Hamilton Public Library Board

Audit Planning Report
For the year ended December 31, 2016

KPMG LLP

February 7, 2017

kpmg.ca/audit



The contacts at KPMG in connection with this report are:

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At KPMG, we are **passionate** about earning your **trust**. We take deep **personal accountability**, individually and as a team, to deliver **exceptional service and value** in all our dealings with you.

At the end of the day, we measure our success from the **only perspective that matters – yours**.

Executive summary

Audit and business risk

Our audit is risk-focused. In planning our audit we have taken into account key areas of focus for financial reporting. These include:

- Government grants
- Prepaid expenses
- Tangible capital assets
- Employee future benefits
- Operating expenditures including salaries and benefits

See pages 4 – 5

KPMG team

The KPMG team will be led by Lois Ouellette. She will be supported by a local Hamilton based team. Subject matter experts and specialists will be involved where appropriate to ensure our approach is appropriate and robust.

See page 8 for further details

Effective communication

We are committed to transparent and thorough reporting of issues to the management team and the Audit Committee. We have planned our work to closely coordinate and communicate with the Audit Committee throughout the annual audit process.

Audit Materiality

Materiality has been determined based on fiscal 2015 audited revenues. We have estimated materiality to be \$800,000 for the year ending December 31, 2016 (2015 - \$610,000).

See page 7

Independence

We are independent and have extensive quality control and conflict checking processes in place. We provide complete transparency on all services and follow approved protocols set by the City of Hamilton.

Current developments

Please refer to Appendix 5.

Audit approach

Professional standards presume the risk of fraudulent revenue recognition and the risk of management override of controls exist in all companies.

The risk of fraudulent recognition can be rebutted, but the risk of management override of control cannot, since management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Professional requirements	Why	Our audit approach
Fraud risk from revenue recognition	This is a presumed fraud risk. We have not identified any specific additional risk of fraud with respect to revenue recognition relating to this audit.	<ul style="list-style-type: none"> Our audit approach will consist of performing substantive procedures to address the relevant assertions associated with revenue.
Fraud risk from management override of controls	This is a presumed fraud risk. We have not identified any specific additional risk of management override relating to this audit. We will perform additional testing over the risk of management override of controls based on the turnover in key Finance role at the Library.	<ul style="list-style-type: none"> Our audit approach incorporates the required procedures in professional standards to address this risk. These procedures include testing of journal entries and other adjustments and making inquiries of the appropriate individuals: <ul style="list-style-type: none"> whether they have been asked to record, or are aware of, unusual or otherwise inappropriate journal entries or adjustments without adequate support or explanation for the entries or adjustments; Inquire whether there have been any instances of overrides of controls through recording of journal entries or other adjustments; Inquire whether there have been any journal entries or other adjustments that have been initiated by management outside the normal course of business, We will perform a retrospective review of estimates and evaluate the business rationale of significant unusual transactions.

Audit approach (continued)

We have not identified any risks that we deem to be significant financial reporting risks.

Other areas of focus include the following:

Other areas of focus	Why	Our audit approach
Government grants	Risk related to completeness and accuracy of timing of revenue recognition	<ul style="list-style-type: none"> We will perform substantive procedures to address relevant risk. This includes agreeing significant receivables to subsequent receipts and confirming significant grant balances.
Prepaid expenses	Completeness and accuracy of prepaid subscriptions. The Library continues to introduce more digital media resulting in more subscriptions	<ul style="list-style-type: none"> Performing a review of significant subscription agreements and assessing the prepaid portion as of the year end date, based on the period covered by the subscription agreements.
Tangible capital assets	Completeness and accuracy of tangible capital assets. Risk also related to the existence, presentation and disclosure of any commitments related to capital projects that may be on the City's financial statements.	<ul style="list-style-type: none"> Performing a review of significant capital additions including vouching to supporting documentation We will examine major capital projects and any commitments requiring disclosure in the audited financial statements.
Employee future benefits	Completeness and accuracy of the post retirement liability and related expenses. Reliance is placed on the actuarial valuation and extrapolations performed by the actuaries in determining the accrued postemployment benefit liability at the end of each fiscal year. Actuarial determination of both post-employment benefits and sick leave benefits is required under PSAB standards.	<ul style="list-style-type: none"> Performing substantive procedures, including review of assumptions and application of assumptions. Obtain access to management's expert (the actuaries) and their reports identifying the accrued benefit obligations for vested sick leave and retirement benefit liabilities. Obtain a copy of the actuarial extrapolation of the liability for the year ending December 31, 2016. We will review note disclosure to ensure it is appropriate.
Operating expenditures including salaries and benefits	Completeness, existence and accuracy of expenses and completeness of related accounts payable and accrued liabilities.	<ul style="list-style-type: none"> We will perform substantive procedures to address the relevant risk. This includes reviewing significant accruals and vouching to supporting documentation, as well as a search for unrecorded liabilities to assess completeness and accuracy of accruals at year-end. We will perform substantive analytical procedures over payroll and non-payroll expenditures.

