

PITC PHARMA, INC.
(A Subsidiary of the Philippine International Trading Corporation)
NOTES TO FINANCIAL STATEMENTS
(All amounts in Philippine Peso unless otherwise stated)

1. AGENCY BACKGROUND

PITC Pharma, Inc. (Company) was initially incorporated in the Philippines on July 13, 1981 as Producers Venture Capital Corporation (PVCC). PVCC was 60 percent owned by Prime Media Holdings, Inc. and 40 percent owned by the National Development Company (NDC). On October 19, 2005, NDC bought out Prime Media's 60 percent ownership, which made PVCC 100 percent owned by NDC.

On November 9, 2005, the Securities and Exchange Commission (SEC) approved the change in PVCC's corporate name from Producers Venture Capital Corporation to PITC Pharma, Inc., and its primary purpose from that of a financing company to a pharmaceutical firm engaged in the business of research, development, production, manufacture, packaging, sale and/or distribution of pharmaceutical products and/or investment and/or management of investments in pharmaceuticals and related commercial ventures.

On September 12, 2006, the SEC approved the increase in the Authorized Capital Stock of the Company from P10 million to P100 million, divided into one million (1,000,000) common shares at a par value of P100 per share. The infusion by Philippine International Trading Corporation (PITC) of P22.5 million in common shares, made the Company 60 percent owned by PITC. With the issuance of Executive Order (EO) 442, PITC was designated as the lead coordinating agency to make quality medicine available, affordable, and accessible to the greater masses of Filipinos. The Company was created to exclusively take the lead in implementing the government's Half-Priced Medicines Program under EO 442.

Pursuant to Section 1 Rule 16 Chapter III of the Implementing Rules and Regulations of Republic Act 9502, otherwise known as the Cheaper Medicines Bill Law, PITC Pharma Inc. was mandated to undertake the centralized importation of pharmaceutical products for the government.

The License to Operate as a Drug Distributor/ Importer/ Wholesaler was granted to the Company on October 16, 2006.

The principal office address of the Company is at 2nd floor, NDC Building, 116 Tordesillas Street, Salcedo Village, Makati City.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Basis of Financial Statements Preparation and Statement of Compliance

The financial statements are presented in Philippine peso, the Company's functional and presentation currency, and all values are rounded to the nearest peso, except when otherwise indicated.

The accompanying financial statements are prepared and presented in accordance with State accounting principles.

b. Cash and cash equivalents

Cash includes cash on hand and in banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with maturity dates of three months or less from the date of acquisition.

c. Accounts receivable - trade

Trade receivables are recognized at their face value less allowance for doubtful accounts.

Allowance for doubtful accounts is provided for potentially uncollectible receivables specifically identified, principally based on the following criteria: accounts with pending legal investigation, clients who have issued bouncing checks and uncollectible accounts aged three years and above (100 percent), uncollectible accounts aged two years (50 percent), and DOH accounts and other uncollectible accounts aged one year (25 percent).

d. Prepaid expenses

Prepayments are amortized over the period of coverage. The account also includes deferred charges from the payment of 2006 Minimum Corporate Income Tax.

e. Inventories

Merchandise Inventory is stated at the lower of cost or net realizable value. Cost includes acquisition cost plus all incidental expenses incurred in acquiring the goods and in bringing them to their present location and condition. Costs are assigned to inventories using the weighted average method.

The provision for allowance of inventory loss is based on the expiration dates of stocks counted during the year-end physical count. Stocks expiring on or before the end of the current year are considered an outright expense, and therefore charged against the inventory account. A 50 percent allowance is provided for medicines that will expire from January to June of the succeeding year and 25 percent for medicines that expire at the end of the same year.

Accountable Forms and Other Supplies Inventory are valued at cost.

f. Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Cost includes expenditure that is directly attributable to the acquisition of the items.

Depreciation is computed using the straight-line method over the estimated useful lives of the depreciable assets in accordance with COA Circular No. 2003-007. In the case of leasehold improvements, the assets are depreciated over the period of the lease or service life of the improvement, whichever comes first.

g. Income and expenses

Income and expenses are recorded on accrual basis.

3. CASH AND CASH EQUIVALENTS

The account is composed of the following:

Particulars	2010	2009
Cash on hand and in banks	2,218,707	7,056,104
Money market placements	21,603,034	20,169,349
Total Cash and cash equivalents	23,821,741	27,225,453

Cash on hand includes cash with the Cash collecting officer.

Money market placements are short-term, highly liquid peso investments with Land Bank of the Philippines with original maturities of three months or less.

