Republic of the Philippines
COMMISSION ON AUDIT
Commonwealth Avenue, Quezon City

INDEPENDENT AUDITOR'S REPORT

The Board of Liquidators
AFP Retirement and Separation Benefits System
424 Capinpin Avenue, Camp General Emilio Aguinaldo
Quezon City, Metro Manila

Report on the Audit of the Financial Statements

Adverse Opinion

We have audited the financial statements of AFP Retirement and Separation Benefits System (AFPRSBS), which comprise the statements of financial position as at December 31, 2017 and 2016, and the statements of comprehensive income, statements of changes in equity and statements of cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, because of the significance of the matters discussed in the Basis for Adverse Opinion paragraph, the financial statements do not present fairly the financial position of the System as at December 31, 2017 and 2016, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards (PFRSs).

Basis for Adverse Opinion

The total assets of AFPRSBS as at year-end is overstated by P2.328 billion in 2017 and P2.474 billion in 2016 due to: (a) the non-consolidation of the financial statements of the System and that of its subsidiaries and failure to eliminate the reciprocal accounts; (b) the unrecorded waived penalty of a foreclosed property; and (c) the difference between the general ledger (GL) and the subsidiary ledger (SL) balances, and the difference between the report of physical count of the property, plant and equipment (RPCPPE) and accounting records.

We conducted our audit in accordance with International Standards of Supreme Audit Institutions (ISSAIs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the AFPRSBS in accordance with the Code of Ethics for Government Auditors in the Philippines (Code of Ethics) together with the ethical requirements that are relevant to our audit of the financial statements in the Philippines, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our adverse opinion.

Key Audit Matters

Except for the matter described in the Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report.

Emphasis of Matter

We draw attention to Note 2 to the financial statements in relation to Note 23 stating that on April 8, 2016, Memorandum Order (MO) No. 90, s. 2016 was issued by the Office of the President of the Philippines directing the abolition of the AFPRSBS, privatization of its subsidiaries, among others. On April 19, 2016, in pursuant to the MO, the System's BOT already convened as Board of Liquidators (BOL). The BOL approved the stoppage of the collection of the five per cent members' contributions and the accrual of interest on members' contributions effective March 31, 2016 as per Board Resolution No. SPL-01-2016. The BOL also approved the continuance of the implementation of discounting of refund of Advance Refund Program to retiring military personnel with approved Order of Retirement from the AFP until the final closure of the System.

We also draw attention to Note 2 in relation to Note 13 stating that the disposal of some of the Investment in Real Estate – Landbanking assets worth P3.295 billion and P3.287 billion as at December 31, 2017 and 2016, respectively is hindered by the unavailability of the titles in the name of the System, some existing legal cases and the presence of illegal tenants on some of the raw lands that were acquired. As a result, the projected profits and returns from these ventures may not be fully realized. The related effects of the adverse conditions, if any, will be reported in the financial statements as they become known and measurable. Therefore, we were unable to conduct a detailed audit of the account.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with PFRSs, 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 System'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 management either intends to liquidate the System or to cease operations, or has no realistic alternative but to do so.

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

Auditors' Responsibilities for the Audit of the Financial Statements

Our 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 our opinion. 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 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.

As part of an audit in accordance with ISSAIs, we exercise professional judgment and maintain professional skepticism throughout the audit. We 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 our 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 control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern 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 System's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the System to cease to continue as a going concern.

- 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.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Report on Other Legal and Regulatory Requirements

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information for the year ended December 31, 2017 required by the Bureau of Internal Revenue as disclosed in Note 33 to the financial statements is presented for purposes of additional analysis and is not a required part of the basic financial statements prepared in accordance with PFRS. Such supplementary information is the responsibility of management. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

COMMISSION ON AUDIT

CECILIA E. CAGA-ANAN
Supervising Auditor

April 18, 2018