



Auditor of Public Accounts
Mike Harmon

FOR IMMEDIATE RELEASE

Contact: Michael Goins
Michael.Goins@ky.gov
502.564.5841
502.209.2867

Harmon Releases Audit of Morgan County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Morgan 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 Morgan County Fiscal Court in accordance with accounting principles generally accepted in the United States of America.

Our responsibility is to express an opinion on this financial statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the *Audit Guide for Fiscal Court Audits* issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free from material misstatement. Because of the matter described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

We were not engaged as auditors of the Morgan County Real Properties I and II Corporation Funds and we were unable to obtain audited financial statements to support the Morgan County Real Properties I and II Corporation Funds at June 30, 2020. The Morgan County Real Properties I and II Corporation Funds are part of the Morgan County Fiscal Court's reporting entity. The omission of the Morgan County Real Properties I and II Corporation Funds are considered material omissions of the Morgan County Fiscal Court's financial statement.

Because of the significance of the matter described in the Basis of Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statement.

In addition, Findings 4 and 8 of the audit report will be referred to the Department for Local Government (DLG).

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 Morgan County Fiscal Court does not have internal controls over the Real Properties I and Real Properties II Corporations: This is a repeat finding and was included in the prior year audit report as Finding 2019-001. The county does not have internal controls over the Real Properties I and Real Properties II Corporations. The Real Properties I Corporation was created for the sole purpose of constructing and equipping the health and wellness center and repairing the old Morgan County courthouse for the benefit of Morgan County after the tornado on March 2, 2012. The Real Properties II Corporation was created for the sole purpose of constructing the Morgan County Cooperative Extension Service building, the Morgan County transit station and parking garage, and repairing the Morgan County Community Center for the benefit of Morgan County after the tornado on March 2, 2012. The Morgan County Fiscal Court did not ensure annual financial statements were prepared for the Real Properties I and Real Properties II Corporations. The Morgan County Fiscal Court also failed to obtain an audit of these corporations. We were not engaged as auditors of these corporations and were told that a private firm was conducting these audits. However, as of the date of this report, they have not been audited.

This is caused by a lack of knowledge by county personnel on the activity of these corporations. They have a complex structure and the personnel responsible for the financial statements did not have the knowledge necessary to prepare them.

As a result, the Real Properties I and Real Properties II Corporations have not been audited. These are significant components of the Morgan County Fiscal Court and therefore we have disclaimed an opinion on the financial statement for the fiscal year ending June 30, 2020. Good internal controls dictate that financial statements are timely prepared and audited.

We recommend management of the Real Properties I and Real Properties II Corporations ensure that financial statements are prepared timely and audited as required.

County Judge/Executive's Response: Real Properties I and Real Properties II Corporations have concluded their intended purpose to rebuild and construct properties that were damaged in the 2012 tornado. Since the New Market Tax Credit has concluded, these entities will be dissolved, effectively correcting this finding.

The Morgan County Fiscal Court's general fund owes the road fund due to inappropriate disbursements: This is a repeat finding and was included in the prior year audit report as Finding 2019-002. Below is a chart that depicts how the general fund owes the road fund monies due to various reasons over the past years, including Local Government Economic Assistance (LGEA) funds that should have been spent 100% on road categories (FY 2018), too much truck license fees being transferred to the general fund (FY 2016 and 2017), transfer station disbursements being paid from the road fund (FY 2014 and 2015), and LGEA funds being transferred to the jail fund that should have been used for transportation (FY 2014).

	<u>General Fund</u>	<u>Road Fund</u>	<u>Jail Fund</u>	<u>LGEA Fund</u>
Interfund Receivable (Liabilities) 2014	(138,775)	165,165	(26,390)	
Interfund Receivable (Liabilities) 2015	(143,238)	143,238		
Interfund Receivable (Liabilities) 2016	(200,892)	200,892		
Interfund Receivable (Liabilities) 2017				(24,677)
Credit given for Truck License Not Transferred in FY 2017	150,788	(201,855)	26,390	24,677
Interfund Receivable (Liabilities) 2018	(2,254)	2,254		
Total	<u>\$ (334,371)</u>	<u>\$ 309,694</u>	<u>\$ 0</u>	<u>\$ 0</u>

Since Fiscal Year 2014, the county has not remedied the issues noted and is not in compliance in the use of restricted monies. The liabilities of the general fund have the fund in a deficit and the road fund is being deprived of money that could be used in the fund.

Road monies are restricted by KRS 177.320 and KRS 177.360. Under the regulatory basis of accounting, fund balances are not adjusted for the unpaid liability on the financial statements.

We recommend the Morgan County Fiscal Court remedy the liabilities owed to the road fund as soon as possible and to avoid having deficit balances.

County Judge/Executive's Response: The General Fund will have paid back the Road Fund in full by the end of this current fiscal year 2021-2022.

