

**REPORT OF THE AUDIT OF THE
LETCHER COUNTY
SHERIFF'S SETTLEMENT - 2018 OIL AND GAS TAXES**

**For The Period
January 7, 2019 Through July 15, 2019**



**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**

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MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
The Honorable Andy Beshear, Governor
Holly M. Johnson, Secretary
Finance and Administration Cabinet
The Honorable Terry Adams, Letcher County Judge/Executive
The Honorable Mickey Stines, Letcher County Sheriff
Members of the Letcher County Fiscal Court

Independent Auditor's Report

Report on the Financial Statement

We have audited the Letcher County Sheriff's Settlement - 2018 Oil & Gas Taxes for the period January 7, 2019 through July 15, 2019 - Regulatory Basis, 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 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 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 Sheriff's Tax Settlements*, 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.



To the People of Kentucky
The Honorable Andy Beshear, Governor
Holly M. Johnson, Secretary
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The Honorable Mickey Stines, Letcher County Sheriff
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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 Letcher County Sheriff on the basis of 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 oil and gas taxes charged, credited, and paid of the Letcher County Sheriff, for the period January 7, 2019 through July 15, 2019.

Opinion on Regulatory Basis of Accounting

In our opinion, the financial statement referred to above presents fairly, in all material respects, the oil and gas taxes charged, credited, and paid for the period January 7, 2019 through July 15, 2019 of the Letcher County Sheriff, 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 January 30, 2020, on our consideration of the Letcher County Sheriff'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 Letcher County Sheriff's internal control over financial reporting and compliance.

To the People of Kentucky
The Honorable Andy Beshear, Governor
Holly M. Johnson, Secretary
Finance and Administration Cabinet
The Honorable Terry Adams, Letcher County Judge/Executive
The Honorable Mickey Stines, Letcher County Sheriff
Members of the Letcher County Fiscal Court

Other Reporting Required by *Government Auditing Standards* (Continued)

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:

- 2018-001 The Letcher County Sheriff's Office Does Not Have Adequate Segregation Of Duties
- 2018-002 The Letcher County Sheriff Did Not Have A Written Agreement To Protect Deposits

Respectfully submitted,

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

Mike Harmon
Auditor of Public Accounts

January 30, 2020

LETCHER COUNTY
 MICKEY STINES, SHERIFF
SHERIFF'S SETTLEMENT - 2018 OIL AND GAS TAXES

For The Period January 7, 2019 Through July 15, 2019

	Special Taxing			
	County	Districts	School	State
<u>Charges</u>				
Oil and Gas Property Taxes	\$ 138,865	\$ 241,493	\$ 446,930	\$ 85,127
Limestone, Sand, and Gravel Reserves				873
Penalties	13	22	41	8
Gross Chargeable to Sheriff	138,878	241,515	446,971	86,008
<u>Credits</u>				
Exonerations	679	1,181	2,185	420
Discounts	2,674	4,648	8,614	1,655
Delinquent Oil & Gas Property Taxes	1,505	2,618	4,845	932
Total Credits	4,858	8,447	15,644	3,007
Taxes Collected	134,020	233,068	431,327	83,001
Less: Sheriff's Commissions*	5,696	9,905	16,544	3,528
Taxes Due Districts	128,324	223,163	414,783	79,473
Taxes Paid	128,324	223,163	414,783	79,473
Taxes Due Districts	\$ 0	\$ 0	\$ 0	\$ 0

* Commissions:

4.25% on	\$	450,089
4% on	\$	360,411
3% on	\$	70,916

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

LETCHER COUNTY
NOTES TO FINANCIAL STATEMENT

July 15, 2019

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. 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.

B. Basis of Accounting

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. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

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. Preparation of State Settlement

The Kentucky Department of Revenue conducts the settlement relating to taxes collected for the state under the provision of KRS 134.192(2)(a). This is reported as the "State Taxes" column on the financial statement.

Note 2. Deposits

The Letcher County Sheriff maintained deposits of public funds with depository institutions insured by the 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. These requirements were not met, because the sheriff did not have a written agreement with the bank.

LETCHER COUNTY
 NOTES TO FINANCIAL STATEMENT
 July 15, 2019
 (Continued)

Note 2. Deposits (Continued)

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 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. On July 15, 2019, the sheriff's bank balance was exposed to custodial credit risk as follows:

- Uncollateralized and Uninsured \$76,463

Note 3. Tax Collection Period

A. Oil and Gas Property Taxes

The oil and gas property tax assessments were levied as of January 1, 2018. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was January 7, 2019 through July 15, 2019.

B. Limestone, Sand, and Gravel Reserves

The limestone, sand, and gravel property tax assessments were levied as of January 1, 2018. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was January 7, 2019 through July 15, 2019. Limestone, sand, and gravel property taxes are included in oil and gas taxes for the county, special taxing, and school taxing districts.

