



Auditor of Public Accounts
Mike Harmon

FOR IMMEDIATE RELEASE

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Harmon Releases Audit of Laurel County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Laurel 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 Laurel 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 High Intensity Drug Trafficking Areas (HIDTA) fund should be treated as a fund of the Laurel County Fiscal Court: The Financial Commission for Appalachia High Intensity Drug Trafficking Areas (HIDTA) fund is not being properly monitored or reported by the Laurel County Fiscal Court. The fund is used to account for the receipts and disbursements of the Appalachia HIDTA program. The fund is being administered by a financial commission, which was established by the Laurel County Fiscal Court, but the activities of this commission are not monitored by the fiscal court itself. The financial commission was created by the fiscal court to administer grant revenues. It is a special revenue fund and an integral part of the overall governmental reporting entity of the Laurel County Fiscal Court. The Laurel County Fiscal Court does not prepare a budget for this fund nor does it include it on its quarterly financial report.

It is the opinion of the Laurel County Attorney that “with the size and its operating budget, the Laurel County Fiscal Court could not offer adequate oversight and to follow auditor’s recommendations would result in a degradation of said oversight.” The county treasurer stated that it was not feasible to include the HIDTA fund as a fund of the fiscal court. She stated that in order for this to happen, all disbursements would have to be approved by fiscal court and due to the nature of the disbursements (undercover drug related), fiscal court could not risk the disbursements being public record. She further stated if HIDTA is made a fund of the fiscal court and made public record, the fiscal court would probably stop receiving the federal funds altogether.

Based upon the opinions of the county attorney and the county treasurer, the Laurel County Fiscal Court has not included the HIDTA fund as a fund of the fiscal court. As a result, the fund is added as an adjustment to the financial statement to properly present the financial activity of the fiscal court to avoid a material misstatement of the financial statement.

The HIDTA Program Policy and Budget Guidance states, “HIDTAs are not legal entities under Federal law, but rather a coalition joined together to receive HIDTA funds to coordinate drug-related law enforcement activities of Federal, state, local, and tribal law enforcement agencies in designated areas.” It states further, “[c]onsequently, ONDCP [Office of National Drug Control Policy] must provide HIDTA Program funds to one or more legal entities, such as a state, local, or tribal agency...to act as the grantee(s) for agencies participating in the HIDTA program. In this role, the grantee is accountable for the use of HIDTA funds and must comply with all applicable Federal statutes and regulations and with its own regulations and policies.” “ONDCP awards HIDTA Program funds to state, local, and tribal government agency, ... in the form of two-year grants....” Per the HIDTA grant agreements, the grant recipient is the Laurel County Fiscal Court and since HIDTA is not legally separate, it should be considered a fund of the fiscal court.

KRS 68.020(4) states, in part, the county treasurer “...shall keep an accurate detailed account of all money received and disbursed by him for the county and shall keep books of accounts of the financial transactions of the county in the manner required by the uniform system of accounting prescribed by the state local finance officer.” In addition, 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 the Department for Local Government’s (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*. The manual requires all money received and paid to be reflected in the county budget and be properly reflected on the financial report as a receipt as well as an “expenditure.” Furthermore, all funds disbursed on the fiscal court’s behalf by third parties should be recorded in receipts and appropriations ledgers.

We recommend the fiscal court consider the HIDTA fund like other funds of the fiscal court by budgeting for this fund and including it on the quarterly financial report. In addition, the fiscal court should approve all claims of the HIDTA fund and the county treasurer should receive, receipt, and record all HIDTA funds. Both the county judge/executive and the county treasurer should sign all disbursements from the HIDTA fund.

County Judge/Executive's Response: Judge Westerfield contacted DLG [names redacted] after speaking with DLG they have given me very helpful input into how this can be corrected. Going forward Hidta and Section 8 will be included in Laurel County Budget.

The Laurel County Section 8 Housing fund should be treated as a fund of the Laurel County Fiscal Court: The Laurel County Section 8 Housing fund is not being properly monitored or reported by the Laurel County Fiscal Court. The Laurel County Section 8 Housing Agency (Agency) was formed by the Laurel County Fiscal Court to operate a Section 8 Housing Assistance Payments program. The fund is used to account for the receipts and disbursements of the Agency. The Laurel County Fiscal Court is the local board for the Housing and Urban Development (HUD) office and the county judge/executive is the board chairperson for the Laurel County Housing Authority. The Laurel County Fiscal Court does not prepare a budget for this fund nor do they include it on their quarterly financial reports even though fiscal court created the Agency, administers their retirement costs, signs the disbursements for rental assistance and serves as the Agency's local board.

