

**REPORT OF THE AUDIT OF THE
FORMER BREATHITT COUNTY
CLERK**

**For The Period
November 14, 2015 Through December 31, 2015**



**MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS
www.auditor.ky.gov**

**209 ST. CLAIR STREET
FRANKFORT, KY 40601-1817
TELEPHONE (502) 564-5841
FACSIMILE (502) 564-2912**

EXECUTIVE SUMMARY

AUDIT OF THE FORMER BREATHITT COUNTY CLERK

**For The Period
November 14, 2015 through December 31, 2015**

The Auditor of Public Accounts has completed the former Breathitt County Clerk's audit for the period November 14, 2015 through December 31, 2015. Based upon the audit work performed, the financial statement presents fairly in all material respects, the receipts, disbursements, and excess fees in conformity with the regulatory basis of accounting.

Financial Condition:

The former Breathitt County Clerk had excess fees of \$31,019 for the period November 14, 2015 through December 31, 2015.

Report Comments:

2015-001 The Former County Clerk's Office Lacked Adequate Segregation Of Duties Over Receipts

Deposits:

The former county clerk's deposits were insured by the Federal Deposit Insurance Corporation.

CONTENTS

PAGE

INDEPENDENT AUDITOR’S REPORT	1
STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES - REGULATORY BASIS.....	3
NOTES TO FINANCIAL STATEMENT	5
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 <i>GOVERNMENT AUDITING STANDARDS</i>	11
COMMENT AND RECOMMENDATION	15



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

The Honorable J. L. Smith, Breathitt County Judge/Executive
The Honorable Mary Lois Stevens, Former Breathitt County Clerk
The Honorable Mary Rebecca Curtis, Breathitt County Clerk
Members of the Breathitt 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 former County Clerk of Breathitt County, Kentucky, for the period November 14, 2015 through December 31, 2015, 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 this 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 as described in Note 1. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of a 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 this 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 J. L. Smith, Breathitt County Judge/Executive
The Honorable Mary Lois Stevens, Former Breathitt County Clerk
The Honorable Mary Rebecca Curtis, Breathitt County Clerk
Members of the Breathitt 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 former Breathitt County Clerk 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 former Breathitt County Clerk, as of December 31, 2015, or changes in financial position or cash flows thereof for the period 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 former Breathitt County Clerk for the period November 14, 2015 through December 31, 2015, 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 March 7, 2017 on our consideration of the former Breathitt County Clerk’s 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 the 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 the entity’s internal control over financial reporting and compliance.

Based on the results of our audit, we have presented the accompanying comment and recommendation, included herein, which discusses the following report comment:

2015-001 The Former County Clerk’s Office Lacked Adequate Segregation Of Duties Over Receipts

Respectfully submitted,



Mike Harmon
Auditor of Public Accounts

March 7, 2017

BREATHITT COUNTY
 MARY LOIS STEVENS, FORMER COUNTY CLERK
STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES - REGULATORY BASIS

For The Period November 14, 2015 Through December 31, 2015

Receipts

Fiscal Court		\$ 9,473
Licenses and Taxes:		
Motor Vehicle-		
Licenses and Transfers	\$ 42,983	
Usage Tax	42,556	
Tangible Personal Property Tax	122,059	
Notary Fees	86	
Other-		
Fish and Game Licenses	15	
Marriage Licenses	461	
Deed Transfer Tax	456	
Delinquent Tax	28,201	236,817
Fees Collected for Services:		
Recordings-		
Deeds, Easements, and Contracts	669	
Real Estate Mortgages	149	
Chattel Mortgages and Financing Statements	3,244	
Powers of Attorney	28	
Affordable Housing Trust	594	
All Other Recordings	744	
Charges for Other Services-		
Copywork	397	5,825
Other:		
Car Liens	688	
Credit Card Fees	209	
Miscellaneous	507	1,404
Interest Earned		22
Total Receipts		253,541

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

BREATHITT COUNTY

MARY LOIS STEVENS, FORMER COUNTY CLERK

STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES - REGULATORY BASIS

For The Period November 14, 2015 Through December 31, 2015

(Continued)

Disbursements

Payments to State:

Motor Vehicle-

Licenses and Transfers \$ 26,389

Usage Tax 41,279

Tangible Personal Property Tax 47,091

Licenses, Taxes, and Fees-

Fish and Game Licenses 18

Delinquent Tax 2,517

Legal Process Tax 798

Affordable Housing Trust 504 \$ 118,596

Payments to Fiscal Court:

Tangible Personal Property Tax 9,775

Delinquent Tax 2,302

Deed Transfer Tax 433 12,510

Payments to Other Districts:

Tangible Personal Property Tax 60,301

Delinquent Tax 15,052 75,353

Payments to Sheriff

2,271

Payments to County Attorney

3,778

Operating Disbursements and Capital Outlay:

Other Charges-

Credit Card Fees 248

Refunds 51

Miscellaneous 242 541

Total Disbursements

\$ 213,049

Net Receipts

40,492

Less: Statutory Maximum *

9,473

Excess Fees Due County for 2015

31,019

Payments to Fiscal Court - Various Dates

31,019

Balance Due Fiscal Court at Completion of Audit

\$ 0

* The county clerk's statutory maximum salary was underpaid by \$2,058 due to a timing issue. However, this underpayment will be corrected with first payroll in January 2016.

