



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

August 6, 2020

James Shepherd, Mayor
PO Box 640
Salyersville, KY 41465

Dear Mayor Shepherd:

The Auditor of Public Accounts (APA), in response to concerns expressed to this office regarding financial management and oversight of tourism funds collected by the City of Salyersville (City), initiated an examination to evaluate those concerns. The purpose of this examination was not to provide an opinion on the City's financial statements, but to review specific matters brought to our attention and make recommendations to strengthen and improve internal controls to ensure the City's financial management activities are accurate, transparent, and follow applicable statutes.

As part of this examination, the APA reviewed information related to the City, such as policies, procedures, ordinances, and council meeting minutes, analyzed financial information, such as accounting ledgers, bank statements, invoices, financial statement audits, and payroll tax documentation, interviewed relevant parties, including the Mayor, City financial staff, Salyersville Tourism Commission (Commission) Members, and the Supervisor for Salyersville's Street Department, and performed other procedures deemed necessary. Unless otherwise indicated, the examination period of this engagement was July 1, 2017 through April 30, 2019.

Two major findings emerged from the examination. Both result from a lack of oversight – the first by the City and the second by the Commission, which appears to have not met since 2009. The findings and corresponding recommendations are discussed below. Due to the nature of these findings, matters addressed in this letter will be referred to the Kentucky Office of Attorney General, the U.S. Department of Housing and Urban Development, as well as the Salyersville Board of Ethics.

1. City provided limited oversight of contract personnel paid through tourism funds, and one contractor, who is also the Mayor's son, reported working approximately 224 hours of duplicate time on behalf of the City and the Magoffin-Salyersville Housing Authority between July 24, 2017 and June 23, 2018.

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Review of City contract employee timesheets submitted for fiscal year 2018 and paid from tourism funds found approximately 78% of those timesheets provided to the APA contained no indication of supervisory review or approval. Two of these City contractors were identified as sons of the Mayor, who began working as contractors for the City in December 2012 and June 2013. City personnel gave conflicting responses as to who supervised the work of the two sons. While the Mayor indicated that he, along with the City Street Superintendent, would make assignments and review the work performed, the City Street Superintendent and other City personnel indicated that the Mayor was the Supervisor for the work performed by his sons. Beyond the time sheets previously mentioned, the City was unable to provide a copy of the labor contracts or any documentation for work performed by his sons/contractors.

If the Mayor is serving as supervisor to his sons in fact or appearance, this creates a conflict of interest and an apparent violation of the City’s Code of Ethics. The City’s Code of Ethics specifies that “[n]o officer or employee of the city ... shall supervise or manage the work of a family member” and that “[n]o family member of the governing body (Mayor or City Council) shall hold a paid position with the City or any of it’s [sic] entities.”

Additionally one son who performed contract labor for the City until May 3, 2019, was identified as being employed at the same time in FY 2018 by the Magoffin – Salyersville Housing Authority (Housing Authority) as its Executive Director. A comparison of time sheets submitted by the contractor to both the City and the Housing Authority for the aforementioned period identified 148 instances in which the time recorded as work time on the city contractor’s timesheet overlapped with the time he reportedly worked at the Housing Authority. These instances resulted in the submission of approximately 224 hours of duplicate time by the contractor. Based on the documentation and information provided it is unclear which entity paid the contractor/Executive Director for work not performed. Regardless, it is clear that the contractor/Executive Director charged duplicate hours to the City and the Housing Authority, both of which are publicly funded. Figure 1 shows a sample of the discrepancies recorded for one week.

Figure 1: Examples of duplicate time submitted by the Mayor’s son

<i>Day</i>	<i>Housing Authority Timesheet</i>		<i>City Timesheet</i>		<i>Amount of time submitted in conflict</i>
	<i>In</i>	<i>Out</i>	<i>In</i>	<i>Out</i>	
5/28/2018	8:30 AM	2:30 PM	8:00 AM	4:00 PM	6 hours
5/29/2018	8:18 AM	4:18 PM	2:30 PM	6:30 PM	1 hour, 48 minutes
5/30/2018	7:36 AM	3:25 PM	2:30 PM	6:30 PM	55 minutes
5/31/2018	8:30 AM	3:49 PM	2:30 PM	6:30 PM	1 hour, 19 minutes
6/1/2018	7:58 AM	2:52 PM	2:30 PM	6:30 PM	22 minutes
Total time recorded in conflict					10 hours, 24 minutes

Source: APA based on timesheets provided by the City of Salyersville and the Magoffin – Salyersville Housing Authority.

We recommend the City enforce the requirements that no family member of the Mayor or a City Council member hold a paid position with the City or any of its affiliated entities and that no officer or employee oversee or manage the work of a family member. In addition, we recommend that the City require all timesheets to be approved by an appropriate supervisor before being paid. Finally, we recommend the Tourism Commission and the Housing Authority seek legal guidance to determine whether any portion of funds paid to the contractor/Executive Director for duplicate hours may be recouped.