The Morgan County Fiscal Court does not have internal controls over bank reconciliations: This is a repeat finding and was included in the prior year audit report as Finding 2019-003. Bank reconciliations were not completed for all bank accounts including payroll, rebuild Morgan County, and the Public Properties Corporation. Bank reconciliations that were completed did not appear to be any review by a second party for accuracy.

Mistakes could occur and not be corrected in a timely manner because internal controls were not in place to ensure that bank reconciliations were completed for all accounts and that those were completed were reviewed by a second party. Good internal controls dictate bank reconciliations should be completed for all bank accounts and should reconcile to supporting financial information. A person independent of the posting and reconciliation process should review the reconciliation and original bank statement.

We recommend the fiscal court determine appropriate internal controls to ensure that reconciliations are performed, and they are reviewed by a second party.

County Judge/Executive's Response: Bank reconciliations will be checked by appropriate staff to ensure accuracy and oversight.

The Morgan County Fiscal Court did not accurately report debt on the quarterly financial statement: This is a repeat finding and was included in the prior year audit report as Finding 2019-004. The debt schedule presented with the fourth quarter report (which serves as the year-end financial statement) inaccurately reported debt obligations. The fourth quarter report understated the principal and interest balances for the Morgan County Justice Center Revenue bonds by \$9,577,387 and \$2,175,043, respectively.

The fiscal court does not have controls in place to ensure that debt obligations are properly reported on the fourth quarter report. By not accurately reporting debt, the county is not in compliance with KRS 68.210. In addition, the fiscal court does not have accurate information on which to base financial decisions.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The uniform system of accounts is set forth in the *County Budget Preparation and State Local Finance Officer Policy Manual*, which requires all county debt be reflected properly on the quarterly financial statement.

We recommend the county ensure that the correct amounts are shown all financial statements presented to the public and to the Department for Local Government (DLG). We further recommend the county review all aspects of the quarterly reports before signing and submitting. This matter will be referred to DLG.

County Judge/Executive's Response: All debt is accurately reported, including the Judicial Center debt moving forward.

The Morgan County Fiscal Court did not have adequate internal controls over disbursements: Internal controls associated over disbursements were not operating as intended. Proper procedures for disbursements were not followed to ensure payments were accurate and timely. Taxpayer monies were not properly spent due to late fees and state taxes being paid.

The deficiencies listed below were able to occur due to lack of monitoring of controls and diminish the effectiveness of the internal controls put in place over disbursements by the fiscal court. These deficiencies could create errors in recording or allow for the possibility of misappropriation of assets.

As a result, the following exceptions were noted:

- Six disbursements totaling \$16,736 were not paid within 30 days.
- Three invoices accumulated late fees in the amount of \$39.
- Three invoices included sales tax in the amount of \$100.
- Two invoices totaling \$22,301 did not have supporting documentation.
- Five invoices totaling \$34,489 were not approved by the fiscal court.

- Four receipts for credit card payments could not be provided.
- Encumbrances reported on the fourth quarter report did not agree to report provided by the county treasurer.

KRS 65.140(2) states, in part, “all bills for goods or services shall be paid within thirty (30) working days of receipt of vendor’s invoice except when payment is delayed because the purchaser has made a written disapproval of improper performance or improper invoicing by the vendor or by the vendor’s subcontractor.”

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The uniform system of accounts is set forth in the *County Budget Preparation and State Local Finance Officer Policy Manual*, which requires the fiscal court is required to submit a quarterly report to the state local finance officer and to report all money received to date in all funds both budgeted and unbudgeted. The report should include by fund, all receipts to date, transfers, borrowed money as well as claims allowed since the beginning of the fiscal year for actual and budgeted amounts. This report should also include encumbrances.

Strong internal controls dictate that there be procedures in place to make sure payments are being made on time, and finance charges and sales tax are not being charged.

We recommend the fiscal court implement proper internal controls over disbursements and ensure they are operating effectively.

County Judge/Executive’s Response: All expenditures are run through the monthly vendor claims, unless on standing order. All claims are approved by the Fiscal Court.

The Morgan County Fiscal Court did not follow competitive bidding requirements: The fiscal court did not follow competitive bidding requirements for three different types of goods (rock, asphalt, and pipes) that were purchased from three vendors. The fiscal court and management failed to follow procedures outlined in the county’s administrative code that outline provisions for bidding. The fiscal court and management did not have adequate oversight and review procedures in place to ensure competitive bidding policies and procedures were followed. The fiscal court is in violation of its administrative code and statutes for competitive bidding.

Competitive bidding ensures that the fiscal court procures materials and services at the best price available. 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 thirty thousand dollars (\$30,000) without first making newspaper advertisement for bids.”

In addition, page 125, section 4.02 B of the Morgan County Fiscal Court Administrative Code states, “The County Judge/Executive shall open all bids publicly at the time and place stated in the advertisement and shall select the lowest and/or best bid by a qualified bidder. If the lowest bid is not selected, the reasons for the selections shall be stated in writing.”