Note 4. Interest Income

The Letcher County Sheriff earned \$99 as interest income on 2018 taxes. The sheriff was in substantial compliance with his statutory responsibilities.

Note 5. Sheriff's 10% Add-On Fee

The Letcher County Sheriff collected \$45 of 10% add-on fees allowed by KRS 134.119(7). This amount was used to operate the sheriff's office.

Note 6. Escrow Account

The sheriff deposited unrefundable payments in an interest-bearing account. The sheriff's escrowed beginning balance was \$6,423. The sheriff received \$2,083 and disbursed \$108 resulting in a total ending balance as of July 15, 2019 of \$8,398. The ending balance consists of: 2012-\$3,639, 2013-\$1,528, 2014-\$230, 2015-\$1,014, 2016-\$144, 2017-\$1,828 and interest of \$15.

KRS 393.090 states that if the funds have not been claimed after three years, they are presumed abandoned. Abandoned funds are required to be sent to the Kentucky State Treasurer pursuant to KRS 393.110 and its accompanying regulations.

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 Terry Adams, Letcher County Judge/Executive
The Honorable Mickey Stines, Letcher County Sheriff
Members of the Letcher 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 Letcher County Sheriff's Settlement - 2018 Oil & Gas Taxes for the period January 7, 2019 through July 15, 2019 - Regulatory Basis and the related notes to the financial statement and have issued our report thereon dated January 30, 2020. The Letcher 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 Letcher 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 Letcher County Sheriff's internal control. Accordingly, we do not express an opinion on the effectiveness of the Letcher County Sheriff'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 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 2018-001 and 2018-002 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 Letcher County Sheriff's financial statement is free from 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 an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Responses as item 2018-002.

Views of Responsible Official and Planned Corrective Action

The Letcher County Sheriff's views and planned corrective action for the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The Letcher County 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,



Mike Harmon
Auditor of Public Accounts

January 30, 2020

SCHEDULE OF FINDINGS AND RESPONSES

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LETCHER COUNTY
MICKEY STINES, SHERIFF
SCHEDULE OF FINDINGS AND RESPONSES

For The Period January 7, 2019 Through July 15, 2019

FINANCIAL STATEMENT FINDINGS:

2018-001 The Letcher County Sheriff's Office Does Not Have Adequate Segregation Of Duties

The sheriff's bookkeeper collects payments from customers, prepares receipts, prepares deposits, posts receipts to the receipts ledger, and reconciles the bank statements. The bookkeeper also prepares disbursement checks and monthly tax reports. There is not sufficient evidence available that would show that the sheriff or another employee periodically reviews deposits, ledgers, monthly reports, or the bank reconciliations to offset the risk caused by the lack of segregation of duties. According to the sheriff's office, this condition is a result of a limited budget, which restricted the number of employees the former sheriff could hire or delegate duties to.

A lack of oversight could have resulted in undetected misappropriation of assets and inaccurate financial reporting to external agencies such as Department of Revenue. The segregation of duties over various accounting functions such as preparing deposits, recording receipts and disbursements, and preparing monthly reports, or the implementation of compensating controls is essential for providing protection from asset misappropriation and inaccurate financial reporting. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

We recommend the sheriff ensure that accounting duties are properly segregated in the future. If this is not feasible, the sheriff should implement adequate compensating controls that would limit the severity of this deficiency in internal controls.

Sheriff's Response: Due to budget constraints this is not possible to attain for our office.

2018-002 The Letcher County Sheriff Did Not Have A Written Agreement To Protect Deposits

The Letcher County Sheriff maintained deposits of public funds with a local financial institution. Acting pursuant to KRS 68.210, the Commonwealth's state local finance officer has established a compilation of minimum accounting and financial reporting standards in the Department for Local Government's County Budget Preparation and State Local Finance Officer Policy Manual. Those standards call for daily deposits in a federally insured institution, the usage of an interest bearing account, and a perfected pledge of collateral to protect deposits in amounts greater than federal insurance limits. For a pledge of collateral to be properly perfected and legally binding, federal law (12 U.S.C.A. § 1823(e)) requires that the agreement be (a) in writing, (b) approved by and recorded in the minutes of the institution's board of directors or its loan committee, and (c) an official record of the depository institution. As of July 15, 2019, the public funds deposited by the sheriff that were in excess of the federal insurance limits were not protected by a properly perfected pledge of collateral, putting public funds in the amount of \$76,463 at risk. The sheriff was unaware this agreement needed to be obtained.

We recommend the sheriff work with the depository institution and obtain a written agreement to ensure that deposits are pledged in the future

Sheriff's Response: This has been corrected for the future audits.