Data & analytics in the audit

We will be integrating Data & Analytics (D&A) procedures into our planned audit approach.

Use of innovative D&A allows us to analyze greater quantities of data, dig deeper and deliver more value from our audit.

We believe that D&A will improve both the quality and effectiveness of our audit by allowing us to analyze large volumes of financial information quickly, enhancing our understanding of your business as well as enabling us to design procedures that better target risks.

Area(s) of focus	Planned D&A routines
Journal entry testing	<ul style="list-style-type: none"><li data-bbox="909 500 1934 565">– Utilizing KPMG application software (IDEA) to evaluate the completeness of the journal entry population through a roll-forward of all accounts<li data-bbox="909 594 1980 659">– Utilizing computer-assisted audit techniques (CAATs) to analyze journal entries and apply certain criteria to identify potential high-risk journal entries for further testing

Detailed results and summary insights gained from D&A will be shared with management and presented in our Audit Findings Report.

Materiality

Professional standards require us to re-assess materiality at the completion of our audit based on period-end results or new information in order to confirm whether the amount determined for planning purposes remains appropriate.



Our assessment of misstatements, if any, in amounts or disclosures at the completion of our audit will include the consideration of both quantitative and qualitative factors.

The first step is the determination of the amounts used for planning purposes as follows.

The determination of materiality requires professional judgment and is based on a combination of quantitative and qualitative assessments including the nature of account balances and financial statement disclosures.

Materiality determination	Comments	Amount
Metrics	Relevant metrics include total revenues, total expenses and net assets	Total Revenues
Benchmark	Based on prior year total revenues. This benchmark is consistent with the prior year.	\$ 31,005,761
% of Benchmark	The Corresponding percentage for the prior year's audit was 2%	2.5%
Materiality	Determined 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 corresponding amount for the prior year's audit was \$610,000.	\$ 800,000
Performance Materiality	Used 75% of materiality, and used primarily to determine the nature, timing and extent of audit procedures. The corresponding amount for the prior year's audit was \$457,500.	\$ 600,000
Audit Misstatement Posting Threshold (AMPT)	Threshold used to accumulate misstatements identified during the audit. The corresponding amount for the previous year's audit was \$30,500	\$ 40,000

Highly talented team

	Team member	Background / experience	Discussion of role
	<p>Lois Ouellette, CPA, CA Lead Audit Engagement Partner louellette@kpmg.ca 905-687-3286</p>	<ul style="list-style-type: none"> Lois has over 30 years in the public sector and not-for-profit sector including acting as the Lead Audit Engagement Partner for the City of Hamilton. Lois is a PSAB resource within the firm which has her well positioned to lead this audit. 	<ul style="list-style-type: none"> Lois will lead our audit and be responsible for the quality and timeliness of everything we do. She will be your main point of contact and will always be available and accessible to management and the Board.
	<p>Scott Plugers, CPA, CA Audit Manager splugers@kpmg.ca 905-687-3286</p>	<ul style="list-style-type: none"> Scott is a 2nd year manager with over 5 years' experience in public sector accounting as well as not-for-profit accounting. He works with a number of not-for-profit organizations in the municipal space. 	<ul style="list-style-type: none"> Scott will work very closely with Lois on all aspects of our audit for the Library. He will be on site and directly oversee and manage our audit field work and work closely with your management team.

Value for fees

The value of our audit services

We recognize that the primary objective of our engagement is the completion of an audit of the consolidated financial statements in accordance with professional standards. We also believe that our role as external auditor of the Library and the access to information and people in conjunction with our audit procedures, place us in a position to provide other forms of value. We know that you expect this of us.

