

A. COMMENTS AND OBSERVATIONS

1. The results of confirmation of various liability accounts disclosed variances amounting to P48,896,138 that cast doubts on the accuracy and validity of the balances presented in the financial statements.

- 1.1 Replies to confirmation requests sent to various suppliers for liability accounts disclosed variances, as follows:

Account	PPI Books	Confir- mation	Variance Over (Under)
Due to DOH	1,775,965	2,787,180	(1,011,215)
Due to NDC	3,951,008	2,988,190	962,818
Interest Payable - NDC	73,471,918	23,126,644	50,345,274
Due to PITC	22,770,172	24,287,708	(1,517,536)
Accounts payable - trade			
Brymar Pharmaceutical	14,564,123	13,098,988	1,465,135
CTSI Logistics	4,798,687	6,375,714	(1,577,027)
Diamond Laboratories, Inc.	11,311,711	11,312,497	(786)
JM Tolmann Laboratories, Inc.	132,189	151,770	(19,581)
Medgen Laboratories	23,237	27,415	(4,178)
Danlex Research Laboratory	250,724	303,937	(53,213)
United Laboratories Inc.	841,948	535,501	306,447
Net amount	133,891,682	84,995,544	48,896,138

- 1.2 Of the 28 confirmation letters sent to suppliers for Accounts payable - trade account, only eight or 28 percent responded, 17 or 61 percent did not respond and three or 11 percent were returned.
- 1.3 The Philippine Charity Sweepstakes Office (PCSO) with the account of P4,947,988 did not also reply.
- 1.4 We also noted the debit balances in the subsidiary ledgers of the following suppliers:

Supplier	Amount
Alphamed Pharma Corp.	3,434
Biolink Pharma, Inc.	1,026,326
JB Orchid Pharmaceuticals	13
Scheele Laboratories Phils	128,765
	1,158,538

- 1.5 The above debit balances reduced the Accounts payable - trade.
- 1.6 The variances disclosed in the confirmation and the negative balances cast doubts on the accuracy and validity of the balances of the liability accounts.

1.7 We recommended that the Accounting Department exert efforts to reconcile the liability accounts with the records of the suppliers, verify the causes of the debit balances of the Accounts payable - trade, and prepare the necessary adjustments in the books.

1.8 We further recommended that periodic confirmation of related party accounts such as those of the DOH and NDC, and of the accounts of suppliers be implemented among the financial control activities of PPI, which could be performed by the internal audit office so that appropriate action could be immediately undertaken on the discrepancies, if any.

1.9 Management commented that reconciliation statements were prepared for the following accounts; DOH, NDC-Interest payable, NDC-Rental and Other receivable, CTSI, Danlex Research Laboratory, Diamond Laboratories and Medgen Laboratories. Likewise, Management agreed to coordinate with them in addressing the reconciling items, and continuous effort will be made for the reconciliation of other accounts which were not yet completed. As regards accounts with debit balances, these were adjusted for proper classification. Moreover, Management agreed to exert all effort to ensure the correct recording of its liability accounts.

2. Confirmation of receivables revealed a total variance of P20,043,362 that cast doubt on the accuracy and validity of the Accounts receivable - trade - Department of Health (DOH) and Due from PITC in the amount of P22,282,812 and P12,340,049 respectively.

2.1 The balance of Accounts receivable - trade DOH and Due from PITC as at December 31, 2010 amounted to P22,282,812 and P12,340,049 respectively.

2.2 Confirmation of balances showed the following variances:

Account	PPI Books	DOH/PITC Confirmation	Variance
Accounts receivable – trade DOH	22,282,812	7,051,250	15,231,562
Due from PITC	12,340,049	7,528,249	4,811,800
Total	34,622,861	14,579,499	20,043,362

2.3 Verification disclosed that one of the causes of the variance of the Accounts receivable – trade DOH was the difference in recording of payments in the books of DOH and PPI, as shown below:

Reference	DOH Books	PPI Books	Variance
Ck#420737/OR#6490952	7,180,190	6,795,537	384,653
Ck#420740/OR#6490950	2,349,203	2,223,353	125,850
Ck#420738/OR#6490953	1,609,300	1,523,088	86,212
Ck#420739/OR#6490954	2,245,302	2,125,018	120,284
Ck#421023/OR#6490968	3,699,967	3,501,755	198,212
Ck#421024/OR#6490969	3,322,725	3,144,722	178,003
Ck#421025/OR#6490970	25,471,920	24,107,353	1,364,567
Ck#421248/OR#6490977	5,200,719	4,922,109	278,610
Ck#421249/OR#6490978	1,296,000	1,226,571	69,429

