



Auditor of Public Accounts  
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**FOR IMMEDIATE RELEASE**

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**Harmon Releases Audit of Estill County Fiscal Court**

**FRANKFORT, Ky.** – State Auditor Mike Harmon has released the audit of the financial statement of the Estill County Fiscal Court for the fiscal year ended June 30, 2021. 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 Estill 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 116 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 Estill County Fiscal Court failed to implement adequate internal controls and oversight for disbursements and transfers:** This is a partial repeat of a finding and was included in the prior year audit report as Finding 2020-002.

- Seven disbursements totaling \$823,067 were not paid timely (within 30 working days of receiving the invoice or bill).
- The unencumbered cash balance of the jail and Chemical Stockpile Emergency Preparedness Program (CSEPP) funds on the fourth quarter financial statement reflected negative balances of \$45,571 and \$107,469

The fiscal court did not implement adequate procedures and oversight regarding the documentation, preparation, and authorization of disbursements and transfers. The county's administrative code outlines proper procedures for disbursements. The absence of significant review procedures or oversight also allowed numerous invoices to not be processed timely and this occurred without detection or knowledge of the fiscal court. Some invoices were not paid timely simply because the funds were not available when the invoice was received. In addition to this, when encumbrances were taken into consideration at the end of the fiscal year the jail fund and CSEPP fund reflected negative unencumbered cash balances. The negative unencumbered cash balances reflected were due to cash transfers from other funds not being completed as expenditures were encumbered.

The fiscal court's failure to establish effective internal controls over disbursements and transfers resulted in numerous instances of noncompliance, violations of statutes, negative unencumbered cash balances, and violations of the county's administrative code as reflected above. The lack of proper accounting practices, internal controls, and oversight increases the risk that undetected misstatements and fraud will occur.

Failure to pay obligations timely is indicative of poor financial management practices and can result in late fees and finance charges, which are a wasteful use of taxpayer resources. It is also a violation of statute for failure to pay invoices within 30 working days of receipt of the invoice or bill.

The risk of overspending the budget or spending in excess of funds available increases significantly without effective internal controls over transfers in place.

Effective internal controls provide for adequate segregation of duties and prevent the same person from having a significant role in incompatible functions. Segregation of duties and proper oversight helps prevent fraud or misappropriation of assets and protects employees in the normal course of performing their daily responsibilities. Effective internal controls and proper oversight also help ensure compliance with laws, regulations, grant agreements, etc.

KRS 65.140(2) stipulates timely payments to vendors by stating, "[u]nless the purchaser and vendor otherwise contract, all bills for goods and services shall be paid within thirty (30) working days of receipt of a vendor's invoice except when payment is delayed because the purchaser has made a written disapproval of improper performances or improper invoicing by the vendor or by the vendor's subcontractor."

Effective internal controls also provide effective monitoring of the encumbering of expenditures and the need for cash transfers to ensure that negative unencumbered cash balances do not occur.

Purchase order requirements are outlined by the Department for Local Government (DLG). KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The *County Budget Preparation and State Local Finance Officer Policy Manual*, page 57, requires purchasing procedures include the following:

1. Purchases shall not be made without approval by the judge/executive (or designee), and/or a department head.
2. Purchase requests shall indicate the proper appropriation account number to which the claim will be posted.
3. Purchase requests shall not be approved in an amount that exceeds the available line-item appropriation unless the necessary and appropriate line item and cash transfers have been made.
4. Each department head issuing purchase requests shall keep an updated appropriation ledger and/or create a system of communication between the department head and the judge/executive or designee who is responsible for maintaining an updated, comprehensive appropriation ledger for the county.

We recommend the fiscal court implement adequate, effective internal control procedures for disbursements and transfers, including segregation of duties, to address each of the areas previously discussed. Additionally, strong management oversight and review procedures should be implemented to prevent and detect errors or fraud. Effective review procedures could be achieved if performed by an employee independent of the person or department initially performing those functions. All oversight and review procedures must be properly documented by initialing source documents, ledgers, reports, or other supporting documentation.

