



Auditor of Public Accounts
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FOR IMMEDIATE RELEASE

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Harmon Releases Audit of Martin County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Martin County Fiscal Court for the fiscal year ended June 30, 2018. 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 Martin 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.

Finding 3 of this report will be referred this matter to U.S. Department of Housing and Urban Development (HUD).

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 Martin County Fiscal Court’s overall design and operations of the control environment needs improvement: Internal controls over the accounting process did not operate as designed resulting in procedures not being followed and creating an overall weak control environment. These numerous weaknesses significantly increase the risk of fraud, misappropriation of funds, and the fiscal court’s ability to ensure that financial data is recorded, processed, and reported in accurate and reliable manner.

The items were noted during the audit that show the accounting process did not operate as designed due to poor internal controls and are discussed further in detail in the following findings:

- The Martin County Fiscal Court Did Not Adequately Identify Federal Grants
- The Martin County Fiscal Court Has \$58,000 of Questioned Cost Relating To HUD Funds
- The Martin County Fiscal Court Does Not Have Adequate Internal Controls Over Disbursements
- The Martin County Fiscal Court Does Not Have Adequate Internal Controls Over Receipts
- The Martin County Fiscal Court Did Not Approve Transfers
- The Martin County Fiscal Court Did Not Have A Policy To Address Reimbursements To The Coroner's Office For Transport
- The Martin County Fiscal Court Does Not Have An Accurate Capital Asset Schedule Or Insurance Listing

Management has a responsibility to implement internal controls that provide reasonable assurance regarding the reliability of financial reporting. Internal control is a management process for keeping an entity on course in achieving its business objectives. These controls should ensure resources are protected from waste, loss, and misuse and ensure reliable data is obtained, maintained, and fairly disclosed. Entities are required to establish controls to provide reasonable assurance that the recording, processing, and reporting of data is properly performed within the framework of financial management system.

We recommend the fiscal court implement internal controls over the financial accounting system that ensure an adequate internal control structure, that includes management oversight, provides reasonable assurance that assets are safeguarded and transactions are processed in accordance with applicable laws and regulations.

Former County Judge/Executive William Davis's Response: Previous administration.

The Martin County Fiscal Court did not adequately identify federal grants: The original Schedule of Expenditures of Federal Awards (SEFA) provided to auditors was materially incorrect and grants were not adequately identified. FEMA expenditures of \$102,503 and HUD expenditures of \$58,000 were not included on the original SEFA.

As stated in 2CFR 200.510(b) "the auditee must also prepare a schedule of expenditures of federal awards for the period covered by the auditee's financial statement which must include the total federal awards expended."

Failure to maintain an accurate SEFA with the required information such as the Catalog of Federal Domestic Assistance (CFDA) numbers could result in a failure to properly obtain a single audit in accordance with uniform guidance. This could endanger future federal awards per 2CFR 200.501(a), "a non-federal entity that expends \$750,000 or more during the non-federal entity's fiscal year in federal awards must have a single or program-specific audit conducted for that year in accordance with the provision of this part."

The auditee shall per 2CFR 200.510(b)(3) “provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number with the CFDA information is not available.”

We recommend the Martin County Fiscal Court implement internal controls to immediately recognize all federal awards and keep track of federal grant information including the identifying CFDA number. An employee should be assigned to track federal expenditures while maintaining an accurate SEFA.

Former County Judge/Executive William Davis’s Response: Previous administration.

The Martin County Fiscal Court has \$58,000 of questioned HUD funds: The sheriff was awarded a USDA grant to purchase cars. On June 7, 2017, the grant was awarded and needed to be executed. Per the fiscal court orders, the sheriff had his portion of the funding for these cars and the county needed to provide their portion. On June 29, 2017, the fiscal court ordered to temporarily transfer \$58,000 from the HUD fund to the federal grant fund to cover their portion. The county judge/executive said the amount would be enough to cover the cars and the money would be put back into the HUD fund. On July 12, 2017, the fiscal court wrote a check from the HUD fund to the federal grant fund in the amount of \$58,000.

The fiscal court had cash flow issues and decided to use restricted federal funds to operate the county.

The federal grant fund owes the HUD fund \$58,000 causing a deficit fund balance of \$54,696, due to the federal fund only having an ending balance cash balance of \$3,304, as of June 30, 2018.

