PITC Pharma, Inc.
Annual Audit Report for CY 2014

EXECUTIVE SUMMARY

Introduction

PITC Pharma, Inc. (PPI) was initially incorporated in the Philippines on July 13, 1981 as Producers Venture Capital Corporation (PVCC). PVCC was 60 per cent owned by Prime Media Holdings, Inc. and 40 per cent owned by the National Development Company (NDC). On October 19, 2005, NDC bought out Prime Media's 60 per cent ownership, which made PVCC 100 per cent 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 PPI from P10 million to P100 million. The infusion by Philippine International Trading Corporation (PITC) of P22.5 million in common shares, made PPI 60 per cent owned by PITC.

With the issuance of Executive Order (EO) No. 442 dated July 4, 2005, PITC was designated as the lead coordinating agency to make quality medicine available, affordable, and accessible to the greater masses of Filipinos. PPI was then created to exclusively take the lead in implementing the government's Half-Priced Medicines Program under EO 442.

Effective November 2008, PPI was designated as the central procurement arm for all government agencies for the importation of drugs and medicines, except for specific programs and instances allowed by the Department of Health. This is embodied in Section 1 Rule 16 Chapter III of the Implementing Rules and Regulations (IRR) of Republic Act (RA) No. 9502 otherwise known as the Cheaper Medicines Law. Likewise, the IRR's Chapter XI Rule 58 gives authority to PPI to establish a common facility for pooled procurement in compliance with RA 9184.

As of December 31, 2014, PPI has a manpower complement of 53 regular and probationary employees. Its principal officers are the following:

Name		Position / Designation
Jose A. Capistrano, Jr.	-	President and CEO
Jacqueline C. Mendoza	-	Vice President - Finance
Jose A. Cortez	-	Vice President - Sales

The audit covered the accounts and operations of PPI for calendar year 2014. It aimed to ascertain the fairness of the presentation of the financial statements. Our audit was also made to assess the propriety of the financial transactions and compliance of PPI with applicable laws, rules and regulations.

Financial Highlights

PPI's financial condition and results of operations (in Philippine peso) are presented below:

	2014	2013	Increase (Decrease)
Financial Condition			
Total Assets	292,595,908	194,370,842	98,225,066
Total Liabilities	600,153,991	486,282,877	113,871,114
Capital Deficiency	307,558,083	291,912,035	15,646,048
Result of Operations			
Gross Profit	41,461,883	53,216,624	(11,754,741)
Total Expenses	57,107,931	44,705,889	12,402,042
Net Income (Loss)	(15,646,048)	8,510,735	(24,156,783)

Despite the significant increase in sales during the last two years, PPI's financial performance did not improve. Even the highest sales achieved in the current year did not generate gross profit that would at least cover the operating expenses. The gross profit of 7.40 per cent of sales or ₱41.461 million was the lowest which was even lower than past year's gross profit of ₱53.216 million. Conversely, the current year operating expenses of ₱57.107 million was higher than the previous year of ₱44.705 million or higher by 27.74 per cent. Current operations resulted in net loss of ₱15.646 million.

After nine years in operation, PPI was not able to manage business effectively to improve its financial position, which has worsened from year to year. The total liabilities is more than twice as much the total assets.

Independent Auditor's Report on the Financial Statements

The Auditor rendered a modified opinion on the fairness of presentation of the financial statements of PPI.

Significant Audit Observations and Recommendations

Below is a summary of significant audit observations and recommendations with details discussed in Part II of this Report:

1. The PPI's financial position and results of operation for CY 2014 shows its inability to meet its liabilities and finance its operations due to the excess of liabilities over its assets and capital deficiencies and the losses continuously incurred from year to year, casting significant doubt on the ability of the Agency to continue as a going concern and carry out its mandated functions.

We recommended that Management -

a. conduct an assessment of the conditions affecting the unfavorable operating performance, such as but not limited to:

   - evaluation of pricing methods such that gross margin would be more than enough to cover operating expenses;

   - reduction of administrative and selling costs;

   - periodic review of operating performance with concern on the volume of sales and knowing the results whether PPI has gained or not; and

   - evaluation of existing internal controls to institute improvements in the different stages of operations.

b. establish business plans and strategies to address the uncertainties and identify areas in the operations for streamlining, to increase sales, reduce costs and avoid losses.

c. intensify collection and initiate more effective and efficient strategies to recover trade receivables.

d. explore opportunities for possible sources of funds such as subsidy from the National Government.

2. The balance of the Cost of Sales (COS) account amounting to ₱518.490 million is understated by ₱0.503 million while the Merchandise Inventory (MI) account of ₱4.358 million has unrecorded amount of ₱0.512 million, due to errors in booking up the cost of merchandise and the absence of properly maintained subsidiary records for inventories.

We recommended that Management -

a. maintain correct, complete and updated subsidiary record of each inventory item which include information necessary to validate the recorded amounts.

b. review the noted deficiencies and prepare the necessary adjusting journal entries to recognize corrections.

c. consider the recommended procedural accounting entries.

d. institute policies and procedures that would –

   - improve accounting and administrative controls to ensure reliable accounting data;

   - improve efficiency and minimize/avoid errors; and

   - promote a system of accountability.

e. require the Internal Audit Department to review the existing internal control system, identify weaknesses and recommend measures for improvement.

3. Performance/Bidders Bond Payable in the total amount of ₱18.802 million as of December 31, 2014 classified under Other Current Liabilities, have not been refunded to bidders and suppliers contrary to Sections 27.5, 28.1, 39.4 and 39.5 of RA 9184.

   We recommended that Management -

   a. refund/return the bid securities of ₱10.875 million and performance securities of ₱7.927 million if the suppliers' obligations have been complied with and the Certificate of Acceptance have been issued.

   b. arrange for schedule/plan of payment for the refunds.

   c. for subsequent posting of bid and performance security, comply with the requirements of Sections 27.5 and 28.1 on the return the bid security and Sections 39.4 and 39.5 on the return of the performance security and avoid the accumulation of such liabilities.

Status of Implementation of Prior Year's Audit Recommendations

Of the ten audit recommendations embodied in the 2013 Annual Audit Report, four were partially implemented and six were not implemented. Details are presented in Part III of this Report.