



The Board of Directors  
Los Angeles County Metropolitan Transportation Authority  
Los Angeles, California

Professional standards require that we communicate certain matters to keep you adequately informed about matters related to the financial statement audit that are, in our professional judgment, significant and relevant to your responsibilities in overseeing the financial reporting process. We communicate such matters in this report.

#### **AUDITOR'S RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA**

Our responsibility is to form and express an opinion about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America. The audit of the financial statements does not relieve you of your responsibilities and does not relieve management of their responsibilities. Refer to our engagement letter with the Los Angeles County Metropolitan Transportation Authority (LACMTA) for further information on the responsibilities of management and of Crowe Horwath LLP.

#### **AUDITOR'S RESPONSIBILITY UNDER GOVERNMENT AUDITING STANDARDS**

As part of obtaining reasonable assurance about whether LACMTA's financial statements are free of material misstatement, we performed tests of LACMTA's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts or disclosures. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

#### **PLANNED SCOPE AND TIMING OF THE AUDIT**

We are to communicate an overview of the planned scope and timing of the audit. Accordingly, the following matters will be discussed during our meeting with you.

- How we addressed the significant risks of material misstatement, whether due to fraud or error.
- Our approach to internal control relevant to the audit.
- The concept of materiality in planning and executing the audit, focusing on the factors considered rather than on specific thresholds or amounts.
- Where the entity has an internal audit function, the extent to which the auditor used the work of internal audit, and how the external and internal auditors best work together.

- Your views and knowledge about matters you consider warrant our attention during the audit, as well as your views on:
  - The allocation of responsibilities between you and management.
  - The entity's objectives and strategies, and the related business risks that may result in material misstatements.
  - Significant communications with regulators.
  - Other matters you believe are relevant to the audit of the financial statements.
- Matters relative to the use of other auditors/other accountants during the audit:
  - An overview of the type of work to be performed by other auditors/other accountants.
  - The basis for the decision to make reference to the audit of the other auditor in our report on the entity's financial statements.
  - An overview of the nature of our planned involvement in the work to be performed by the other auditor/other accountant.

**SIGNIFICANT ACCOUNTING POLICIES AND MANAGEMENT JUDGMENTS AND ACCOUNTING ESTIMATES**

Significant Accounting Policies: The Board of Directors should be informed of the initial selection of and changes in significant accounting policies or their application. Also, the Board of Directors should be aware of methods used to account for significant unusual transactions and the effect of significant accounting policies in controversial or emerging areas where there is a lack of authoritative consensus. We believe management has the primary responsibility to inform the Board of Directors about such matters. To assist the Board of Directors in its oversight role, we also provide the following.

| <b>Accounting Standard</b>  | <b>Impact of Adoption</b>  |
|---|--|
| <p><b>GASB Statement No. 68, Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27.</b> The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities.</p>  | <p>Upon adoption of this Statement, LACMTA reduced beginning unrestricted net position by \$397.7 million. This was comprised of a net pension liability of \$467.2 million and deferred outflows of resources for pension contributions made after the actuarial measurement date of \$69.5 million at June 30, 2014.</p> |
| <p><b>GASB Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB Statement No. 68.</b> This standard requires a government to recognize a beginning deferred outflow of resources for its pension contributions made during the time between the measurement date of the beginning net pension liability and the beginning of the initial fiscal year of implementation of the new pension standards. Recognition of this amount will eliminate a potential source of understatement of restated beginning net position and expense in the first year of a government's implementation of GASB Statement No. 68, "Accounting and Financial Reporting for Pensions."</p> | <p>This Statement was adopted concurrently with GASB Statement No. 68 above.</p>   |

Management Judgments and Accounting Estimates: Further, accounting estimates are an integral part of the financial statements prepared by management and are based upon management's current judgments. These judgments are based upon knowledge and experience about past and current events and assumptions about future events. Certain estimates are particularly sensitive because of their significance and because of the possibility that future events affecting them may differ markedly from management's current judgments and may be subject to significant change in the near term.

The following describes the significant accounting estimates reflected in LACMTA's year-end financial statements, the process used by management in formulating these particularly sensitive accounting estimates and the primary basis for our conclusions regarding the reasonableness of those estimates.

