



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

September 16, 2020

Jeffrey J. Wilder, District Manager
Cumberland Falls Highway Water District
6926 Cumberland Falls Highway
Corbin, KY 40701

RE: Summary of Review Results

Dear District Manager Jeffrey J. Wilder:

The Auditor of Public Accounts (APA) has completed a limited-scope examination of the Cumberland Falls Highway Water District (District). This examination was initiated after our office received concerns regarding the occurrence of bonuses and nepotism within the District. The purpose of this examination was not to provide an opinion on the District's financial statements, but to review specific matters brought to our attention and make recommendations to ensure the District's management activities are accurate, transparent, and follow applicable criteria.

To address the concerns expressed, the APA reviewed certain information related to the District, such as the District Code of Conduct, District Board of Commissioners (Board) meeting minutes, personnel policies, and personnel records, analyzed financial documentation, such as payroll records and the check register for the Petty Cash Fund account, and performed other procedures deemed necessary. Unless otherwise indicated, the examination period of this engagement was January 1, 2018 to December 31, 2019.

Two findings emerged from the examination and are presented in this letter, along with corresponding recommendations.

Finding 1: The District awarded employee bonuses unrelated to individual employee job performance violating both its policy and the Kentucky Constitution.

In December 2018, seven District employees who had been with the District the entire year each received a \$3,284 bonus. The Board approved the bonuses without documentation of merit or performance, a violation of the District Code of Conduct and Section 3 of the Kentucky Constitution.



The District Code of Conduct states, “[i]f employees are entitled to a monetary bonus, no bonus will be given based on the relationship with any member of the Board of Commissioner’s. A bonus will be based on merit and job performance only.” However, no documentation was provided to support the bonus payments and the current District Manager indicated that the award of bonuses was not based on individual job performance. The minutes from the October 15, 2018 Board meeting, in which the bonuses were approved, also do not document consideration of merit or performance.

The award of bonuses with no documentation linking them to individual job performance is also a violation of Section 3 of the Kentucky Constitution. The Kentucky Office of Attorney General (OAG) opinion 62-1 states the awarding of a bonus from public funds would violate Section 3 of the Kentucky Constitution, as it would be using public funds to pay for services not actually performed. The Kentucky Constitution does not prohibit changes in compensation due to raises, which was the approach taken by the Board in 2019 when it passed a motion to increase all employees’ hourly rates by \$1, with the exception of the District Manager who received a larger raise in order to “be brought up to the previous manager’s pay.”

We recommend the Board discontinue awarding bonuses to employees in violation of Section 3 of the Kentucky Constitution and the District Code of Conduct. Copies of Section 3 of the Kentucky Constitution and OAG opinion 62-1 are enclosed with this letter.

We further recommend the Board consider more fully developing its policy of providing payments based on merit and job performance to provide additional structure and greater controls over the award process. Controls that should be considered include, but are not limited to, identifying the type of work or work effort required for an employee to receive an award, establishing the frequency upon which an employee may receive an award, and establishing an award scale or limit on the amount of award that may be received.

Finding 2: The District Transfers Funds from its Operations and Maintenance Fund Account to a Separate Account from which Expenditures are Not Fully Reported to the Board.

The District routinely transfers funds from its Operations and Maintenance Account to a separate bank account referred to as its Petty Cash Fund account. All expenditures from this account occur via check rather than through a distribution of cash maintained onsite. The District does not have a written policy related to the use of its Petty Cash Fund account, which is the only bank account that does not require two signatures on checks. Additionally, the District only provides the Board with monthly cash balances for the Petty Cash Fund account instead of check registers that would more fully exhibit account activity. A review of the check register for the period of December 1, 2019 through June 12, 2020 found expenditures from the Petty Cash Fund account appear to be operational in nature; however, they are atypical of the usual purpose for petty cash and included bereavement expenditures.

The District has acknowledged the maintenance of a petty cash account; however, the District's account is not a typical petty cash account in the sense that it is not cash on hand maintained in the office to reimburse for smaller expenses. The District's Petty Cash Fund account is a bank account from which checks are written. Although all purchases are to be pre-approved by the District Manager, no written policy exists discussing the proper use of these funds and only one signature is required to execute a check. Checks written from the District's remaining nine accounts each require two signatures.

The District did not provide the Board with detailed financial information regarding numerous accounts, including the Petty Cash Fund account. The District currently has ten bank accounts, but only check registers from the two primary accounts, the Operating and Maintenance (O & M) Fund and Meter Deposit Fund, were presented during monthly Board meetings during the examination period. A cursory review of these registers showed that a check was written from the O & M Fund account nearly every month to replenish the amount of petty cash used. Checks written ranged from \$1,565 to \$2,892 and total payments from the O & M Fund to reimburse the Petty Cash Fund between January 11, 2018 and December 16, 2019, totaled \$41,491. The monthly cash report section of the financials provided at the Board meetings did not clearly reflect this income, as well as any expenditures from the account, within the single line for the Petty Cash Fund account. Thirteen of 18 monthly cash reports provided to the Board during the examination period showed no change in the starting and ending balances for the month despite evidence of account activity within the same meeting packet.

