



Auditor of Public Accounts  
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**FOR IMMEDIATE RELEASE**

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**Harmon Releases Audit of Graves County Fiscal Court**

**FRANKFORT, Ky.** – State Auditor Mike Harmon has released the audit of the financial statement of the Graves County Fiscal Court for the fiscal year ended June 30, 2017. 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 Graves 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 internal control over financial operations and reporting.

The audit contains the following comments:

**The Graves County Fiscal Court’s fourth quarter financial statement was materially misstated:** The general fund and jail fund both consist of several individual bank accounts. Each individual bank account’s activity was posted to the receipts and disbursements ledgers in order to reconcile the bank statements. Inter-account transfers within the funds were accounted for twice as a revenue and twice as a disbursement on the fourth quarter financial statement. Additionally, the treasurer eliminated the jail escrow fund when she combined the jail escrow fund into the jail fund. The treasurer failed to book combining entries into the accounting system to eliminate the jail escrow fund.

The fourth quarter financial statement was materially misstated due to the improper accounting for inter-account transfers and fund eliminations/combination. Due to the nature of the software used, each transaction must be recorded in order to reconcile the account. The treasurer failed to make the necessary adjustments to eliminate the doubling up effect of the inter-account transfers. Additionally, the treasurer was unaware of the accounting requirements for the elimination and combination of funds.

Strong internal controls over financial reporting are vital in ensuring the county's financial reports accurately reflect the financial activity of the county.

We recommend the county implement strong internal controls, such as a thorough review of the receipts and disbursements ledgers and bank reconciliations by someone independent of the accounting function and make adjusting entries as needed. Additionally, the fiscal court should adopt policies and procedures to give guidance to the treasurer for the elimination or combination of individual funds.

*County Judge/Executive's Response: The County Treasurer and County Finance Officer will thoroughly review receipts and disbursement ledgers and make necessary adjustments so the Quarterly Financial Statement will not be misstated due to the Inter Account Transfers.*

**Material weaknesses and noncompliances exist over disbursements:** This is a repeat finding and was included in the prior year audit report as Finding 2016-001. Material weaknesses and noncompliances exist over the disbursements of Graves County.

The following exceptions were noted during testing:

- Sixty-nine disbursements totaling \$67,848 did not have a properly executed purchase order as required by the county's administrative code.
- Invoices were not stamped when received, therefore the accuracy of reported encumbrances could not be determined.
- A total of \$228,798 of disbursements related to the Agency for Substance Abuse Prevention (ASAP) grant were not properly reviewed by the fiscal court prior to payment.
- Two invoices totaling \$793 were not paid within 30 working days as required by KRS 65.140.
- One disbursement for \$812 was not presented to fiscal court prior to payment.

The exceptions noted above are the result of oversight errors as well as management's lack of understanding of a properly executed purchase order system. Also, management's lack of understanding of the ASAP grant led to improper oversight of grant disbursements because management believed the ASAP grant to be a pass-through grant in which ASAP grant disbursements were not true obligations of the fiscal court.

Because weak internal controls over disbursements exist, the above exceptions occurred. The county also assumes a higher risk of misstatement and fraud.

Strong internal controls over disbursements are essential in ensuring disbursements are properly approved and recorded. Also, KRS 65.140(2) states, “[u]nless the purchaser and vendor otherwise contract, all bills for goods or services shall be paid within thirty (30) working days of receipt of a vendor’s invoice except when payment is delayed because the purchaser has made a written disapproval of improper performances or improper invoicing by the vendor or by the vendor’s subcontractor.” Additionally, the Commonwealth of Kentucky Office of Drug Control Policy Justice & Public Safety Cabinet KY - Agency For Substance Abuse Policy Local Board Workbook states “[t]he fiscal agent [Graves County Fiscal Court], as the second party to the contract, should do whatever is appropriate to assure third party (the local board) compliance with the contract as to those activities regarding the coordination work and the semi-annual report to the state KY-ASAP office. As to expenditures of funds, the fiscal agent has complete authority to monitor expenditures to insure that they are in compliance with the approved budget and to say “no” to unapproved expenditures.”