Section 3 of the HUD program guidelines states these funds are to be spent on “replacing existing roofing material and sheathing, installation of permanent block foundation, doors and windows, exterior siding, insulation, replacement of damaged sheetrock, heating and cooling systems, replacement of existing plumbing and electrical system, installation of a potable drinking water supply and septic system, and renovations for handicapped accessibility.”

We recommend that the fiscal court not spend restricted funds to operate the county. In addition, we recommend the fiscal court immediately transfer these funds back to the HUD Fund. We will refer this matter to Department of Housing and Urban Development.

Former County Judge/Executive William Davis’s Response: Previous administration.

The Martin County Fiscal Court does not have adequate internal controls over disbursements: This is a repeat finding and was included in the prior year audit report as Finding 2017-003. The fiscal court’s controls over disbursements were not operating as intended. Based on items tested, disbursements were not properly authorized, supporting documentation was not maintained, and appropriate and proper procedures were not followed.

The deficiencies listed below were able to occur due to lack of monitoring of controls, which diminish the effectiveness of the controls put in place over disbursements by fiscal court. These

deficiencies could create errors in recording or allow for the possibility of misappropriation of assets.

As a result, the following exceptions were noted:

- The Martin County Fiscal Court did not follow Department for Local Government's (DLG) policies regarding prepayment of services. We noted that the fiscal court prepaid three months of cleaning services totaling \$10,500.
- Fifty eight disbursements totaling \$652,879 were not paid within 30 days.
- Eleven instances totaling \$66,996 were noted for insufficient supporting documentation for items purchased.
- Five transactions totaling \$22,755 that were prior year expenditures and not paid within 30 days.
- The county did not provide proper bid documentation for seven purchases that exceed the county's administrative code bid threshold of \$10,000. These purchases include \$33,200 of steel drilling for a FEMA project, \$10,856 of gravel, and \$19,588 of supplies.
- State grant fund line item for general government exceeded appropriations by \$95.
- Three jail invoices, totaling \$73,114, for April 2018, May 2018, and June 2018 inmate housing were not paid until August 6, 2019, which is 14 - 15 months late.
- The county issued purchase orders when they did not have the cash balance to cover. The county reported encumbrances for the general fund of \$139,052 and jail fund of \$81,267 at June 30, 2018, however the ending cash balance in these funds was only \$62,003 and \$10,694, respectively.

Proper internal controls over expenditures are important to ensure purchase orders are created with sufficient funds available, include proper supporting documentation, and are paid in a timely manner. KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. Per the DLG *County Budget Preparation and State Local Finance Officer Policy Manual*, "purchases shall not be made prior to approval by the County Judge/Executive (or designee) or department head."

In addition, according to the fiscal court's administrative code, "all purchases of items of like or similar nature in excess of \$10,000 in a fiscal year shall be advertised for bids, except otherwise provided in this administrative code. Items normally supplied as a unit shall not be artificially divided for the purpose of avoiding the competitive bidding procedure of this administrative code." Furthermore, KRS 65.140 requires invoices to be paid within 30 days of being received.

We recommend fiscal court implement proper internal controls over expenditures and ensure they are operating effectively.

Former County Judge/Executive William Davis's Response: Previous administration.

The Martin County Fiscal Court did not have adequate internal controls over receipts: The Martin County Treasurer prepared and deposited receipts, posted receipts to the accounting system, prepared monthly reports for fiscal court and quarterly reports for the Department for

Local Government (DLG), made cash transfers between funds and bank accounts, and performed bank reconciliations. There was no review by another person to ensure daily deposits agree to the receipts ledger.

The lack of adequate segregation of duties and too much control by one individual could result in the undetected misappropriation of assets and errors that could go unnoticed, and inaccurate financial reporting to occur.

Good internal controls dictate adequate segregation of duties to prevent the same person from having complete control in the receiving, recording, and reporting of funds. A strong internal control structure includes adequate segregation of duties or strong compensating controls to offset the risk caused by the lack of segregation of duties. Without proper segregation or strong compensating controls, the county cannot ensure all receipts are deposited and all bank activity is appropriately documented in the accounting system.

We recommend the fiscal court strengthen internal controls by segregating the duties involved in receiving, recording, reconciling, and reporting receipts. If segregation is not possible, we recommend compensating controls, such as a receipt listing prepared by another person to compare to deposit tickets and ledger posting and documentation of oversight and review by a second person.

