



Auditor of Public Accounts
Mike Harmon

FOR IMMEDIATE RELEASE

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Harmon Releases Audit of Magoffin County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Magoffin County Fiscal Court for the fiscal year ended June 30, 2013. State law requires annual audits of county fiscal courts.

Auditing standards require the auditor’s letter to communicate whether the financial statement presents fairly the receipts, disbursements and changes in cash and cash equivalents of the Magoffin County Fiscal Court in accordance with accounting principles generally accepted in the United States of America. The fiscal court’s financial statement did not follow this format. However, the fiscal court’s financial statement is fairly presented in conformity with the regulatory basis of accounting, which is an acceptable reporting methodology. This reporting methodology is followed for 115 of 120 fiscal court audits in Kentucky.

As part of the audit process, the auditor must comment on non-compliance with laws, regulations, contracts and grants. The auditor must also comment on material weaknesses involving the internal control over financial operations and reporting.

The audit contains the following comments:

The county treasurer did not monitor disbursements which caused total budgeted appropriations to be over spent. The county treasurer did not monitor the disbursements of the Road Fund, LGEA Fund, Solid Waste Fund, and 911 Fund, which caused the total budgeted appropriations for these funds to be overspent. The Road Fund, LGEA Fund, Solid Waste Fund, and 911 Fund disbursements were in excess of budgeted appropriations by \$531,567, \$40,207, \$117,738, and \$37,051, respectively. By not monitoring disbursements, the county is in noncompliance with KRS 68.300. Had the county treasurer performed her duties as outlined in the *County Budget Preparation and State Local Finance Officer Policy Manual*, the overspending would not have occurred. KRS 68.300 states, “Any appropriation made or claim allowed by the fiscal court in excess of any budget fund, and any warrant or contract not within

the budget appropriation, shall be void. No member of the fiscal court shall vote for any such illegal appropriation or claim. The county treasurer shall be liable on his official bond for the amount of any county warrant willfully or negligently signed or countersigned by him in excess of the budget fund out of which the warrant is payable.” In addition, the *County Budget Preparation and State Local Finance Officer Policy Manual* lists the duties of the county treasurer. One of the duties listed requires the county treasurer to countersign checks only when the following three conditions exist: (1) claim is reviewed by the fiscal court, (2) sufficient fund balance, and adequate cash in the bank to cover the check, and (3) adequate free balance in a properly budgeted appropriation account to cover the check. We recommend the county treasurer monitor disbursements and perform her duties as outlined in the *County Budget Preparation and State Local Finance Officer Policy Manual* to prevent noncompliance with KRS 68.300.

Official’s Response: In March 2012 an F-3 Tornado struck Magoffin County. We operated under emergency declaration for several months. During this time the County was required to financially respond to numerous unanticipated expenses. Federal-State-Regional support along with individual organizations-church generosity helped defray much of this burden. Our budget was now dramatically increased both in the revenue and expense columns. Our contractors, suppliers and workers needed payed quickly and we needed to assure that our citizens continued to receive help to recovery from this disaster. We were confronted with the dilemma of complying with KRS requiring County bills to be paid in 30 days and amending the budget. Amending the budget requires: 1. First reading and approval by Fiscal Court. 2. Approval by the State Local Finance Officer. 3. Notice of second reading published between 7-21 days. 4. Second reading of Amendment. 5. Publish after adoption. The usual time frame is two (2) months. As the lead field auditor pointed out, the County had the money but the budget amendment needed to be passed Magoffin County Judge-Executive Dr. Hardin and I decided to pay the bills, continue services to our citizens and take the audit hit. I and he believe that we did the Right Thing. Kila Keeton, Magoffin County Treasurer & Charles Doc Hardin, M.D. Magoffin County Judge Executive.

Auditor’s Response: As stated in your response, the tornado struck Magoffin County in March 2012 (Fiscal Year 2012). Thus, the tornado occurred 4 months prior to the beginning of the Fiscal Year 2013 and 16 months prior to the end of fiscal year 2013. Events that took place during Fiscal Year 2012 would have no bearing on the county’s failure to comply with KRS 68.300 and KRS 68.280 in Fiscal Year 2013.

