



Auditor of Public Accounts
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Edelen Releases Audit of LaRue County Fiscal Court

FRANKFORT, Ky. – State Auditor Adam Edelen has released the audit of the financial statements of the LaRue County Fiscal Court for the fiscal year ended June 30, 2014. State law requires annual audits of county fiscal courts.

Recent changes in 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 LaRue County Fiscal Court in accordance with generally accepted accounting principles in the United States. The report found that the financial statement of the Fiscal Court 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 Fiscal Court should improve controls over disbursements. As a result of our audit, we noted Fiscal Court had deficiencies in internal controls over disbursements. During our testing of disbursements, the following deficiencies were noted:

- Fiscal Court approved claims and made appropriations in excess of budgeted appropriation amounts two hundred ninety-seven (297) times during the fiscal year without requesting budget transfers prior to overspending. Two hundred ninety-seven claims (297) were approved and paid even though the budget line item had a negative free balance when

payment was approved and made. Budget transfers were not obtained until two weeks to seven months later.

- Two operating disbursements tested were not approved prior to payment.
- Payroll related items were not included in the annual budget standing order and not approved for payment by Fiscal Court as they occurred.

These deficiencies in internal controls over disbursements were allowed to occur because the Fiscal Court's controls and oversight over disbursements did not operate properly. Proper internal controls over disbursements are important to ensure the budget is not overspent; disbursements are approved by Fiscal Court prior to payment.

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..." and KRS 68.275(1) states, "claims against the county that are within the amount of line items of the county budget and arise pursuant to contracts duly authorized by the fiscal court shall be paid by the County Judge/Executive by a warrant drawn on the county and co-signed by the County Treasurer." In addition, KRS 68.275(2) requires the County Judge/Executive to present all claims to the Fiscal Court for review prior to payment unless the expenses are included on a standing order adopted by the Fiscal Court. Good internal controls also dictate that Fiscal Court approve budget transfers prior to overspending budget line items, approve disbursements prior to payment. We recommend budget transfers be obtained prior to overspending budget line items, all disbursements be presented to Fiscal Court prior to payment unless a standing order has been obtained.

County Judge/Executive's response: This is, for the most part, a hold over comment from the last audit. Auditor Edelen fails to mention that when it was recommended last year to change our method of budget transfers, it was done immediately and was implemented in April 2014. However, since the implementation was during the fiscal year, we knew this comment would be carried forward to the 2013-2014 (current) Audit even though it was changed a year ago. The procedures we followed up until April 2014 were the same procedures we had used for many, many years, with each being audited by the Auditor with no comment or recommendation to do them differently.

The two (2) operating expenditures tested that had not been approved prior to payment are not operating expenditures. Auditor Edelen failed to recognize these were delinquent tax payments that were made to the County Clerk. By statute, the Clerk forwards the payment to the Fiscal Court and we in turn make payment out to the proper district. These are not operating expenditures and are pass through funds that are handed to county government and we then hand them to the proper agency. Statute requires this. The two expenditures that received comments were a \$39 payment to the New Hope Fire Department and a \$130 payment to the LaRue County Fire Department.

Regarding the Payroll items not included in the standing order list, these involved employee benefits such as Social Security, Retirement and Health Insurance. These items are required by state and federal law. I cannot reason as to why Auditor Edelen feels they are necessary to list in a standing order as they are required by state and federal law which supersedes any standing order of the Fiscal Court. This question arose last year and we challenged the comment. We

were instructed by Auditor Edelen to consult with the Department for Local Government (DLG) regarding the proper method for standing orders of this type. The Department stated our method was correct. We then received word from the Auditor that DLG had instructed us improperly. These type actions certainly leave counties in a quandary as to what they should do and results in a no win situation, allowing the Auditor to write a comment in either case. In other words, the Auditor can't tell us how to do a procedure, to find out we are told by the Auditor we must consult the DLG. DLG tells us we are doing it correctly but we are then told by the Auditor the Dept. has instructed incorrectly. This is no win situation and the result is an audit comment written either way.

Auditors' response: We appreciate the County's willingness to try and correct the budget problem; however, we found many instances still in May 2014 and June 2014 where disbursements were made when there was no budget available. The transfers to cover the amounts were not made until the end of June 2014. So the process the County has attempted to put in place needs to be looked at again.

The County Judge is correct when he states the two disbursements noted were payments made to taxing districts. However, that does not prevent the county from having to follow KRS 68.275(2) which requires the County Judge/Executive to present ALL claims to the Fiscal Court for review prior to payment unless the expenses are included on a standing order adopted by the Fiscal Court.

Although many payroll related disbursements are required by state and federal law, this still does not preclude the county from following KRS 68.275(2) and KRS 68.275(3). Again, KRS 68.275(2) requires the County Judge/Executive to present ALL claims to the Fiscal Court for review prior to payment unless the expenses are included on a standing order adopted by the Fiscal Court. KRS 638.275(3) states, "The fiscal court may adopt an order to pre-approve the payment of monthly payroll and utility expenses. No other expenses shall be pre-approved pursuant to this subsection without the written consent of the State Local Finance Officer. It is understood that payroll items are recurring, necessary items. Hence, the creation of the standing order.

The Fiscal Court has a lack of adequate segregation of duties over cash and receipts. A lack of segregation of duties exists over cash and receipts. The County Treasurer receives the mail, prepares and deposits the receipts, prepares bank reconciliations, and prepares financial reports. Adequate segregation of duties would prevent the same person from having a significant role in the receiving, recording, and reporting of receipts. The Fiscal Court should strengthen internal controls by either segregating the duties or by implementing and documenting compensating controls. If one employee is solely responsible for the receipt, reporting and reconciling process, the risk of misappropriation of assets and/or inaccurate financial reporting increases. We recommend the Fiscal Court separate the duties in preparing and depositing receipts, recording transactions, reconciling bank accounts, and preparing financial reports. If these duties cannot be segregated due to limited number of staff or budget, strong oversight should be provided over the employee responsible for these duties. Any compensating controls performed should be documented.

County Judge/Executive's response: This comment is contained in nearly every audit performed on counties, cities, special districts and nonprofit organizations. The only remedy is to have more people involved, which in turn means more employees. We manage as efficiently as possible with as small a staff as possible in an attempt to save the citizens tax dollars.

The Jailer should prepare an accurate financial statement and maintain required records for the Jail Commissary Fund. During our review of the Jail Commissary Fund, we noted the following deficiencies:

- The yearly financial statement of the Jail Commissary Fund was not provided to the County Treasurer at fiscal year end. The Jailer did prepare a Cash Flow Summary for the auditor which did not accurately reflect the Commissary's records. Receipts were overstated by \$35,654 and disbursements were overstated by \$43,754.
- The yearly financial statement of the Jail Commissary Fund did not agree to the daily checkout sheets and checks written.
- Monthly reconciliations were not prepared for throughout the fiscal year.

These deficiencies in Jail Commissary Fund were allowed to occur because the Jailer's controls and oversight over reporting did not operate properly. Failing to maintain accurate records can result in inaccurate information as to funds available for use for benefit of the inmates. Good internal controls dictate that adequate reporting be maintained for all receipts and disbursements.

Kentucky Revised Statute (KRS) 441.135 requires the Jailer to maintain records of receipts and disbursements of the Jail Commissary Fund and to prepare a report annually for the county treasurer. In addition, KRS 68.210 gives the State Local Finance Officer the authority to prescribe a uniform system of accounts. The Instructional Guide for County Budget Preparation and State Local Finance Officer Policy Manual provides guidelines to maintaining records for the Jail Commissary Fund. In accordance with these guidelines, the Jailer should maintain the following records:

In accordance with these guidelines, the Jailer should maintain the following records:

- Daily checkout sheets should include a category for all funds collected to be posted to the Jail Commissary Receipts Journal.
- Jail Commissary Receipts Journal should agree to the daily checkout sheets and include a category for all funds collected.
- Jail Commissary Disbursements Journal should include every check written. Each check written should be posted to the proper category.
- Jail Commissary Summary and Reconciliation can be used as a monthly cash reconciliation and as the year-end report to be submitted to the County Treasurer. The year to date summary section of this report will provide a cash balance at anytime during the fiscal year. Information for this section is obtained from totaled categories from the receipt and disbursement journals. A monthly cash balance shall be maintained. The Reconciliation section of this report reconciles the bank balance to the cash balance.

We recommend the Jailer comply with the applicable statutes by maintaining required records, preparing and submitting an accurate annual Commissary report to the County Treasurer at year-end that includes all receipts and disbursements and reconciles to the receipts ledger and disbursements ledger.

County Judge/Executive's response: The Fiscal Court does not collect, manage or control the Jail Commissary Fund. This is a responsibility of the Jailer and his response should be included.

Jailer's response: Agreed.

The Jailer lacks an adequate segregation of duties. A lack of segregation of duties exists over all Jail Commissary Fund accounting functions. The bookkeeper receives the mail, prepares and deposits the receipts, and writes checks. Adequate segregation of duties would prevent the same person from having a significant role in the receiving process, recording, and reporting of receipts and disbursements. The Jailer should strengthen internal controls by either segregating the duties or by implementing and documenting compensating controls. If one employee is solely responsible for the receipt, disbursement, and reporting and reconciling process, the risk of misappropriation of assets and/or inaccurate financial reporting increases. We recommend the Jailer separate the duties in preparing and depositing receipts, recording transactions, preparing checks, and reconciling bank accounts. If these duties cannot be segregated due to limited number of staff or budget, strong oversight should be provided over the employee responsible for these duties. Any compensating controls performed should be documented.

County Judge/Executive's response: The Jailer is responsible for collection and management of funds under his control. However, comment 2014-002 would be appropriate in this situation.

Jailer's response: Agreed.

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

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