



Auditor of Public Accounts
Mike Harmon

FOR IMMEDIATE RELEASE

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Harmon Releases Audit of Magoffin County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Magoffin 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 Magoffin 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 fiscal court did not maintain capital asset schedules in accordance with regulatory requirements: This is a repeat finding and was included in the prior year audit report as Finding 2016-001. The Department for Local Government (DLG) requires fiscal courts to track capital assets (i.e. land, buildings, equipment, vehicles, infrastructure, etc.) and maintain a listing of capital assets to be provided to auditors for inclusion in the audit report. This list should include all current year additions/purchases, retirements, disposals/sale of assets, etc. Any related documentation for capital asset additions, retirements, and disposals in the form of invoices, deeds, purchase orders, sales records, titles, liens, etc. should be maintained in a manner that facilitates easy access, retrieval, and verification of capital asset amounts recorded.

The fiscal court did not maintain a complete and accurate capital asset schedule for the fiscal year ending June 30, 2017. The fiscal court has historically not maintained a fixed asset register and has relied upon the auditor to update fixed asset information within the financial statement based upon information related to additions, retirements, and disposals provided by the fiscal court. As a result, the fiscal court is not in compliance with DLG requirements and fixed asset information in the financial statement may be misstated.

We recommend the fiscal court implement procedures to identify and track capital asset additions, retirements, and disposals in order for capital asset schedules to be complete and accurate. Additionally, we recommend the fiscal court perform physical inventories periodically to further ensure the accuracy and completeness of capital asset schedules.

County Judge/Executive's Response: Recommendation accepted and working to improve compliance.

The fiscal court's administrative code does not address commuting mileage or the personal use of a county vehicle: This is a repeat finding and was included in the prior year audit report as Finding 2016-002. Internal Revenue Service (IRS) Code Section 61(a) states that the commuting value of a vehicle owned or leased by a public entity represents taxable income to the employee. The fiscal court's administrative code should address the use of vehicles and other assets owned by the fiscal court.

Fiscal court employees' personal use (e.g. commuting mileage) of a vehicle, or other asset, owned by the fiscal court is not being reported as compensation to the employees.

The fiscal court's administrative code does not address the use of vehicles and other assets owned by the fiscal court; therefore, it is unclear as to whether personal use of the vehicles and other assets is authorized by the fiscal court.

Personal use of public resources is permitted if the fiscal court has approved such use and should be reported as compensation to employees. Historically, the fiscal court has not maintained the appropriate documentation or complied with IRS Code Section 61(a).

The fiscal court understands the recommendation, but as of June 30, 2017, has not been able to implement the recommendation.

We recommend the fiscal court establish internal controls over vehicles by implementing the following:

- Report personal use and commuting mileage for vehicles as compensation/employee benefit on W-2 wage and tax statements in accordance with IRS regulations. Several methods can be used to determine the vehicle use that is taxable income to the employees, including the cents-per-mile rule, the lease value rule, and the commuting rule.
- Every employee and every department that has vehicles should maintain vehicle logs. The logs should include, at a minimum, the date, destination, purpose, and mileage for all use of the vehicle.

- The fiscal court should amend the current administrative code to include a policy on the authorization and use of vehicles (and other assets) owned by the fiscal court. In addition, it should address the tax implications of using a vehicle for personal use or commuting travel.

County Judge/Executive's Response: No Fiscal Court offices use vehicles for personal matters.

Auditor's Reply: As noted in the finding, the county's administrative code does not address the personal use of county vehicles nor does it address the potential tax implications.

The fiscal court lacks adequate segregation of duties over payroll: This is a repeat finding and was included in the prior year audit report as Finding 2016-004. Segregation of duties is an essential element of sustainable risk management and internal controls. The principle of segregation of duties is based on shared responsibilities of a key process that disperses the critical functions of that process to more than one person or department. A strong internal control system does not allow one person to perform processing, documentation, and reporting functions.

We noted inadequate segregation of duties for payroll. The county treasurer is responsible for maintaining timesheets, entering payroll information into the computer system for processing, posting to the payroll ledgers, transferring funds to the revolving payroll account, administering health reimbursement and flex spending programs, preparing pay checks, preparing state and local withholding reports, and reconciling the payroll account. By delegating all these duties to the same individual, the risk of undetected fraud and errors increases.

According to the fiscal court, they have a small accounting/payroll department and segregation of duties has been challenging to achieve.

We recommend the fiscal court find ways to segregate key duties related to payroll or implement other controls to compensate for these weaknesses (for example, designating an individual to review the payroll ledgers, reconciliations, and reports, and requiring the individual to document their review by initialing the documents that were reviewed).

County Judge/Executive's Response: Changes were made after the FY2015 audit. The E.M. director reviews and signs the timesheets. The finance officer posts checks to the ledger and the secretary reviews and distributes the checks.

Auditor's Reply: The controls noted in the county's response do not sufficiently address the risk of inadequately segregated duties.

The fiscal court does not have adequate internal controls over gravel inventory: This is a repeat finding and was included in the prior year audit report as Finding 2016-005. The fiscal court does not have adequate internal controls over gravel purchased and stored at the road department. The fiscal court should have appropriate controls over gravel inventory in order to protect the fiscal court against theft of gravel inventory.