2. The City expended tourism funds for non-tourism related purposes without input or approval of the Salversville Tourism Commission.

City records indicate that the Commission has not met since August 6, 2009; however tourism funds have continued to be spent by the City, often for non-tourism purposes. In a sample of 63 expenditures from the tourism funds during the period of July 1, 2017 through April 30, 2019, 48 did not appear to be tourism related, such as spending on health insurance for city workers, excavation of a county road, and “payday advances” to a city contractor. While many of those 48 expenditures appeared to be related to the general operation of a city, by state law it should be the responsibility of the Commission to oversee the use of tourism funds and make the determination of whether or not an operating expense of the City is a valid use of those funds. Additionally, tourism funds, like other public funds, should not be used for personal purposes.

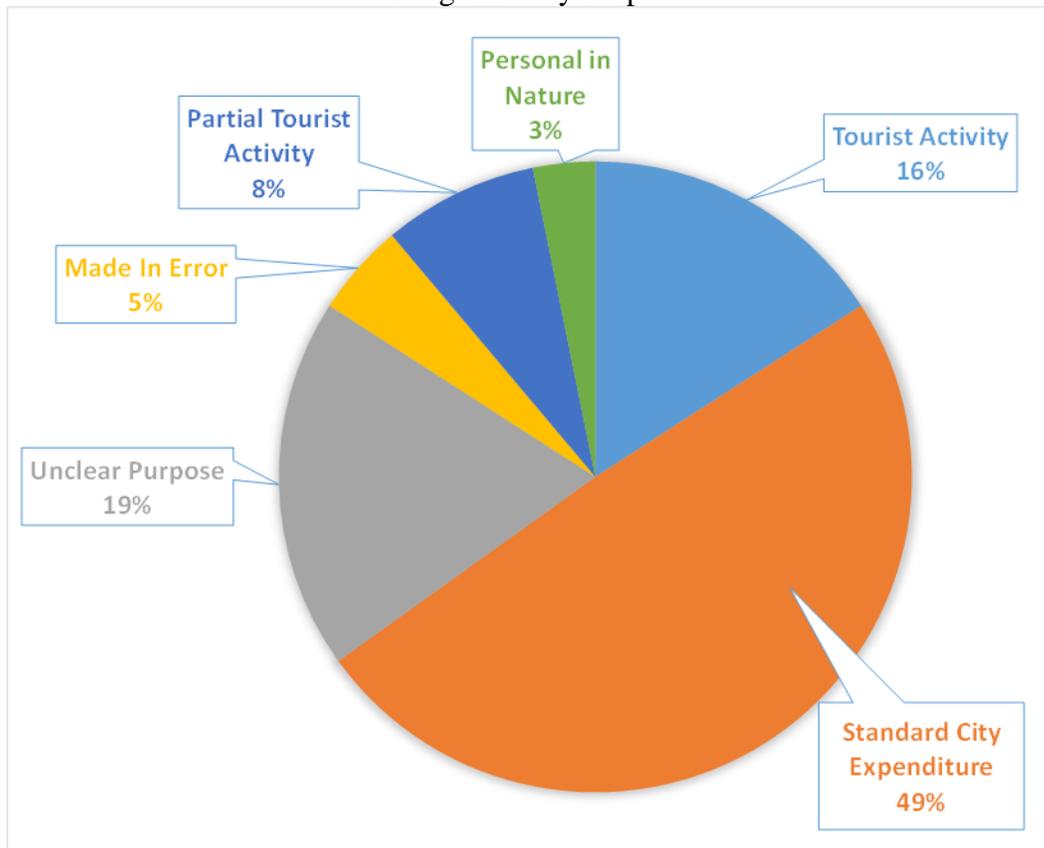
In February 1997, the City enacted a restaurant tax to generate funds for the operation of the Commission and to promote tourism within the City. Although KRS 91A.360 requires the tourism and convention commission to oversee the use of monies collected through the enactment of a restaurant tax, the Commission has not played an active role in the use of those funds since August 6, 2009, the last meeting of the Commission as reported by the Mayor. While the City has attempted to appoint members to the Commission since that time, it has not ensured regularly scheduled meetings of the Commission have occurred.

Statutory guidance on the use of tourism funds is non-specific other than to simply require the funds be used for the purpose of tourism. The lack of statutory restrictions places greater importance on the need for an independent board or commission to make decisions concerning the use of the funds. Without an active commission to make decisions on how the funds are to be spent, the tourism fund has in essence become just another fund of the City, falling under the discretion of the Mayor and the City Council.