The fiscal court did not amend the county’s budget for unanticipated receipts. The fiscal court did not amend the budgets for the Road Fund, LGEA Fund, and Solid Waste Fund. By not amending these funds the fiscal court overspent the total budgeted appropriations. Overspending total budgeted appropriations is a violation KRS 68.300. This was due to the fiscal court not being fiscally responsible and their disregard of the applicable laws relating to the county’s budget. KRS 68.280 states, “The fiscal court may make provision for the expenditure of receipts unanticipated in the original budget by preparing an amendment to the budget, showing the source and amount of the unanticipated receipts and specifying the budget funds that are to be increased thereby.” We recommend the fiscal court follow the provisions of KRS 68.280 to avoid noncompliance with KRS 68.300.

Official's Response: See Response Number 1. I take the responsibility for this audit finding. Judge Hardin.

The county treasurer did not present an annual settlement to the fiscal court within the time period required by state law. The county treasurer did not present an annual settlement to the fiscal court within the time period required by state law. By not presenting the annual settlement on a timely basis, the fiscal court did not have timely financial information that could have influenced decisions regarding the county's financial condition. Had the county treasurer reviewed her duties as outlined in the *County Budget Preparation and State Local Finance Officer Policy Manual*, the annual settlement may have been presented in a timely manner. KRS 68.020(5) requires an annual settlement to be presented to the fiscal court within 30 days after the close of the fiscal year. The annual settlement was presented to the fiscal court on August 20, 2013. We recommend the county treasurer present an annual settlement to the fiscal court within 30 days after the close of the fiscal year as required by KRS 68.020(5).

Official's Response: Recommendation accepted.

The county treasurer did not monitor fund cash balances which caused the 911 Fund to have a negative balance. The county treasurer did not monitor fund cash balances which caused the 911 Fund to have a negative balance at the end of the fiscal year. By not monitoring the cash balance of the 911 Fund, the county is in noncompliance with KRS 68.300. Had the county treasurer performed her duties as outlined in the *County Budget Preparation and State Local Finance Officer Policy Manual*, the negative balance in the 911 Fund would not have occurred. One of the duties listed requires the county treasurer to countersign checks only when the following three conditions exist: (1) claim is reviewed by the fiscal court, (2) sufficient fund balance, and adequate cash in the bank to cover the check, and (3) adequate free balance in a properly budgeted appropriation account to cover the check. We recommend the county treasurer monitor the cash balance in each fund and perform her duties as outlined in the *County Budget Preparation and State Local Finance Officer Policy Manual* to prevent noncompliance with KRS 68.300.

Official's Response: This was due to the timing of a deposit. I will prevent this in the future.

The county did not maintain capital asset schedules in accordance with regulatory requirements. The county did not maintain a complete and accurate capital asset schedule for fiscal year ending June 30, 2013. The Department for Local Government requires counties to track capital assets (i.e. land, buildings, equipment, vehicles, infrastructure, etc.) and maintain a listing of capital assets to be provided to auditors for inclusion in the audit report. This list should include all current year additions/purchases, retirements, disposals/sale of assets, etc. Any related documentation for capital asset additions, retirements, and disposals in the form of invoices, deeds, purchase orders, sales records, titles, liens, etc. should be maintained in a manner that facilitates easy access, retrieval, and verification of capital asset amounts recorded. We recommend the county implement procedures to identify and track capital asset additions, retirements, and disposals in order for capital asset schedules to be complete and accurate.

Additionally, we recommend the county perform physical inventories periodically to further ensure the accuracy and completeness of capital asset schedules.

Official's Response: Since this requirement is no longer in place, we will update our thresh hold amount on inventory.

Auditor's Response: Accurate inventory schedule requirements have not changed. Please see Department for Local Government's County Budget Preparation and State Local Finance Officer Policy Manual.

The county's administrative code does not address commuting mileage or the personal use of a county vehicle. The county judge/executive's personal use and commuting mileage of a county vehicle are not being reported as compensation or employee benefit on form W-2 wage and tax statement. The maintenance and fuel costs associated with the personal use of a county vehicle significantly increase costs to taxpayers. The county's administrative code does not address the use of a county vehicle for personal use or commuting travel. Therefore, we were unable to determine if the county judge/executive was authorized to use a county vehicle for any reason other than business related to the county. Personal use of public resources is permitted if the entity has approved such use; however, personal use should be reported as compensation on employees' form W-2 wage and tax statements. Internal Revenue Code Section 61(a) states that the commuting value of a vehicle owned or leased by a public entity represents taxable income to the employee.