We want to ensure we understand your expectations. To facilitate a discussion (either in the upcoming meeting or in separate discussions), we have outlined some of the attributes of our team and our processes that we believe enhance the value of our audit service. We recognize that certain of these items are necessary components of a rigorous audit. We welcome your feedback.

- Extensive industry experience on our audit team – as outlined in our team summary, the senior members of our team have extensive experience in audits of companies in your industry. This experience ensures that we are well positioned to identify and discuss observations and insights that are important to you;
- Involvement of KPMG specialists – Our audit team is supported by specialists in income and other taxes, information risk management, and others as required. We expect each of the specialists to provide insights and observations resulting from their audit support processes;

Value for fees (continued)

In determining the fees for our services, we have considered the nature, extent and timing of our planned audit procedures as described above. Our fees are consistent with those outlined in our audit proposal to you.

Our fees are estimated as follows:

	Current period (budget)	Prior period (actual)
Audit of the annual financial statements	\$6,600	\$6,600
Audit of the trust funds	\$1,000	\$1,000

Matters that could impact our fee

The proposed fees outlined above are based on the assumptions described in our audit proposal. The critical assumptions, and factors that cause a change in our fees, include:

- Significant changes in the nature or size of the operations of the Library beyond those contemplated in our planning processes;
- Changes in professional standards or requirements arising as a result of changes in professional standards or the interpretation thereof;
- Changes in the time of our work; and
- Management will provide agreed upon working papers and financial statements for audit based upon the agreed upon timeline.

Audit cycle and timetable

Our key activities during the year are designed to achieve our one principal objective:

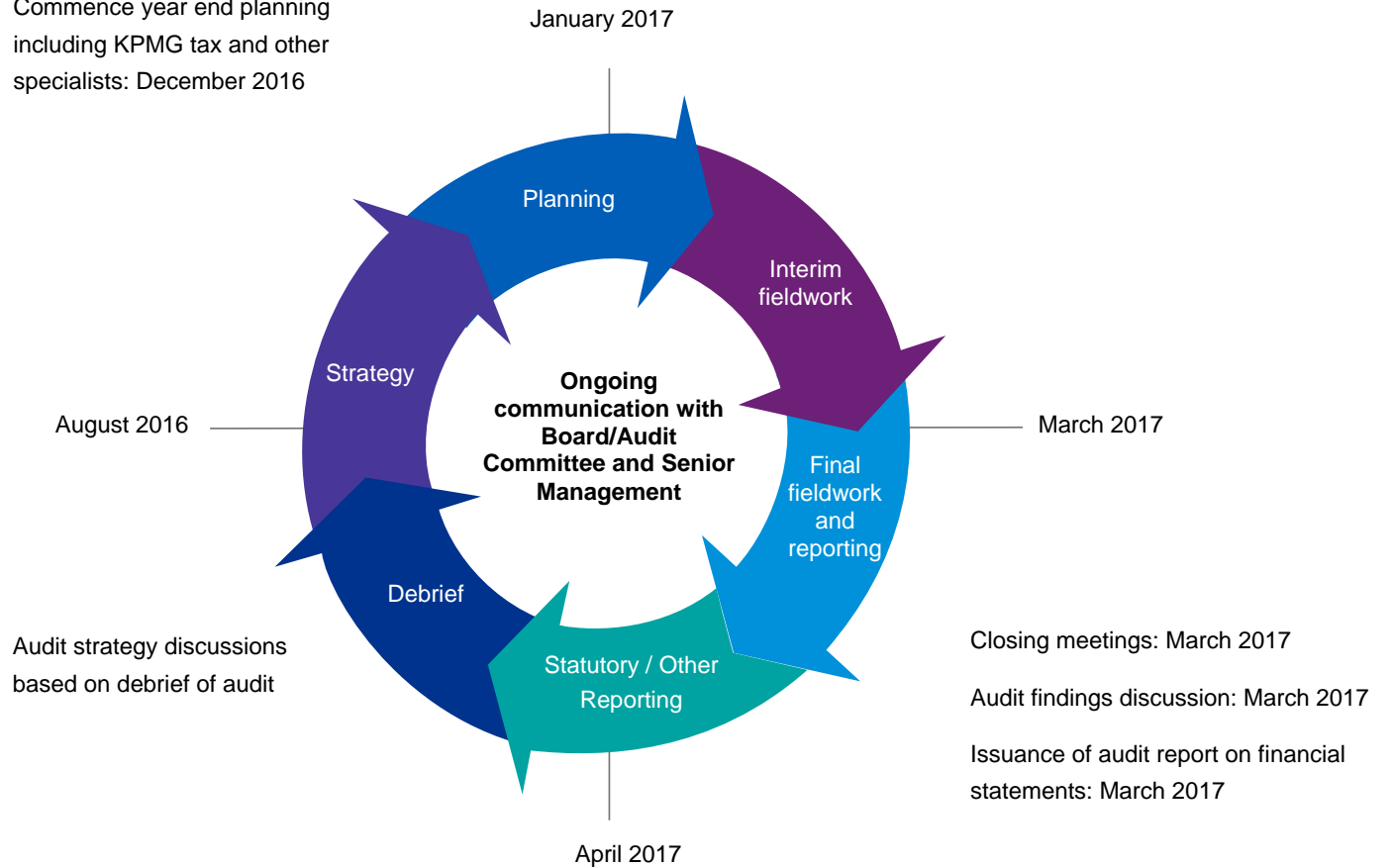
To provide a robust audit, efficiently delivered by a high quality team focused on key issues.