| <b>Significant Accounting Estimate</b>                               | <b>Process Used by Management</b>  | <b>Basis for Our Conclusions</b>  |
|--|--|---|
| Allowance for Doubtful Accounts and Bad Debt Expense                 | The allowance for doubtful accounts was determined by management by a process involving consideration of past experiences, current aging information, information from credit reports, contacts with the customers, and other available data including environmental factors such as industry, geographical, economic and political factors.                         | We tested this accounting estimate by reviewing, on a test basis, the information listed and by testing information in certain customers' credit files. |
| Fair Values of Investment Securities and Other Financial Instruments | The disclosure of fair values of securities and other financial instruments requires management to use certain assumptions and estimates pertaining to the fair values of its financial assets and financial liabilities.  | We tested the propriety of information underlying management's estimates.   |
| Accrued Compensated Absences   | Accrued compensated absences are estimated based on vacation and sick hours accumulated by each employee and the respective pay rate of each employee.   | We tested the propriety of information underlying management's estimates.   |
| Useful Lives of Capital Assets                                       | Management has determined the economic useful lives of capital assets based on past history of similar types of assets, future plans as to their use, and other factors that impact their economic value to LACMTA.  | We tested the propriety of information underlying management's estimates.   |
| Pension and Postretirement Obligations                               | Amounts reported for pension and postretirement obligations require management to use estimates that may be subject to significant change in the near term. These estimates are based on projection of the weighted average discount rate, rate of increase in future compensation levels, and weighted average expected long-term rate of return on pension assets. | We reviewed the reasonableness of these estimates and assumptions.  |



| Significant Accounting Estimate | Process Used by Management  | Basis for Our Conclusions  |
|---------------------------------|---|--|
| Derivatives and Hedging         | LACMTA uses derivatives to hedge the cash flows of price fluctuations in diesel fuel. Management has recorded this hedge based on the provisions of GASB Statement No. 53, <i>Accounting and Financial Reporting for Derivative Instruments</i> (GASB 53). The investment in the derivative investment is recorded in the Statements of Net Position as part of current assets/liabilities and other non-current assets/liabilities, as appropriate. The change in fair value of the derivative investment is recorded as a deferred inflow/outflow, as appropriate. Any gain (loss) on the sale of the derivative is recorded in the Statements of Revenues, Expenses and Changes in Net Position. | We tested the completeness of the list of derivatives entered into, the reasonableness of management's assumptions in determining the overall effectiveness of the hedge, the amount of ineffectiveness included in earnings and the method used to determine the fair value of the commodity swap, and the documentation maintained by management at inception and each reporting period. We also evaluated the resulting financial statement disclosures for completeness. |
| Self-Insurance Liability        | Management has determined this liability based on the estimated loss of known claims as well as an estimate of incurred but not reported claims based on historical claims data.  | We tested the propriety of information underlying management's estimates.  |

**AUDITOR'S JUDGMENTS ABOUT QUALITATIVE ASPECTS OF SIGNIFICANT ACCOUNTING PRACTICES**

We are to discuss with you our comments about the following matters related to LACMTA's accounting policies and financial statement disclosures. Accordingly, these matters will be discussed during our meeting with you.

- The appropriateness of the accounting policies to the particular circumstances of the entity, considering the need to balance the cost of providing information with the likely benefit to users of the entity's financial statements.
- The overall neutrality, consistency, and clarity of the disclosures in the financial statements.
- The effect of the timing of transactions in relation to the period in which they are recorded.
- The potential effect on the financial statements of significant risks and exposures, and uncertainties that are disclosed in the financial statements.
- The extent to which the financial statements are affected by unusual transactions including nonrecurring amounts recognized during the period, and the extent to which such transactions are separately disclosed in the financial statements.
- The issues involved, and related judgments made, in formulating particularly sensitive financial statement disclosures.
- The factors affecting asset and liability carrying values, including the entity's basis for determining useful lives assigned to tangible and intangible assets.
- The selective correction of misstatements, for example, correcting misstatements with the effect of increasing reported earnings, but not those that have the effect of decreasing reported earnings.

## CORRECTED AND UNCORRECTED MISSTATEMENTS

Corrected Misstatements: We are to inform you of material corrected misstatements that were brought to the attention of management as a result of our audit procedures.

- A prior period adjustment of \$215.0 million was recommended and made by management to decrease the business-type activities' beginning unrestricted net position and increase the net OPEB obligation liability by \$215.0 million. The impact on change in net position for the year ended June 30, 2014 was a reduction of \$215.0 million. There was no impact on the change in net position at June 30, 2014. This adjustment was made to recognize lifetime benefit provisions for ATU employees that were not reflected in the previous actuarial valuations used to calculate the net OPEB obligation. With the addition of the OPEB benefit provision, the actuarial calculation of prior Annual Required Contributions were understated and resulted in the Net OPEB Obligation liability being understated.

Uncorrected Misstatements: We are to inform you of uncorrected misstatements that were aggregated by us during the current engagement and pertaining to the latest and prior period(s) presented that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements taken as a whole. For your consideration, we have distinguished misstatements between known misstatements and likely misstatements.