We recommend the fiscal court establish controls over county vehicles by implementing the following:

- Personal use and commuting mileage for county vehicles should be properly reported as compensation/employee benefit on W-2 wage and tax statements in accordance with IRS regulations. Several methods can be used to determine the vehicle use that is taxable income to the employees, including the cents-per-mile rule, the lease value rule, and the commuting rule.
- Every employee and every department that has county vehicles should maintain vehicle logs. The logs should include, at a minimum, the date, destination, purpose, and mileage for all use of the vehicle.

The fiscal court should amend the current administrative code to include a policy on the authorization and use of county vehicles. In addition, it should address the tax implications of using a county vehicle for personal use or commuting travel.

Official's Response: It is correct that the County Administrative Code does not address the issue of personal use of county vehicles by Officials or Employees. The Chief Executive of Magoffin County Judge-Executive Hardin has authorized essential personnel, who would reasonably be needed in Emergencies to drive their vehicles home at night and on week-ends. This authorization is only for Officials and Employees who would need to be able to respond quickly to an emergency. This authorization Is for Officials and Employees whose timely response to

emergencies is critical for the health and safety of Magoffin County Citizens and Magoffin County Property.

It is reasonable to classify the County Judge of Magoffin County as an essential part of the Emergency Response team for several reasons.

- 1. The County Judge is the official who declares a local state of emergency in Magoffin County.*
- 2. The Magoffin County Judge is trained in Emergency Incident Management having completed the 100, 200, 300 and 400 level training courses*
- 3. The County Judge has been designated by Magoffin County and Approved by the Commonwealth of Kentucky Emergency Management Department to Act as Emergency Management Director In the absence of Magoffin County Emergency Management Director.*
- 4. In a Magoffin County Emergency, the Magoffin County Judge Is the Public Information Officer charged with informing the public and media outlets as to the emergency and actions needed to be taken to protect health, safety and lives of Magoffin County Citizens.*
- 5. The Magoffin County Judge is a Kentucky Licensed Medical Doctor who is an invaluable asset in emergencies that could easily help save lives and protect health.*
- 6. The County Judge makes the ultimate decision on what resources and by whom these resources are to be utilized in an emergency.*

The wisdom of designating the County Judge Executive as essential emergency personnel was well illustrated on March 2, 2012 when a Category F3 Tornado with winds up to 160 miles per hour, tore a 3/4 mile path across parts of Magoffin County and the County Seat of Salyersville. In my role as County Judge Executive-Emergency Responder I left my home and closed down several restaurants and directed people to safe areas. The U.S. Department of Commerce, National Oceanic and Atmospheric Administration, National Weather Service awarded Magoffin County Emergency Director-Deputy Judge Mike Wilson and myself the Community Hero Award and credited us with directly saving at least fifty lives.

Auditor's Response: As stated, we recommend the fiscal court address the use of county vehicles for personal use in the county's administrative code. In addition, we recommend the county seek guidance from the Internal Revenue Service to ensure the county properly reports taxable fringe benefits for personal use of county owned vehicles.

The fiscal court did not prepare a Schedule of Expenditures of Federal Awards. The fiscal court did not prepare a Schedule of Expenditures of Federal Awards for the fiscal year ended June 30, 2013 in accordance with OMB Circular A-133. This was caused by the fiscal court not complying with the requirements of OMB Circular A-133. By not preparing a Schedule of Expenditures of Federal Awards, the fiscal court creates the risk of a single audit not being performed, if needed, which could affect the fiscal court's ability to receive Federal funding. *OMB Circular A-133 Audits of States, Local Governments, and Non-Profit Organizations, Section 310(B)* requires the county to prepare a Schedule of Expenditures of Federal Awards from the county's financial records. At a minimum, the schedule should include the following, if applicable:

- A listing of individual federal programs by federal agency.
- For federal awards received as a subrecipient, the name of the pass-through entity and identifying number assigned by the pass-through entity shall be included.
- Provide total federal awards expended for each individual federal program and the Catalogue of Federal Domestic Assistance (CFDA) number or other identifying number when the CFDA information is not available.
- Includes notes that describe the significant accounting policies used in preparing the schedule.
- To the extent practical, pass-through entities should identify in the schedule the total amount provided to subrecipients from each federal program.
- Include either in the schedule, or a note to the schedule, the value of the federal awards expended in the form of non-cash assistance, the amount of insurance in effect during the year, and loans or loan guarantees outstanding at year-end. While not required, it is preferable to present this information in the schedule.

We recommend that the fiscal court ensure that a complete and accurate Schedule of Expenditures of Federal Awards is prepared.

Official's Response: As you state, this schedule is not required but preferred it be completed.

Auditor's Response: The Schedule of Expenditures of Federal Awards is required per OMB Circular A-133 as stated clearly in the comment. The last bullet point only mentions that the "non cash assistance" is preferred to be presented as information in the "required" Schedule of Expenditures of Federal Awards.

The fiscal court lacks adequate segregation of duties over payroll. We noted inadequate segregation of duties for payroll. The treasurer is responsible for maintaining timesheets, entering payroll information into the computer system for processing, posting to the payroll ledgers, transferring funds to the revolving payroll account, administering health reimbursement and flex spending programs, preparing pay checks, preparing state and local withholding reports, and reconciling the payroll account. A strong internal control system does not allow one person to perform processing, documentation, and reporting functions. By delegating all these duties to the same individual, it increases the risk of undetected fraud and errors.

In order to strengthen internal controls, we recommend the fiscal court adequately segregate duties related to payroll or implement other controls to compensate for these weaknesses. For example, designate an individual to review the receipts and payroll ledgers, reconciliations, and reports. This individual can document their review by initialing the documents that were reviewed.

Official's Response: As was agreed by two field auditors this is very common in small counties with limited staff and resources. I'm glad in ten audits no Issue of fraud has been Identified. Will review your suggestion of documentation review by Secretary.

The fiscal court does not have adequate controls over gravel inventory. The fiscal court does not have adequate controls over gravel purchased and stored at the county's road department. Our review of the controls over gravel stockpiled at the county's road department revealed the county does maintain a log for gravel transported out to the county roads; however, the log is not kept on a consistent basis. In addition, the log does not track the gravel hauled to the road department from the rock quarry, making it impossible to estimate how much gravel should be in the stockpile. During our procedures relating to disbursements we noted gravel purchases for fiscal years 2012 and 2013 were \$109,800 and \$256,821, respectively. The dollar variance of \$147,021 is a 134% increase from fiscal year 2012. The fiscal court's lack of planned controls has created an opportunity for misappropriation of the county's assets to occur. When controls are not in place to protect the county's resources, there is an increased risk of fraud. We recommend the county maintain a log that tracks the gravel being hauled to the road department and also tracks the gravel hauled from the road department. This would allow an estimate of the gravel on hand and determine if a shortage existed.

Official's Response: Magoffin County Road Dept utilizes a gravel log control sheet to accurately account for delivery of gravel to county roads. Transported gravel is unloaded at the county garage and load tickets are required to be submitted to the foreman for daily processing. Total aggregate delivered to the county garage stockpile is reconciled with load tickets, provided by transport drivers that have signed for aggregate at the quarry. These signed load tickets are then reconciled with the monthly statement provided by the vendor. Upon reconciliation, any issues are promptly addressed to resolution.

