

**REPORT OF THE AUDIT OF THE
JACKSON COUNTY
SHERIFF**

**For The Year Ended
December 31, 2016**



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MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Shane Gabbard, Jackson County Judge/Executive
The Honorable Paul Hays, Jackson County Sheriff
Members of the Jackson County Fiscal Court

Independent Auditor's Report

Report on the Financial Statement

We have audited the accompanying Statement of Receipts, Disbursements, and Excess Fees - Regulatory Basis of the Sheriff of Jackson County, Kentucky, for the year ended December 31, 2016, and the related notes to the financial statement.

Management's Responsibility for the Financial Statement

Management is responsible for the preparation and fair presentation of the financial statement in accordance with accounting practices prescribed or permitted by the laws of Kentucky to demonstrate compliance with the Commonwealth of Kentucky's regulatory basis of accounting and budget laws. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, 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 financial statement 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 financial statement.

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



The Honorable Shane Gabbard, Jackson County Judge/Executive
The Honorable Paul Hays, Jackson County Sheriff
Members of the Jackson County Fiscal Court

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 1 of the financial statement, the financial statement is prepared by the Jackson County Sheriff on the basis of the accounting practices prescribed or permitted by the laws of Kentucky to demonstrate compliance with the Commonwealth of Kentucky's regulatory basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the financial statement of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles paragraph, the financial statement referred to above does not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of each fund of the Jackson County Sheriff, as of December 31, 2016, or changes in financial position or cash flows thereof for the year then ended.

Opinion on Regulatory Basis of Accounting

In our opinion, the financial statement referred to above presents fairly, in all material respects, the receipts, disbursements, and excess fees of the Jackson County Sheriff for the year ended December 31, 2016, in accordance with the basis of accounting practices prescribed or permitted by the Commonwealth of Kentucky as described in Note 1.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 20, 2017, on our consideration of the Jackson County Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is solely 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 the internal control over financial reporting 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 over financial reporting and compliance.

Based on the results of our audit, we have presented the accompanying Schedule of Findings and Responses, included herein, which discusses the following report comments:

- 2016-001 The Jackson County Sheriff's Financial Statement Was Materially Misstated
- 2016-002 The Jackson County Sheriff's Office Lacks Adequate Segregation Of Duties Over Receipts, Bank Reconciliations, And Disbursements

Respectfully submitted,



Mike Harmon
Auditor of Public Accounts

September 20, 2017

JACKSON COUNTY
PAUL HAYS, SHERIFF
STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES - REGULATORY BASIS

For The Year Ended December 31, 2016

Receipts

State - Kentucky Law Enforcement Foundation Program Fund (KLEFPF)	\$	15,146
State Fees For Services:		
Finance and Administration Cabinet	\$	73,396
Sheriff Security Service		2,479
Cabinet For Health And Family Services		3,625
Delinquent Tax - State		11,416
		90,916
Circuit Court Clerk:		
Fines and Fees Collected		456
Fiscal Court		27,296
County Clerk - Delinquent Taxes		9,374
Commission On Taxes Collected		152,337
Fees Collected For Services:		
Auto Inspections		2,655
Accident and Police Reports		1,220
Serving Papers		12,610
Carry Concealed Deadly Weapon Permits		7,035
		23,520
Other:		
Add-On Fees		16,477
Miscellaneous		3,767
		20,244
Interest Earned		103
Borrowed Money:		
State Advancement		56,000
		56,000
Total Receipts		395,392

The accompanying notes are an integral part of this financial statement.

JACKSON COUNTY
 PAUL HAYS, SHERIFF
 STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES - REGULATORY BASIS
 For The Year Ended December 31, 2016
 (Continued)

Disbursements

Operating Disbursements:

Personnel Services-

Deputies' Salaries	\$	90,258	
Part-Time Salaries		9,732	
Other Gross Salaries - KLEFPF		13,425	
Court Security Salaries		45,846	
Court Security Salaries Part-Time		27,904	

Materials and Supplies-

Office Materials and Supplies		13,975	
Uniforms		118	

Auto Expense-

Gasoline		9,589	
Maintenance and Repairs		14,157	

Other Charges-

Conventions and Travel		300	
Dues		443	
Postage		23	
Meal Reimbursement		265	
Other		2,689	
		<u>2,689</u>	\$ 228,724

Debt Service:

State Advancement			<u>56,000</u>
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Total Disbursements			<u>\$ 284,724</u>
Net Receipts			110,668
Less: Statutory Maximum			<u>79,386</u>
Excess Fees			31,282
Less: Training Incentive Benefit			<u>1,984</u>
Excess Fees Due County for 2016			29,298
Payment to Fiscal Court - January 12, 2017			<u>29,298</u>
Balance Due Fiscal Court at Completion of Audit			<u><u>\$ 0</u></u>

The accompanying notes are an integral part of this financial statement.