4. ACCOUNTS RECEIVABLE - TRADE - NET

The Accounts receivable - trade account is categorized into the following:

Particulars	2010	2009
Commercial Accounts including		
Territorial Wholesalers	34,137,233	36,114,765
Department of Health (DOH)	22,282,812	20,823,578
Other Government Accounts	8,871,846	15,851,249
	65,291,891	72,789,592
Less: Allowance for doubtful accounts	35,772,352	30,673,021
Accounts receivable - trade - net	29,519,539	42,116,571

5. ACCOUNTS RECEIVABLE - NON-TRADE

The Accounts receivable - non-trade account is composed of the following:

Particulars	2010	2009
Due from BIR	28,758,202	22,072,635
Due from affiliates - PITC	12,340,049	10,431,736
Due from DOH	38,486	411,161
Due from officers and employees	549,295	125,381
Due from SSS	124,949	72,299
Other receivables	2,112,903	1,973,204
Total Accounts receivable - non-trade	43,923,884	35,086,416

The Due from BIR Input tax is net of recorded Output tax as of year-end.

Due from affiliates - PITC represents payments made by PITC Pharma, Inc. clients to PITC and other PPI advances for account of PITC.

Due from DOH represents advances made by PPI for the First Generic Expo.

6. INVENTORIES - NET

This account is composed of the following:

Particulars	Note	2010	2009 (As restated)
Merchandise Inventory		32,902,951	63,871,905
Accountable Forms		540,558	241,077
		33,443,509	64,112,982
Less: Allowance for Inventory Loss/Obsolescence	18	2,104,253	3,114,042
Inventories - net		31,339,256	60,998,940

7. PREPAID EXPENSES

This account consists of the following:

Particulars	2010	2009
Prepaid rent	220,976	220,976
Prepaid Insurance	274,462	351,065
Deferred charges	680	7,069
Others	25,137	9,548
Total Prepaid expenses	521,255	588,658

Prepaid rent represents the two months security deposit to Dexter Go Co for the pharmacy and office space at the Orient Mansion.

8. PROPERTY PLANT AND EQUIPMENT - NET

This account consists of the following:

Particulars	Leasehold improvements	Furniture and fixtures/ library books	Communication equipment and other machineries	IT Equipment and software	Office equipment	Total
CY 2010						
<u>Costs</u>						
January 01	4,478,383	1,644,194	348,956	3,740,423	210,553	10,422,509
Additions	-	-	-	45,777	-	45,777
December 31	4,478,383	1,644,194	348,956	3,786,200	210,553	10,468,286
<u>Accumulated Depreciation</u>						
January 01	2,286,992	312,471	63,326	1,542,435	60,872	4,266,096
Depreciation	216,766	147,978	31,491	679,159	37,898	1,113,292
December 31	2,503,758	460,449	94,817	2,221,594	98,770	5,379,388
Net Book Value						
December 31	1,974,625	1,183,745	254,139	1,564,606	111,783	5,088,898
CY 2009						
Net Book Value						
December 31	2,191,391	1,331,723	285,630	2,197,988	149,681	6,156,413

Leasehold improvements represent the cost of the renovation of the Company's leased office space and Company-operated Botika ng Bayan at the ground floor of the Orient Mansion and the renovation of the Company's main office at the 2nd floor of the NDC building.

9. ACCOUNTS PAYABLE

This account consists of:

Particulars	2010	2009
Accounts payable - trade	55,082,399	53,769,576
Accounts payable - non-trade	2,197,997	1,168,054
Total Accounts payable	57,280,396	54,937,630

Accounts payable - trade represents amount due to various suppliers for the purchase of merchandise for sale.

Accounts payable - non-trade are liabilities arising from various services such as security, janitorial, expenses for utility, communications and expenses other than purchase of merchandise for sale.

10. INTER-AGENCY PAYABLES

This account consists of:

Particulars	2010	2009
Due to PCSO	4,947,988	4,947,988
Due to DOH	1,775,965	2,388,135
Due to BIR	1,655,478	1,009,980
Due to SSS	111,358	126,420
Due to Pag-IBIG	48,131	26,898
Due to Philhealth	29,050	31,525
Total Inter-agency payables	8,567,970	8,530,946

The account Due to DOH represents the unliquidated balance of the P50 million fund transfers intended for the DOH P100 project pursuant to DOH Administrative Order No. 2008-0013, covered by a Memorandum of Agreement by and between DOH and PPI.

The liability to the BIR includes withholding taxes for remittance in January of the following year. Due to SSS represents social security benefits, likewise for remittance in January of the following year.

11. OTHER CURRENT LIABILITIES

This account is broken down as follows:

Particulars	2010	2009
Current portion of long-term loan	185,000,000	185,000,000
Interest payable	73,471,918	55,500,000
Performance/bidders bond	5,066,662	2,564,170
Vacation and sick leave	1,655,860	1,552,575
Due to officers and employees	1,275,904	1,134,051
Others	2,801,139	2,777,665
Total Other current liabilities	269,271,483	248,528,461

Other current liabilities include the current portion of the four-year loans payable to NDC which expired on December 26, 2009. Interest payable represents accrued interest on the loans availed from NDC as disclosed in Note 12.

Vacation and sick leave payable is recognized corresponding to the monetary value of the unused accumulated vacation and sick leave credit balances as at December 31, 2010.

Other payables include overpayments made by various clients and a fund entrusted by a supplier for the payment of advocacy expenses.