*County Judge/Executive's Response: Disbursements in question were for emergency road work under a FEMA project. The Judge explained to the vendor that payment could not be made until funds were available from FEMA. Being fully informed, the vendor came anyway and was very efficient and quick about getting the repairs made to twenty-six (26) road breaks throughout the county. The FEMA funds still had not been received and the county felt like this vendor should be paid. Therefore, the necessary funds were borrowed on short-term loan, paid to vendor and loan paid off when FEMA funding was received. It is the practice of the fiscal court to pay invoices timely, unless something is in question or there is an understanding with the vendor.*

*The negative balances reflected on Jail and CSEPP were unencumbered cash balances and were due to P.O.'s being issued, not actual negative cash in the bank. The Jail is supported by the General Fund and CSEPP is reimbursed from federal funding. When claims are presented to Fiscal Court, interfund transfers and/or line of credit draws would have been approved to cover said balances. The necessary funds were available to be transferred at that time. It is the practice of the Fiscal Court to approve transfers before claims are paid, not when encumbered for both the Jail and CSEPP funds.*

**Internal controls over occupational tax collections are not adequate:** This is a repeat finding and was included in the prior year audit report as Finding 2020-003. Occupational tax collections comprise about 51% of the county's general fund operating revenue – by far the single biggest source of revenue for this fund. Internal controls over occupational taxes are not adequate to ensure amounts reported are complete, accurate, and free of material misstatement due to the following issues:

- Occupational taxes were not reconciled to the ledgers by someone independent of receiving and posting occupational tax receipts.

- Deposits for occupational taxes received were not reviewed and agreed to the detailed daily tax form register.
- Delinquent occupational tax notices are not sent out with any regularity or consistency.
- There are no effective review or oversight procedures for occupational tax collections.

The fiscal court failed to adequately assess risk associated with occupational tax collections and has not implemented effective internal controls, review procedures, or oversight for occupational tax collections.

Failure to implement adequate controls over occupational tax collections increases the risk that material misstatements and fraud will occur and go undetected, especially considering occupational taxes comprise such a large portion of general fund revenues.

Proper segregation of duties, internal controls and maintaining documentation of control procedures completed is essential to protect the fiscal court against misappropriation of assets and inaccurate financial reporting, while also protecting employees in the normal course of performing their job responsibilities.

In order for internal controls to be effective in preventing and detecting errors, misstatements, and fraud, the functions of any significant area should be separated. If segregation is not possible or practical, the fiscal court could implement and document compensating controls to reduce the risk associated with inadequate segregation of duties. A strong compensating control could include review of deposit tickets, tax returns, and occupational tax ledger by someone independent of occupational tax collections. This could be documented by initialing all supporting documentation after the review is complete.

We recommend the fiscal court implement effective internal controls, review procedures, and oversight for occupational tax collections and document the procedures performed that ensure recorded amounts are complete, accurate, and free of material misstatement.

*County Judge/Executive's Response: Occupational taxes are entered daily by the occupational tax administrator. Treasurer then reviews, posts and deposits said taxes. Deposits are reconciled to daily receipts. In addition to reviewing, we will document doing so. At this time, notices are sent for late filing and incorrect tax payments as returns are received. Once accounts have been reconciled from prior years delinquent notices will be sent with regularity.*

**Internal controls, review procedures, and oversight for payroll processing are not adequate:**

This is a repeat finding and was included in the prior year audit report as Finding 2020-004. The following issues were noted for payroll processing:

- The fiscal court did not provide the same level of health insurance coverage to all employees (see Finding 2021-004 for additional detail).
- Pay rates were not properly implemented and documented. The fiscal court approved a salary schedule for all employees on August 20, 2018, but the pay rates and ranges approved were not implemented and applied to all employees and these wage rate changes were not documented in personnel files.

- Payroll was not properly supported six employees did not have a supervisor signature or approval.

The fiscal court failed to adequately assess the risk associated with payroll processing and failed to implement adequate internal controls regarding the documentation, preparation, and authorization of payroll. There were no significant review procedures in place nor adequate oversight for the majority of the audit period to ensure the completeness and accuracy of payroll information.

Failure to implement adequate controls over payroll increases the risk that material misstatements and fraud will occur and go undetected, especially considering payroll accounts for a large portion of the county's budget. Numerous undetected errors were noted for payroll processing and the fiscal court is in violation of various statutes.

In order for internal controls to be effective in preventing and detecting errors, misstatements, and fraud, the functions of any significant area should be separated. If segregation is not possible or practical, the fiscal court could implement and document compensating controls to reduce the risk associated with inadequate segregation of duties. A strong compensating control could include review of payroll reports, review of payroll payments, comparison of payroll documentation to amounts recorded, and reconciliation of withholding and matching reports to supporting documentation. Further, review procedures and oversight should be exercised consistently to detect errors and to reconcile payroll to supporting documentation.

We recommend the fiscal court implement effective internal controls, review procedures, and oversight for payroll processing to ensure the completeness and accuracy of all payroll information.

