

The Directors
The Water Authority of the Cayman Islands
P. O. Box 1104
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CAYMAN ISLANDS

22 June 2018

Dear Sirs/Madams:

In planning and performing our audit of the financial statements of the Water Authority of the Cayman Islands (the "Water Authority") for the 18 month period ended 31 December 2017, we obtained an understanding of internal control over financial reporting (ICFR) relevant to the Water Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on ICFR. Accordingly, we do not express an opinion on the effectiveness of the Water Authority's ICFR.

Our understanding of ICFR was for the limited purpose described above and was not designed to identify all control deficiencies that might be significant deficiencies and therefore, there can be no assurance that all significant deficiencies and other control deficiencies have been identified. As a result, any matters reported below are limited to those deficiencies in ICFR that we identified during the audit.

Our awareness of control deficiencies varies with each audit and is influenced by the nature, timing, and extent of audit procedures performed, as well as other factors.

Refer to the Appendices for the definitions of various control deficiencies.

SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROLS CARRIED FORWARD FROM PRIOR PERIOD

We identified significant deficiencies in internal controls that have been communicated to management in the 30 June 2016 audit but have not been addressed by management in the current period.

Issue	Potential effect and recommendation	Management's Response
The Water Authority's employment contracts have not been updated to reflect the change in Legislation and Regulations. This change specifically relates to the General Orders governing the way civil servants work which was revoked on December 31, 2006 and replaced by Personnel Regulations which are required under the Public Service Management Law.	<p>The effect was that the contracts did not accurately reflect the changes in the legislation which resulted in misinterpretations between what employees had expected and what was in their contracts in relation to the post-retirement healthcare benefits.</p> <p>Recommendation:</p> <p>It is recommended that the Water Authority review and amend contracts periodically to reflect changes in laws and or regulations as required.</p>	<p>Management acknowledges that employee contracts need to be updated to accurately document the terms and conditions of employment and to reflect the changes in benefits, most specifically the entitlement to Post-Retirement Health benefits.</p> <p>As at 22 June 2018 this is in progress.</p>

DEFICIENCIES IN INTERNAL CONTROLS

We identified deficiencies in controls that have not been communicated to management by other parties and that, in our professional judgment, are of sufficient importance to merit management's attention.

Issue	Potential effect and recommendation	Management's Response
During the audit it was noted that certain costs capitalized within property, plant and equipment included directly attributable charges and other costs incurred to bring the assets to the location and condition necessary for	<p>Without performing a retrospective review of the inputs into the estimates, the amounts capitalized could be either over or understated; and potentially not meet the capitalization criteria in IAS16.</p> <p>Recommendation:</p>	<p>The Water Authority is confident that the allocated plant costs do not overstate the value of the assets, however it is acknowledged that the methodology for capitalization, and to be more in line with IAS16 standards could be slightly modified.</p>

Issue	Potential effect and recommendation	Management's Response
its intended use. The amounts capitalized in some instances are based on assumptions and estimates, for which a retrospective review had not been performed to assess reasonableness and accuracy of assumptions.	It is recommended that the Water Authority performs a retrospective review on the reasonableness of inputs into the estimate at least once per year.	Going forward the Water Authority will analyze and monitor the estimated plant costs and compare back to the actual costs during the year and assess for reasonableness.
There was no evidence that a purchase from Argo was sent to the internal Tenders Committee in compliance with the Financial Regulations (2013 Revision) sections 36 – 41.	<p>Non-compliance with the Financial Regulations could result in potential sanctions against the Authority.</p> <p>Value-for-money may not be achieved where the appropriate tendering rules had not been adhered to.</p> <p>Recommendation:</p> <p>Ensure all tendering is in compliance with the Financial Regulations (2013 Revision).</p>	<p>The purchase from Argo American was for an addition to the CYB fleet of water delivery trucks, all of which are custom made for the harsh working conditions in Cayman Brac.</p> <p>The Water Authority does recognize and acknowledge that this purchase should be accompanied by documentation supporting the internal tenders committee review.</p>
A scholarship student was employed as an Intern during 2017. The Intern was granted administrative access rights similar to the IT administrator, which means that the Intern had access to all areas of the network.	<p>The potential effect is that the Intern could gain access to various areas and cause potential issues surrounding data manipulation both through error and intent.</p> <p>Recommendation:</p> <p>Limit administrative access rights to senior IT staff only.</p>	The Water Authority, and more specifically the IT department is fully aware of this level of access being granted. It was in fact the IT's scholarship student, who reports to and was supervised by the Applications Support Manager that was granted these rights in direct

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		relation and under a high level of supervision in order to complete the tasks to which she was assigned.
<p>The allowance for doubtful accounts in the amount of \$1,919,667 has remained consistent for all accounting periods since 30 June 2015. This approach indicates a point estimate bias and is not in accordance with IAS39.</p>	<p>The allowance for doubtful accounts could be materially over-or-understated if not appropriately assessed.</p> <p>Recommendation:</p> <p>Perform an analysis over the credit risk of customers within accounts receivable and then ensure the allowance for doubtful accounts is aligned to this assessment.</p>	<p>The Water Authority has set the allowance for doubtful accounts in 2013 of CI\$1,421,014; 2014 of CI\$1,643,766; 2015 of CI\$1,919,667; 2016 of CI\$1,919,667; and 2017 of CI\$1,919,667. A comprehensive analysis has been consistently performed to ensure that the bad provision is adequate.</p> <p>After the analysis was performed in 2017 it was confirmed that the provision was slightly higher than necessary (according to internal policies), however a business decision was made not to write the amount down but rather to continue to monitor and book/release additional provisions at such a time that the analysis required it.</p> <p>With conscious effort and consistent follow-up, the Water Authority has maintained a strong control over aging receivables, and will continue to perform procedures (phone calls, disconnect service etc.) to minimize overdue balances.</p>

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<p>It was noted that OfReg and the Water Authority have not arrived at an agreement as how to account for the royalties paid by the Cayman Water Company under their current license to the Authority between regulatory fees for OfReg and statutory fees for the Authority.</p>	<p>The amount owed to OfReg is currently undetermined and if an agreement is not reached the potential payable may continue to increase without being appropriately recorded in the financial statements.</p> <p>Recommendation:</p> <p>Seek legal advice surrounding drafting an agreement with OfReg, on the amount and timing of royalty payments between the Authority and OfReg.</p>	<p>The Water Authority confirms that there is no formal agreement with OfReg currently in place for the Royalties collected.</p> <p>The Water Authority will continue to foster and develop professional relationships with the OfReg Office to ensure that funding is available for both the Regulatory and Statutory functions of the government bodies.</p>

MANAGEMENT'S RESPONSES

Management's responses have not been subjected to the audit procedures applied in the audit, and accordingly, we express no opinion on them.

USE OF LETTER

This letter is for the use of management and those charged with governance in carrying out and discharging their responsibilities and should not be used for any other purpose or by anyone other than management and those charged with governance. KPMG and the Office of the Auditor General shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this letter has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

Yours faithfully,

KPMG



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Appendices

Terminology	Definition
Deficiency in Internal Control	A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing; or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.
Significant Deficiency in Internal Control	A significant deficiency in internal control is a deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance.