



Auditor of Public Accounts
Mike Harmon

FOR IMMEDIATE RELEASE

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Harmon Releases Audit of LaRue County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the LaRue County Fiscal Court for the fiscal year ended June 30, 2016. 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 fund balances of the LaRue 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 noncompliance 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 LaRue County Fiscal Court lacks adequate segregation of duties over cash and receipts. This is a repeat finding which was included in the prior year audit report as Finding 2015-001. The LaRue County Treasurer prepared and deposited receipts, posted receipts to the accounting system, prepared monthly reports for fiscal court and quarterly reports for the Department for Local Government, made cash transfers between funds and bank accounts, and performed bank reconciliations for all bank accounts. The fiscal court has not implemented a policy to ensure segregated duties or sufficient compensating controls. The lack of adequate segregation of duties and too much control by one individual could result in undetected misappropriation of assets, errors, and inaccurate financial reporting.

Good internal controls dictate adequate segregation of duties to prevent the same person from having complete control in the receiving, recording, and reporting of funds. A strong internal control structure includes adequate segregation of duties or strong compensating controls to offset the risk caused by the lack of segregation of duties. Without proper segregation or strong compensating controls, the county cannot ensure all receipts are deposited and all bank activity is appropriately documented in the accounting system.

We recommend the fiscal court strengthen internal controls by segregating the duties involved in receiving, recording, reconciling, and reporting receipts. If segregation is not possible, we recommend further compensating controls, such as a receipt listing prepared by another person to compare to deposit tickets and ledger posting and implementing reconciliation of ambulance receipts with other personnel and the county treasurer.

County Judge/Executive's response: This comment is found in most small county audit reports. In fact, it is so common that former Auditor Ed Hatchett would never include it in his audit reports. Additional segregation often means additional staffing resulting in additional costs. We will save the county money and receive the write up.

Auditor's Reply: The lack of adequate segregation of duties is a material weakness in the internal control system of the LaRue County Fiscal Court. If the county cannot properly segregate duties due to a limited budget, they can help offset the material weakness with compensating controls as recommended. Many of these compensating controls would not require hiring additional personnel and can be completed by existing personnel, including local officials.

The LaRue County Fiscal court lacks adequate controls over reconciliation of the payroll revolving bank account. This is a repeat finding which was included in the prior year audit report as Finding 2015-004. The county has not completed regular, accurate reconciliations for the payroll revolving bank account. Insufficient records and management oversight resulted in a control weakness over this bank account. Not reconciling the payroll revolving bank account monthly could result in misappropriation of funds and inaccurate financial reporting. Good internal controls require timely, accurate reconciliations to ensure all funds are properly accounted for.

We recommend the county complete monthly reconciliations of the payroll revolving bank account and reconcile the account to zero every month. A listing of outstanding checks and liabilities should be attached to each monthly report.

County Judge/Executive's response: When the Larue County Sheriff resigned from office there had not been an application made to the state for funds advancement to pay salaries. When the new Sheriff took office the time had expired and no advancement could be received. As a result, county funds had to be placed in the payroll revolving account to pay the Sheriff's payroll. This caused the audit comment received above. While this matter involved the Sheriff's office, due to the county having a unified payroll system the comment is placed in the Fiscal Court Audit rather than the Sheriff's audit. This comment will no longer appear in the Audit Report after this year.

Auditor's Reply: This finding is due to LaRue County Fiscal Court personnel not performing reconciliations of the county's payroll account, which is not addressed in the explanation provided in the county's response. To clear this finding for future audits, LaRue County Fiscal Court personnel should complete accurate monthly reconciliations of the payroll account.

The LaRue County Fiscal Court did not follow the Department for Local Government's guidance for reporting general obligation bond proceeds. The county did not include all funds on the Fourth Quarter Financial Report, resulting in unreported General Obligation Bond proceeds of \$264,255 at June 30, 2016. The county was not ready to expend the funds, so the fiscal court did not budget or include them on the county's financial statement. When the fiscal court does not include all county money on the financial statement, taxpayers may not be aware of all funds available for expenditure. Furthermore, if the fiscal court does not budget the funds before expending them, they are in danger of overspending their budget and violating KRS 68.220.