Our timeline is in line with prior year.

Planning meeting with management: November 2016

Commence year end planning including KPMG tax and other specialists: December 2016

Audit plan discussion: February 2017



Appendices

Appendix 1: Audit quality and risk management

Appendix 2: KPMG's audit approach and methodology

Appendix 3: Required communications

Appendix 4: Data & analytics in audit

Appendix 5: Current developments

Appendix 1: 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 our [Audit Quality Resources](#) page for more information including access to our audit quality report, [Audit quality: Our hands-on process](#).

- Other controls include:
 - Before the firm issues its audit report, 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 2: KPMG's audit approach and methodology

Technology-enabled audit workflow (eAudit)

Engagement Setup

- Tailor the eAudit workflow to your circumstances
- Access global knowledge specific to your industry
- Team selection and timetable

Completion

- Tailor the eAudit workflow to your circumstances
- Update risk assessment
- Perform completion procedures and overall evaluation of results and financial statements
- Form and issue audit opinion on financial statements
- Obtain written representation from management
- Required Audit Committee communications
- Debrief audit process



Risk Assessment

- Tailor the eAudit workflow to your circumstances
- Understand your business and financial processes
- Identify significant risks
- Plan the use of KPMG specialists and others including auditor's external experts, management experts, internal auditors, service organizations auditors and component auditors
- Determine audit approach
- Evaluate design and implementation of internal controls (as required or considered necessary)

Testing

- Tailor the eAudit workflow to your circumstances
- Perform tests of operating effectiveness of internal controls (as required or considered necessary)
- Perform substantive tests

Appendix 3: Required communications

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

- **Engagement letter** – the objectives of the audit, our responsibilities in carrying out our audit, as well as management’s responsibilities, are set out in the engagement letter and any subsequent amendment letters
- **Audit planning report** – as attached
- **Required inquiries** – professional standards require that during the planning of our audit we obtain your views on risk of fraud and other matters. We make similar inquiries to management as part of our planning process; responses to these will assist us in planning our overall audit strategy and audit approach accordingly
- **Management representation letter** – we will obtain from management certain representations at the completion of the annual audit. In accordance with professional standards, copies of the representation letter will be provided to the Audit Committee
- **Audit findings report** – at the completion of our audit, we will provide a report to the Audit Committee

Appendix 4: Data & analytics in audit

Turning data into value

KPMG continues to make significant investments in our Data & Analytics (D&A) capabilities to help enhance audit quality and provide actionable insight to our clients by unlocking the rich information that entities hold.

When D&A is applied to the audit, it enables us to test complete data populations and understand the business reasons behind outliers and anomalies.

Advancements in D&A tools allow us to analyze data at more granular levels, focusing on higher risk areas of the audit and developing insights you can then leverage to improve compliance, potentially uncover fraud, manage risk and more.

KPMG is enhancing the audit

The combination of our proven industry experience, technical know-how and external data allows us to focus our audit on the key business risks, while providing relevant insights of value to you.