12. LOANS PAYABLE

This account consists of loans availed from NDC under the Loan Agreement entered into by and between NDC and the Company for organizational and operational expenditures in pursuit of the Half-Priced Medicines Program. The loans bear an interest rate of 10 percent per annum. The principal and interest are payable every quarter reckoned from each drawdown date for a period of four years, with a one year grace period on the principal, but in no case shall the repayment period extend beyond December 26, 2009. However, due to failure to pay, PPI has requested NDC a restructuring of the matured loan with a possible reduction of interest rate.

In the absence of a restructuring agreement, the total amount of P185 million is presented in the financial statements as current (Note 11).

13. DUE TO AFFILIATES

The breakdown of this account is as follows:

Particulars	2010	2009
Due to PITC	22,770,172	22,780,440
Due to NDC	3,951,008	3,481,280
Total Due to affiliates	26,721,180	26,261,720

The liability to PITC includes portion of cost of stocks transferred from PITC, trade returns accepted from previous PITC sales, and other direct expenses unpaid as at December 31, 2010.

14. CAPITAL STOCK

With the Securities and Exchange Commission's approval of the increase in capitalization, the Company presently has an authorized capital stock of P100 million, divided into one million (1,000,000) common shares at a par value of P100 per share.

As at December 31, 2010, the Company has Subscribed and Paid-in Capital of P37,500,000, consisting of:

Investors	Percentage	Amount
Philippine International Trading Corporation	60%	22,500,000
National Development Company	40%	15,000,000
Total	100%	37,500,000

15. SALES

Sales is broken down into the following categories of customers:

Particulars	2010	2009
Department of Health	101,314,165	122,422,199
BnB Orient Mansion	4,217,345	14,375,350
Commercial Accounts	7,423,120	11,996,807
Other Government Accounts	7,469,812	10,289,280
Others	1,143,184	526,962
Total Sales	121,567,626	159,610,598

16. OPERATING EXPENSES

Operating Expenses are broken down as follows:

Particulars	Note	2010	2009 (As restated)
Personal Services			
Salaries and wages		17,025,607	17,935,322
Other compensation		9,663,773	9,937,529
Personnel benefits		1,047,590	1,084,205
		27,736,970	28,957,056
Maintenance and other operating expenses			
Donation expense		22,096,467	11,590,647
Bad debt expense		5,099,331	5,754,006
Rent expense		3,851,323	4,349,393
Professional services		3,913,380	3,967,922
Depreciation expense		1,113,292	1,631,802
Travelling expense		1,528,258	1,546,881
Communication expense		1,449,754	1,418,679
Taxes, insurance premiums and other fees		1,363,462	1,266,984
Utility expense		1,217,954	1,259,146
Supplies and materials expense		536,797	665,029
Advertising expense		514,631	421,548
Representation expense		259,522	347,456
Training expense		60,763	171,708
Repairs and maintenance expense		130,198	99,346
Printing and binding expense		3,288	-
Subscription expense		9,184	9,134
Membership dues and contributions to organization		5,000	7,500
Loss on inventory	18	-	3,931,953
Miscellaneous expense		512,504	1,445,823
		43,665,108	39,884,957
Total Operating expenses		71,402,078	68,842,013

17. OTHER INCOME (EXPENSES)

This account is broken down as follows:

Particulars	2010	2009
Other Income (expenses)		
Financial charges	(6,514)	(226)
Interest income	562,536	762,677
Interest expense	(16,517,857)	(13,812,541)
Other service income	238,039	-
Miscellaneous Income	253,456	272,712
Total Other Income (expenses)	(15,470,340)	(12,777,378)

18. RESTATEMENT OF ACCOUNTS

Certain accounts in 2009 were restated to conform to 2010 financial statements presentation for proper disclosure and to reflect the impact of the adjustments to prior years' income and expenses and related accounts in accordance with the Philippine Accounting Standards (PAS).

Prior year's accounts were restated as follows:

Inventories	Note	Allowance for Inventory Loss/ Obsolescence	Inventories - net
As previously reported	6	(5,485,731)	58,627,251
Prior Year's Adjustments due to double recording		2,371,689	2,371,689
As restated		(3,114,042)	60,998,940

Operating expenses	Note	Loss on Inventory	Maintenance and Other Operating Expenses
As previously reported	16	6,303,642	42,256,646
Prior Year's Adjustments due to double recording		(2,371,689)	(2,371,689)
As restated		3,931,953	39,884,957

19. NET OF LOSSES CARRIED OVER (NOLCO)

PPI did not set up a deferred tax asset on the NOLCO since 2007. Details of the Company's NOLCO as at December 31, 2010 are as follows:

Inception Year	Amount	Applied/Expired	Balance	Expiry Year
2007	32,286,338	(32,286,338)	-	2010
2008	72,917,168	-	72,917,168	2011
2009	37,591,703	-	110,508,871	2012

As at December 31, 2010, PPI's operation resulted in a zero tax liability due to losses incurred for the current and the preceding two years.