*County Judge/Executive's Response: Timecards are approved by department heads and reviewed by both the payroll clerk and treasurer. Any questions arising are discussed with department heads. When necessary, these are referred to the Judge for review and any additional action needed. Currently the Judge signs off on time cards. These reviews will start being documented by reviewer initialing document.*

*Notations are made in payroll system for pay rate changes, copies of fiscal court minutes are kept for all pay rate changes. Copies are also being filed in personnel files at this time.*

*Payroll reports, pay rates and benefits are reviewed and reconciled by treasurer on regular basis. Treasurer will start documenting the review by initialing reports.*

*The pay rates approved August 2018 by prior administration were not implemented at that time. Current administration approved and implemented the pay rate in FY 20. Pay rates were adjusted and back-pay was paid to all employees entitled to adjustment. All pay rates have been approved by fiscal court since that time and notations are made.*

*We are continuing to make improvements in this area. Also, in addition to reviewing, we will document doing so.*

**The Estill County Fiscal Court did not provide the same level of health insurance coverage to all county employees:** This is similar to a repeat finding and was included in the prior year audit report as Finding 2020-005. Three county employees received health insurance coverage that was not made available to all other county employees. County employees are provided individual health insurance coverage. If the employee chooses to elect additional coverage for a spouse, children, or family coverage they may do so but are responsible for the cost of the health insurance premium that exceeds the individual coverage premium. For Fiscal Year 2021, the cost of an individual health insurance premium was \$500. Three employees elected to add coverage for dependents, which was an additional amount per month per employee. This additional cost was not paid by the employees via payroll deduction.

The fiscal court did not have adequate internal controls in place to ensure health insurance benefits were applied equally among all classes of employees and that proper wage deductions were applied to employees that requested coverage in excess of standard county employee coverage.

The fiscal court has applied employee benefits in an unequitable manner. Additionally, county funds are being spent for the personal benefit of select employees that could have been expended on other items to benefit the entire county.

Since the local procedure for health insurance benefits provides single/individual coverage, the amount in excess of that is not an allowable expense of the program. OAG 94-15 states, "The basic statute providing for governmentally funded health coverage (KRS 79.080) for public employees does not provide for one level of coverage for officers, and another level for employees. Accordingly, we believe such differing coverage would not be lawful as not authorized by statute."

We recommend management ensure that employee benefits are applied equally among all employees and that proper amounts are withheld from employees' wages for elective/optional employee benefits.

*County Judge/Executive's Response: This is the way health insurance has been handled for many years prior to the current administration. As soon as the exit conference for the fiscal year 2019 audit was conducted in June 2021, the current administration took steps to correct this issue. This issue has been corrected as of the present date.*

**Remaining balance of the line of credit was not paid by the end of the fiscal year:** This is a repeat finding and was included in the prior year audit report as Finding 2020-006. On June 7, 2021, the fiscal court closed the existing line of credit account for the Chemical Stockpile Emergency Preparedness Program (CSEPP) and opened up a new line of credit in the amount of \$1,000,000. This line of credit provides the fiscal court a mechanism to pay for the CSEPP funded projects and subsequently seek financial reimbursement from the Kentucky Division of Emergency Management (KyEM). The line of credit was for one year and renewable on an annual basis. As of the end of the fiscal year the fiscal court owed \$452,928.

The treasurer was waiting on reimbursement from CSEPP and was unaware that the loan had to be paid off at the end of the fiscal year.

As a result, the fiscal court is not in compliance with requirements set by the Department for Local Government (DLG) when entering into financial obligations.

Per KRS 65.7701 - 65.7721 and DLG's *County Budget Preparation and State Local Finance Officer Policy Manual* allows notes, however, they must be paid off before the end of the fiscal year in which they are borrowed.

We recommend the fiscal court seek guidance from DLG before entering into any financial obligation of any nature, to ensure they are in compliance with the state and local debt officer.

