



Auditor of Public Accounts
Mike Harmon

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

Harmon Releases Audit of Todd County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Todd County Fiscal Court for the fiscal year ended June 30, 2022. 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 Todd 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 findings:

The Todd County Fiscal Court failed to implement adequate internal controls to ensure complete and accurate accounting records were maintained: The fiscal court failed to provide adequate oversight, allowing the county treasurer complete control over the accounting and reporting functions. The following errors and reporting violations were noted during the performance of the audit:

- The fourth quarter financial report was inaccurate:
 - The June 9, 2022 and June 23, 2022 payrolls in the amount of \$151,877 were omitted.

- Only \$70,225 of the \$232,225 received for the sale of a solid waste truck was recorded.
- Failed to record \$11,505 in interest earned on CDs.
- Recorded proceeds from CDs redeemed in the amount of \$391,902 as miscellaneous revenue.
- Posted \$11,200 for a sheriff's employee to the solid waste fund.
- Budget amendments #2 and #3 in the amounts of \$300,000 and \$20,757, respectively, adopted by the fiscal court on February 25, 2022 and May 11, 2022, were not entered into the accounting software by the county treasurer.
- Budget appropriations were overspent for general fund capital projects line item in the amount of \$41, road fund general government line item by \$8,576, jail fund debt service line item by \$334, and economic assistance fund capital projects line item by \$1,528,782.
- The cash balances and financial activity of the jail and economic assistance bond accounts were not accounted for on the fourth quarter financial report. As a result, the economic assistance fund receipts were understated by \$404, expenditures were overstated by \$56,724, and the ending cash balance was understated by \$1,175,277. Additionally, expenditures of the jail fund were understated by \$334.
- The Tax Revenue Anticipation Note, Series 2022 proceeds of \$1,528,782 and the corresponding land purchase were omitted from the fourth quarter financial report. In addition, the total budget of the economic assistance fund was overspent by \$1,471,877.

The Todd 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, without adequate oversight. Additionally, this was the county treasurer's first year serving as county treasurer; therefore, she was learning all accounting concepts and responsibilities.

Due to the fiscal court's lack of effective oversight of the treasury's functions, and the treasurer's lack of full understanding of her duties as prescribed by the Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*, the deficiencies, noncompliances, and undetected errors noted above pertaining to required record-keeping were allowed to occur. Also, by not including all budget amendments into the accounting software and presenting them accurately on the fourth quarter financial report, the fiscal court could spend over amounts budgeted for funds. 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 preparation and reporting processes are vital to ensure the fiscal court's financial reports accurately reflect the financial activity of the fiscal court, as well as adhere to applicable laws and regulations.

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 "[p]repare a quarterly financial report for the State Local Finance Officer." The manual also provides a format to be used when

preparing the quarterly financial statement. This format includes reporting original budget estimates, budget amendments, and actual receipts and disbursements and totals available in each line item.

KRS 68.020(4) states the county treasurer, “[s]hall 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.”

KRS 68.300 states, “[a]ny appropriation made or claim allowed by the fiscal court in excess of any budget fund, and any warrant or contract not within the budget appropriation, shall be void. No member of the fiscal court shall vote for any such illegal appropriation or claim. The county treasurer shall be liable on his official bond for the amount of any county warrant willfully or negligently signed or countersigned by him in excess of the budget fund out of which the warrant is payable.”

We recommend the Todd 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.

County Judge/Executive’s Response: As the county anticipates new debt, if any, appropriate reporting measures will take place and if new debt occurs, appropriate reporting measures and budget amendments will be implemented. New accounting software was purchased by the county, enabling the new treasurer to understand requirements more accurately. Payrolls are completed by the Finance Officer, signed off on by the Treasurer and triple checked by the Judge Executive. All receipts received from surplus or sale will be recorded in its entirety rather than splitting into appropriate funds. Budget appropriations will be recorded in new software by the Treasurer, checked by the Finance Officer and approved by court, then entered into court meeting minutes. Budget amendments will be entered into accounting software and reviewed by Treasurer and Finance Officer. New software and support by the software will strengthen these controls.