JACKSON COUNTY
NOTES TO FINANCIAL STATEMENT

December 31, 2016

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

A fee official uses a fund to report on the results of operations. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fee official uses a fund for fees to account for activities for which the government desires periodic determination of the excess of receipts over disbursements to facilitate management control, accountability, and compliance with laws.

B. Basis of Accounting

KRS 64.820 directs the fiscal court to collect any amount, including excess fees, due from the sheriff as determined by the audit. KRS 134.192 requires the sheriff to settle excess fees with the fiscal court at the time he files his annual settlement with the fiscal court on or before September 1 of each year. KRS 64.830 requires an outgoing sheriff to settle excess fees with the fiscal court of his county by March 15 immediately following the expiration of his term of office.

The financial statement has been prepared on a regulatory basis of accounting, which demonstrates compliance with the laws of Kentucky and is a special purpose framework. Under this regulatory basis of accounting, receipts and disbursements are generally recognized when cash is received or disbursed, with the exception of accrual of the following items (not all-inclusive) at December 31 that may be included in the excess fees calculation:

- Interest receivable
- Collection on accounts due from others for 2016 services
- Reimbursements for 2016 activities
- Tax commissions due from December tax collections
- Payments due other governmental entities for payroll
- Payments due vendors for goods or services provided in 2016

The measurement focus of a fee official is upon excess fees. Remittance of excess fees is due to the county treasurer in the subsequent year.

C. Cash and Investments

KRS 66.480 authorizes the sheriff's office to invest in obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

D. Fee Pooling

The Jackson County Sheriff's office is required by the fiscal court to participate in fee pooling system. Fee officials who are required to participate in fee pooling deposit all funds collected into their official operating account. The fee official is responsible for paying all amounts collected for others. Residual funds are then paid to the county treasurer on a monthly basis. Invoices are submitted to the county treasurer to document operating expenses. The fiscal court pays all operating expenses for the fee official.

JACKSON COUNTY
 NOTES TO FINANCIAL STATEMENT
 December 31, 2016
 (Continued)

Note 2. Employee Retirement System and Other Post-Employment Benefits

The county official and employees have elected to participate, pursuant to KRS 78.530, in the County Employees Retirement System (CERS), which is administered by the Board of Trustees of the Kentucky Retirement Systems (KRS). This is a cost-sharing, multiple-employer, defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability, and death benefits to plan members. Benefit contributions and provisions are established by statute.

Nonhazardous

Nonhazardous covered employees are required to contribute five percent of their salary to the plan. Nonhazardous covered employees who begin participation on or after September 1, 2008, are required to contribute six percent of their salary to be allocated as follows: five percent will go to the member's account and one percent will go to the KRS insurance fund.

In accordance with Senate Bill 2, signed by the Governor on April 4, 2013, plan members who began participating on, or after, January 1, 2014, were required to contribute to the Cash Balance Plan. The Cash Balance Plan is known as a hybrid plan because it has characteristics of both a defined benefit plan and a defined contribution plan. Members in the plan contribute a set percentage of their salary each month to their own accounts. Nonhazardous covered employees contribute five percent of their annual creditable compensation. Nonhazardous members also contribute one percent to the health insurance fund which is not credited to the member's account and is not refundable. The employer contribution rate is set annually by the Board based on an actuarial valuation. The employer contributes a set percentage of the member's salary. Each month, when employer contributions are received, an employer pay credit is deposited to the member's account. A member's account is credited with a four percent employer pay credit. The employer pay credit represents a portion of the employer contribution.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Nonhazardous employees who begin participation on or after September 1, 2008, must meet the rule of 87 (member's age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months service credit.

The county's contribution rate for nonhazardous employees was 17.06 percent for the first six months and 18.68 percent for the last six months.