Reference	DOH Books	PPI Books	Variance
Ck#421247/OR#6490976	325,500	308,063	17,437
Ck#421309/OR#6490985	4,748,400	2,119,821	2,628,579
Ck#421311/OR#6490983	4,182,890	1,867,362	2,315,528
Ck#421310/OR#6490984	3,346,500	1,493,973	1,852,527
Ck#421312/OR#6490982	4,606,200	2,056,339	2,549,861
Ck#421352/OR#6490981	1,190,700	531,563	659,137
CK#421520/OR#6490991	233,461	220,954	12,507
Ck#421518/OR#6490992	4,712,040	2,103,589	2,608,451
Ck#421519/OR#6490989	2,350,065	1,049,136	1,300,929
Ck#421556/OR#6490994	18,971,544	8,469,439	10,502,105
Ck#421521/OR#6490990	156,375	147,998	8,377
Ck#421531/OR#6490993	2,501,055	1,116,542	1,384,513
Ck#421782/OR#6490997	5,302,704	2,367,279	2,935,425
Ck#422036/OR#6491008	2,599,290	2,460,042	139,248
Ck#422061/OR#6491009	589,580	263,205	326,375
Total	108,191,630	76,144,811	32,046,819

- 2.4 The variances resulting from confirmation of accounts affected the accuracy and validity of the balances of the Accounts receivable - trade DOH and Due from PITC accounts presented in the financial statements.
- 2.5 We recommended that Management require the Accounting Department to analyze and reconcile the accounts with DOH and PITC, and make the necessary adjustments.**
- 2.6 Management commented that as regards the differences in the recording of payments, they correctly recorded the receipt of collection while DOH did not. Likewise, they still need to discuss with DOH the treatment of the withholding taxes, since DOH has been late in releasing the tax certificates, which also affected the balance of the account. Moreover, Management commented that they had called the attention of the Sales and Marketing Group for the 2006 and 2008 unpaid balances of sales which were contracted directly with the Centers for Health Development (CHDs) of Eastern Visayas, Cebu and Cagayan de Oro and were not recorded in the books of DOH. Furthermore, Management commented that the variance in the accounts as at December 31, 2010 may be attributed to the timing of recording only.

As regards the PITC account, Management also explained that the transactions were all properly substantiated and communicated to PITC but they will still continue to exert their best effort to reconcile the intercompany accounts.

3. Failure of the Management to collect the Accounts receivables amounting to P36,493,057 had deprived the Company of the funds that could be utilized for the operations.

3.1 The balance of Accounts receivable - trade as at December 31, 2010 amounted to P65,291,891, as follows:

Particular	Amount
Department of Health (DOH)	22,282,812
Commercial Accounts	34,137,233
Other Government Accounts	8,871,846
Total	65,291,891

3.2 Records showed that receivables referred to Legal/OGCC amounted to P31,190,481 or 48 percent of the total Accounts receivable, as follows:

Customer	Amount
Alphamed Pharma Corp.	1,494,225
Azolsa Enterprises	3,712,002
Bilmed Corporation	2,495,748
Botika Jansa	37,975
Erle Pharmacy	366,369
Farmacia Gonzales	37,309
Farmacia Layla	10,843
FKRS Pharmacy	93,061
Gerden Pharmaceuticals Lab	321,274
HJM Pharmacy	37,774
Immaculate Virgin Pharmacy	1,680
JHO James Drugstore & Distributor	342,459
Jolimed Pharmacy	942,246
LJ & J Pharmacy	208,320
Provincial Capitol of Cavite	1,627,000
Qualiprose Inc.	18,218,199
Rolbis Enterprises	9,755
Sabijon Pharmacy & Gen. Mdse.	81,546
Sumagang Dev't. Foundation, Inc.	184,022
Sunica Advent Pharma Trading	850,533
Wyna's Drugstore	118,141
Total	31,190,481

3.3 Likewise, receivables totaling P3,201,649 remained in the books but were claimed to have been paid, or that items were not received, returned and not accepted by clients, or accounts needed certificate of withholding tax from the clients.

3.4 Moreover, receivables in the amount of P2,100,926 were collectible from clients whose businesses were already closed/inactive.

3.5 The above-mentioned deficiencies affected the collectibility of Accounts receivables - trade that could result in losses of PPI funds. Proceeds from these receivables could have been source of funds for the operations.