We recommend the Graves County Fiscal Court strengthen internal controls over disbursements by ensuring that properly executed purchase orders are issued for all disbursements. We also recommend the fiscal court implement controls over ASAP grant disbursements. We further recommend the fiscal court strengthen internal controls over disbursements by stamping invoices upon receipt and ensuring that all disbursements are presented to fiscal court prior to payment. We also recommend the fiscal court comply with KRS 65.140 by paying all invoices within 30 working days of receipt.

*County Judge/Executive’s Response: In February 2017, we hired two part time employees to help with the execution of Purchase Orders, among other duties. We believe this has helped with complying regarding disbursements. Also, it is common practice for all invoices to be paid within 30 working days per KRS 65.140.*

*The Agency for Substance Abuse Prevention (ASAP) has a local board who approves expenditures and oversees operations of grant monies. The only disbursements made are what the board approves. Therefore, we believe it should not be the responsibility of the Graves County Fiscal Court for approval.*

Auditor’s Reply: As stated above, the fiscal agent [Graves County Fiscal Court] should monitor disbursements for compliance and say no to unapproved expenditures.

**The Graves County Fiscal Court lacks adequate segregation of duties over cash and receipts:** The administrative assistant opens all incoming mail receipts, receives cash from walk-in customers, prepares daily deposits, and makes the daily deposit. The county treasurer posts to the ledgers and does the monthly reconciliations.

Due to the lack of internal controls in place, the duties associated with the custody, recordkeeping, and authorization of cash and receipts are not segregated. A lack of segregation of duties or strong oversight increases the risk of undetected errors or fraud.

Segregation of duties or the implementation of compensating controls, when limited by the number of staff, is essential for providing protection against the misappropriation of assets and

inaccurate financial reporting. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

To adequately protect against the misappropriation of assets and financial reporting, we recommend that the fiscal court segregate the duties noted above by implementing that an individual independent of the cash receipts process review a daily checkout sheet documenting all receipts for the day and comparing it to the daily deposit slip. We further recommend that an individual independent of the cash receipts process review postings to the ledgers and monthly bank reconciliations. Documentation, such as the reviewer's initials or signature, should be provided on those items that are reviewed.

*County Judge/Executive's Response: We will have all daily receipts and deposits reviewed and initialed, to provide a better segregation of duties.*

**Material weaknesses and noncompliances exist over the payroll process:** The Graves County Fiscal Court has material weaknesses and noncompliances regarding payroll and timekeeping. The following findings were noted with Graves County's payroll:

- A salary schedule was approved by the fiscal court, however it did not specify the compensation for each employee required by KRS 64.530.
- Timesheets required by KRS 337.320(1)(b) were not turned in or approved by the appropriate supervisor. Of individuals selected for testing, five salaried employee's timesheets were not turned in and three employee's timesheets were not signed by a supervisor documenting approval.
- Leave balances are not always updated and maintained for salaried employees.
- Overtime hours were not properly attributed to a part-time employee as required by KRS 337.285. The overtime hours were being held until the next pay period.
- Of the individuals selected for testing, one salaried employee's FICA calculation was incorrect due to a 401-K deduction.
- Personnel files did not include all employee's pay rate and salary information.
- One employee did not have money withheld from their paycheck for their flexible spending account.

The findings listed above are due to the lack of effective internal controls. Internal controls over the payroll and timekeeping process are designed effectively, but the controls are not functioning properly. Thus, the aforementioned findings occurred.