Health Insurance Coverage

CERS also provides post-retirement health care coverage as follows:

For members participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

Years of Service	% Paid by Insurance Fund	% Paid by Member through Payroll Deduction
20 or more	100%	0%
15-19	75%	25%
10-14	50%	50%
4-9	25%	75%
Less than 4	0%	100%

JACKSON COUNTY
NOTES TO FINANCIAL STATEMENT
December 31, 2016
(Continued)

Note 2. Employee Retirement System and Other Post-Employment Benefits (Continued)

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, non-hazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount. This dollar amount is subject to adjustment annually based on the retiree cost of living adjustment, which is updated annually due to changes in the Consumer Price Index.

KRS issues a publicly available annual financial report that includes financial statements and required supplementary information on CERS. This report may be obtained by writing the Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, KY 40601-6124, or by telephone at (502) 564-4646.

Note 3. Deposits

The Jackson County Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240, the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the sheriff's deposits may not be returned. The Jackson County Sheriff does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 66.480(1)(d) and KRS 41.240. As of December 31, 2016, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

Note 4. Forfeiture Account

The Jackson County Sheriff's office maintains an account funded by proceeds from the confiscation, surrender, or sale of real and personal property involved in drug related convictions. The balance on January 1, 2016, was \$3,484. During calendar year 2016, the sheriff deposited \$4,107 and expended \$5,500, leaving a remaining balance of \$2,091 as of December 31, 2016. The use of these funds is determined by court order granting forfeiture funds to the sheriff's office; therefore, they are not included as part of excess fees.

Note 5. Donation Account

The Jackson County Sheriff's office maintains a donation account to account for private and public donations to the sheriff's office. On January 1, 2016, the balance was \$2,500. During calendar year 2016, the sheriff's office received \$2,505 in donations and expended \$4,694. The balance in the account was \$311 as of December 31, 2016.

JACKSON COUNTY
NOTES TO FINANCIAL STATEMENT
December 31, 2016
(Continued)

Note 6. On Behalf Payment

The Jackson County Sheriff's office is required by the fiscal court to participate in a fee pooling system. The Jackson County Fiscal Court paid the Jackson County Sheriff's training incentive benefit as reflected on the Jackson County Sheriff's financial statement. For the year ended December 31, 2016, the Jackson County Fiscal Court's contributions recognized by the Jackson County Sheriff included the amount that was based on the training incentive benefit as required by KRS 64.5275(6). The Jackson County Sheriff recognized receipts from the fiscal court and disbursements for training incentive benefit of \$1,984 for the year ended December 31, 2016.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

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MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Shane Gabbard, Jackson County Judge/Executive
The Honorable Paul Hays, Jackson County Sheriff
Members of the Jackson County Fiscal Court

Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With *Government Auditing Standards*

Independent Auditor's Report

We have audited, 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, the Statement of Receipts, Disbursements, and Excess Fees - Regulatory Basis of the Jackson County Sheriff for the year ended December 31, 2016, and the related notes to the financial statement and have issued our report thereon dated September 20, 2017. The Jackson County Sheriff's financial statement is prepared on a regulatory basis of accounting, which demonstrates compliance with the Commonwealth of Kentucky's regulatory basis of accounting and budget laws, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statement, we considered the Jackson County Sheriff's 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 financial statement, but not for the purpose of expressing an opinion on the effectiveness of the Jackson County Sheriff's internal control. Accordingly, we do not express an opinion on the effectiveness of the Jackson County Sheriff's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Responses, we identified certain deficiencies in internal control that we consider to be material weaknesses.

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 financial statement will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as items 2016-001 and 2016-002 to be material weaknesses.



Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With *Government Auditing Standards*
(Continued)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Jackson County Sheriff's financial statement is free of 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 financial statement 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*.

Views of Responsible Official and Planned Corrective Action

The Jackson County Sheriff's views and planned corrective action to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The sheriff's responses were not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on them.

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.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Mike Harmon", with a long horizontal line extending to the right.

