

EXECUTIVE SUMMARY

A. INTRODUCTION

Northern Foods Corporation (NFC) was originally a private corporation registered with the Securities and Exchange Commission on March 16, 1984 under SEC Registration No. 119668.

By virtue of Executive Order (E.O.) No. 233 dated April 26, 2000, Livelihood Corporation (LIVECOR) and all its subsidiaries, to include NFC, were attached, for supervision, control and policy/program coordination, to the Department of Agriculture.

In late part of 2007, however, LIVECOR and National Livelihood Support Fund (NLSF) were merged into a body corporate known as "LIVECOR," by virtue of E.O. No. 681 dated November 22, 2007. Such E.O. was further amended by E.O. No. 681-A dated February 1, 2008 to state the name of the merged NLSF and LIVECOR as the "National Livelihood Development Corporation (NLDC)". With this development, NLDC is now attached for supervision to the Land Bank of the Philippines, therefore being the mother company of NFC, it follows that NFC is now under the supervision of LBP.

An audit was conducted, on a test basis, covering the accounts and operations of NFC for the fiscal year ending May 31, 2018. The examination included the review of operating procedures, interview with concerned officials and employees, verification/confirmation, reconciliation and analysis of accounts, and such other procedures considered necessary. The audit was aimed to: (a) verify the level of assurance that may be placed on management assertions on the financial statements; (b) recommend agency improvement opportunities; and (c) determine extent of implementation of prior years' audit recommendations.

B. OPERATIONAL HIGHLIGHTS

The agency derives its income mainly from sale of tomato paste. In addition, NFC sells tomato seeds at a higher price to farmers who are not contract growers. Moreover, sale of un-refurbished drums and pallets are sources of income, as well.

Hereunder are the plans and targets vis-à-vis accomplishments of NFC for the Fiscal Year 2018, which were validated by the Audit Team:

Activities	Performance Indicator	Target	Accomplishment	
			Quantity	%
1. Land Campaign	Production Area	813 hectares	677	83%
2. Fruit Production	Fruit Volume	28,982 tons	19,983	69%
3. Tomato Paste Production	Tomato Paste Vol.	4,300 tons	2,920	68%
4. Sales	Volume	3,955 tons	3,797	96%

The non-attainment of targeted production area for Land Campaign was due to the reduction in the number of participating farmers by 34% (212 hectares) due to dissatisfaction in the delay of fruit payments despite the 142 hectares commitment of new farmers to plant for NFC. The low farm yield was due to unfavorable weather condition and high demand for Ilocos tomato fresh fruits all throughout the months of March and April with higher farm gate prices at P11/kg to P14/kg compared to the P5.9/kg for the same period last year. On the other hand, actual production of tomato paste was recorded at 68% only due to the shortfall of raw materials (fresh fruit) as presented in the table and the higher fruit-to-paste conversion rate of 6.86 kg tomato fruit-to-paste versus the target of 6.74 kg. Moreover, the non-attainment of the targeted Sales Volume (in metric tons) was due mainly to the effect of the 464 metric tons reduced volume of customers' demand and the increase in sales returns despite the 307 metric tons increase in sales made to other customers.

C. FINANCIAL HIGHLIGHTS

The agency's assets and liabilities as of May 31, 2018 were ₱268,824,352.84 and ₱870,848,349.85, respectively. Thus, capital deficiency soared to (₱602,023,997.01). Comparison of Financial Position is summarized in the table below:

Particulars	2018 (In Peso)	2017 (In Peso)	Increase (Decrease)
Assets	268,824,352.84	299,724,020.57	(30,899,667.73)
Liabilities/Deferred Credits	870,848,349.85	868,972,636.73	1,875,713.12
Equity(Capital Deficiency)	(602,023,997.01)	(569,248,616.16)	(32,775,380.85)

NFC is funded from the following sources for FY 2018 with comparative figures for FY 2017. The total gross income showed an increase of ₱46,407,216.48.

