

REPORT OF THE AUDITOR-GENERAL ON AGRICULTURAL FINANCE CORPORATION FOR THE YEAR ENDED 30 JUNE, 2023

PREAMBLE

I draw your attention to the contents of my report which is in three parts:

- A. Report on the Financial Statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.
- B. Report on Lawfulness and Effectiveness in Use of Public Resources which considers compliance with applicable laws, regulations, policies, gazette notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure the Government achieves value for money and that such funds are applied for the intended purpose.
- C. Report on the Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, risk management environment and internal controls, developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations and that its internal controls, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution, the Public Finance Management Act, 2012 and the Public Audit Act, 2015. The three parts of the report when read together constitute the report of the Auditor-General.

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of the Agricultural Finance Corporation set out on pages 1 to 77, which comprise of the statement of financial position as at 30 June, 2023, and the statement of profit or loss and other comprehensive income, statement of changes in equity, statement of cash flows and statement of comparison of budget and actual amounts for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit.

In my opinion, except for the effect of the matters described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material

respects, the financial position of Agricultural Finance Corporation as at 30 June, 2023, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Agricultural Finance Corporation Act, Cap 323 of the laws of Kenya and Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Unsupported Property, Plant and Equipment

The statement of financial position reflects property, plant and equipment balance of Kshs.1,173,874,000 and as disclosed in Note 8(a) to the financial statements. As previously reported, the balance includes twenty-nine (29) developed plots measuring a total of 5.3324 hectares valued at Kshs.191,627,798 and four (4) undeveloped plots measuring a total of 0.8191 hectares with no ownership documents.

Further, the value of land excludes unvalued parcels of land located in Nanyuki and Kerugoya and includes the value of a parcel in Chogoria, which Management has explained was repossessed by the respective County Governments due to failure by the Corporation to develop the property within the stipulated time. Management has also explained that the Kerugoya plot has since been developed by the Judiciary and similarly, the Chogoria plot has been developed by Meru South Co-operative Union, with a building named Mwalimu Sacco Plaza. However, no evidence to support the repossession was provided. The balance also excludes land located in Kimilili and Busia whose ownership document was not provided. Although the Management has explained that it continues to pursue the ownership documents through the Ministry of Lands and the National Land Commission, the documents had not been obtained as at the time of audit.

In addition, included in the net book value of Kshs.34,523,000 for land is an amount of Kshs.523,382 that was utilized in the acquisition of five (5) parcels of land in Kimilili, Molo, Bungoma, Chogoria and Kisumu Municipality at a cost of Kshs.18,000, Kshs.4,010, Kshs.54,262, Kshs.438,820 and Kshs.8,290, respectively. The five (5) parcels of land have not been revalued contrary to the International Accounting Standard No.16 which requires sufficient regularity in revaluation of property, plant and equipment to ensure that the carrying amount does not differ materially from that which would be determined using fair values at the end of reporting period. In addition, the ownership documents for two (2) of the parcels of land have not been secured.

Moreover, the statement of financial position reflects net book value for property and equipment and intangible assets of Kshs.1,173,874,000 and Kshs.58,747,000 respectively as disclosed in Note 8(a) and 8 (b) to the financial statements. However, assets with a total historical cost of Kshs.992,674,000 were fully depreciated and had not been revalued yet they were still in use.

In the circumstances, the accuracy, completeness and ownership of property plant and equipment net book value of Kshs.1,173,874,000 and intangible assets balance of Kshs.58,747,000 could not be confirmed.

2. Medium Term Loans Issued on Doubtful Title Deeds

The statement of financial position reflects net medium-term loans to customers balance of Kshs.9,193,566,000 and as disclosed in Note 9 (a) to the financial statements. As previously reported, includes an amount of Kshs.22,661,000 being principal loan advanced plus interest and other loan fees to thirteen (13) farmers in Kapsabet. Information available indicates that the Corporation advanced the amount against various collaterals in form of title deeds that were fraudulent. The Corporation filed seven (7) cases in Court against the fraudsters and judgement was entered in favor of the Corporation. However, the Corporation had not executed the warrants issued as at 30 June, 2023 and details on the other cases have not been provided.