We recommend the fiscal court and management abide by the competitive bidding requirements outlined in the county's administrative code and KRS 424.260. We recommend adequate oversight procedures be implemented to ensure this process is followed for any purchases of like type items that exceed \$30,000 during the fiscal year.

County Judge/Executive's Response: The Fiscal Court will follow competitive bidding requirements moving forward. The exception was made to be fiscally responsible and choose multiple bids at the same pricing to be more efficient in executing ongoing projects.

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 2019-006. The following issues were noted for payroll processing:

- Eleven timesheets were not signed by a supervisor.
- One timesheet was missing.
- The payroll revolving account was not reconciled to zero on a monthly basis.
- Retirement contributions did not appear to be accurate or properly recorded. Out of the three months tested, one was paid late, and three employee's matches were paid over to the treasurer but not included on the retirement reports.
- A 1099 was not issued for compensation paid for monthly bookkeeping expenses from Morgan County Real Properties I and II Corporations and Rebuild Morgan County.

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.

Employee hours worked could not be substantiated because the county failed to maintain signed timesheets. Since the payroll account has not been reconciled to zero there could be monies in the payroll account which belong to other funds of the fiscal court. Also, the amount of wages reported to County Employees Retirement System (CERS) determines employees' retirement benefits. It is imperative that the reported wages are complete, accurate, and supported by payroll documentation. Failure to pay accurate amounts to CERS timely can result in penalties and interest charges, which are not an efficient use of taxpayer resources.

KRS 337.320(1) states, in part, "[e]very employer shall keep a record of: (a) The amount paid each pay period to each employee; (b) The hours worked each day and each week by each employee[.]" Payroll revolving accounts are established in order to process individual payroll transactions and should zero out or reconcile to a minimal carrying balance.

KRS 78.625(2) states, "[t]he agency reporting official of the county shall file the following at the retirement office on or before the tenth day of the month following the period being reported: (a) The employee and employer contributions required under KRS 78.610 and 78.635; (b) The employer contributions and reimbursements for retiree health insurance premiums required under KRS 78.5540; and (c) A record of all contributions to the system on the forms prescribed by the systems. KRS 78.625(3) states, "(a) If the agency reporting official fails to file at the retirement

office all contributions and reports on or before the tenth day of the month following the period being reported, interest on the delinquent contributions at the actuarial rate adopted by the board compounded annually, but not less than one thousand dollars (\$1,000), shall be added to the amount due the system. (b) Delinquent contributions, with interest at the rate adopted by the board compounded annually, or penalties may be recovered by action in the Franklin Circuit Court against the county liable or may, at the request of the board, be deducted from any other moneys payable to the county by any department or agency of the state. KRS 78.625(4) states, “[i]f an agency is delinquent in the payment of contributions due in accordance with any of the provisions of KRS 78.510 to 78.852, refunds and retirement allowance payments to members of this agency may be suspended until the delinquent contributions, with interest at the rate adopted by the board compounded annually, or penalties have been paid to the system.”

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: More oversight and internal controls will be implemented to remedy this finding.

The Morgan County Fiscal Court did not establish adequate controls over the justice center corporation fund: The fiscal court did not maintain adequate controls over the justice center corporation fund. No financial statements were prepared for these funds and no information regarding the activity in these funds was submitted to the fiscal court for review. Also, the county’s debt schedule presented with the fourth quarter report (which serves as the year-end financial statement) did not report debt obligations of the Morgan County Justice Center Bonds, resulting in an understatement of debt of \$11,895,043.

The treasurer was unaware she had to prepare a financial statement for the justice center corporation fund. By not preparing an annual financial statement, the fiscal court is not aware of the transactions that are occurring relating to the receipts and disbursements of the unbudgeted funds. This could result in undetected fraud, errors, and misstatements. Also, not presenting all debt that the county has outstanding does not give users of the county’s financial information a true picture of the county’s financial well-being. The fiscal court is financially accountable and legally obligated for the justice center corporation fund. The fiscal court should establish adequate controls over these funds so that proper records are maintained, and complete and accurate information is available for review.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The uniform system of accounts, set forth in the *County Budget Preparation and State Local Finance Officer Policy Manual*, requires all county debt be reflected properly on the quarterly financial statement.

We recommend the county treasurer reconcile these accounts and prepare a financial statement for the justice center corporation fund and include all debt of the county on the quarterly financial statement as required. This matter will be referred to the Department for Local Government (DLG).

County Judge/Executive's Response: A ledger is now maintained to establish adequate controls over the Justice Center Corporation Fund.

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

###

The Auditor of Public Accounts ensures that public resources are protected, accurately valued, properly accounted for, and effectively employed to raise the quality of life of Kentuckians.

Call 1-800-KY-ALERT or visit our website to report suspected waste and abuse.

