



Auditor of Public Accounts
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FOR IMMEDIATE RELEASE

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Harmon Releases Audit of Clay County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Clay County Fiscal Court for the fiscal year ended June 30, 2018. 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 Clay 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 115 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 Kentucky Infrastructure Authority debt payments were not paid as required by the debt agreement: The Kentucky Infrastructure Authority (KIA) debt payments were not made in accordance with the debt schedule as required by the agreement with KIA. The schedule requires 12 monthly payments of \$12,582 to be made the first of each month; however, only seven payments were made during the fiscal year. Principal payments and interest payments totaling \$49,335 and \$14,495, respectively were not made for the last five months of the fiscal year.

The Clay County Fiscal Court entered into the debt with KIA in order to obtain funding for waterlines on behalf of North Manchester Water Association. The fiscal court further entered into a lease agreement with North Manchester Water Association where they would make lease

payments equaling the debt service payments directly to KIA. North Manchester made payments through January 2018 but then failed to make required subsequent payments as required by the lease agreement.

The county is in default on the debt agreement with KIA by not ensuring proper debt payments were made in accordance with their agreement.

The loan agreement the county entered into with KIA requires monthly loan payments to be made the first of each month in accordance with the debt amortization schedule.

We recommend the Clay County Fiscal Court comply with the terms of the KIA agreement by making all required debt payments in the future. We further recommend the fiscal court contact KIA in order to become in compliance with the terms of the agreement regarding unpaid principal and interest payments. In addition, the county should consult with the county attorney regarding the agreement in place with North Manchester Water Association.

County Judge/Executive's Response: Have met with North Manchester Water Association and Co. Attorney to try and work out a solution. NMW advised they have requested a rate increase which would cover the loan payment amount.

The Clay County Fiscal Court lacks adequate segregation of duties over receipts: This is a repeat finding and was included in the prior year audit report as Finding 2017-002. The Clay County Fiscal Court does not have adequate segregation of duties over receipts. The county treasurer opens mail, prepares all deposits, posts to receipt ledgers, and prepares bank reconciliations. In January 2018, the receipt process was changed and the secretary started opening the mail and creating a receipt list. This list was compared to the deposit slip which is still prepared by the treasurer. The treasurer posts to the receipt ledgers and prepares the bank reconciliation with no documented review.

A limited budget places restrictions on the number of employees the fiscal court can hire. When faced with a limited number of staff, strong compensating controls should have been implemented to offset the lack of segregation of duties.

The lack of oversight could result in undetected misappropriation of assets and inaccurate financial reporting to external agencies such as the Department for Local Government (DLG).

Segregation of duties over various accounting functions, such as opening mail, collecting receipts, preparing bank deposits, preparing reports and reconciliations, 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.

To adequately protect against undetected misappropriation of assets and inaccurate financial reporting, we recommend the fiscal court separate the duties involving the opening of mail, collecting and depositing of receipts, and preparation of reports and reconciliations. If this is not

feasible due to a limited budget, strong oversight over these areas could occur and involve an employee that isn't currently performing any of those functions. Additionally, the county judge/executive could provide this oversight and document it on the appropriate source documents.

County Judge/Executive's Response: This is due to low office staff. Two people in County Judges Office does record receipts.

The Clay County Fiscal Court lacks adequate segregation of duties over occupational tax receipts: The Clay County Fiscal Court does not have adequate segregation of duties over occupational tax receipts. The occupational tax clerk sends out occupational tax bills, opens mail, matches the checks to the occupational tax bills, prepares a list of receipts, prepares deposits, posts receipt to the tax manager program, and compares the deposits to the receipt list and the report produced by the tax manager program. The deposit is taken to the bank by the occupational tax clerk or the tax administrator. The original deposit slip is provided to the county treasurer who compares the deposit slip to the bank statement and prepares bank reconciliations. No documented review of the receipt process was noted.

The county has two employees working in the occupational tax office. In addition, occupational tax information is restricted and can only be accessed by authorized personal. This along with a limited budget, places restrictions on the number of employees the fiscal court can hire. When faced with a limited number of staff, strong compensating controls should have been implemented to offset the lack of segregation of duties.

The lack of oversight could result in undetected misappropriation of assets and inaccurate financial reporting to external agencies such as the Department for Local Government (DLG).

Segregation of duties over various accounting functions, such as opening mail, collecting receipts, preparing bank deposits, preparing reports and reconciliations, 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.

To adequately protect against undetected misappropriation of assets and inaccurate financial reporting, we recommend the fiscal court separate the duties involving mailing of the bills, opening of mail, preparing the receipt list, collecting and depositing of receipts, and preparation of the deposit. If this is not feasible due to a limited budget, strong oversight over these areas could occur and involve an employee that isn't currently performing any of those functions.

County Judge/Executive's Response: This is due to low Office Staff, financially unable to change the office staff at this time.

The Clay County Fiscal Court does not have adequate internal controls over the purchase order system: This is a repeat finding and was included in the prior year audit report as Finding 2017-006. The Clay County Fiscal Court is not properly utilizing a purchase order system. The purchasing procedures in place do not comply with the required purchase order system required

by the state local finance officer. In addition, the internal controls over the purchase order system allowed the system to be circumvented. As a result, four invoices were paid before a purchase order was issued.

Internal controls over purchase orders were not operating as intended during Fiscal Year 2018. The treasurer stated that each department has been giving guidelines for making purchases; however, some still fail to follow guidelines and will make purchases without receiving a purchase order.

As a result of not monitoring controls, the county could over spend their line item budget amounts.

Proper internal controls over disbursements are important to ensure purchase orders are created when sufficient funds are available. KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. According to the *County Budget Preparation and State Local Finance Officer Policy Manual*, issued by the Department for Local Government, “[p]urchases shall not be made without approval by the judge/executive (or designee) and/or department head” and “[p]urchase requests shall not be approved in an amount that exceeds the available line item appropriation unless the necessary and appropriate transfers have been made.”

We recommend the Clay County Fiscal Court strengthen internal controls by ensuring that purchases orders are issued for all disbursements and sufficient funds are available prior to issuing a purchase order.

County Judge/Executive's Response: The County Judge/Executive has advised all Departments to call for purchase orders.

The Clay County Fiscal Court did not obtain bids when required: This is a repeat finding and was included in the prior year audit report as Finding 2017-007. The Clay County Fiscal Court did not properly bid \$85,175 to one vendor. For Fiscal Year 2018, fiscal court orders documented that multiple bids were accepted and approved on bids for contracts for steel drilling and road pipe instead of choosing one bid. The vendor that was paid over \$20,000 was the secondary bidder. According to the county, they were unaware that multiple bids could not be accepted.

By limiting competition or not receiving bids at all, the fiscal court may not get the benefits of the best price available. Competitive bidding ensures the fiscal court procures equipment and services at the best price available.

KRS 424.260(1) states, in part, “[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 perishable meat, fish, and vegetables, equipment, or for contractual services other than professional, involving an expenditure of more than twenty thousand dollars (\$20,000) without first making newspaper advertisement for bids.” In addition, fiscal court’s own administrative code requires that purchases over \$20,000 be bid.

KRS 178.140(1)(2) states, “[a]ll bids for the construction or maintenance of county roads and bridges shall be received at the time and place specified in the advertisement, and shall be opened publicly at the time of awarding, and the amount of items comprising each bid shall be publicly announced. The contract shall be awarded to the lowest and best bidder, who shall furnish satisfactory security in an amount equal to the amount of the contract in question, to be approved by the county judge/executive of the county.”

We recommend the Clay County Fiscal Court follow proper bid laws and regulations by ensuring all purchases of \$20,000 or more be made in compliance with KRS 424.260.

County Judge/Executive’s Response: In the future the Clay County Fiscal Court will accept only one vendor per bid.

The Clay County Fiscal Court lacks internal control over payroll: This is a repeat finding and was included in the prior year audit report as Finding 2017-009. The Clay County Fiscal Court does not have proper internal controls over the payroll process. During the fiscal year ending June 30, 2018, the following issues were noted:

- Four timesheets did not annotate actual hours worked.
- One timecard was approved without employee signature.
- Three timecards were processed without supervisor approvals.
- One employee was paid without timecard documentation.
- Four timesheets were not calculated correctly.
- One employee worked more than 40 hours in a week without receiving compensatory time.
- One employee timesheet was not accurate.

Weak internal controls over payroll have allowed these issues to go undetected. As a result, the fiscal court is not in compliance with federal and state labor regulations or the county’s administrative code.

KRS 337.320(1) requires every employer to “keep a record of: (a) [t]he amount paid each pay period to each employee; (b) [t]he hours worked each day and each week by each employee; and (c) [s]uch other information as the commissioner requires.”

Clay County Administrative Code Section XII: Personnel Policies and Procedures (1)(a) states, “Hours of Work (a) The work day shall consist of not less than eight (8) consecutive hours, and the work week shall consist of at least forty (40) hours in five (5) consecutive days.” Additionally, Amendment #6 of the Clay County Administrative Code states, “[a]ll salary personnel working for Clay County, Kentucky shall be allowed to accumulate one-half (1/2) day each month for vacation time” and “[a]ll salary personnel working for Clay County, Kentucky shall be allowed to accumulate one-half (1/2) day each month for sick leave time.”

Timesheets should be kept for payroll verification, as a record of leave time used, and to document employees are working at least the minimum number of hours to be eligible for full-time benefits such as retirement and health insurance.