For the audit

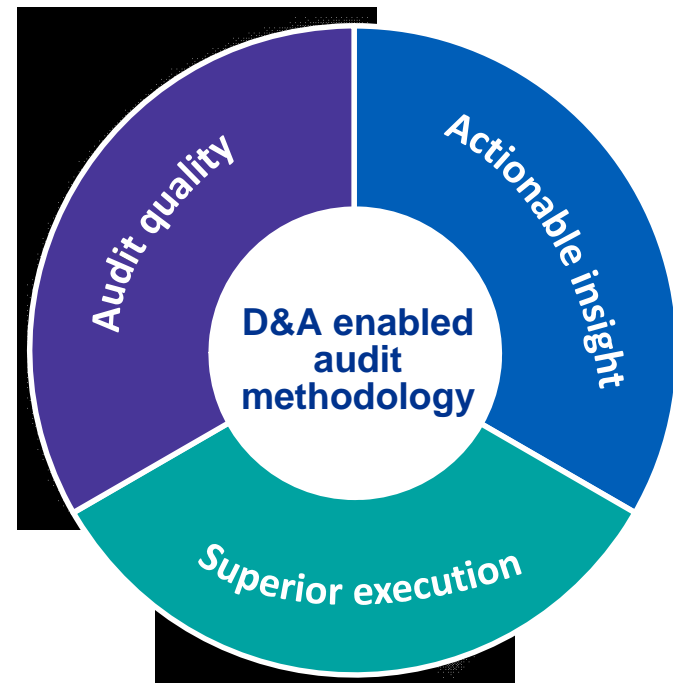
Audit quality

- Automated testing of 100% of a population
- Focuses manual audit effort on key exceptions and identified risk areas

For your utility

Actionable insight

- Helping you see your utility from a different perspective
- How effectively is your organization using your systems?



Appendix 5: Current developments

Current Developments, created by the KPMG Public Sector and Not-for-Profit Practice, summarizes regulatory and governance matters impacting charities and not-for-profit organizations today, or expected to impact over the next few years. We provide this information to help not-for-profit organizations understand upcoming changes and challenges they may face in their industry. We attach this summary to every audit plan and audit findings report that we provide to our public sector and not-for-profit clients. Some of these developments may not impact your organization directly but we believe it is important for audit committee members of charities and not-for-profit organizations to understand what is happening in the sector.

Annual Accounting, Tax and Risk Update for Not-for-Profit Organizations

KPMG will be holding its Annual Accounting, Tax & Risk Update for Not-for-Profit Organizations in early April 2017 at the KPMG office in downtown Ottawa. The seminar will cover current accounting, tax, technology and risk issues, including those discussed below, in greater detail to provide not-for-profit organizations and charities with guidance on new standards, regulations and best practices.

In prior years, this event has consistently attracted over 100 executives, financial officers and Board members from the Ottawa and area not-for-profit and charity community. Invitations and additional details will be provided to management in the near future. We are looking forward to a great event.

Audit Committee members are also invited to attend this session. If you wish to have your name included on the invite list, please e-mail Chelsey Croteau at ccroteau@kpmg.ca

Fraud Risk in Charities and Not-for-Profit Organizations

You only have to read the local and national news to understand the significant, adverse impact that a fraudulent or illegal act can have on an entity's financial position, on-going operations and public reputation. For charities and not-for-profit organizations, a fraudulent or illegal act can be absolutely devastating not only because of their reliance on public financial support but also their need to maintain public confidence and trust in their activities. With social media, and the 24-hour continuous news cycle, the financial, operational and reputational risk of a fraud on a charity or not-for-profit organization has never been higher.

Therefore, fraud risk management is now a very important element of an organization's overall governance and risk management. To protect against the risk of fraud, Boards and management need to have a heightened awareness of fraud including an understanding of the profile of a fraudster and what may drive otherwise good people to do bad things. As a result, Boards and management of charities and not-for-profit organizations are beginning to incorporate fraud awareness in their training programs to increase their personal

individual fraud awareness, and to develop a greater understanding of the key organizational elements of a robust anti-fraud program, designed to address the core objectives of prevention, detection and response.

