

MAINE STATE LEGISLATURE

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STATE OF MAINE
DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES
BUREAU OF ALCOHOLIC BEVERAGES AND LOTTERY OPERATIONS
8 STATE HOUSE STATION
AUGUSTA, MAINE 04330-0008

RICHARD W. ROSEN
COMMISSIONER

GREGORY R. MINEO
DIRECTOR

PAUL R. LEPAGE
GOVERNOR

March 24, 2017

Senator James M. Hamper, Chair
Representative Drew Gattine, Chair
Joint Standing Committee on Appropriations
Financial Affairs
5 State House Station
Augusta, ME 04333-0005

Senator Garrett P. Mason, Chair
Representative Louis J. Luchini, Chair
Joint Standing Committee on Veterans and
Legal Affairs
100 State House Station
Augusta, ME 04333-0100

Dear Senators Hamper and Mason and Representatives Gattine and Luchini:

Pursuant to Title 28-A, Section 90, subsection 6, please find enclosed the Fiscal Year 2016 audited financial report of Pine State Spirits, a Division of Pine State Trading Co., the Bureau's contractor in Maine's spirits business.

If you have any questions regarding this report, please do not hesitate to contact me.

Sincerely,

Gregory R. Mineo
Director

cc: Richard W. Rosen, Commissioner, Dept. of Administrative & Financial Services

Enclosure



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To the Board of Directors
Pine State Trading Co.
Gardiner, Maine

In planning and performing our audit of the Schedule of Spirits Reconciliation (the Schedule) of Pine State Spirits (a division of Pine State Trading Co.) for the year ended June 30, 2016, in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, we considered Pine State Spirits' internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the Schedule, but not for the purpose of expressing an opinion on the effectiveness of Pine State Spirits' internal control. Accordingly, we do not express an opinion on the effectiveness of Pine State Spirits' internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the Schedule will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

This communication is intended solely for the information and use of the Board of Directors and management of Pine State Trading Co., the State of Maine Bureau of Alcoholic Beverages and Lottery Operations, the State of Maine Controller's Office and the joint standing committees of the State of Maine legislature having jurisdiction over appropriations and financial affairs and alcoholic beverages matters, and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Macpage LLC".

Augusta, Maine
October 27, 2016

Macpage LLC

30 Long Creek Drive, South Portland, ME 04106-2437 | 207-774-5701 | 207-774-7835 fax | cpa@macpage.com
One Market Square, Augusta, ME 04330-4637 | 207-622-4766 | 207-622-6545 fax

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To the Board of Directors
Pine State Trading Co.
Gardiner, Maine

We have audited the Schedule of Spirits Reconciliation (the Schedule) of Pine State Spirits (a division of Pine State Trading Co.) for the year ended June 30, 2016, and have issued our report thereon dated October 27, 2016. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Governmental Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter dated July 15, 2016. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Pine State Spirits are described in Note 1 to the Schedule. No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 2016. We noted no transactions entered into by Pine State Spirits during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the Schedule in the proper period.

Accounting estimates are an integral part of the Schedule prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the Schedule and because of the possibility that future events affecting them may differ significantly from those expected. We did not consider any estimates to be significant to the Schedule.

Certain Schedule disclosures are particularly sensitive because of their significance to the Schedule users. The most sensitive disclosure affecting the Schedule was:

The disclosure of concentrations in Note 3 of the Schedule which describes that the top four suppliers account for approximately 50% of total product cost.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

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Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the Schedule or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 27, 2016.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to Pine State Spirits' Schedule or a determination of the type of auditors' opinion that may be expressed on the Schedule, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as Pine State Spirits' auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

This information is intended solely for the use of the Board of Directors and management of Pine State Trading Co. and is not intended to be, and should not be, used by anyone other than these specified parties.

Mapary LLC

Augusta, Maine
October 27, 2016

Pine State Spirits
(a Division of Pine State Trading Co.)

Schedule of Spirits Reconciliation

June 30, 2016

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Independent Auditors' Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of a Schedule
Performed in Accordance with Government Auditing Standards

To the Board of Directors
Pine State Trading Co.
Gardiner, Maine

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Schedule of Spirits Reconciliation of Pine State Spirits (a division of Pine State Trading Co.) for the year ended June 30, 2016, and the related notes to the Schedule of Spirits Reconciliation (the Schedule), and have issued our report thereon dated October 27, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the Schedule, we considered Pine State Spirits' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the Schedule, but not for the purpose of expressing an opinion on the effectiveness of Pine State Spirits' internal control. Accordingly, we do not express an opinion on the effectiveness of Pine State Spirits' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's Schedule will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Pine State Spirits' Schedule of Spirits Reconciliation is free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the Schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.



Board of Directors
Pine State Trading Co.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Macpige LLC

Augusta, Maine
October 27, 2016



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Independent Auditors' Report

To the Board of Directors
Pine State Trading Co.
Gardiner, Maine

We have audited the accompanying Schedule of Spirits Reconciliation (the Schedule) of Pine State Spirits (a division of Pine State Trading Co.), for the year ended June 30, 2016, and the related notes to the Schedule.

