



Auditor of Public Accounts
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Harmon Releases Audit of Fulton County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Fulton County Fiscal Court for the fiscal year ended June 30, 2020. 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 Fulton 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 Fulton County Fiscal Court lacks adequate segregation of duties over accounting functions and financial reporting: This is a repeat finding and was included in the prior year audit report as Finding 2019-001. The Fulton County Fiscal Court lacks adequate segregation of duties over accounting functions and financial reporting of fund balances, cash balances, and debt service. The Fulton County treasurer was responsible for preparing monthly, quarterly, and annual reports, financial reports, preparing debt schedules, and reconciling bank accounts.

The following control deficiencies occurred due to the lack of segregation of duties over these areas:

- As reported in Finding 2020-002, beginning and ending fund balances were overstated, and a large variance was noted between the total unencumbered cash balance and the total reconciled cash balance.
- As reported in Finding 2020-003, outstanding debt balances do not agree with the long-term liabilities section of the fourth quarter financial statement.
- As reported in Finding 2020-004, the payroll revolving account does not properly reconcile to zero.

While it may be customary for the county treasurer to perform these functions, the fiscal court failed to adequately segregate the duties involved. The fiscal court also failed to establish adequate management oversight to ensure receipts and disbursements were properly recorded and that completed bank reconciliations were accurate. Furthermore, the fiscal court failed to establish adequate management oversight to ensure fund balances, cash balances, and outstanding debt balances were accurately reported.

The lack of adequate segregation of duties, coupled with a lack of adequate management oversight, provides an environment in which an individual could manipulate financial records and misappropriate or misdirect county funds.

The segregation of duties over various accounting functions such as recording receipts and disbursements, performing bank reconciliations, and preparing monthly, quarterly, and annual financial reports is essential for providing protection from asset misappropriation and inaccurate financial reporting. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

We recommend the fiscal court segregate the duties involved in recording receipts and disbursements, reconciling bank accounts, and preparing monthly, quarterly, and annual financial reports. If segregation of duties is not possible due to the limited number of staff, appropriate management oversight should be provided to ensure the completion of accurate, timely financial reports. This oversight should include a documented review of financial reports by management.

County Judge/Executive's Response: Although state law requires the Treasurer to perform certain duties, it appears these duties, purely interpreted, may be in conflict with general account practices. Segregations of duties in a small office environment is difficult due to limited staff. Going forward, the County Judge and Administrative Assistant will add additional interactions relative to internal controls of the accounting process by reviewing work preformed by the Treasurer and Finance Officer.

The Fulton County Fiscal Court failed to implement adequate internal controls to ensure complete and accurate accounting records were maintained: This is a repeat finding and was included in the prior year audit report as Finding 2019-002. There were no functioning internal controls in place over the work performed by the county treasurer. The fiscal court failed to provide adequate oversight, allowing the county treasurer control over the accounting and reporting functions. The following deficiencies and errors were noted during the performance of the audit:

- The fourth quarter financial report was inaccurate:

- The beginning fund balance of the general fund was overstated by \$417,798.
- The ending fund balances of the general fund and jail fund were overstated by \$659,104 and \$605, respectively.
- There was a \$692,990 variance noted between the total reported unencumbered cash balance and total reconciled cash balance.
- There was no record in the fiscal court minutes that the quarterly reports for the second and fourth quarters were presented to the fiscal court as required by KRS 68.360.

The Fulton County Fiscal Court failed to implement a strong internal control system or provide proper oversight to ensure complete and accurate accounting records were maintained. Instead, the county placed reliance on the county treasurer, and chose not to scrutinize the discrepancies noted on the quarterly reports. The overstatement of beginning and ending fund balances of the general fund was primarily related to the fact that the amounts recorded for payroll expenditures did not agree with the amounts transferred to the payroll fund. The overstatement of the ending balance of the jail fund was the result of posting errors.

According to the county judge/executive, the quarterly reports for the second and fourth quarters were not approved by the fiscal court due to an oversight.

Due to the fiscal court's lack of effective oversight of the treasury functions, the deficiencies, noncompliances, and undetected errors noted above pertaining to required record-keeping occurred without detection. Additionally, the fiscal court was unable to properly budget and plan for the following fiscal year due to inaccurate financial information being presented.

Strong internal controls over the reporting process are vital in ensuring the financial reports accurately reflect the financial activity of the fiscal court as well as ensuring adherence to applicable laws and regulations.