While not specifically addressing allowable uses of tourism funds, both the Kentucky Constitution and KRS 65.125 emphasize that reallocating tax proceeds for a purpose other than intended is not permissible. Section 180 of the Kentucky Constitution specifically states that ordinances which levy a tax, such as the City’s restaurant tax, “shall specify distinctly the purpose for which said tax is levied, and no tax levied and collected for one purpose shall ever be devoted to another purpose.” KRS 65.125(4) reiterates this by stating that “[t]he revenues generated shall be ... used solely for the specified project, program, or service as designated by the ordinance enacting the tax.”

In an effort to evaluate whether or not restaurant tax proceeds were used for the specified purpose of promoting tourism and supporting the Commission, auditors sampled 63 expenditures from the hand-written disbursement ledgers of the Tourism fund covering the period July 1, 2017 through April 30, 2019. Figure 2 depicts the categorization by purpose of expenses examined in the sample.

Figure 2: Sample of Tourism Fund Expenditures from July 1, 2017 and April 30, 2019, Categorized by Purpose



Source: APA, based on a sample of Tourism Fund expenditures examined from the period July 1, 2017 through April 30, 2019.

Of the 63 expenditures sampled, 10 transactions (16%) appeared entirely related to tourism, five transactions (8%) appeared to be partially related to tourism, 12 transactions (19%) had an unclear purpose, and three transactions (5%) were made in error. Approximately 49% (31 transactions) of tourism fund expenditures examined from the period July 1, 2017 through April 30, 2019 appeared to be associated with the general or standard operation of a city rather than supporting the Commission and its goal to increase tourism.

Examples of expenditures identified as a Standard City Expenditure or as having an Unclear Purpose include:

- Contract labor for three people for election work \$360
- Mowing a cemetery \$250

- Payment of two city workers' medical bills \$263
- Health insurance for city workers \$1,662
- Christmas gifts to be given away at community event \$2,502
- Excavation of public road \$1,120
- Concrete work for tornado shelter \$5,000
- General use gasoline \$2,919
- Portion of workers compensation insurance \$13,187
- Monthly financial support for rescue squad \$1,000
- Coffee for City Hall and Fire Department \$259
- Pumper truck for Fire Department \$4,000
- Boots for street department workers \$1,378
- Gasoline for storm victims \$249
- Laundering uniforms for 5 workers \$122
- Contract labor for Street and Parks Departments \$342

Finally, two of the sixty-three expenditures (3%) appeared personal in nature. First, the City paid \$367 to a local florist from tourism funds on April 25, 2018. The bill consisted of an unknown balance of \$267 carried forward and charges for two \$50 arrangements of funeral flowers. Flowers for funerals are personal in nature and are not a valid use of public funds. Second, on August 2, 2018, the City used Tourism funds to make a "payday advance" of \$800 to a contract worker who normally is paid from the General fund. Documentation of the advance indicates that the worker already had a cumulative balance of \$700 owed to the City from prior "payday advances." While the City describes these payments to the city contractor as "payday advances," the payments function as a series of interest-free personal loans from public funds. Regardless of the classification, such action by the City is in direct conflict with Section 3 of the Kentucky Constitution, which requires that any payment to a public employee be for consideration of public service (in other words, salary and wages for work performed).

While state statutes do not define "personal expenditures," the Commonwealth's highest court has offered guidance in this void. In *Funk v. Milliken*, 317 S.W.2d 499 (Ky. 1958), Kentucky's highest court reaffirmed that expenses should be "reasonable in amount, beneficial to the public, and not predominately personal to the officer in the sense that by common understanding and practice they are considered to be personal expenses." While this ruling was specifically for county officials, all public officials entrusted with control of public funds should expend those funds in such a manner for the benefit of the taxpayers.

Without an active Commission to make decisions on how tourism funds were to be spent or policies by the City as to the allowable uses of public funds, personal expenditures like the ones identified in the sample could continue to occur, despite guidance from the state level.

Mayor James Shepherd

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We recommend the City reestablish routine meetings of the Commission, reappoint members, if necessary, and transfer oversight of tourism funds to the Commission to ensure tax proceeds are used in accordance with the purpose of the Ordinance.

We recommend the City discontinue the practice of issuing loans or pay advancements from public funds.

We also recommend the Commission work with the City to create and enforce a policy describing the types of expenditures that are and are not appropriate for payment with funds received from the restaurant tax. This policy should include a prohibition of expenditures which are personal in nature and expenditures that are not tourism related or approved by the Commission.

Thank you for your attention to this matter. 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 stroke at the end.

Mike Harmon

Auditor of Public Accounts

CC Tommy Bailey, City Councilmember
Michael Connelley, City Councilmember
Patricia Frazier, City Councilmember
Herbert Tex Holbrook, City Councilmember
Jarrod Howard, City Councilmember
Paul Montgomery, City Councilmember