Mike Harmon
Auditor of Public Accounts

September 20, 2017

SCHEDULE OF FINDINGS AND RESPONSES

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JACKSON COUNTY
PAUL HAYS, SHERIFF
SCHEDULE OF FINDINGS AND RESPONSES

For The Year Ended December 31, 2016

INTERNAL CONTROL - MATERIAL WEAKNESSES:

2016-001 The Jackson County Sheriff's Financial Statement Was Materially Misstated

The Jackson County Sheriff's 2016 financial statement was materially misstated due to the following issues:

- Receipts from the Kentucky Law Enforcement Foundation Program Fund (KLEFPF), the fiscal court, and the Kentucky State Treasurer for sheriff security services were posted to the ledgers as negative expenditures, causing a material misstatement.
- Receipt and disbursement amounts posted to the financial statement were inconsistently treated. Receipt line items for various fees were not handled the same each quarter, making agreement between the ledger and fourth quarter financial statement impossible.

Numerous adjustments were required to reclassify receipts and disbursements that had been misclassified on the ledgers. This has resulted in multiple posting errors to both receipts and disbursements, which in aggregate materially misstate the financial statement.

The majority of the issues were caused by errors in bookkeeping and a lack of oversight of the preparation of the financial statement. The sheriff's bookkeeper was new and had limited training. The prior year fee audit was completed in 2017. As a result, the sheriff did not have time for corrective action to be applied for the calendar year 2016 audit.

KRS 68.210 requires the State Local Finance Officer to create a system of uniform accounts for all counties and county officials. The *County Budget Preparation and State Local Finance Officer Policy Manual* outlines minimum requirements for handling public funds. Good internal controls dictate that all transactions should be posted to the ledgers to produce an accurate representation of the financial activity. Furthermore, line items on ledgers should be given the same treatment each time a financial statement is produced in order to give a clear representation of the year's finances.

We recommend the Jackson County Sheriff improve procedures over financial reporting to ensure transactions are properly recorded and financial statements are materially stated.

Sheriff's Response: Software for 2016 ledger report were recorded in Quick Books. The KLEFPF Payroll Expense Account was incorrectly set up as income account. Accounts have been correctly set up for Income-KY State Reimbursements and for Expenses – Actual KLEFPF expense (Payroll).

Both Monthly Advancement Reports and Quarterly Finance Reports were reported correctly and reconciled to bank statements.

Auditor's Reply: The quarterly financial statements submitted to the Department for Local Government were not accurate. As stated in the comment above, there were material misstatements resulting from posting errors.

JACKSON COUNTY
PAUL HAYS, SHERIFF
SCHEDULE OF FINDINGS AND RESPONSES
For The Year Ended December 31, 2016
(Continued)

INTERNAL CONTROL - MATERIAL WEAKNESSES: (Continued)

2016-002 The Jackson County Sheriff's Office Lacks Adequate Segregation Of Duties Over Receipts, Bank Reconciliations, And Disbursements

This is a repeat finding and was included in the prior year audit report as finding 2015-001. The sheriff's bookkeeper is responsible for collecting receipts, preparing deposits, preparing daily checkout sheets, posting to ledgers, and performing bank reconciliations. The sheriff or another employee did not document oversight of bank reconciliations. The sheriff's bookkeeper is also responsible for preparing purchase orders, preparing checks, and signing checks. The sheriff has implemented compensating controls, including having an outside bookkeeper review monthly ledgers and bank statements and the sheriff signing checks as a second signature after comparison to invoices. However, the compensating controls were not effective at preventing or detecting mistakes made by the bookkeeper.

According to the sheriff, the lack of segregation of duties is a result of a limited budget, which restricts the number of employees the sheriff can hire and delegate responsibilities to.

This deficiency increases the risk of misappropriation of assets, errors, and inaccurate financial reporting to external agencies, such as the Department for Local Government.

The segregation of duties over various accounting functions such as preparing deposits, preparing daily checkout sheets, and issuing cash receipts is essential for providing protection from asset misappropriation and inaccurate financial reporting. Good internal controls dictate that duties of preparing purchase orders, preparing checks, signing checks, posting to ledgers, and reconciliations of ledgers to bank accounts be segregated. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

We recommend the sheriff segregate duties over receipts, bank reconciliations, and disbursements. If segregation of duties is not feasible, the sheriff should implement compensating controls that are effective.

Sheriff's Response: Due to budget limitations, Sheriff can only employ one full-time bookkeeper. Compensating controls have been in place since July, 2016 to review reports. An outside contract accountant has been hired to reconcile bank accounts to the monthly and quarterly reports.