Income/Sources of Funds	2018 (In Peso)	2017 (In Peso)	Increase (Decrease)
Sales, net of Sales Returns	198,472,006.18	151,992,146.12	46,479,860.06
Interest Income	36,309.55	49,096.75	(12,787.20)
Miscellaneous Income	575,506.03	635,362.41	(59,856.38)
TOTAL	199,083,821.76	152,676,605.28	46,407,216.48

Conversely, the trend of total expenses, however, for FY 2018 has decreased by ₱21,743,695.22. A comparative figure of expenses for FY 2017 is shown below:

Expense Classification	2018 (In Peso)	2017 (In Peso)	Increase (Decrease)
Manufacturing Expenses	131,794,857.60	154,088,794.66	(22,293,937.06)
• Raw Materials	88,127,457.76	106,648,245.05	(18,520,787.29)
• Direct Labor	7,629,175.81	7,452,455.50	176,720.61
• Processing Overhead	32,550,933.76	37,462,083.83	(4,911,150.07)
• Plant Depreciation	3,487,290.27	2,526,009.42	961,280.85

Personnel Services	15,549,706.06	13,679,070.74	1,870,635.32
• Operating	13,481,852.69	12,154,236.69	1,327,616.00
• Selling	2,067,853.37	1,524,834.05	543,019.32
MOOE	13,703,210.82	14,405,507.11	(702,296.29)
• Operating	8,339,656.02	10,560,803.24	(2,221,147.22)
• Selling	5,363,554.80	3,844,703.87	1,518,850.93
Non-Financial Expenses	2,548,761.83	5,541,292.00	(2,992,530.17)
Financial Expenses	41,710,189.17	39,335,756.19	2,374,432.98
TOTAL EXPENSES	205,306,725.48	227,050,420.70	(21,743,695.22)

For FY 2018, the agency appropriated and utilized the following amounts for each expenditure class. A comparison also of FY 2017 appropriation and utilization is presented below:

	Corporate Operating Budget	Personnel Services	MOOE	Capital Expenditures	Financing Charges
<u>2018</u>					
Budget		34,926,202.00	219,463,887.00	12,226,235.00	0.00
Utilization		30,007,532.00	149,358,499.00	2,792,914.00	0.00
Disbursement		30,007,532.00	149,358,499.00	2,792,914.00	0.00
Variance		4,918,670.00	70,105,388.00	9,433,321.00	0.00
<u>2017</u>					
Budget		29,724,392.00	211,274,814.00	23,609,126.00	0.00
Utilization		28,301,762.65	171,685,048.00	11,282,242.00	0.00
Disbursement		28,301,762.65	171,685,048.00	11,282,242.00	0.00
Variance		1,422,629.35	39,589,766.00	12,326,884.00	0.00

D. INDEPENDENT AUDITOR'S REPORT

The Auditor rendered a qualified audit opinion on the fairness of presentation of financial statements because of the following: (1) Unreliable balance of Other Supplies and Materials Inventory-Drums and Pallets in the amount of P34,979,733.40 and P6,406,334.17, respectively (2) Recognition of Deferred Tax Asset of the agency in the amount of P1,500,509.78 which is not in accordance with IAS 12; and (3) Unreliable net decrease of the total cost of Property, Plant and Equipment in the amount of P3,067,389.96. Details of these are discussed in the Independent Auditor's Report.

E. SUMMARY OF SIGNIFICANT OBSERVATIONS & RECOMMENDATIONS

Favorable audit observations on the operations of the agency included the following:

1. Northern Foods Corporation is compliant with the environmental laws and regulations relevant to its operations, making it a responsible manufacturing entity that is mindful of its obligations to protect the environment and uphold the rights of future generations who will inherit the same.

We recommended that Management continue with its practice of safeguarding the integrity and health of the environment by complying with the relevant laws and regulations in place.

2. The Emergency and Preparedness Response Guidelines of NFC which took effect on September 16, 2014 constitutes the disaster risk management plan of the agency and found to be consistent with the requirements of the law for every government instrumentalities. Thus, we commended Management for formulating such guidelines that include, among others, the conduct of one fire and earthquake drill every year.