Cyber Security - It's more than just Technology

Organizations are subject to increasing amounts of legislative and public pressures to show they are managing and protecting their information appropriately. Simultaneously, the threats from cyber criminals and hackers are growing in scale and sophistication. Organizations are also increasingly vulnerable as a result of technological advances and changing working practices including remote access, cloud computing, mobile technology and services on demand. The financial and reputational costs of not being prepared against a cyber-attack could be significant.

Cyber Security is not solely about Information Technology; it is fundamentally an operational and governance issue. Not-for-profit organizations should develop an operations-wide understanding of their threats, safeguards, and responses. Preparing this summary diagnostic will require the involvement of individuals in all areas of the organization, including those involved in hiring, procurement, customer relations and management. Key elements to consider include:

- Assessing the likelihood and intensity of a cyber-attack, based on the value of your information and your public profile
- Assessing your vulnerabilities to a cyber-attack
- Preparing your people, processes, infrastructure and technology to resist a cyber-attack, and to minimize its impact
- Detecting a cyber-attack and initiating your response
- Containing and investigating the cyber-attack
- Recovering from a cyber-attack and resuming business operations
- Reporting on and improving security

Not-for-profit organizations are at particular risk due to the information they maintain, including research data, member or student data, and health information. The reputational risk of this information not being adequately protected can often outweigh the financial consequences of a breach.

Not-for-profit organizations need to review their operations and consider cyber risks, then assess the organization's cyber maturity in addressing those risks. Structured models for completing this exercise exist for organizations of all sizes, as no one is immune to the risk of a cyber-attack.

KPMG in Canada, in collaboration with Imagine Canada, presented a webinar called "Cyber Security: The new threat for Not-for-Profit Organizations". We encourage you to view this webinar on Imagine Canada's website at: <http://sectorsource.ca/resource/video/cyber-security-not-profit-organizations-presented-kpmg>

Commodity Tax Considerations

The GST/HST is constantly evolving. The kinds and pace of the changes affecting your organization will depend on your status and activities, and may result from new legislative and regulatory rules, court cases, and changes in the CRA's administrative policies. In addition, major organization changes, such as reorganizations, cessation of activities, major capital projects, new relationships (e.g., shared service arrangements), and new revenue generating activities may have significant GST/HST implications.

The Canada Revenue Agency (CRA) continues to increase its focus on public service bodies (e.g., municipalities, universities, colleges, hospitals, schools, associations, charities, non-profits etc.) for purposes of conducting GST/HST audits. These audits may be undertaken by GST/HST audit teams dedicated to the public sector or by auditors attached to the CRA's GST/HST Refund Integrity Unit. Many organizations have undergone audits over the past couple of years. Based on our work with audited organization, we offer the following general observations on the impact of the CRA's ongoing focus on the public sector:

- The CRA has been focusing on documentation, cost sharing and buying group arrangements, grants and sponsorships, as well as the allocation of inputs between taxable and exempt activities for input tax credit purposes (e.g. the filing of a Section 211 election and claiming of input tax credits on the use of real property).
- The CRA has not consistently been applying audit offsets (e.g., allowing unclaimed input tax credits or rebates) that would help minimize the impact of any assessments.
- Proposed assessments based on sampling and alternative valuation or allocation methodologies conducted by CRA auditors should be reviewed as fair and reasonable alternatives may be available that could significantly reduce an GST/HST assessment.
- The CRA is required to communicate the amount and basis for a proposed to the registrant, and should allow the registrant a reasonable amount of time to review and respond to the assessment (i.e., generally 30-days). It is entirely appropriate to carefully review and question a proposed assessment. Our experience is that proposed assessments can often be significantly reduced at the audit stage. If a Notice of Assessment is issued, you will have 90 days to file a Notice of Objection with the CRA.
- It is important that you have a plan in place for a GST/HST audit, including having a fixed point of contact for the auditor. Planning and managing the audit is as important as having the appropriate policies and procedures.
- Organizations that have undergone significant changes in operations are more likely to be selected for an audit. Many of these organizations are completing compliance reviews by indirect tax professionals in advance of a potential GST/HST audit to verify that the GST/HST is being appropriately handled.

Our experience with GST/HST auditors has varied from audit to audit. However, in each case, the taxpayer has the burden of proof. The best approach is to be prepared in advance of receiving that audit notification from CRA.

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