Section 213(a)(1) of the Fair Labor Standards Act exempts bona fide executive, administrative, and professional employees, outside sales employees, and certain skilled computer professionals from both the minimum wage and overtime pay requirements.

We recommend the Clay County Fiscal Court strengthen internal controls over payroll by requiring employees and supervisors to sign timecards, ensure timecards reflect actual hours worked, keep leave balances current on all employees, and require all employees to maintain timecards. We further recommend the Clay County Fiscal Court obtain a legal opinion from the county attorney as to whether county employees considered salaried qualify as such under labor laws.

County Judge/Executive's Response: Salaried employees and supervisors have been notified of turning in documentation of hours worked. We have also advised them to have time sheets/cards signed.

The Clay County Fiscal Court did not maintain all haul tickets for asphalt: The Clay County Fiscal Court is responsible for maintenance of county roads, including resurfacing. The county contracts the resurfacing of roads to vendors because it is not feasible for the county to perform the resurfacing on its own due to equipment and supply costs. The county does not maintain all asphalt haul tickets. The vendor attaches the last haul ticket for each job with the invoice delivered to the county treasurer for payment, but there is no review of asphalt haul tickets to make sure all loads were delivered to the county job site. The county also does not have an employee present at the jobsite to sign off that the asphalt is delivered to the county jobsite.

According to the county, they were unaware that this was required. These deficiencies could result in inaccurate reporting and misappropriation of assets. Strong internal controls require adequate documentation be maintained to support all county expenditures.

We recommend the county have an employee present at the jobsite each time a delivery is made. The employee should sign the haul tickets for each load of asphalt that is delivered. The county should then compare each signed haul ticket back to the bill received from the asphalt company to ensure they are only paying for materials delivered to the county.

County Judge/Executive's Response: Believes an employee was on site collecting tickets this past fall. County Judge will advise Road Supervisor to make sure all tickets are kept.

The Clay County Jail Commissary lacks segregation of duties over receipts, disbursements, and the bank reconciliation process: The Clay County Jail Commissary bookkeeper's duties include posting receipts, preparing and posting disbursements, and completing the bank reconciliation. When one employee is responsible for the receipt, disbursement, and reconciliation process, the risk of misappropriation of assets, errors, and inaccurate financial reporting increases. The Clay County Jailer has implemented some compensating controls over these functions by reviewing deposits, reviewing invoices, reviewing bank reconciliations, and documenting her review by initials or signature. This review, however, is not effective as evidenced by the issues noted in Finding 2018-009.

The limited number of Clay County jail staff in the office prevents a proper segregation of duties. This could result in undetected misappropriation of assets and incorrect reporting.

Effective internal controls require proper segregation of duties over accounting functions, such as making deposits, preparing disbursements, and reconciling the bank account. Segregation of duties, or the implementation of compensating controls, is essential for providing protection to employees in the normal course of performing their daily responsibilities.

We recommend the Clay County Jailer segregate duties over receipts, disbursements, and the bank reconciliation process. If segregation of duties is not possible, the Clay County Jailer should continue to implement compensating controls by monitoring the financial activities of the jail commissary and continue to document her review. The review should ensure accurate financial reporting and bank reconciliations.

Jailer's Response: This process goes through four employees now. I do not have enough staff to segregate any further. Jailer will continue to sign all deposits and go over reconciliations.

The Clay County Jail's year-end commissary report was misstated and the June 30, 2018 bank reconciliation was inaccurate: The Clay County Jail's year-end commissary report for June 30, 2018 was not an accurate representation of the financial activity that occurred during the period. At the end of each fiscal year, the jailer is required to submit a report reflecting the financial activity of the commissary account to the county treasurer. The jailer's report required 16 adjustments to receipts totaling \$8,520 in order to reconcile to bank activity for the period.

Additionally, the jail's June 30, 2018 bank reconciliation was inaccurate. The bank reconciliation's reconciled balance of \$573,307 agreed to the confirmed bank balance. But the reconciliation listed outstanding checks of \$4,440 and outstanding deposits of \$5,888 that do not agree to the audited amounts of \$13,596 and \$2,192, respectively.

The jailer's former bookkeeper left employment with the jail in August 2018 and the new bookkeeper was hired. According to the jailer, the new bookkeeper did not have sufficient training time. The jailer's year end commissary report and bank reconciliation were inaccurate due to errors made by the new bookkeeper.

Inmate accounts, as well as the jailer's commissary account, may not have full use of all the funds they are entitled to since the account is not being properly maintained.

Good internal controls dictate financial statements are properly prepared and all bank accounts are reconciled accurately and timely.

The jailer should establish a policy requiring monthly reconciliations of ledger and bank balances to minimize financial reporting errors and ensure proper disbursement of funds.

Jailer's Response: The jailer will make sure that the bank reconciliation is done properly, and that monthly ledger and bank balances is done correctly to minimize financial reporting errors and ensure proper disbursement of funds.

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

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