However, presented below is a summary of the significant audit observations and recommendations, which were discussed with the agency officials concerned during the exit conference on September 19, 2018 and their corresponding comments, where appropriate, were incorporated in Part II of the report:

3. The valuation, existence and accuracy of the Other Supplies and Materials Inventory- Drums and Pallets account in the amount of P34,979,733.40 and P6,406,334.17, respectively, could not be ascertained due to the unreconciled records of the agency with the actual physical count and those supposed to be in the custody of customers thus, casting doubt as to the reliability of the accounts.

We reiterated the auditor's previous recommendation to (a) direct the accountant to drop/derecognize from the NFC's books the amount of drums and pallets that can no longer be accounted for based on existing records especially those considered as "INACTIVE". In addition, we further recommended that Management (b) make it a policy to implement a reasonable amount of deposit on returnable containers (drums) in order to oblige the customers to promptly return the drums and pallets to prevent losses on the unreturned drums and pallets.

4. Poor collection strategy of Accounts Receivable resulted in an outstanding balance of P22,933,683.38 as of May 31, 2018, of which the amount of P9,548,028.29 represent those receivables ranging from one month to one year and above which may no longer be collected at all and may result to loss of government funds.

We recommended that management adopt strategies to collect from its clients and if feasible, deduct from the salaries and benefits of employees the outstanding balances guaranteed by them to avoid the accumulation of overdue accounts.

5. The recognition of Deferred Tax Asset of the agency in the amount of P1,500,509.78 is not in accordance with IAS 12 because it is not probable that taxable profit will be available within which the unused tax losses or unused tax credits can be utilized.

We therefore recommended that Management direct the Accountant to consider the provisions of IAS 12 and discontinue recognizing Deferred Tax Assets especially when it is not probable that taxable profit is available.

6. The Other Receivables-Others account included receivables in the total amount of P2,443,761.69 which have been outstanding and non-moving for more than 10 years, thus, considered Dormant Receivable Accounts pursuant to COA Circular 2016-005 on the Guidelines and Procedures on the Write-off of Dormant Receivable Accounts, Unliquidated Cash Advances, and Fund Transfers of National Government Agencies (NGAs), Local Government Units (LGUs) and Government-Owned and Controlled Corporations (GOCCs) dated December 19, 2016.

We recommended that management:

- (a) Exert exhaustive efforts to collect from Agriman Consulting Services and if efforts prove futile, a request for write-off in consonance with COA Circular 2016-005 be undertaken and;
- (b) Formulate a policy/program to strictly monitor and collect all receivables accruing to the agency in order to prevent possible losses.

F. STATUS OF AUDIT SUSPENSIONS, DISALLOWANCES AND CHARGES

The agency's disbursements were audited using the Test Audit Months Sampling Scheme. As of May 31, 2018, the total disallowances per accounting record amounted to ₱4,302,088.25 broken down as follows:

- a) Notices of Disallowance (NDs) prior to 2009 Revised Rules on Settlement of Accounts (RRSA), which have become final and executory summed up to ₱3,906,455.39. These disallowances include the Board of Directors' compensation, per diems, RATA, Executive Committee Allowances, financial assistance, Fuel and Oil and Discretionary Fund granted in 1999, 2005 to 2007.
- b) NDs, which were issued after the effectivity of RRSA totaled to ₱395,632.86. This consists of payments of Mid-Year and Year-end Financial Assistance, consultancy and acceptance fee.

Details of the foregoing are presented in Part II of the report.

G. STATUS OF PRIOR YEARS' AUDIT RECOMMENDATIONS

Below is the status of implementation of prior years' audit recommendations embodied in the 2017 Annual Audit Report, details of which are shown in Part III of this report.

STATUS	NUMBER	PERCENTAGE
Fully Implemented	9	19%
Partially Implemented	29	60%
Not Implemented	10	21%
Total	48	100%