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Harmon Releases Audit of Mercer County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Mercer 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 Mercer 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 Mercer County Fiscal Court did not have an effective purchase order system: This is a repeat finding and was included in the prior year audit report as Finding 2016-002. During testing of disbursements, auditors noted the following issues:

- Twenty-three of 64 invoices tested did not have a purchase order, with examples of purchases being asphalt, elevator maintenance, and reimbursement for conference hotel expenses. Of the 23 exceptions, 11 of the disbursements were for utilities.
- The county paid two invoices for asphalt that did not use bid prices, which resulted in an overpayment of \$2,809.

Although policies were in place requiring the issuance of purchase orders, the fiscal court did not ensure that all departments adhered to established policies. The Mercer County Judge/Executive stated that the asphalt invoice paid with non-bid prices was due to the location of the project at the park. The county judge/executive believed that the park had their own contract with the vendor and paid the vendor's contracted rates.

The lack of purchase orders is neither compliant with purchasing requirement for counties, nor an effective implementation of internal control. As a result, management is unable to determine where potential issues with spending are before the expense is already incurred, creating the opportunity for waste, fraud, or abuse. Paying non-contract prices for items that have been previously bid out can result in the county overpaying for goods and services.

KRS 68.210 requires the State Local Finance Officer to create a system of uniform accounts for all counties and county officials. The Department for Local Government's *County Budget Preparation and State Local Finance Officer Policy Manual* outlines requirements for handling of public funds, including required purchasing procedures for counties. These requirements prescribe that (1) purchases shall not be made without approval by the judge/executive (or designee) and/or a department head and (2) purchase requests shall not be approved in an amount that exceeds the available line item appropriation unless the necessary and appropriate transfers have been made. Furthermore, per the manual, purchase order systems are required for fiscal courts and should be issued for all goods and services utilized by the fiscal court. This allows for fiscal court to ensure that sufficient budget allocation is available for all expenses and provides a better representation of financial status by reflecting more accurate encumbrances.

The Department for Local Government issued a memorandum on August 4, 2016, in which it "highly recommends" implementation of issuing purchase orders for payroll and utilities. This control allows for the fiscal court to ensure that sufficient budget allocation is available for all expenses.

We recommend the fiscal court improve procedures over purchase orders to ensure they are obtained for all purchases of goods and services. Additionally, the fiscal court should ensure that all purchases of bid items utilize the contract pricing.

County Judge/Executive's Response: At the end of Fiscal Year 2016-2017, we began issuing Purchase Orders for ALL purchases, utility bills, payrolls, and anything else that requires a check to be written. All departments have been made aware that they must call for a purchase order BEFORE they can make a purchase. The asphalt invoices were for blacktopping a parking lot at Anderson/Dean Community Park. The company who paves our county roads had a third party perform the work, due to their equipment being too large for the park. We were unaware there was a difference in pricing, but will check pricing in the future.

The Mercer County Fiscal Court did not comply with bidding requirements: During testing of disbursements, auditors noted there were two purchases that should have been bid by the fiscal court. One purchase was for a forklift for the county landfill, totaling \$41,889.

The second purchase was for three leased tractors with mowers. The purchase price for all three tractors combined totaled \$345,227, which includes a down payment of \$58,427 and trade-in value of \$52,000.

Internal controls were not in place to ensure that purchases and leases exceeding \$20,000 were bid out prior to purchase.

Competitive bidding ensures that the county procures materials and services at the best price available. By limiting competition, the county may not get this benefit. Additionally, the county is not in compliance with KRS 424.260.

KRS 424.260(1) states, “[e]xcept where a statute specifically fixes a larger sum as the minimum for a requirement of advertisement for bids, no city, county, or district, or board or commission of a city or county, or sheriff or county clerk, may make a contract, lease, or other agreement for materials, supplies except for perishable meat, fish, and vegetables, equipment, or for contractual services other than professional, involving an expenditure of more than twenty thousand dollars (\$20,000) without first making newspaper advertisement for bids.”

We recommend the fiscal court follow the requirements of KRS 424.260 by requiring purchases of \$20,000 or more to be competitively bid.

County Judge/Executive’s Response: The Mercer County Judge Executive joined the National Joint Powers Alliance under the impression that membership enabled the county to make purchases that fulfilled the procurement process under KRS 45A.300. This membership was used for the purchase of the tractors.

The forklift was purchased using funds from a Solid Waste Grant. The Kentucky Division of Solid Waste asked for a quote on the forklift and approved the grant. It was the county judge executive’s opinion that when awarded the grant, it was ok to make the purchase. Through this audit we learned bids should have been obtained. Mercer County will follow the requirements of KRS 424.260 in the future and make certain all purchases of \$20,000.00 or more are competitively bid per our Administrative Code.

The Mercer County Fiscal Court did not have adequate controls in place over payroll: This is a repeat finding and was included in the prior year audit report as Finding 2016-003. The fiscal court has a lack of segregation of duties over payroll processing. The finance officer is responsible for handling payroll for the fiscal court. All timecards are turned in to the finance officer, who enters employee time into the payroll system and processes the payroll. The tax administrator reviews payroll summary reports and compares to timecards for accuracy. The finance officer is also responsible for entering new employees, removing terminated employees, maintaining personnel files, and posting payroll to the disbursements ledgers.

The county treasurer and finance officer indicated duties had not been segregated because the county operates with limited staff.

When control procedures are performed by the same employee, the risk for material misstatement significantly increases due to undetected error or fraud. The employee could change pay rates, create fake employees, or adjust leave time without detection.

Good internal controls dictate that adequate controls and segregation of duties would prevent the same person from having a significant role over all phases of the payroll process.

We recommend the fiscal court implement adequate controls over payroll by segregating the duties over the handling of payroll. If that is not possible, we recommend the fiscal court provide strong oversight with compensating controls.

County Judge/Executive's Response: The Mercer County Fiscal Court will continue to provide strong oversight with compensating controls. The tax administrator will continue reviewing payroll summary reports and compare them to timecards for accuracy.

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

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