Management's Responsibility for the Schedule

Management is responsible for the preparation and fair presentation of this Schedule in accordance with the agreement between Pine State Trading Co. and the State of Maine Bureau of Alcoholic Beverages and Lottery Operations, dated June 25, 2014; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the Schedule that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the Schedule based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Schedule is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Schedule. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the Schedule, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Schedule 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 entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Schedule.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Schedule of Spirits Reconciliation referred to above presents fairly, in all material respects, the spirits activity of Pine State Spirits, for the year ended June 30, 2016, on the basis of accounting specified in the agreement referred to above.



Board of Directors
Pine State Trading Co.

Basis of Accounting

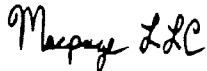
We draw attention to Note 1 to the Schedule, which describes the basis of accounting. The Schedule was prepared by Pine State Spirits, on the basis of the agreement between Pine State Trading Co. and the State of Maine Bureau of Alcoholic Beverages and Lottery Operations, dated June 25, 2014, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to comply with the provisions of the agreement referred to above. Our opinion is not modified with respect to that matter.

Restriction on Use

This report is intended solely for the information and use of the Board of Directors and management of Pine State Trading Co., the State of Maine Bureau of Alcoholic Beverages and Lottery Operations, the State of Maine Controller's Office and the joint standing committees of the State of Maine legislature having jurisdiction over appropriations and financial affairs and alcoholic beverage matters, and is not intended to be, and should not be, used by anyone other than these specified parties.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of Pine State Spirits' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Pine State Spirits' internal control over financial reporting and compliance.



Augusta, Maine
October 27, 2016

Schedule of Spirits Reconciliation

Year Ended June 30, 2016

| | Net Sales | | | | | | | | | | |
|--|--------------------------|------------------------|------------------|------------------|--------------|-----------------|--------------------|-----------------------|-----------------|--|--|
| | Total Invoiced Amount | In-State Distillers | Spirits Sales | Premium Taxes | Deposit | Product Cost | Part A Contract | Marketing Contract | State Profit | | |
| July | \$ 17,605,045 | \$ 53,585 | \$ 17,139,957 | \$ 262,381 | \$ 149,122 | \$ 11,219,400 | \$ 792,343 | \$ 371,212 | \$ 4,810,587 | | |
| August | 16,422,559 | 57,682 | 15,992,354 | 239,638 | 132,885 | 10,167,757 | 719,952 | 336,622 | 4,825,705 | | |
| September | 13,929,526 | 35,944 | 13,571,061 | 204,383 | 118,138 | 8,465,439 | 609,511 | 285,074 | 4,246,981 | | |
| October | 13,494,785 | 56,977 | 13,121,391 | 199,013 | 117,404 | 8,293,518 | 610,715 | 285,563 | 3,988,572 | | |
| November | 12,516,373 | 28,106 | 12,183,369 | 194,870 | 110,028 | 7,977,883 | 565,738 | 263,924 | 3,403,930 | | |
| December | 17,623,961 | 29,563 | 17,184,703 | 259,527 | 150,168 | 11,404,458 | 793,880 | 372,695 | 4,643,233 | | |
| January | 11,011,470 | 8,050 | 10,763,411 | 150,938 | 89,071 | 6,199,445 | 462,908 | 215,054 | 3,894,054 | | |
| February | 11,547,334 | 24,451 | 11,245,221 | 176,562 | 101,100 | 7,223,861 | 528,177 | 245,121 | 3,272,513 | | |
| March | 12,924,295 | 23,319 | 12,591,334 | 197,666 | 111,976 | 8,275,264 | 588,124 | 275,390 | 3,475,875 | | |
| April | 11,748,326 | 26,538 | 11,444,516 | 176,862 | 100,410 | 7,209,918 | 550,596 | 244,026 | 3,466,514 | | |
| May | 14,047,292 | 26,583 | 13,681,293 | 218,279 | 121,137 | 9,123,966 | 675,004 | 300,208 | 3,608,698 | | |
| June | 16,377,484 | 31,880 | 15,952,710 | 245,891 | 137,003 | 10,516,342 | 742,112 | 346,027 | 4,390,109 | | |
| | 169,248,450 | 402,678 | 164,881,320 | 2,526,010 | 1,438,442 | 106,077,251 | 7,639,060 | 3,540,916 | 48,026,771 | | |
| Part A Contract Reconciliation | | | | | | | | | | | |
| July 2015 0.25% rate increase, billed August 2016 | | | | | | | 42,145 | | (42,145) | | |
| August 2015 - March 2016 0.25% rate increase, billed April 2016 | | | | | | | 259,525 | | (259,525) | | |
| June 3, 2016 - June 30, 2016 0.25% rate increase, billed July 2016 | | | | | | | 34,892 | | (34,892) | | |
| Total | \$ 169,248,450 | \$ 402,678 | \$ 164,881,320 | \$ 2,526,010 | \$ 1,438,442 | \$ 106,077,251 | \$ 7,975,622 | \$ 3,540,916 | \$ 47,690,209 | | |

See independent auditors' report.
The accompanying notes are an integral part of this schedule.