KRS 68.210 gives the State Local Finance Officer the authority to prescribe a uniform system of accounts. Guidance in the *County Budget Preparation and State Local Finance Officer Policy Manual* provides that "[a]ll county money is to be reported on the financial statement whether it is included in the budget or not."

KRS 68.220 requires all funds to be budgeted and states "[t]he fiscal affairs of each county, except those pertaining to education, shall be administered by the fiscal court under a uniform budget system. The county budget shall provide for all the funds to be expended by the county from current revenue for each fiscal year. The state local finance officer shall classify the counties for budget purposes upon the basis of their populations and expenditures, or upon some other proper basis, and may classify them in the same manner for the purpose of prescribing accounts."

The LaRue County Fiscal Court has funds totaling \$264,255 in a bank from a financing lease obligation for future improvements to the courthouse. According to the Department for Local Government (DLG), these funds should be budgeted in the county's annual budget before they are expended and included in the financial statement. By not including this information, the financial statement and notes are not providing a complete overview of the county's available funds. We recommend the fiscal court include all funds in the county's annual financial statement and budget.

Judge/Executive's response: I challenge this audit comment as being incorrect. General Obligation (GO) proceeds are exactly that, a general obligation of the county. All funds were budgeted under the "Carryover" category on the budget. GO funds are a general receipt and obligation of the county and can be placed directly in the general fund. These funds have been carried forward from year to year until they were expended. The auditor refers to statutes 68.210 and 68.220. These statutes were written in 1984 and 1978 respectively and the GO Constitutional Amendment was adopted in November 1994. The Auditor has failed to show that the funds placed in the carryover account does not include the GO proceeds mentioned in this comment.

Auditor's Reply: As stated, the General Obligation Bond was not budgeted in the county's budget or included on the fourth quarter report. The receipts and expenditures are included as an unbudgeted fund on the county's financial statement. The county is required by DLG to budget the activity of this fund as a separate budgeted fund of the county or budget it in an existing fund.

The LaRue County Fiscal Court lacks strong internal controls over disbursements. This is a repeat finding which was included in the prior year audit report as Finding 2015-002. The LaRue County Fiscal Court had a deficiency in internal controls over disbursements which caused the county not to be in compliance with state budget law. The LaRue County Fiscal Court approved claims and made appropriations in excess of budgeted appropriations 31 times during the fiscal year without approval of budget transfers prior to overspending. These claims were approved and paid even though the budget line item did not have sufficient budgeted free balance. The fiscal court does not have sufficient internal controls in place to ensure compliance with state budget laws. Strong internal controls over disbursements are important to ensure the budget is not overspent.

The lack of internal controls increases the risk of material misstatement due to fraud or error. KRS 68.275(1), states "[c]laims 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." Strong internal controls dictate that the fiscal court approve budget transfers prior to disbursing funds to prevent overspending budget line items.

We recommend the fiscal court implement strong internal controls over disbursements to ensure that budget transfers are obtained prior to disbursing funds to prevent overspending budget line items.

County Judge/Executive's response: As indicated by the Auditor, this is a comment carried forward from a prior audit. The accounting program used by the county can cause the disbursements, on paper, to show it's made prior to the transfer to the account to make the account whole. The problem has been isolated and was reduced from 200 entries in the prior fiscal year to 31 entries in the audited fiscal year. Adjustment has been made in the accounting program and this comment will "tail off" for future audit periods.