KRS 68.360(1) states, "[t]he county treasurer shall balance his books on the first day of each month, so as to show the correct amount on hand belonging to each fund on the day the balance is made, and shall within ten (10) days file with the county judge/executive and members of the fiscal court a monthly statement containing a list of warrants paid by him during the month, showing all cash receipts and the cash balance at the beginning and at the end of the month, and certifying that each warrant or contract is within the budget appropriation." Additionally, KRS 68.360(2) states, "[t]he county judge/executive shall, within fifteen (15) days after the end of each quarter of each fiscal year, prepare a statement showing for the current fiscal year to date actual receipts from each county revenue source, the totals of all encumbrances and expenditures charged against each budget fund, the unencumbered balance of the fund, and any transfers made to or from the fund. The county judge/executive shall post the statement in a conspicuous place in the courthouse near the front door for at least ten (10) consecutive days, and transmit a copy to the fiscal court and to the state-local finance officer. The statement shall be read at the next meeting of the fiscal court."

KRS 65.905(2) requires, "[t]he final quarterly report filed by a county within fifteen (15) days after the end of the last quarter of the fiscal year, in accordance with KRS 68.360(2), shall be deemed the uniform financial information report for that county for purposes of compliance with KRS 65.900 to 65.925."

KRS 68.020(4) states that county treasurer, “shall keep an accurate detailed account of all money received and disbursed by him for the county, and shall keep books of account of the financial transactions of the county in the manner required by the uniform system of accounting prescribed by the state local finance officer.”

We recommend the Fulton County Fiscal Court strengthen oversight and internal controls in order to ensure complete and accurate accounting records are maintained and that no one individual has control over the accounting functions without establishing checks and balances to verify amounts recorded and reported are accurate. We also recommend the fiscal court scrutinize any unusual amounts or variances noted on the quarterly reports.

County Judge/Executive’s Response: Same response as 1 above. It is difficult to separate the nature of finding 1 and 2 since they appear to be closely related in work being performed in a small government office. Additionally, the county will discontinue the use of consolidated bank account. The Fiscal Court has ordered that all funds be maintained in independent bank accounts making reconciling accounts less cumbersome. This is scheduled to begin July 1, 2022.

Debt balances do not agree with the long-term liabilities section of the fourth quarter financial statement: This is a repeat finding and was included in the prior year audit report as Finding 2019-003. On the liabilities section of the June 30, 2020 quarterly financial statement, the Fulton County Fiscal Court reported outstanding debt principal in the amount of \$4,202,694 and outstanding interest in the amount of \$1,297,536. However, the confirmed outstanding principal balance was \$4,428,897, and the outstanding interest balance was \$1,353,467 thereby resulting in variances of \$226,203 and \$55,931, respectively.

According to the county treasurer, the misstatement occurred due to clerical errors that were not caught. This condition is also the result of the lack of segregation of duties and fiscal court’s failure to establish adequate management oversight as reported in Finding 2020-001.

As a result, the fourth quarter financial statement was materially understated. Additionally, by not accurately reporting outstanding liabilities, the fiscal court cannot make effective management decisions relating to debt service.

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* requires accurate financial records be maintained, which includes the schedule of liabilities. Furthermore, good internal controls require accurate information be presented in order for the fiscal court to make informed financial decisions during budget preparation or when making large purchases.

We recommend the Fulton County Fiscal Court review debt schedules and the debt liabilities section of the quarterly financial statements to ensure that accurate outstanding principal and interest is reported.

County Judge/Executive's Response: Often amortization charts indicating debt will shift as interest rates change or prepayment, etc. occur creating the demand for revised amortizations charts. When this happens, county financial records may not have indicated the shift at any given time. Therefore, we will increase our efforts to maintain in our files any updated long term debt documentation.

The Fulton County Fiscal Court lacks proper oversight of the payroll revolving account: As of June 30, 2020, the payroll revolving account had a reconciled balance of \$89,313. This was due to incorrect amounts being transferred from the operating funds to the payroll revolving account. Because there are no internal controls verifying payments to and from the payroll account, as well as no review of the payroll revolving account activity to verify transactions were properly handled and recorded, the payroll revolving account does not reconcile to zero.

As a result, individual operating fund disbursements and ending balances were misstated on the fourth quarter financial statement.

Good internal controls over the payroll account require oversight by fiscal court to protect employees while performing duties and to protect county assets against misappropriation. The payroll account is a revolving account and should reconcile to zero.

We recommend the fiscal court implement strong internal controls over the payroll revolving account. These controls should include having someone independent of the payroll function verify proper amounts are transferred to the payroll revolving account from the corresponding operating funds. These controls should also include verifying that any accumulated balance is properly allocated and reflected on the county's financial statement.

County Judge/Executive's Response: One of the issues that has driven this finding is due to the way Fulton County has always done payroll. The County operates from a single payroll account. The payroll account supports payroll activity for offices that pay weekly, bi-weekly, monthly and the County Attorney's office. When examining balances in the account at a given point, there may be differences because some of the contributors to the account may not have transferred their portion of withholdings to the account creating misstated balances. This could be corrected by requiring the Sheriff, County Clerk and others to maintain their own payroll account. This will be discussed with the Fiscal Court for corrective action.

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

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