According to the District, the Petty Cash Fund account is used for expenditures such as postage, cleaning and office supplies, Department of Transportation physicals, and continuing education classes for personnel and Commissioners. Analysis of the check register for the period of December 1, 2019 through June 12, 2020 confirmed this use of petty cash to cover standard operational expenses. Additionally, the District expended \$380 from the Petty Cash Fund account during this period of time on bereavement gifts for family members of Commissioners and District employees. While this may be a kind gesture by the District, this is a personal expenditure and District funds should not be used for such purposes.

We recommend the District develop a formal written policy as to the use of the Petty Cash Fund. We also recommend the usage of petty cash funds, as well as all other accounts held by the District, be fully reflected in the reports provided to the Board to provide increased transparency.

Observation

In addition to the two findings above, it was identified that the District's current Code of Conduct allows for relatives to be hired as long as an individual has completed an application and "meets the job requirements set forth in the job description." Currently, six of the eight employees at the District have a familial relationship with at least one other employee or a former Commissioner at the District. While not a violation of the District's Code of Conduct, nepotism, or even the

Mr. Jeffrey J. Wilder

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perception of nepotism, can have an adverse effect on the workforce, regardless of who the hiring authority is. We suggest the Board consider its policy to determine whether a more restrictive policy for hiring and supervising of employees with familial relationships is needed. It is further suggested that appointments to the Board have no relationship with District employees.

Thank you for your attention to these matters and the District's cooperation with this limited-scope examination. If you have any questions regarding this letter, please contact me, or Tiffany Welch, Executive Director, at 502-564-5841.

Thanks and God Bless,

A handwritten signature in black ink, appearing to read "Mike Harmon". The signature is written in a cursive style with a long horizontal line extending to the right.

Mike Harmon

Auditor of Public Accounts

CC Pat White, Jr., Whitley County Judge Executive
Scotty Harrison, Magistrate
Mondo Cima, Magistrate
Michael Jarboe, Magistrate
Raleigh Meadors, Magistrate
Johnny Collette, District Board Commissioner
Teddy Dean Prewitt, District Board Commissioner
Marshall Lovitt, District Board Commissioner
R.L. McCullah, District Board Commissioner
Everett Angel, District Board Commission

Section 3 Men are equal -- No exclusive grant except for public services -- Property not to be exempted from taxation -- Grants revocable.

All men, when they form a social compact, are equal; and no grant of exclusive, separate public emoluments or privileges shall be made to any man or set of men, except in consideration of public services; but no property shall be exempt from taxation except as provided in this Constitution, and every grant of a franchise, privilege or exemption, shall remain subject to revocation, alteration or amendment.

Text as Ratified on: August 3, 1891, and revised September 28, 1891.

History: Not yet amended.

CITIES GENERALLY - Employees, bonus for

To: J. Gordon Lisanby, City Attorney, Princeton, Ky.
By: Walter C. Herdman, Asst. Atty. Genl., January 2, 1962

This is in answer to your telegram of December 27 in which you request an opinion as to whether or not it is legal for the City of Princeton to give a bonus to its city employees and policemen.

We must first consider the fact that the city is dealing with public funds and public employees. § 3 of the Kentucky Constitution prohibits the granting of separate public emoluments to any person or a set of persons except in consideration of public services. Now the employees referred to are paid a salary and this salary is required to be fixed by the city legislative body under the provisions of KRS 64.580 (1950). The granting or awarding of a bonus would seem to us to contravene the section of the Constitution referred to since it would seem to be using public funds for services not actually rendered.

Referring next to McQuillin, Municipal Corporations, Vol. 4, § 12.193, we find the general rule expressed regarding the granting of extra compensation as follows:

"Extra compensation is compensation over and above that fixed by contract or by law when the services were rendered. Where an officer performs duties imposed by law he is entitled to the compensation therefor fixed by law and no other. He is not entitled to extra compensation for services performed in the line of his official duty...."

In connection with the above quote, we refer you to the case of Ludlow Board of Education v. Ritchie, 149 Ky. 674, 149 S.W. 985 (1912). We also wish to refer you to the terms of KRS 64.410(2)(c) which prohibit a public officer from receiving for his services any fee for services not actually rendered and KRS 434.250 which prohibits any officer from paying any person any sum for services not actually rendered.

There is, of course, no prohibition against a city legislative body changing the compensation of city officers as fixed by it during their employment. This, however, would require an amendment to the ordinance setting forth the compensation of city employees.

Under the circumstances, therefore, we do not believe that the city is legally authorized to grant a bonus or additional compensation to city employees out of public funds over and above that amount fixed according to law.