

REPORT OF THE AUDITOR-GENERAL ON AGRICULTURAL FINANCE CORPORATION FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Disclaimer of Opinion

I have audited the accompanying financial statements of Agricultural Finance Corporation set out on pages 39 to 104, which comprise the statement of financial position as at 30 June 2017, and the statement of 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 do not express an opinion on the accompanying financial statements. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

In addition, as required by Article 229(6) of the Constitution, I have not been able to obtain sufficient appropriate audit evidence to confirm that public money has been applied lawfully and in an effective way.

Basis for Disclaimer of Opinion

1. Property and Equipment

(i) Land and Buildings

As previously reported in 2015/2016, the property and equipment balance of Kshs.1,079,401,000 as at 30 June 2017 includes twenty-nine developed plots measuring 5.3324 hectares valued at Kshs.191,627,798 and seven undeveloped plots measuring 1.5383 hectares valued at Kshs.927,245,000 with no ownership documents. In addition, the value of land and buildings with a net book value of Kshs.949,666,000 as disclosed in Note 8 (a) to the financial statements, excludes unvalued parcels of land located in Busia, Nanyuki and Kerugoya whose ownership is in dispute. In the circumstances, it has not been possible to confirm whether the property and equipment balance of Kshs.1,079,401,000 reflected in the statement of financial position as at 30 June 2017 is fairly stated.

(ii) Fixed Assets Transfer Account

Note 8 (a) to the financial statements reflects an amount of Kshs.180,371,000 disclosed as fixed assets transfer account, and which relates to assets transferred during the year. However, the management has not disclosed the nature of this class of property and equipment in these financial statements. In addition, no evidence has been provided to support the transfer and the corresponding entries to the transfer have not been explained. In the circumstances, it has not been possible to confirm the validity and completeness of the amount of Kshs.180,371,000.

(iii) Budgetary Control-Staff Insurance

The statement of comprehensive income reflects an amount of Kshs.737,510,000 under staff costs, which includes an amount of Kshs.61,301,000 paid on staff medical insurance. This payment exceeded the budgeted and approved amount of Kshs.53,000,000 by Kshs.8,301,000. The excess expenditure was more than 15% of the budget on staff medical and insurance during the year 2016/2017 contrary to Section 12 of the State Corporations Act, Cap 446, which states that no State Corporation shall without the prior approval in writing of the Minister and Treasury incur any expenditure for which provision has not been made in annual estimate prepared and approved in accordance with Section 11 of the same Act. The Corporation was therefore in breach of the Law.

2. Trade and Other Receivables

The statement of financial position reflects a balance of Kshs.600,215,000 (2015/2016 - Kshs.61,611,000) under trade and other receivables and as disclosed in Note 15 to the financial statements, which is an increase of Kshs.538,604,000 or 800% over the previous year. Note 1 (f) to the financial statements indicates that trade and other receivables are recognized at fair values less allowances for uncollectible amounts which are assessed for impairment on a continuing basis and an estimate made. However, Note 15 to the financial statements does not show an assessment for impairment loss and neither has management provided documentary evidence showing how the specific provision for bad debts figure of Kshs.23,174,000 in respect to trade and other receivables was determined. Consequently, the accuracy of the trade and other receivables balance and charge for doubtful debts cannot be confirmed.

3. Loss of Cash

As previously reported in 2015/2016 and earlier years, examination of records between January 2005 and November 2010 revealed that the Corporation lost a sum of Kshs.35,840,714 through fraudulent transactions involving encashment of 196 cheques by various staff members. The case is still in court and any provisions for the loss and disclosures that would have been necessary in relation to this uncertainty have not been incorporated in these financial statements.

4. Net Loan to Customers

(i) As reported in the previous year, Note 1 (m) to the financial statements on provision for doubtful debts indicates that loans have been classified into five categories as follows: normal, watch, sub-standard, doubtful and loss, as adopted from the Central Bank of Kenya prudential guidelines with modifications to reflect the risk and uncertainties specific to agriculture sector. However, a review of the Corporation records did not reveal the actual classification of the loans as indicated in the Note.

(ii) As reported in 2015/2016 and in previous years and as disclosed in Note 9 (a) to the financial statements, net loans to customers of Kshs.4,896,537,000 as at 30 June 2017 includes an amount of Kshs.22,661,000 advanced to thirteen farmers in Kapsabet. Information available indicates that the Corporation advanced the amount

against various collaterals in form of title deeds which appeared fraudulent. In the circumstances, the recoverability of the amount of Kshs.22,661,000 is doubtful.

(iii) Similarly, and as previously reported, included in the loans to customers balance are loans to staff totalling Kshs.299,306,000 relating to personal advances, house and car loans. Although the Corporation has made a provision of Kshs.27,369,000 (2016-Kshs.20,387,000), the provision is inadequate as available information reflects non-performing accounts that have not been provided for. In addition, management has not provided an analysis of the loan balance showing the portions that relates to staff and directors separately.

(iv) As previously reported, included under Note 12(b) to the financial statements in relation to accumulated provisions for doubtful debts are specific provisions-adjustments and write back figures of Kshs.223,618,000 and Kshs.607,443,000 respectively. Further, the general provisions include a write back of Kshs.80,166,000 described as interest concession-farm loans while the staff loans specific provisions include a write back of Kshs. 4,205,000 described as interest concession-ex staff. The analyses of these figures have however not been provided for audit verification. Consequently, their validity and completeness cannot be confirmed.

5. Current Tax Payables

As previously reported, the statement of financial position reflects current tax payable of Kshs.170,732,000 which is an increase of Kshs.100,250,000 over the previous year's balance of Kshs.70,482,000. However, no tax computations have been provided to show how the current tax payable figure of Kshs.170,732,000 and the corporation tax for the year of Kshs.143,721,000 respectively were determined. Consequently, the accuracy of the current tax payable of Kshs.170,732,000 cannot be confirmed.

6. Income from Doubtful Debts

The statement of comprehensive income reflects an amount of Kshs.607,443,000 (2015/2016 - Kshs.60,845,000) under income from doubtful debts. Note 6 to the financial statements states that all loans prior to January 2003 had been fully provided for as doubtful debts as at 30 June 2005 and interest accruals on such loans suspended and recoveries from the portfolio have been recognized as income. However, no documentary evidence has been produced by management showing the loan portfolio prior to January 2003 and the provision for the same as at 30 June 2005. Under the circumstances, it is not possible to confirm whether income from doubtful debts figure of Kshs.607,443,000 as at 30 June 2017 is fairly stated.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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.

In preparing the financial statements, management is responsible for assessing the Corporation's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the management either intends to liquidate the corporation or to cease operations, or have no realistic alternative but to do so.

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

Those charged with governance are responsible for overseeing the Corporation's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

My responsibility is to conduct an audit of the Agricultural Finance Corporation's financial statements in accordance with International Standards of Supreme Audit Institutions (ISSAIs) 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. However, because of the matters described in the Basis for Disclaimer Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

I am independent of Agricultural Finance Corporation in accordance with ISSAI 30 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.



FCPA Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

23 May 2018