3.6 We recommended that Management:

- a. **Follow up progress of cases referred to legal/OGCC.**
- b. **Conduct investigation on the accounts of clients handled by concerned Account Officers, which were claimed to have been paid, or that items were returned and not received. Likewise, require the submission of necessary withholding tax certificates.**
- c. **Exhaust all efforts to collect from clients whose businesses were already closed.**

3.7 Management informed us that cognizant of the effect of poor collection on the financial condition of the Company, Management had been exerting extra effort to collect through the following:

- a. The collaboration among Finance and Sales and Marketing Groups in addressing the long outstanding LGU and other Government Accounts that had yielded a collection of about P5.6 million from 2006 to 2008 Accounts receivable - trade balances;
- b. Improved collection efforts by the Sales and Marketing Group as evidenced by the more agreeable status of 2010 and 2011 transactions;
- c. Constant follow-ups on the submission of withholding tax certificates;
- d. Constant follow-up of accounts referred to OGCC and Legal Department;
- e. Coordination with the Distribution Department as regards claims of non-delivery; and
- f. Verification of claims of payment.

Moreover, the Board of Directors advised Management to explore the possibility of utilizing a collection agency for old accounts with private clients. Payments to the agency shall be purely on a “no cure-no pay” basis.

4. Unrecorded Sales Invoices (SIs) in the amount of P1,187,688 resulted in the understatement of Accounts receivable, Income and Cost of sales and overstatement of Inventory account.

4.1 Test of the recorded SIs issued in CY 2010 disclosed the following deficiencies:

Several SIs amounting to P1,187,688 were not recorded in the books as at December 31, 2010, as follows:

Date	Sales Invoice No.	Amount
11/18/10	8440	690
11/18/10	8442	417
11/18/10	8443	336

Date	Sales Invoice No.	Amount
11/18/10	8444	460
12/09/10	8467	508,058
12/09/10	8468	642,920
12/20/10	8469	3,518
12/20/10	8470	3,540
12/20/10	8471	1,633
12/20/10	8472	415
12/20/10	8473	1,386
12/20/10	8474	2,194
12/20/10	8475	1,883
12/20/10	8476	2,700
12/20/10	8477	935
12/20/10	8478	770
12/22/10	8481	8,274
12/22/10	8482	1,763
12/22/10	8483	441
12/22/10	8484	2,116
12/20/10	8573	141
12/20/10	8574	115
12/20/10	8575	230
12/20/10	8576	796
12/21/10	8580	71
12/30/10	8587	460
12/30/10	8588	460
12/30/10	8589	230
12/30/10	8590	161
12/30/10	8591	345
12/30/10	8592	230
Total		1,187,688

- 4.2 The above unrecorded SIs understated the Accounts receivable, Income and Cost of sales accounts and overstated the Inventory account as at December 31, 2010.
- 4.3 Unrecorded sales resulted from late recording since most of the SIs were not recorded in the month/period that these were issued.
- 4.4 The SIs issued in January 2010 in the total amount of P27,340,217.95 were taken up in the Sales Reports of February and March 2010 amounting to P26,974,501.95 and P365,716, respectively. Likewise, SIs issued in February amounting to P2,822,373.67 were recorded in the Sales Report of March and April in the amount of P2,708,262.37 and P114,111.30, respectively. With this practice, the actual sales and collections in a given period/month could not be easily determined, and transactions would not be recorded in the proper accounting period. Hence, vital information for Management's decision making would not be reliable.
- 4.5 Likewise, Sales Invoices Nos. 8383 and 8396 were missing and not accounted for.

4.6 We recommended that Management:

- a. **Put in place a monitoring control on recording of sales by assigning responsible personnel to perform periodic matching of the issued Sales Invoices with recorded sales, and prepare a report thereon for appropriate action.**
- b. **Take up in the books the unrecorded Sales as at December 31, 2010, and locate the missing SI Nos. 8383 and 8396 for proper disposition.**

4.7 Management commented that the unrecorded sales were taken up in the books in January and February 2011. The missing SIs Nos. 8396 and 8383 were already located and recorded in the books.

Likewise, Management commented that in order to avoid similar incidents of unrecorded or delayed recording of sales invoices, the following steps were taken:

- a. Record sales and cost of sales upon issuance of the Sales Invoices and Withdrawal Report, respectively, instead of the present practice of recording them upon receipt of proof of deliveries (PODs). The PODs shall, instead, be used as references for payment to the forwarder and as basis for the collection and/or aging of Accounts receivable – trade;
- b. The Distribution Department, who has the responsibility of preparing the sales Invoices and withdrawal reports, shall assign a staff to monitor and match issued sales invoices with recorded sales, follow-up the submission of PODs from the forwarder and prepare monthly Report of Accountability for Accountable Forms.

5. Issuance of Sales Invoices (SIs) in numerical sequence was not observed. Likewise, Report of Accountability for Accountable Forms was not prepared for monitoring and control purposes.