The Todd County Fiscal Court did not have adequate controls over disbursements: This is a repeat finding and was included in the prior year audit report as Findings 2021-001 and 2021-002. During Fiscal Year 2022, the Todd County Fiscal Court had material weaknesses in internal control and noncompliances over disbursements. The following findings were noted regarding the Todd County Fiscal Court’s disbursements:

- One invoice of \$4,200 was not paid within 30 days.
- Encumbrances were not reported on the fourth quarter financial statement nor were a list of encumbrances maintained by the county.
- Purchase orders were not properly utilized. Of the 23 total transactions tested, 11 purchase orders totaling \$1,205,141 were not dated. Three purchase orders totaling \$4,843 were dated after the invoices were received. Finally, one purchase order totaling \$182,157 was not signed by the finance officer.
- There was not adequate documentation for two transactions on a credit card statement totaling \$25.

According to the county treasurer, the findings listed above were due to an oversight and lack of knowledge regarding the reporting of encumbrances.

Failure to pay obligations timely (within 30 days) is indicative of poor financial management practices and can result in late fees and finance charges, which are poor use of taxpayer resources. Also, by not maintaining itemized invoices, purchases could be made, which are personal in nature. When failing to maintain adequate documentation, the fiscal court is increasing the risk of paying invoices for goods and services that are not allowable or were not provided to the county. Additionally, the county was not in compliance with various state statutes when not properly documenting purchase orders, reporting encumbrances, or paying invoices within 30 working days.

KRS 65.140(2), states, in part, “[a]ll bids for goods and services shall be paid within thirty (30) working days of receipt of a vendor’s invoice[.]”

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 Department for Local Government’s (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual* which requires the county to disclose encumbrances on the face of the fourth quarter financial report. It also requires a purchase order system for all counties and each county is responsible for ensuring their purchase order system is executed and working properly.

According to a memorandum from DLG dated August 4, 2016, “[t]he main purpose of this system is to ensure that purchases can be made if there are sufficient appropriations available within the amount of line items in the county’s budget. Because of this, it is a requirement by the State Local Finance Officer that all counties have a purchase order system and follow the guidelines prescribed on Page 54 of the *County Budget Preparation and State Local Finance Officer Policy Manual*”. Furthermore, “DLG highly recommends that counties accept that practice of issuing PO’s for payroll and utility claims.”

Good internal controls dictate that adequate supporting documentation be maintained for all disbursements and credit card transactions. All vendor invoices and receipts should be maintained including any additional supporting documentation and agreed to the corresponding purchase order and reports. Furthermore, good internal controls also dictate the fiscal court monitor line items to ensure that there is ample cash and budget appropriations prior to approving payment of bills.

We make the following recommendations to the fiscal court:

- All invoices should be paid within 30 days of receipt of the vendor’s invoice in accordance with KRS 65.140(2).
- A list of encumbrances should be maintained by the county and reported on the quarterly reports in accordance with DLG requirements and KRS 68.210.
- Internal control procedures regarding purchase orders should be strengthened by requiring that purchase orders be issued prior to purchases being made or services rendered in accordance with DLG requirements and KRS 68.210.

- Proper documentation should be maintained for all disbursements to properly support claims.

County Judge/Executive's Response: New accounting software has been purchased by the county. Encumbrances will be reported on the quarterly reports and for upcoming fiscal year, including purchase orders. New software generates electronic purchase orders, where in the past were handwritten. This will allow the Finance Officer stronger controls over payment and obligations. Finance Officer and Treasurer will work together to ensure proper documentation for county spending going forward.

The Todd County Fiscal Court failed to approve all cash transfers: The Todd County Fiscal Court failed to approve all cash transfers made by the county treasurer. We tested 13 cash transfers totaling \$1,440,297. Four cash transfers totaling \$511,180 were not approved by the fiscal court. Two cash transfers totaling \$224,117 should have been appropriation transfers and not cash transfers. Lastly, the fiscal court approved cash transfers on October 22, 2021, however the fiscal court orders did not disclose the funds from which the transfers were being made or the amounts of the transfers.