*County Judge/Executive's Response: Due to disclaimed audits of the county for prior administration, the CSEPP funding went from being paid in advance of an expenditure to being on a reimbursement basis. Therefore, a line of credit was necessary in order to pay CSEPP expenditures while awaiting reimbursement. Approval and guidance were requested from DLG regarding this issue. Once invoices have been paid, reimbursements are received, and line of credit is paid back. If a draw is made near the end of the fiscal year, federal funds may not be received in time to pay the line of credit off before year-end. In this case, a draw was made on June 24, 2021, and reimbursement of funds were not received prior to June 31, 2021.*

*No draw will be made near FY 22 end, and pay off will be made prior to FY end. We have received our first advance pay this year and hope to eliminate the need for line of credit in future.*

**Draws On CSEPP line of Credit were posted to the incorrect line item on the quarterly report:**

Estill County has a line of credit with the local bank that provides the fiscal court a mechanism to pay for the Chemical Stockpile Emergency Preparedness Program (CSEPP) funded projects until they can subsequently seek financial reimbursement from the Kentucky Division of Emergency Management (KyEM). During Fiscal Year 2021, Estill County drew down \$1,547,594 on the line of credit and posted those draws they received to account code 4732 Revolving Loan Revenue according to the Department for Local Government's (DLG) Budget Manual. However, since the money is drawn down on a loan, the amounts received should have been posted to account code 4911 Borrowed Money. As a result, a material adjusting journal entry had to be made to reclassify this amount from account code 75-4732 to 75-4911.

The draws on this line of credit have been posted to account code 4732 since it began and the county was never made aware that it should have been posted elsewhere.

As a result, the fiscal court is not in compliance with requirements set by DLG when recording proceeds from financial obligations.

Per KRS 68.210, the DLG's *County Budget Preparation and State Local Finance Officer Policy Manual* specifies a uniform system of accounts to be followed by county governments. This manual designates account code 4911 as the proper code for borrowed money proceeds.

We recommend the fiscal court start recording draws on lines of credit to account code 4911 to ensure they are in compliance with DLG's Uniform System of Accounts.

*County Judge/Executive's Response: Draws received from revolving line of credit were posted to account code 75-4732 Revolving Loan Revenue since first revolving loan originated in 2019. This account was used from the County Budget Manual.*

*Line of credit draws will be reclassified to revenue code 75-4911 Borrowed Money as recommended in this audit.*

**The Estill County Fiscal Court's Schedule of Expenditures of Federal Awards submitted to the Department for Local Government was not accurate:** The Estill County Schedule of Expenditures of Federal Awards (SEFA) submitted to the Department for Local Government (DLG) did not accurately report federal grant disbursements for the fiscal year ended June 30, 2021. The county treasurer tracks federal grant activity receipts and disbursements to prepare the SEFA each fiscal year based on her records and information provided from the various department heads. The treasurer prepared the SEFA for fiscal year ending June 30, 2021 and submitted it to DLG with her fourth quarter report as required. After the exit conference for the fiscal year ending June 30, 2020 audit, the treasurer realized some adjustments needed to be made to the SEFA she had submitted. The total amount of federal expenditures changed from \$3,666,567 on the original submission to \$3,161,172 on the revised copy. This is a material difference of \$505,395. The treasurer made those changes and had a revised SEFA available for auditors upon the start of the fiscal year 2021 audit; however, she did not resubmit a revised SEFA to DLG.

The current administration was new starting in Fiscal Year 2019. The treasurer was just not aware that she needed to submit a revised SEFA to DLG if changes were made subsequent to submission.

The fiscal court is not in compliance with DLG reporting requirements for federal awards.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. Pursuant to KRS 68.210, the state local finance officer has prescribed minimum accounting and reporting standards in DLG's *County Budget Preparation and State Local Finance Officer Policy Manual*. The manual requires the county treasurer to prepare a schedule of expenditures of federal awards and submit this schedule with the fourth quarter report to DLG.

Additionally, *OMB Uniform Administrative Requirements, Cost Principles and Audit Requirements For Federal Awards* 2 CFR 200.508(b) requires the auditee to "[p]repare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with 200.510 Financial statements." 2 CFR 200.510(b) states, in part, "The auditee must also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements which must include the total Federal awards expended as determined in accordance with CFR 200.502 Basis for determining Federal awards expended." In addition, good internal controls dictate the SEFA be complete and accurate.

We recommend the Estill County Fiscal Court ensure the SEFA is complete and accurately prepared for each fiscal year federal monies are expended. This will be best achieved by the



treasurer preparing the SEFA and having the department heads double check the numbers reported to ensure the correct amount of the federal portion of expenditures is being reported.

*County Judge/Executive's Response: Guidance was requested from Department for Local Government and from auditors before completion of the SEFA report. The report was submitted with total expenditures reported for all federal projects that were worked on during the fiscal year. After submission and further discussion with auditors, adjustments were made to reflect only federal portion of total expenditures.*

*We will continue to seek guidance from Department for Local Government and auditors. Any adjusted reports will be forwarded to Department for Local Government.*

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

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