Expenditures of gravel purchases for fiscal year 2012 and 2013 were \$109,800 and \$256,821 respectively, this variance is significant due to a few reasons. Collectively, Magoffin County Road System has 938 roads that must be maintained, with this fact in mind gravel purchases account for the highest expense in county road expenditures. Magoffin County suffers from having a multitude of gravel roads. Many conditions exist that will negatively impact this infrastructure system water, vegetation, man-made phenomenon, everyday wear and tear. However, the most severe is the expansion and contraction of road base materials. Although this condition exists throughout the year it is profoundly dominate during inclement weather conditions such as snow and rain. As road base materials freeze and thaw out these roads will require constant maintenance to prevent hazard conditions. In Feb and March 2013 alone, \$98,852.03 of aggregate was purchased to respond to the adverse road conditions of Magoffin County from inclement weather of rain and snow. During the months of Feb and March 2014, \$112,428.91 of aggregate was purchased to stabilize similar road conditions. Also, during the period in question Magoffin County had a tornado disaster declared. During this incident period we also were struck by a flooding event. Several roads and bridges received damages during this time period. Magoffin County's Road Dept. responded to this emergency situation with resources and aggregate. In 2015 alone, Magoffin County received 3 federally declared flooding events. This factor could represent an additional variance of aggregate purchased during the fiscal year in question.

Auditor's Response: During our testing, the gravel inventory controls you have described in your response were not in place. We do not question any decision a fiscal court feels is a need for the county, such as road improvements. That is a local governing body decision. What we are concerned with is the lack of controls over the purchase, receipt, storage, and distribution of those assets. Without adequate controls in place over the county's assets, the risks of misappropriation fraud increase. We recommend the controls over the gravel inventory be strengthened.

The fiscal court did not follow proper procedures for timesheets. During our testing of payroll, we noted several deficiencies related to timesheets. Of the 15 employees tested, we noted three instances in which employees did not sign the timesheet, three instances in which supervisors did not sign timesheets, and two instances in which neither the employee nor the supervisor signed the timesheet. KRS 337.320 requires that every employer keep a record of the hours worked each day and each week by each employee. Additionally, good internal controls dictate that all timesheets be signed by employees and their supervisors to ensure hours are recorded accurately and reflect hours worked. Failure to implement strong internal controls over timesheets could result in inaccurate time reporting and improper compensation. We recommend the fiscal court require all timesheets be signed by employees and supervisors.

Official's Response: This has already been corrected.

The fiscal court does not have adequate controls over health reimbursement accounts and flexible spending accounts. The fiscal court does not adequately track health reimbursement account and flexible spending account contributions. The amounts contributed to these accounts are not maintained separately from regular county funds and payroll funds and cannot be easily identified in the accounting records. These monies do not belong to the county, and good internal controls require that these monies be maintained and tracked separately in the accounting system. Failure to track these accounts separately increases the risk that the monies could be misappropriated. We recommend the fiscal court implement procedures to track and identify health reimbursement and flexible spending accounts for all employees who participate in these programs.

Official's Response: We will start a new bank account for the flex spending.

County did not update insurance policies for capital asset changes. During testing of capital assets and insurance coverage, auditors discovered two items that were purchased during the year and were not properly added to the fiscal court's insurance policy. Insurance policies must be updated timely in order for the county to avoid unnecessary costs associated with insurance coverage on assets no longer owned by the county and to ensure that all county assets are properly insured in the event of loss. The county needs to periodically review insurance coverage and compare to the capital asset schedules and assets on hand to make changes and adjustments as necessary so that the proper assets are adequately covered at all times. Accurate capital asset listings are essential to complete and accurate financial reporting. We recommend the county periodically review and compare capital asset schedules and insurance coverage to ensure both are complete, accurate, and updated timely.

Official's Response: This was an oversight. Capital assets are insured within twenty-four hours of purchase.

The fiscal court does not have adequate controls over notes receivable. The fiscal court does not have proper oversight and controls over notes receivable. In August 2008, the fiscal court loaned the Magoffin County Water District \$20,000 for a water project. The water district has not made any payments to date and the entire amount is still outstanding. In September 2011, the fiscal court gave \$50,000 to the City of Salyersville for water projects related to Salyersville Water Works. The fiscal court minutes indicate this was a loan; however, the county judge/executive and the treasurer stated it was not a loan and is not expected to be paid back. Failure to follow up on outstanding notes receivable and establish payment plans, deprives the county of needed funds. We recommend management and the fiscal court review the terms of all notes receivable to determine if the county will pursue collection or alternate disposition (i.e. loan forgiveness).

Official's Response: With respect to the \$50,000 given to the City of Salyersville, the fiscal court will review the terms of the loan. The loan to the Magoffin County Water District was forgiven.

The audit report can be found on the [auditor's website](#).

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