The county treasurer wasn't sure why all the cash transfers were not approved by fiscal court, but she thought some of the issues were due to her being new a new county treasurer and mixing up appropriation transfers with cash transfers. It was her belief that it was just an oversight that the detail for the October 22, 2021 was omitted from the fiscal court orders. By not having fiscal court approval for cash transfers, the risks for misappropriation increases and limits the controls to ensure financial records are accurate.

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* states, "[a]ll transfers require a court order." Additionally, good internal controls dictate that all transfers be approved by fiscal court prior to being made by the county treasurer and the fiscal court orders should include the funds the transfers are being made from/to, as well as the amount of the transfers.

We recommend all cash transfers be approved by fiscal court prior to being made by the county treasurer, and the fiscal court orders include the funds the transfers are being made from/to, as well as the amount of the transfers.

County Judge/Executive's Response: Fiscal Court was made aware of transfers but documentation was not provided due to an oversight and misunderstanding of the county treasurer. New implemented software has allowed the treasurer with a better understanding of cash transfers and appropriation transfers. Going forward the county treasurer will ensure that fiscal court approves all transfers and appropriate documentation will be included in the recorded minutes.

The Todd County Fiscal Court's schedule of leases was materially misstated: The Todd County Treasurer prepared a schedule of leases for Fiscal Year 2022; however, this schedule was materially misstated. The June 30, 2022 outstanding balance for the lease between the Todd

County Fiscal Court and the Administrative Office of the Courts (AOC) for the AOC building was disclosed as \$960,000, when the outstanding balance should have been \$6,336,059. Additionally, the value of payments received for the current fiscal year were \$160,000 but should have been \$790,294.

These misstatements were caused by a lack of fully understanding the new reporting requirements. Because the county's schedule of leases was misstated, the Todd County Fiscal Court was not compliant with the requirements of Governmental Accounting Standards Board (GASB) Statement 87.

GASB Statement No. 87 establishes standards of accounting and financial reporting for leases by lessees and lessors. The note disclosure requirements of this Statement apply to financial statements of all regulatory basis local governments as required by the regulator, the Department for Local Government (DLG).

Additionally, strong internal controls dictate that the fiscal court maintain an up-to-date schedule of leases to ensure note disclosures are complete and accurate.

We recommend the Todd County Fiscal Court maintain an up-to-date schedule of all leases and follow the standards set forth by DLG and GASB 87 to ensure note disclosures are complete and accurate.

County Judge/Executive's Response: County Treasurer did not fully understand the new reporting requirements leading to the misstatements. Going forward the county treasurer will prepare the GASB Statement 87 appropriately.

The Todd County Jail does not have adequate segregation of duties over the jail commissary and inmate accounts: The Todd County Jail does not have adequate segregation of duties over the jail commissary and inmate accounts. The same deputy prepares deposits and daily checkout sheets for both accounts, and posts to the receipts ledgers for the inmate account. The same deputy can also write and sign checks for both accounts, posts to the disbursements ledger for the inmate account, and prepares the monthly bank reconciliations. Compensating controls such as the review of reconciliations by another deputy, review and initialing of invoices by the jailer, and the requirement of dual signatures on all checks from the inmate fund were implemented but are not functioning as designed to prevent and detect errors.

Due to the small size of staff and limited resources, the Todd County Jail has limited options for establishing segregation of duties. The lack of segregation of duties could result in misappropriation of assets and inaccurate financial reporting to external agencies such as the Department for Local Government (DLG), which could occur but go undetected.

Good internal controls dictate that duties over the various accounting functions such as preparation of deposits, checkout sheet preparation, posting to ledgers, preparation of checks, and preparation of reconciliations be segregated in order to lower the risk of misappropriation of assets and inaccurate financial reporting occurring and going unnoticed.

We recommend the Todd County Jail segregate duties to the extent possible. If proper segregation of duties is not possible due to budget constraints, we recommend that the Todd County Jail implement effective compensating controls over jail commissary and inmate accounts.

Jailer's Response: The jail has a small, limited staff size. A compensating control on the Jail Commissary account will be to add an extra signature for all purchases.

County Judge/Executive's Response: The Todd County Fiscal Court is always willing to help, within reason, the Jailer in whatever area that is lacking. We will defer to the Jailer for specific actions.

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

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