The county treasurer stated that it was not feasible to include the Section 8 Housing fund as a fund of the fiscal court. She stated that in order for this to happen, all disbursements would have to be approved by fiscal court and due to the nature of the disbursements (low-income data), fiscal court could not risk the disbursements being public record.

Based upon the opinions of the fiscal court and the county treasurer, the Laurel County Fiscal Court has not included the Section 8 Housing fund as a fund of the fiscal court. As a result, this fund is being added as an adjustment to the financial statement to properly present the financial activity of the fiscal court to avoid a material misstatement of the financial statement.

The Section 8 Housing does not have powers granted to it in a corporate charter or enabling legislation. Since it is not legally separate, then accounting standards state it belongs to the primary government, which is the Laurel County Fiscal Court. In addition, the governing board is substantively the same as the primary government's governing board: The fiscal court is the local board for the HUD office and the county judge/executive is the board chairperson for the Laurel County Housing Authority. Therefore, the Section 8 Housing Fund should be included as a fund of the fiscal court.

KRS 68.020(4) states, in part, the county treasurer "...shall keep an accurate detailed account of all money received and disbursed by him for the county and shall keep books of accounts of the financial transactions of the county in the manner required by the uniform system of accounting prescribed by the state local finance officer." In addition, 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 the Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*. The manual requires all money received and paid to be reflected in the county budget and be properly reflected on the financial report as a receipt as well as an "expenditure." Furthermore, all funds disbursed on the fiscal court's behalf by third parties should be recorded in receipts and appropriations ledgers.

We recommend the fiscal court determine whether to continue to operate the Section 8 Housing Agency as an entity of the fiscal court or as a legally separate entity. As a legally separate entity, the fiscal court may choose to pass-through Section 8 federal funds it receives and establish appropriate subrecipient monitoring procedures, but still report the funds in the financial statement as pass-through disbursements. If it is not a legally separate entity, the fiscal court should consider the Section 8 Housing fund like other funds of the fiscal court by budgeting for this fund and including it on the quarterly financial report. In addition, the fiscal court should approve all claims of the Section 8 Housing fund and the county treasurer should receive, receipt, and record all Section 8 Housing funds.

County Judge/Executive's Response: Refer to response 2021-001 Section 8 will be in Laurel Co budget in 2022-2023.

The Laurel County Fiscal Court lacks adequate segregation of duties over occupational tax collections and net profit tax collections: The Laurel County Fiscal Court collects occupational taxes and net profit tax collections as established per local ordinance. These payments are collected either by walk-in or by mail-in payments in the occupational tax administrator's office. The occupational tax administrator and his employees are all responsible for collection of payments, processing payments, and deposit preparation. There is no documented secondary review of these collections.

A limited budget places restrictions on the number of employees the fiscal court can hire to process payments. Without adequate segregation of duties in place over receipt processing, assets could be misappropriated, or errors could occur without detection. Segregation of duties over various accounting functions, such as opening mail, collecting receipts, preparing bank deposits, preparing reports, or the implementation of compensating controls, when needed because the number of staff is limited, 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 strengthen internal controls by segregating duties over occupational tax and net profit tax collections. If segregation is not possible, strong oversight should be implemented. We also recommend the receipts listing be compared to the daily deposit by an individual not involved in the receipt collection process. The employee providing this oversight should document his or her review by initialing all source documentation.

County Judge/Executive's Response: Segregation of duties have been addressed.

The Laurel County Fiscal Court did not accurately report financial information related to debt: The Laurel County Fiscal Court has not budgeted or incorporated funds paid for debt service by a third party on their behalf on the fourth quarter financial statement resulting in the financial statement being materially misstated. The fiscal court issued three separate bonds on behalf of Laurel Housing, which has not been previously recorded on the fiscal court's financial statement or financial records. The bond accounts had a beginning balance of \$67,209, receipts totaling \$1,779,448, and disbursements of \$1,778,693 to pay the debt payments for the fiscal year. The remaining balance as of June 30, 2021 of the bond accounts was \$64,964.

The county judge and county treasurer were unaware the debt service payments made directly by Laurel Housing needed to be processed through the fiscal court's financial records. The fiscal court has helped Laurel Housing obtain funds through bond issues for several years. The financial information for this debt has never been included in the fiscal court's budget or financial statement and the debt has always been paid directly by Laurel Housing. They thought they were handling it correctly since it has not been previously addressed with them.

