



Auditor of Public Accounts
Mike Harmon

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Contact: **Michael Goins**
Michael.Goins@ky.gov
502.564.5841
502.209.2867

Harmon Releases Audit of Franklin County Sheriff's Tax Settlement

FRANKFORT, Ky. – State Auditor Mike Harmon today released the audit of the sheriff's settlement – 2016 taxes for Franklin County Sheriff Pat Melton. State law requires the auditor to annually audit the accounts of each county sheriff. In compliance with this law, the auditor issues two sheriff's reports each year: one reporting on the audit of the sheriff's tax account, and the other reporting on the audit of the fee account used to operate the office.

Auditing standards require the auditor's letter to communicate whether the sheriff's settlement presents fairly the taxes charged, credited and paid in accordance with accounting principles generally accepted in the United States of America. The sheriff's settlement is prepared on the regulatory basis, which is described in the auditor's opinion letter. Regulatory basis reporting for the sheriff's settlement is an acceptable reporting methodology, and this reporting methodology is followed for all 120 sheriff settlements in Kentucky.

The sheriff's financial statement fairly presents the taxes charged, credited and paid for the period April 16, 2016 through April 17, 2017 in conformity with the regulatory basis of accounting.

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 internal control over financial operations and reporting.

The audit contains the following comments:

The Franklin County Sheriff lacks adequate segregation of duties over the daily accounting and reporting functions: The sheriff lacks adequate segregation of duties over accounting and reporting functions of the sheriff's office. The bookkeeper assists in collecting tax bill payments, posts to the financial software program, pulls monthly reports for all districts, prepares checks for districts, and prepares the monthly bank reconciliation. The auditor noted that the sheriff had a

signature stamp that was utilized by the bookkeeper in his absence with his approval. The signature stamp was utilized on checks and monthly tax reports.

Internal controls were not in place to ensure duties were adequately segregated and sufficient compensating controls were not implemented.

The lack of adequate segregation of duties increases the risk that undetected errors could occur. Utilizing a signature stamp circumvents the controls over disbursements and report review because the same person preparing the check or report would be the same person approving the transaction.

When faced with a limited number of staff, strong compensating controls should be in place to offset the lack of adequate segregation of duties. Proper segregation of duties, or the implementation of compensating controls, is essential for providing protection from asset misappropriation and inaccurate financial reporting, while also protecting employees in the normal course of performing their responsibilities.

We recommend the sheriff evaluate the controls that are in place and consider the following controls to adequately protect against misappropriation of assets and inaccurate financial reporting:

- Authorize someone other than the person performing closeout procedures, preparing the deposit, and performing the bank reconciliation to agree daily tax collection totals to the deposit slip. This person should also ensure the cash/checks per report agree to deposit slip, then document the review by initialing the bank deposit.
- Authorize someone other than the check preparer to review supporting documentation and sign checks in the sheriff's absence.
- The sheriff or a designated employee should reconcile the daily work to the ledger and monthly reports to ensure accuracy, then document the review by initialing or signing reports.

Sheriff's Response: We have compensating controls in place and have taken steps to correct any issues found in the findings. Deposits are initialed by person preparing the deposit and by the person taking deposit to the bank. An office employee [name redacted] prepares the daily balancing and enters the daily deposits. These deposits are checked and initialed by the Office Manager. The mail is brought to us by the County Runner. The mail is then opened by a part time staff member. The Sheriff's signature stamp will not be used in the future.

Auditor's Reply: The auditor was unable to confirm compensating controls as they were not properly documented.

The Franklin County Sheriff did not ensure tax collections were deposited daily: The sheriff is not depositing tax collections into the bank daily as required by KRS 68.210. Tax collection deposits were found to be deposited in the bank anywhere from one to five business days after collection date with multiple daily collections deposited in the same day:

- Collections on 12/12, 12/14, and 12/15 were all deposited at the bank on 12/16;
- Collections on 03/03 was not deposited at bank until 03/06;

- Collections on 03/07, 03/08, and 03/09 were all deposited at the bank on 03/10;
- Collections on 03/10, 03/13, and 03/14 were all deposited at the bank on 03/15;
- Collections on 03/17, 03/20, and 03/21 were all deposited at the bank on 03/23;
- Collections on 03/23 and 03/24 were all deposited at the bank on 03/27;
- Collections on 03/27, 03/28, and 03/29 were all deposited at the bank on 03/30; and
- Collections on 03/30 and 03/31 were all deposited at the bank on 04/04.

The sheriff did not have internal controls in place to ensure daily collections were deposited intact daily.

The practice of making daily deposits reduces the risk of misappropriation of cash, which is the asset most susceptible to theft. Delaying processing of deposits can be used to conceal the theft of tax payments to the sheriff's office.