Strong internal controls over payroll and timekeeping are vital in ensuring that payroll amounts are calculated and accounted for properly. Strong internal controls are also important in safeguarding the county's assets and those given the responsibility of accounting for them, as well as helping make certain the county is in compliance with state statutes. KRS 64.530(1) requires that, "the fiscal court of each county shall fix the reasonable compensation of every county officer and employee[.]" Also, KRS 337.320(1) requires that, "[e]very employer shall keep a record of: (a) The amount paid each pay period to each employee; (b) The hours worked each day and each week by each employee; and (c) Such other information as the commissioner requires." KRS 337.285(1) states, "[n]o employer shall employ any of his employees for a work

week longer than forty (40) hours, unless such employee receives compensation for his employment in excess of forty (40) hours in a work week at a rate of not less than one and one-half (1-1/2) times the hourly wage rate at which he is employed.”

We make the following recommendations to address these findings:

- The fiscal court should set and approve salaries of county officers and employees.
- Timesheets should be maintained by all non-exempt employees as required by KRS 337.320(1)(b). Said timesheets should document the hours worked each day and each week by each employee.
- All timesheets should be signed by the corresponding employee and his or her supervisor.
- Leave balances should be maintained for all employees.
- Overtime should be awarded to all employees based on hours actually worked, including any applicable overtime in accordance with KRS 337.285(1). No hours shall be held until the next pay period.
- An individual independent of the payroll process should review payroll transactions to verify that all amounts have been calculated properly and that they are properly supported.
- Personnel files should be complete and kept up to date with pay rate/salary changes, position changes, and authorized withholdings, including withholdings for an employee’s flexible spending account.

In addition to the above specific recommendations, we recommend that the internal controls designed over the payroll and timekeeping process be implemented with all proper documentation to show all steps and reviews have been completed in the payroll and timekeeping process. By implementing the above recommendations, the county can strengthen its internal control system over payroll and timekeeping and reduce the risks of noncompliance and payroll errors. Such procedures will also protect the county against potential payroll disputes.

*County Judge/Executive’s Response: The Fiscal Court will set and approve salaries of county officers and employee by Job Title.*

*On July 1, 2017 the Fiscal Court began using a time tracking software, which has been very beneficial for the County. All time sheets are required to be signed by Employee and Supervisor.*

**The Graves County Fiscal Court failed to properly account for Alcohol Regulatory Licensing fees:** The Graves County Fiscal Court’s Alcohol Regulatory License (ARL) fees are not deposited into any fund of the fiscal court. The Graves County Sheriff has been collecting the ARL fees and depositing them into his fee (operating) account. The ARL fee is not accounted for separately by the sheriff and is comingled with the other fees that the sheriff collects. There is no documentation as to what the ARL fees were used for. Excess fees of the sheriff (if any) are turned over to the county treasurer after the end of the calendar year. The sheriff remitted \$20,650 of excess fees to the fiscal court February 8, 2017 for calendar year 2016, but the comingling made it impossible to tell how much, if any, of the excess funds are

attributable to ARL fees. As a result, the fiscal court did not deposit any of the excess fees into an ARL fee fund or account.

Due to the lack of internal controls over the collection and handling of the ARL fees, and a lack of knowledge of the requirement of KRS 243.075, which governs ARL fees, the Graves County Fiscal Court did not ensure that ARL fees were used for purposes allowed by the statute. The failure to properly segregate the collections made it impossible to trace sheriff office expenditures to the source of funding, and also impaired the fiscal court's ability to monitor the level and types of expenditures.

Strong internal controls over ARL fees are essential to ensure that the ARL fees are being properly handled by tracking receipts and disbursements according to legal requirements. KRS 243.075 authorizes a qualified city or a county containing a qualified city that is wet through a local option election to impose a regulatory license fee upon the gross receipts of the sale of alcoholic beverages of each establishment located in the city or county licensed to alcoholic beverages.

Also, KRS 243.075(4) states, “[a]fter July 15, 2014, any fee authorized under subsections (1) and (2) of this section shall be established at a rate that will generate revenue that does not exceed the total of the reasonable expenses actually incurred by the city or county in the immediately previous fiscal year for the additional cost, as demonstrated by reasonable evidence, of: (a) Policing; (b) Regulation; and (c) Administration; as a result of the sale of alcoholic beverages within the city or county.”