In the circumstances, the accuracy and recoverability of loans amounting to Kshs.22,661,000 issued on fraudulent titles could not be confirmed.

3. Long Outstanding Short-Term Loans to Customers

The statement of financial position reflects net short term loans to customers of Kshs.795,177,000 and as disclosed in Note 9(b) to the financial statements. Included in the balance is gross short-term loans to customers balance of Kshs.815,396,000. Review of the short-term loan portfolio schedule provided reflects arrears of loans amounting to Kshs.225,135,805 that have been outstanding for more than one year as their maturity period was 30 June, 2023 and earlier periods with some being outstanding for more than ten (10) years. No sufficient explanation was provided by Management on the steps taken to recover these amounts.

In the circumstances, the accuracy, completeness and recoverability of short-term loans to customers of Kshs.225,135,805 could not be confirmed.

4. Non-Performing Loans to Directors

The statement of financial position reflects net medium-term loans to customers balance of Kshs.9,193,566,000 which includes Kshs.58,193,000 under Directors' loans as disclosed in Note 9 (a) to the financial statements. The balance comprises of seven (7) loan accounts out of which five (5) of the loan accounts are in arrears amounting to Kshs.35,660,367 and which have been referred to the debt recovery unit. Records provided for audit revealed that the six (6) accounts have been graded as non-collectable even upon disposal of attached securities as per the existing credit policy. Although a provision of Kshs.4,832,000 has been made on directors' loans, this may be inadequate.

In the circumstances, the accuracy and recoverability of the Directors loans balance of Kshs.58,193,000 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Agricultural Finance Corporation Management in accordance with ISSAI 130 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. There were no key audit matters to report in the year under review.

Other Matter

Unresolved Prior Year Matters

Various prior year audit issues remained unresolved as at 30 June, 2023. Management has not provided reasons for the delay in resolving the prior year audit issues as required by the Public Sector Accounting Standards Board.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matter described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that, nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

Non-Disposal of Repossessed Farm Properties

The statement of financial position reflects repossessed farm properties balance of Kshs.389,920,000 and as disclosed in Note 11 to the financial statements. Review of the supporting schedule of the properties revealed that the Corporation held one hundred and thirty-eight (138) properties of repossessed parcels' of land. These had been repossessed in various years with the earliest acquisition done in the year 1976 and the latest in the year 2023. However, contrary to the guidelines of the credit policy, the entity did not dispose of any of these properties during the year under review which affects the liquidity of the Corporation and which is a compromise of its money lending objective.

In the circumstances, the financial capital held in these properties affects the liquidity of the Corporation and is a compromise on its credit policy and money lending objective.

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether processes and systems of internal control, risk management and overall governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

Responsibilities of Management and Board of Directors

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for such internal control as Management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error and for its assessment of the effectiveness of internal controls, risk management and overall governance.

In preparing the financial statements, Management is responsible for assessing the Corporation's ability to continue to sustain its services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless Management is aware of the intention to terminate the Corporation or to cease operations.

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

In addition to the responsibility for the preparation and presentation of the financial statements described above, Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective way.

Those charged with governance are responsible for overseeing the Corporation's financial reporting process, reviewing the effectiveness of how Management monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to overall governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

In addition to the audit of the financial statements, a compliance audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them, and that public resources are applied in an effective way, in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal controls in order to give an assurance on the effectiveness of internal controls, risk management and overall governance processes and systems in accordance with the provisions of Section 7(1)(a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal controls that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal controls may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.
- Conclude on the appropriateness of the Management's use of the applicable basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Corporation's ability to continue to sustain its services. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Corporation to cease to continue to sustain its services.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Corporation to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide with a statement that I have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.



FCPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

05 January, 2024