The Department for Local Government (DLG) was given authority by KRS 68.210 to prescribe a uniform system of accounts. The minimum requirements for handling public funds as stated in the *County Budget Preparation and State Local Finance Officer Policy Manual* requires daily deposits intact into a federally insured banking institution.

We recommend the sheriff implement controls to ensure that tax collections are deposited intact daily.

Sheriff's Response: We have added existing staff to comply with this request. The Sheriff, Major and Lieutenant are now making the deposits.

The Franklin County Sheriff did not present his 2016 tax settlement to the fiscal court: The Franklin County Sheriff's tax settlement was not presented to the fiscal court as required by KRS 134.192(5). The sheriff's settlement was not presented until September 21, 2017.

According to the sheriff, the sheriff's computer system maintaining the tax collection program malfunctioned in April 2017 and the sheriff's settlement was not able to be prepared until the data was reentered into the accounting software. The sheriff had a backup plan in place; however, it did not function properly and the sheriff lost three years of data.

Failure to comply with these regulations result in a lack of availability of financial records to approving authorities. The sheriff cannot collect taxes for the following year until the settlement has been submitted to the fiscal court and a quietus obtained from the Department of Revenue. Information relative to the financial reporting of the 2016 tax year was lost and had to be recreated. Furthermore, taxing districts and other governmental agencies were deprived of funds for significant time periods.

KRS 134.192(5) states, "[t]he report of the state and local settlement shall be filed in the county clerk's office and approved by the governing body of the county no later than September 1 of each year. The settlement shall show the amount of ad valorem tax collected for the county, the school district, and all taxing districts, and an itemized statement of the money disbursed to or on behalf of the county, the school district, and all taxing districts."

Ensuring good internal controls are maintained over backing up computers retaining pertinent financial data will lessen the risk of losing important information, ensure deadlines are met for reporting purposes, and reduce inaccuracies from recreating financial data that was lost.

We recommend the sheriff submit the tax settlement to the fiscal court as required by KRS 134.192(5). Furthermore, we recommend the sheriff ensure that the computer maintaining financial data is properly backed up to one or more sources to prevent this from happening again.

Sheriff's Response: The Sheriff's Office was not able to present the 2016 Tax Settlement to the Fiscal Court by September 21, 2016. The computer used by the office manager crashed which required records to be reconstructed. Backup hard copies were used to reconstruct, all information was restored. The backup system that we had did not work. We now have a separate back up system for the accounting computer.

The Franklin County Sheriff lacked adequate internal controls over the daily receipt and deposit process: The following deficiencies were identified related to the preparation of the daily deposits that suggest deposits were not made intact:

- Four instances in which cash and checks from the tax processing software did not correspond to cash and checks from the bank deposit slip for the daily deposit;
- No documentation on the software report that cash and checks counted from cash drawer by a deputy agreed to report;
- No indication that a review of the deposit was performed;
- Two franchise bills paid during November 2016 did not actually show up in the tax system until it was reentered in March 2017. The checks for these two bills were processed with the November deposit;
- Tax Software does not have capability to track the employee who took each tax bill collection;
- Various employees work out of the same drawer with the same log-in credentials. No control is in place to track which employee processes a tax bill payment; and
- Deposits were not made daily – See finding 2016-002.

Because of a lack of control and understanding of state statutes, required daily checkout procedures were not performed.

By not performing required daily checkout procedures, tax receipts were left vulnerable to misappropriation and loss. Additionally, the sheriff is not in compliance with the Department for Local Government's (DLG) accounting requirements. Failure to implement controls over the receipt process increases the risk of undetected errors and misappropriation of assets.

Effective internal control procedures over daily deposits require that deposits be made intact and contain all cash and checks received for payments. DLG was given the authority by KRS 68.210 to prescribe a uniform system of accounts. The minimum requirements for handling public funds as stated in the *County Budget Preparation and State Local Finance Office Policy Manual* requires

daily deposits intact into a federally insured banking institution and utilization of daily cash checkout sheets.

We recommend the sheriff strengthen internal controls over daily checkout procedures to ensure checkout sheets are prepared and agree to manual and computerized records. Deposits should be made intact daily. Furthermore, we recommend the sheriff work with the software programmer to see if an audit trail could be added.

Sheriff's Response: We have compensating controls in place and have taken steps to correct any issues found in the findings. Deposits are initialed by person preparing the deposit and by the person taking deposit to the bank. [Name redacted] prepares the daily balancing and enters the daily deposits. These deposits are checked and initialed by the Office Manager. We have added existing staff to make the daily deposits which are The Sheriff, Major and Lieutenant.

Auditor's Reply: The auditor was unable to confirm compensating controls as they were not properly documented.

The sheriff's responsibilities include collecting property taxes, providing law enforcement and performing services for the county fiscal court and courts of justice. The sheriff's office is funded through statutory commissions and fees collected in conjunction with these duties.

The audit report, which includes an additional letter in response from Sheriff Melton, can be found on the [auditor's website](#).

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