Additionally, KRS 243.075 (6) states that, “[t]he revenue received from the imposition of the regulatory license fee authorized under subsections (1) and (2) of this section shall be: (a) Deposited into a segregated fund of the city or county; (b) Spent only in accordance with the requirements of subsections (1) and (2) of this section; and (c) Audited under an annual audit performed pursuant to KRS 43.070, 64.810, and 91A.040.” Section 7 of KRS 243.075 lists the ramifications if a city or county fails to properly handle and account for the ARL fees.

We recommend the Graves County Fiscal Court comply with KRS 243.075 by having the treasurer collect the ARL fees determined in accordance with KRS 243.075(4) and depositing those ARL fees into a separate fund of the county in order to track disbursements appropriately. Additionally the fiscal court should implement internal controls to oversee the determination, collection and disbursement of the ARL fees to ensure compliance with the provisions of KRS 243.075.

*County Judge/Executive's Response: On August 21, 2018 there was a separate bank account open to properly account for the Alcohol Regulatory Licensing Fees.*

**The Graves County Fiscal Court overspent the budget in certain general, road, and LGEA fund categories:** The Graves County Fiscal Court overspent the budget in two general fund categories by \$1,158, one road fund category by \$114,536, which was borrowed money for the purchase of equipment, and one Local Government Economic Assistance (LGEA) fund category by \$81.

Budget amendments were obtained within the fiscal year, but the two general fund categories and the LGEA category were overlooked by the fiscal court, because of their small amounts. Since the county didn't actually receive the funds associated with the borrowed money, this transaction was never budgeted. Therefore, by not having the proper budget amendments, the county was not in compliance with KRS 68.300 and KRS 68.280.

KRS 68.300 states, "[a]ny appropriation made or claim allowed by the fiscal court in excess of any budget fund, and any warrant or contract not within budget appropriation, shall be void." KRS 68.280 states "[t]he fiscal court may make provision for the expenditure of receipts unanticipated in the original budget by preparing an amendment to the budget, showing the source and amount of the unanticipated receipts and specifying the budget funds that are to be increased thereby."

We recommend the county comply with KRS 68.300 by budgeting all county transactions, including those handled by a third-party lender, monitoring the budget throughout the year, and obtain budget amendments when necessary.

*County Judge/Executive's Response: We will comply with KRS 68.300 by budgeting all county transactions, including those handled by third-party lenders.*

**The Graves County Jail lacks adequate segregation of duties over commissary operations:**

The Graves County Jail lacks adequate segregation of duties. The bookkeeper is required to perform multiple tasks: daily checkout procedures, deposit preparation, authorization of invoices, check preparation, check signing, bookkeeping, and bank reconciliations. This lack of segregation of duties is caused by the diversity of operations with a limited number of bookkeeping staff.

A lack of segregation of duties or strong oversight increases the risk of undetected errors or fraud. Segregation of duties or the implementation of compensating controls, when limited by the number of staff, is essential for providing protection against the misappropriation of assets and inaccurate financial reporting. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

To adequately protect against the misappropriation of assets and financial reporting, we recommend that the jailer segregate the duties noted above by allowing different deputies to perform these functions. For those duties that cannot be segregated due to a limited number staff, strong management oversight by the jailer or designee can be a cost effective alternative. This oversight should include reviewing monthly bank reconciliations and ledgers and requiring dual signatures on checks. Documentation, such as the jailer's or a designee's initials or signature, should be provided on those items that are reviewed.

*County Jailer's Response: To protect against misappropriation of assets and financial reporting, the designee will review monthly reconciliation and ledgers. Documentation (designee's initial or signature) will be provided on the items that are reviewed.*

*We will have these items reviewed by the designee to provide a better segregation of duties, as recommend by the auditor.*

*We now have a designed put in place to correct this issue.*

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

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