- A likely misstatement was waived by management to capitalize bus improvement costs and record depreciation in the proper period. LACMTA has a bus repair/upgrade mid-life program and an engine replacement program that are designed to ensure that the buses last at least as long as their estimated life, if not further. The misstatement is due to the fact that they only place these assets into service once every two to three years, which results in the cost not being capitalized in the proper period and depreciation not starting when it should. As a result of waiving this adjustment, beginning unrestricted net position and current year depreciation expense on LACMTA business-type activities are both overstated by \$31.8 million.
- As noted above, a prior period adjustment of \$215.0 million was made to decrease the business-type activities' beginning net position and increase the net OPEB obligation by \$215.0 million. This adjustment brought the June 30, 2014 balance to the correct amount, however, an adjustment to account for the current fiscal year change of \$34.4 million was waived by management. As a result, the net OPEB obligation and fringe benefits are both understated by \$34.4 million at June 30, 2015 and unrestricted net position is overstated by the same amount.
- LACMTA has three long term notes receivables attributable to governmental funds. (A \$44.9 million note on the Proposition A Fund, a \$18.0 million note on the Measure R Fund, and a \$4.0 million note on the General Fund.) The proper treatment of these notes receivables is to exclude the balances from the governmental fund balance sheet, as they do not represent assets available in the current period. They should, however, be recorded on the government-wide statement of net position and included as a reconciling item between the balance sheet and statement of net position.

We noted that the Proposition A notes receivable balance is properly excluded from the governmental fund balance sheet but improperly excluded from the government-wide statement of net position. The Measure R and General Fund notes receivable balances have been improperly included in the governmental fund balance sheet but properly included in the government-wide statement of net position.

Management chose to waive these known misstatements, and as a result, the notes receivable and unrestricted net position on the government-wide statement of net position is understated by \$44.9 million. On the governmental fund balance sheet, the Measure R Fund notes receivable and unrestricted net position is overstated by \$18.0 million and the General Fund notes receivable and unrestricted net position is overstated by \$4.0 million.

- A known misstatement to properly accrue \$1.8 million of subsidy expense was waived by management. As a result, accrued expense liability and subsidy expense on the General Fund are understated by \$1.8 million.



## OTHER COMMUNICATIONS

| Communication Item  | Results   |
|---|---|
| <p><b>Other Information In Documents Containing Audited Financial Statements</b></p> <p>Information may be prepared by management that accompanies the financial statements. To assist your consideration of this information, you should know that we are required by audit standards to read such information and consider whether such information, or the manner of its presentation, is materially inconsistent with information in the financial statements. If we consider the information materially inconsistent based on this reading, we are to seek a resolution of the matter.</p> | <p>We read the following items and noted no material inconsistencies or misstatement of facts in such information based on our reading thereof.</p> <ul style="list-style-type: none"> <li>• Comprehensive Annual Financial Report</li> </ul>   |
| <p><b>Significant Difficulties Encountered During the Audit</b></p> <p>We are to inform you of any significant difficulties encountered in dealing with management related to the performance of the audit.</p>   | <p>There were no significant difficulties encountered in dealing with management related to the performance of the audit.</p>   |
| <p><b>Disagreements With Management</b></p> <p>We are to discuss with you any disagreements with management, whether or not satisfactorily resolved, about matters that individually or in the aggregate could be significant to LACMTA's financial statements or the auditor's report.</p>   | <p>During our audit, there were no such disagreements with management.</p>  |
| <p><b>Consultations With Other Accountants</b></p> <p>If management consulted with other accountants about auditing and accounting matters, we are to inform you of such consultation, if we are aware of it, and provide our views on the significant matters that were the subject of such consultation.</p>  | <p>We are not aware of any instances where management consulted with other accountants about auditing or accounting matters since no other accountants contacted us, which they are required to do by Statement on Auditing Standards No. 50, before they provide written or oral advice.</p> |
| <p><b>Representations The Auditor Is Requesting From Management</b></p> <p>We are to provide you with a copy of management's requested written representations to us.</p>   | <p>We direct your attention to a copy of the letter of management's representation to us provided separately.</p>   |
| <p><b>Significant Issues Discussed, or Subject to Correspondence, With Management</b></p> <p>We are to communicate to you any significant issues that were discussed or were the subject of correspondence with management.</p>   | <p>There were no such significant issues discussed, or subject to correspondence, with management.</p>  |
| <p><b>Significant Related Party Findings and Issues</b></p> <p>We are to communicate to you significant findings and issues arising during the audit in connection with LACMTA's related parties.</p>   | <p>There were no such findings or issues that are, in our judgment, significant and relevant to you regarding your oversight of the financial reporting process.</p>  |

| Communication Item   | Results  |
|--|--|
| <p><b>Other Findings or Issues We Find Relevant or Significant</b></p> <p>We are to communicate to you other findings or issues, if any, arising from the audit that are, in our professional judgment, significant and relevant to you regarding your oversight of the financial reporting process.</p> | <p>There were no such other findings or issues that are, in our judgment, significant and relevant to you regarding your oversight of the financial reporting process.</p> |

We are pleased to serve LACMTA as its independent auditors and look forward to our continued relationship. We provide the above information to assist you in performing your oversight responsibilities, and would be pleased to discuss this letter or any matters further, should you desire. This letter is intended solely for the information and use of the Board of Directors and, if appropriate, management, and is not intended to be and should not be used by anyone other than these specified parties.

*Crowe Horwath LLP*

Crowe Horwath LLP

Indianapolis, Indiana  
December 22, 2015