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

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENT

December 31, 2015

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 county clerk as determined by the audit. KRS 64.152 requires the county clerk to settle excess fees with the fiscal court by March 15 each year.

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), from November 14, 2015 through December 31, 2015 that may be included in the excess fees calculation:

- Interest receivable
- Collection on accounts due from others for 2015 services
- Reimbursements for 2015 activities
- Payments due other governmental entities for December tax and fee collections and payroll
- Payments due vendors for goods or services provided in 2015

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 county clerk'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).

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENT
December 31, 2015
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

D. Fee Pooling

The former Breathitt County Clerk's office was required by the fiscal court to participate in a fee pooling system. Fee officials who are required to participate in fee pooling deposit all funds collected into their official operating account. The former county clerk is responsible for paying all amounts collected for others and applicable refunds to customers. 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.

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

The county official and employees have elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 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 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 the plan. The county's contribution rate for nonhazardous employees was 17.67 percent for the first six months and 17.06 percent for the last six months.

In accordance with Senate Bill 2, signed by the Governor on April 4, 2014, 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. Members contribute five percent (nonhazardous) of their annual creditable compensation and 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 (nonhazardous) 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.

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:

BREATHITT COUNTY
 NOTES TO FINANCIAL STATEMENT
 December 31, 2015
 (Continued)

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

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%

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.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report. 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 former Breathitt County Clerk 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 former county clerk 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 county clerk's deposits may not be returned. The former Breathitt County Clerk did not have a deposit policy for custodial credit risk but rather followed the requirements of KRS 66.480(1)(d) and KRS 41.240. As of December 31, 2015, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

Note 4. Lease Agreement

On April 1, 2014, the Breathitt County Clerk's office committed to a lease agreement for a software license and service agreement. The lease requires a monthly payment of \$475 for 60 months to be completed on March 31, 2019. Under the fee pooling system, the fiscal court makes the payments on this lease.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENT
December 31, 2015
(Continued)

Note 5. On Behalf Payments

The former Breathitt County Clerk's office was required by the fiscal court to participate in a fee pooling system. Since the former Breathitt County Clerk is fee pooling, the Breathitt County Fiscal Court paid the former Breathitt County Clerk's statutory maximum as reflected on the former Breathitt County Clerk's financial statement. For the year ended December 31, 2015, the Breathitt County Fiscal Court's contributions recognized by the former Breathitt County Clerk included the amounts that were based on the statutory maximum as required by KRS 64.5275. The former Breathitt County Clerk recognized receipts from fiscal court and disbursements for statutory maximum of \$9,473 for the period November 14, 2015 through December 31, 2015.

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



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

The Honorable J. L. Smith, Breathitt County Judge/Executive
The Honorable Mary Lois Stevens, Former Breathitt County Clerk
The Honorable Mary Rebecca Curtis, Breathitt County Clerk
Members of the Breathitt 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 former Breathitt County Clerk for the period November 14, 2015 through December 31, 2015, and the related notes to the financial statement and have issued our report thereon dated March 7, 2017. The former Breathitt County Clerk'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 former Breathitt County Clerk'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 former Breathitt County Clerk's internal control. Accordingly, we do not express an opinion on the effectiveness of the former Breathitt County Clerk's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting 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 comment and recommendation, we identified a certain deficiency in internal control that we consider to be a material weakness.

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 deficiency described in the accompanying comment and recommendation as item 2015-001 to be a material weakness.



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 former Breathitt County Clerk'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*.

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

March 7, 2017

COMMENT AND RECOMMENDATION

BREATHITT COUNTY
MARY LOIS STEVENS, FORMER COUNTY CLERK
COMMENT AND RECOMMENDATION

For The Period November 14, 2015 Through December 31, 2015

INTERNAL CONTROL - MATERIAL WEAKNESS:

2015-001 The Former County Clerk's Office Lacked Adequate Segregation Of Duties Over Receipts

The former county clerk's office lacked adequate segregation of duties over receipts. The employee who collected cash receipts also prepared the daily checkout sheets, the deposit slips, and the bank reconciliations. The same employee also took the deposit to the bank. Good internal controls dictate that different individuals should perform these duties. Numerous adjustments and reclassifications (three of which were material) were necessary to make the former clerk's financial information complete and accurate. The lack of segregation of duties allowed material errors to occur and go undetected. As a result, inaccurate financial reporting to external agencies occurred. Likewise, lack of segregation of duties could have resulted in misappropriation of assets as well. If these duties could not be segregated, the former county clerk should have implemented compensating controls. The former county clerk could have reviewed the deposit and compared it to the daily checkout sheet and receipts ledger as a compensating control. This procedure could have been documented by the former county clerk initialing the checkout sheet, receipts ledger, deposit slip, and the bank reconciliation.

Former County Clerk's Response: No response.