Review of the controls over gravel revealed the fiscal court maintains a log for gravel transported out to county roads; however, the log is not updated consistently. In addition, the log does not track

the gravel hauled to the Road Department from the rock quarry. During our procedures relating to expenditures, we noted gravel purchases for Fiscal Year 2017 were \$52,542.

The fiscal court's lack of internal controls has created an opportunity for misappropriation of the assets to occur and for undetected errors in the value of the gravel inventory.

The fiscal court understands the recommendation, but as of June 30, 2017, has not been able to implement the recommendation.

We recommend the fiscal court maintain a log that tracks the gravel being hauled to and from the Road Department. This would allow an estimate of the gravel on hand to be calculated and costed. The gravel inventory should be periodically assessed to determine if a shortage exists.

County Judge/Executive's Response: Gravel logs are kept including incoming and outgoing loads of gravel.

Auditor's Reply: As noted in the finding, the gravel logs are not updated consistently and do not track the gravel hauled to the Road Department from the rock quarry.

The fiscal court does not have adequate controls over notes receivable: This is a repeat finding and was included in the prior year audit report as Finding 2016-007. The fiscal court does not have proper oversight and controls over notes receivable. To ensure that the fiscal court's assets are properly safeguarded and the fiscal court has the appropriate remedies available for lack of payment of receivables, the fiscal court should ensure that internal controls and agreements related to receivables are properly maintained.

In August 2008, the fiscal court loaned the Magoffin County Water District \$20,000 for a water project. The water district has not made any payments to date and the entire amount is still outstanding.

In September 2011, the fiscal court loaned \$50,000 to the Magoffin County Water District, who then loaned the money to the Salyersville Waterworks for water projects. The fiscal court minutes indicate this was a loan, but it has not been repaid.

Failure to follow up on notes receivable, a lack of payment plans, and having notes receivable outstanding for significant time periods deprives the fiscal court of needed funds. The fiscal court understands the recommendation, but as of June 30, 2017, has not been able to implement the recommendation.

We recommend the fiscal court review the terms of all notes receivable to determine if the fiscal court will pursue collection and document those decisions in the fiscal court minutes.

County Judge/Executive's Response: The fiscal court directed the county attorney in the April 26, 2018 meeting to collect on the \$50,000 loan. Magoffin County Water District will collect the payments from Salyersville Waterworks to repay the county as stated in the fiscal court minutes.

The fiscal court does not have adequate oversight of monthly reconciliation processes: This is a repeat finding and was included in the prior year audit report as Finding 2016-008. The finance officer's appropriation ledger is not reconciled monthly with the county treasurer's information. The Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual* requires that the finance officer's appropriation ledger is reconciled monthly with the county treasurer's information. Historically, this reconciliation has not been performed. As a result, errors that would be identified by performing this reconciliation may remain undetected in the financial statements.

According to the fiscal court, they have a small accounting department and performing all required reconciliations on a timely basis has been challenging to achieve.

We recommend the county treasurer and finance officer's appropriation ledgers are reconciled monthly.

County Judge/Executive's Response: Reconciliations have been done on a monthly basis since August 2017. The Treasurer and Finance Office sign off on the bank reconciliation statement.

The fiscal court did not consistently utilize the purchase order system: This is a repeat finding and was included in the prior year audit report as Finding 2016-009. The fiscal court is not consistently utilizing the purchase order system in accordance with the Department for Local Government's (DLG) guidelines. Purchases for certain services, such as election expenses, pest control, landscaping and routine maintenance did not have purchase orders. Failure to maintain appropriate records for purchase orders could result in incorrect amounts being paid or not having adequate funds or sufficient budget appropriation available.

The DLG *County Budget Preparation and State Local Finance Officer Policy Manual* states, "purchases shall not be made prior to approval by the County Judge/Executive (or designee) or department head." The DLG guidelines require that the fiscal court issue purchase orders for all purchases.

According to the fiscal court, they have a small accounting department and preparing purchase orders for all purchases is challenging to achieve.

We recommend the fiscal court require purchase orders be obtained prior to items being ordered or services received to determine adequate funds and budget appropriations are available for the purchase. Purchase orders should be completely filled out at the time of issuance. Additionally, we recommend that the fiscal court properly utilize the purchase order system in order to comply with DLG requirements.

County Judge/Executive's Response: The Judge Executive approves all purchase orders prior to purchases or services in real time by utilizing the Ring Central App.

Auditor's Reply: The new control was operational for only a portion of the period under audit. The control was not in place long enough during the period to alleviate the significant deficiency in the purchase order system.

The fiscal court did not have adequate controls over credit card disbursements: The fiscal court is not consistently maintaining receipts for approved credit card transactions. During our testing of credit card disbursements, it was noted that the fiscal court did not maintain a proper receipt for four of the transactions tested. The Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual* requires that all expenditures are substantiated by a receipt. By failing to maintain adequate documentation, the fiscal court is increasing the risk of paying for goods or services that were not provided to the county or for items that are not allowable. According to the fiscal court, they have a small accounting department and maintaining receipts for all purchases is challenging to achieve. We recommend the county further develop internal control procedures to ensure that credit card transactions are properly supported.

County Judge/Executive's Response: Utilization of an app send receipts in real time with the Ring Central App.

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

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