Notes To Schedule of Spirits Reconciliation

June 30, 2016

NOTE 1 - NATURE OF THE BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

Pine State Spirits is a division of Pine State Trading Co. (the Company). The Company operates four divisions for the wholesale distribution of restaurant food and related products; malt beverages and wine; services of vending machines; and distribution and marketing of spirits under contract with the State of Maine. Pine State Spirits was formed for the purpose of distributing and marketing spirits under contract with the State of Maine. Note 2 of the Notes to Schedule of Spirits Reconciliation further outlines the nature of the liquor contracts with the State of Maine.

Basis of Accounting

The Schedule of Spirits Reconciliation is presented on a basis of accounting in conformity with the agreement between the Company and the State of Maine Bureau of Alcoholic Beverages and Lottery Operations, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Revenue Recognition

Revenues are recognized upon delivery of goods to customers.

NOTE 2 - STATE OF MAINE LIQUOR CONTRACTS

Part A Contract

During 2014, the Company was awarded the State of Maine wholesale liquor contract for warehousing, distribution and administration of the Maine spirits business for a ten year period effective July 1, 2014 to June 30, 2024. The contract calls for the Company to receive a services fee of 4.70% of the net sales and bailment revenue received by the State of Maine, Department of Administration & Financial Services, Bureau of Alcoholic Beverages and Lottery Offices (the Department) on a monthly basis. An amended agreement, dated February 9, 2016, enacted a retroactive rate change effective July 1, 2015, which increased the services fee to 4.95%. The Company receives the services fee after submitting an electronic reconciliation report of the previous month's sales and costs of products sold for the Department to review.

The Company provides sufficient warehouse space to house the spirits products and to prepare and deliver orders. Products that are delivered and stored by the Company are the property of the supplier. The product becomes the property of the Department upon removal and shipment to an agency liquor store. The agency liquor store gains ownership of the product at the time of delivery. At no time does the Company take legal title to the products. For storage of the spirits products, on behalf of the Department, the Company charges a bailment fee to the supplier based on the negotiated rates contained in the contract with the Department.

The Company is responsible for paying all invoices from suppliers and is entitled to full reimbursement from the Department for all invoice amounts paid to suppliers. The Company is also responsible for invoicing agency liquor stores on behalf of the Department for products when delivered. The electronic payment of these invoices into the Department's bank account is initiated by the Company. The Company accepts 100% of the risk of default by the agency liquor stores. When an agency liquor store is unable to pay, the Company is to develop a product-retrieval process with the Department.

It is the responsibility of the Company to calculate and track all taxes imposed on products sold to the agency liquor stores as required by law, but the Company does not bear payment responsibility for premium taxes on the products. The total premium tax collected on the sale of products to the agency liquor stores is provided as part of the Company's monthly reconciliation.

Notes To Schedule of Spirits Reconciliation

June 30, 2016

NOTE 2 - STATE OF MAINE LIQUOR CONTRACTS - CONTINUED

Part A Contract - Continued

Twice monthly the Company provides the suppliers with a purchase order outlining the products distributed from the Company's warehouse. Upon receipt, the supplier invoices the Company at which point the Company is responsible for payment. The Department is responsible for remitting to the Company all payments due to suppliers and the Company is not responsible for making these payments using its own funds or the services fees.

The Department established a Net Receipts Clearing Account which is to be used for depositing all accounts receivable and distributing funds for accounts payable. The Company, in its accounts receivable and accounts payable capacity, acts solely as an agent of the State. The Company is prohibited from commingling funds and financial activity as an agent of the State with any other funds and financial activity of the Company in its individual capacity. Furthermore, the Company does not have access to funds in the Net Receipts Clearing Account. The Department is responsible for paying all amounts to which the Company is entitled as a result of the agreement from the Net Receipts Clearing Account.

Marketing Contract

During 2014, Company was also awarded the contract for spirits trade marketing for the period October 21, 2014 to June 30, 2024. The marketing contract calls for the Company to receive, on a monthly basis, 2.25% of the total net sales of spirits in the State for the preceding month. Under the marketing contract, the Company, at their sole expense, is responsible for providing, directly or indirectly, all trade marketing activities.

The Department has sole discretion to license agency liquor stores above those existing at the time of the agreement. The Department also agrees to enter into contract negotiations for increased costs due directly to the increase in number of agency liquor stores, if the number of new agency liquor stores increases more than 5% in any year of the agreement.

NOTE 3 - CONCENTRATIONS

During the year ended June 30, 2016, payments to the top four suppliers for liquor products accounted for approximately 50% of total product cost.

NOTE 4 - SUBSEQUENT EVENTS

Management has made an evaluation of subsequent events through October 27, 2016, which represents the date on which the Schedule of Spirits Reconciliation was available to be issued and determined that any subsequent events that would require recognition or disclosure have been considered in the preparation of the Schedule of Spirits Reconciliation.