This deficiency resulted in inaccurate financial reporting to the fiscal court and Department for Local Government (DLG). Misstatements of receipts and disbursements were noted due to errors requiring adjustments on the fourth quarter financial statement as noted above

Strong internal controls over the reporting process are vital in ensuring the fiscal court's financial reports accurately reflect the financial activity of the fiscal court.

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

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 the DLG's *County Budget Preparation and State Local Finance Officer Policy Manual*. The manual requires all money received and paid to be reflected in the county budget and be properly reflected on the financial report as a receipt as well as an "expenditure." Furthermore, all funds disbursed on the fiscal court's behalf by third parties should be recorded in receipts and appropriations ledgers.

We recommend the fiscal court implement stronger internal controls over the reporting process to ensure receipts, disbursements, and cash balances from all bank accounts are properly recorded to the fiscal court's ledgers and to the financial statements submitted to DLG..

County Judge/Executive's Response: This will be corrected on the 2021-2022 financial report.

The Laurel County Fiscal Court failed to implement internal controls to ensure costs submitted for reimbursement were for eligible expenses:

Federal Program: 21.019 – COVID-19 - Coronavirus Relief Fund

Award Number and Year: C327 2020 and C2-156 2020

Name of Federal Agency: U.S. Department of Treasury

Pass-Through Agency: Commonwealth of Kentucky, Department for Local Government – Office of Grants

Compliance Requirements: Activities Allowed or Unallowed; Allowable Costs; Period of Performance

Type of Finding: Significant Deficiency; Noncompliance

Amount of Questioned Costs: \$41,665

COVID Related - Yes

The Laurel County Fiscal Court submitted payroll expenses that did not qualify for reimbursement from the Coronavirus Relief Fund (CRF) administered by the Commonwealth of Kentucky's Department for Local Government (DLG). Reimbursement requests submitted to DLG included accrued vacation leave pay outs totaling \$41,665.

The fiscal court did not have controls in place to ensure expenditures submitted for reimbursement from the CRF were allowable and incurred during the period of availability. The deputy county judge/executive stated she was unaware that some of the payroll expenditures submitted for reimbursement were not allowable.

As a result, the Laurel County Fiscal Court submitted payroll expenses that did not qualify for reimbursement from the CRF administered by DLG. This resulted in \$41,665 of questioned costs. In addition, the fiscal court could be required to repay the questioned costs back to the granting agency.

The Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") established the Coronavirus Relief Fund (the "Fund") and appropriated \$150 billion for payments by Treasury to States, tribal governments, and certain local governments. The CARES Act provides that payments from the Fund may only be used to cover costs that—

1. are necessary expenditures incurred due to the public health emergency with respect to the Coronavirus Disease 2019 (COVID-19);
2. were not accounted for in the budget most recently approved as of March 27, 2020 (the date of enactment of the CARES Act) for the State or government; and
3. were incurred during the period that begins on March 1, 2020 and ends on December 31, 2021.

Initial guidance released on April 22, 2020, provided that the cost of an expenditure is incurred when the recipient has expended funds to cover the cost. Upon further consideration and informed by an understanding of State, local, and tribal government practices, Treasury is clarifying that for a cost to be considered to have been incurred, performance or delivery must occur during the covered period, but payment of funds need not be made during that time (though it is generally expected that this will take place within 90 days of a cost being incurred).

Additionally, 2 CFR § 200.303 requires a non-federal entity to "[e]stablish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award."

Total known questioned costs are \$41,665. Questioned costs were computed by comparing requests for reimbursement to payroll earnings reports to determine the total amount of paid out vacation time included on the requests.

Not a repeat finding.

We recommend the fiscal court strengthen internal controls over federal awards to ensure expenditures submitted for reimbursement are allowable and incurred during the period of availability. We also recommend that the fiscal court contact DLG to determine if questioned costs should be repaid or if they can resubmit requests with eligible expenditures.

County Judge/Executive's Response: The fiscal court will send additional payroll expenses for actual time worked when this program was implemented, we were told by DLG that the coverage included all time. However the court will send additional payroll records so we will comply. In addition, we contacted [name redacted], Executive Director, office of grants @ DLG. She instructed us to submit additional eligible expenditures in the 2021 year to account for the questioned costs totaling \$41,665.00. Our original submission only encompassed 2020-year data. She approved our addition submission See attached email correspondence.

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

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