5.1 The use of pre-numbered SIs and issuing the same sequentially is a basic accounting control to ensure the accuracy and completeness of recorded transactions pertaining to sales on account and, to a greater extent, to detect and prevent the occurrence of fraud and to properly establish money accountability.

5.2 We observed, however, that the pre-numbered SIs were not issued in numeral sequence, as shown below:

Sales Invoice No.	Date Issued
7542	January 13, 2010
7543	January 14, 2010
7544	January 13, 2010
7661	February 15, 2010
7662	February 16, 2010
7663	February 15, 2010
7668	February 18, 2010
7669	cancelled
7670	February 17, 2010
7671	February 18, 2010

Sales Invoice No.	Date Issued
7931	April 26, 2010
7932	April 23, 2010
7933	April 23, 2010
7934	April 23, 2010
7435	April 26, 2010
8058	May 14, 2010
8059	May 15, 2010
8060	May 14, 2010
8145	June 11, 2010
8146	June 9, 2010
8147	June 9, 2010
8148	June 11, 2010
8214	July 20, 2010
8215	July 16, 2010
8216	July 20, 2010
8234	July 27, 2010
8235	July 28, 2010
8236	July 27, 2010
8328	August 11, 2010
8329	August 16, 2011
8330	August 13, 2010
8331	August 17, 2010
8351	September 1, 2010
8353	August 31, 2010
8368	September 15, 2010
8369	September 16, 2010
8370	September 15, 2010
8410	October 20, 2010
8411	October 26, 2010
8412	October 20, 2010
8541	November 15, 2010
8542	November 12, 2010
8543	November 15, 2010
8604	December 7, 2010
8605	Cancelled
8606	December 8, 2010
8607	Cancelled
8608	December 7, 2010

- 5.3 When SIs are not issued in numerical sequence, it is difficult to detect unrecorded sales and unauthorized use of SI forms. This could have contributed to the unrecorded sale transactions discussed in Comments and Observations No. 4.
- 5.4 Moreover, under existing government accounting and auditing regulations, accountable officers shall render a report on their accountability for accountable forms at least once a month in the prescribed form. Such report shall also be prepared in case of transfer of office or accountability by the accountable officer. The report shall include, among others, the name/type, quantity and serial number and/or value, of the accountable forms as of last month/period, the forms received and issued during the month/period and the balances as at end of month/period.

5.5 We observed, however, that sales personnel who were issued SI booklets were not preparing the required Report of Accountability for Accountable Forms.

5.6 We recommended that Management:

- a. **Designate an accountable officer for the custody and distribution of the SI booklets to the Account Officers; and**
- b. **Instruct the Account Officers to issue SI in numerical sequence, and submit Monthly Report of Accountability for Accountable Forms (SIs) for monitoring and control purposes.**

5.7 Management explained that since personnel of the Distribution Department prepare Sales Invoices upon receipt of the pick and pack report from the warehousing/forwarding service provider, the Sales and Marketing Group (SAM) and the LSC/Distribution Department have agreed that SAM's Sales Support and Administration Department (SSAD) shall turn over to a designated employee in the Distribution Department the unused invoices in SSAD's possession for the Distribution Department's accountability, custody, monitoring and control. Relative to this, the designated accountable officer was instructed to release/use the forms in numerical sequence and prepare the monthly Report of Accountability for Accountable Forms.

6. Donation of medicines totaling P22,096,467 resulted from overstocking of merchandise that contributed to 51 percent of the total maintenance and other operating expenses in CY 2010.

6.1 The Policy Guidelines, Systems and Procedures on the disposition of near expiring/expired medicines provides that all locally produced medicines (LPMs) in PPI's inventory as of July 2009 with shelf-life of one to three months shall be disposed of through donation.

6.2 As at December 31, 2010, Donation amounted to P22,096,467.

6.3 It is the practice of PPI to donate the medicines with the remaining shelf-life of three months in stock through donation to government agencies, civic organizations and employees. Donation of medicines caused by overstocking and slow turn-over of some brands represented 51 percent of the total maintenance and other operating expenses during the year. This mode of disposal also resulted in losses of PPI funds.

6.4 We recommended that Management put in place the:

- a. **Continuous study and monitoring of the market/public demand to determine the appropriate product items that will meet the needs of the consumers/beneficiaries; and**
- b. **Close monitoring of the stock inventory, lead time in purchasing of medicines, packaging and distribution to ensure the right quantity and quality of stocks and minimize inventory losses.**

- 6.5 Management commented that the Procurement Department is now more prudent in the procurement of drugs and medicines. They are now closely coordinating with Sales and Marketing and Distribution Department for the just in time inventory stock keeping level to avoid unnecessary loss of resources through product obsolescence and warehousing expense.