Former County Judge/Executive William Davis's Response: Previous administration.

The Martin County Fiscal Court did not properly approve transfers: Fund transfers in the amount of \$126,600 did not have prior approval from the fiscal court before being made. However, transfers were later approved by the court in total.

During the review of the quarterly financial statement, we noted that a transfer was made resulting in the final budget having a negative balance. This caused a claim to be in excess of that line item budget. By the treasurer not getting prior approval, the fiscal court lost its ability to have proper management oversight of the county's limited financial resources and the practice could cause funds to be misappropriated or misused without the fiscal court's knowledge.

As stated in the *County Budget Preparation and State and Local Finance Officer Policy Manual*, "all transfers require a fiscal court order." In addition, 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 the budget appropriation, shall be void."

We recommend all transfers be approved by the fiscal court prior to the treasurer executing them. In addition, we recommend that the fiscal court implement procedures to ensure appropriations or claims are made within the budget appropriations.

Former County Judge/Executive William Davis's Response: Previous administration.

The Martin County Fiscal Court did not have a policy to address reimbursements to the coroner's office for transports: The coroner bills the fiscal court \$300 for reimbursement of expenses to include payments for the transportation of bodies to the chief medical examiner's office in Frankfort. These flat fee transports are performed by either the coroner or one of his deputies and whoever performs the transport receives the \$300. All other county employees are reimbursed for actual expenses per the county's administrative code. These \$300 lump sum reimbursements totaling \$1,800 are not included on the employees' W-2s. The fiscal court did not follow their approved expense reimbursement policy.

By not following the county's administrative code which states "(1) Officials and employees of the Court may be reimbursed for personal expenses incurred while performing their duties as an employee of the Court. Personal expenses shall include food, lodging and travel. (3) Receipts shall be required for hotel bills, airline tickets, and automobile expense where travel is by court-owned vehicle. The use of court owned vehicles is encouraged while on court business. Employees shall be reimbursed \$4.00 for breakfast, \$5.00 for lunch, and \$12.00 for dinner without a receipt. Request for reimbursements in excess of these amounts shall be accompanied by a receipt." The coroner and his deputies are receiving lump sum payments as a fee for services provided, instead of a reimbursement of actual expenses for the coroner's office. Also since the reimbursements are for a flat rate and not actual expenses, the amounts are taxable; however, they were not included on their W-2's.

KRS 64.410(2) states, in part, "[n]o officer shall demand or receive any fee for his services:...(b) Any fee for services rendered when the law has not fixed compensation therefor[.]" Furthermore, KRS 64.530(4) allows the fiscal court to provide a salary for county officers and their deputies and assistants to be fixed no later than the first Monday in May in the year the officer was elected. The elected officer's compensation may not be changed but the deputies or assistants may be reviewed and adjusted by the fiscal court no later than the first Monday in May in any successive year upon written request by the officer. In addition, KRS 64.185 addresses monthly coroner and deputy coroner salaries based on county population as well as allows for a per month expense allowance up to \$300/month.

We recommend the fiscal court follow their county's adopted policies and procedures, applicable statutes, and IRS regulations.

Former County Judge/Executive William Davis's Response: Previous administration.

The Martin County Fiscal Court does not maintain an accurate capital asset schedule or insurance listing: The county's capital asset listing and insurance listing are inaccurate. The capital asset listing did not include all items that are on the insurance listing. Controls are not in place to ensure that capital assets are being added and removed from the capital asset listing and/or insurance listing.

Not maintaining an accurate list of capital assets or insurance policy could cause capital assets to be uninsured or result in paying for insurance for an asset the county no longer owns. It also leaves capital assets vulnerable to misappropriation and misstatement.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. Per the *County Budget Preparation and State Local Finance Officer Policy Manual*, capital asset records are necessary for proper valuation, adequate and accurate insurance coverage, internal control, and long range planning for property replacement. Additionally, good internal controls dictate management oversight of capital assets to prevent misappropriation or theft.

We recommend insurance policies be updated timely in order for the county to avoid unnecessary costs associated with insurance coverage on assets no longer owned by the county and to ensure that all county assets are properly insured in the event of loss. The county should also conduct a physical inspection of county assets at the end of each year and make comparisons to the county's list of inventoried assets and insurance policy.

Former County Judge/Executive William Davis's Response: Previous administration.

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

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