The LaRue County Fiscal Court lacks adequate controls over capital assets. This is a repeat finding which was included in the prior year audit report as Finding 2015-003. The capital asset schedule prepared by the county did not include all additions or disposals to accurately reflect the prior year ending balances. There is no annual inventory count review or reconciliation of the inventories to the capital asset schedule to ensure accuracy. Insufficient records and management oversight resulted in noncompliance with the Department for Local Government's policy documented in the *County Budget Preparation and State Local Finance Officer Policy Manual*. Not implementing an annual inventory count, or maintaining an accurate list of capital assets could result in new assets not being insured and retired assets not being removed from the insurance policy. Furthermore, the capital asset schedule included in the financial statements could be materially incorrect. According to the Department for Local Government's policy, the asset inventory listing should provide the following detail: property tag number, asset description, serial number-if applicable, quantity-if applicable, cost, date of acquisition, date of

disposal, property location, and manager/individual responsible. Good internal controls over compliance dictate adequate supporting documentation is maintained for assets and the capital asset schedule updated regularly throughout the year to ensure accurate information is recorded.

In order to strengthen controls over capital assets and infrastructure, we recommend the fiscal court conduct annual inventories and require departments to submit completed inventory sheets to the county judge/executive's office. The submitted inventory should then be reconciled to the capital asset schedule. We recommend the county's capital asset schedule include the date of acquisition and additions, disposals, and retirements be documented accordingly.

County Judge/Executive's response: Capital Assets threshold levels have been lowered from preceding years. Also, a capital asset was found to not be removed from the asset list once it was taken out of service. The asset inventory has been updated to reflect this.

The LaRue County Jail Commissary Fund lacks adequate segregation of duties. This is a prior year finding which was included in the prior year audit report as Finding 2015-006. A lack of segregation of duties exists over all jail commissary fund accounting functions with no management supervision or oversight. The bookkeeper receives the mail, prepares and deposits receipts, posts to computer accounting software, receives invoices, and writes checks without management review. Jailer and jail personnel lack understanding of the financial information provided from new accounting system. If one employee is solely responsible for the receipt, disbursement, reconciliation process, and reporting, the risk of misappropriation of assets and inaccurate financial reporting increases. 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. Good internal controls dictate adequate segregation of duties to prevent the same person from having complete control in the receiving, recording, and reporting of funds. A strong internal control structure includes adequate segregation of duties or strong compensating controls to offset the risk caused by the lack of segregation of duties. Without proper segregation or strong compensating controls, the jailer cannot ensure all receipts and disbursements are properly recorded and accounted for.

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 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: Jail Commissary Funds are under the control and responsibility of the Jailer, not the Fiscal Court. However, the Jail Audit appears in the Fiscal Court audit as a branch of county government. The Jailer will have to respond as to how he will address this comment.

Jailer's response: The jailer did not provide a response.

The LaRue County Jailer did not properly oversee the jail commissary fund. Throughout the year, there were less than five deposits made monthly, resulting in funds on hand for long periods of time. In addition, computer reports for checkouts were not detailed by source. Disbursements were not paid timely, with invoices submitted for payments to the county over 30 days past due. Accounting records were not up to date and jail personnel were not knowledgeable about the new accounting software. The bank accounts had not been reconciled and the jailer entered into contracts without fiscal court approval.

The lack of management oversight, supervision, and review caused deficiencies in accounting and reporting for the jail commissary fund. 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.

KRS 441.135 requires the jailer to maintain records of receipts and disbursements of the jail commissary fund. In addition, KRS 68.210 gives the State Local Finance Officer the authority to prescribe a uniform system of accounts. The *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:

- 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.

We recommend the jailer properly oversee the jail commissary fund to ensure compliance with applicable statutes. Furthermore, we recommend the jailer implement internal controls to ensure deposits are made timely, invoices are paid within 30 days, and bank accounts are properly reconciled to promote accurate financial reporting.

County Judge/Executive's response: Jail Commissary Funds are under the control and responsibility of the Jailer, not the Fiscal Court. However, the Jail Audit appears in the Fiscal Court audit as a branch of county government. The Jailer will have to respond as to how he will address this comment.

Jailer's response: The jailer did not provide a response.

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

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