

**REPORT OF THE AUDIT OF THE
ESTILL COUNTY
SHERIFF'S SETTLEMENT - 2015 TAXES**

**For The Period
April 16, 2015 Through April 15, 2016**



**MIKE HARMON
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EXECUTIVE SUMMARY
AUDIT OF THE
ESTILL COUNTY
SHERIFF'S SETTLEMENT - 2015 TAXES

For The Period
April 16, 2015 Through April 15, 2016

The Auditor of Public Accounts has completed the audit of the Sheriff's Settlement - 2015 Taxes for the Estill County Sheriff for the period April 16, 2015 through April 15, 2016. We have issued an unmodified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

The sheriff collected 2015 taxes of \$4,626,286 for the districts, retaining commissions of \$185,655 to operate the sheriff's office. The sheriff distributed 2015 taxes of \$4,410,198 to the districts. Taxes of \$928 are due to the districts from the sheriff and refunds of \$104 are due to the sheriff from the taxing districts.

Report Comments:

- 2015-001 The Sheriff Did Not Distribute Tax Collections By The Tenth Of Each Month
- 2015-002 The Sheriff Did Not Make Daily Deposits
- 2015-003 The Sheriff's Office Lacks Adequate Segregation Of Duties

Deposits:

The sheriff's deposits were insured and collateralized by bank securities.

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MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Matthew G. Bevin, Governor
William M. Landrum III, Secretary
Finance and Administration Cabinet
Honorable Wallace C. Taylor, Estill County Judge/Executive
Honorable Gary Freeman, Estill County Sheriff
Members of the Estill County Fiscal Court

Independent Auditor's Report

Report on the Financial Statement

We have audited the Estill County Sheriff's Settlement - 2015 Taxes for the period April 16, 2015 through April 15, 2016 - Regulatory Basis, and the related notes to the financial statement.

Management's Responsibility for the Financial Statement

Management is responsible for the preparation and fair presentation of the financial statement in accordance with accounting practices prescribed or permitted by the laws of Kentucky to demonstrate compliance with the Commonwealth of Kentucky's regulatory basis of accounting as described in Note 1. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of a financial statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the 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 Sheriff's Tax Settlements* 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.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statement in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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To the People of Kentucky
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Members of the Estill County Fiscal Court

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 1 of the financial statement, the financial statement is prepared by the Estill County Sheriff on the basis of accounting practices prescribed or permitted by the laws of Kentucky to demonstrate compliance with the Commonwealth of Kentucky's regulatory basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the financial statement of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles paragraph, the financial statement referred to above does not present fairly, in accordance with accounting principles generally accepted in the United States of America, the taxes charged, credited, and paid of the Estill County Sheriff, for the period April 16, 2015 through April 15, 2016.

Opinion on Regulatory Basis of Accounting

In our opinion, the financial statement referred to above presents fairly, in all material respects, the taxes charged, credited, and paid for the period April 16, 2015 through April 15, 2016 of the Estill County Sheriff, in accordance with the basis of accounting practices prescribed or permitted by the Commonwealth of Kentucky as described in Note 1.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 13, 2017, on our consideration of the Estill County Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Estill County Sheriff's internal control over financial reporting and compliance.

To the People of Kentucky

Honorable Matthew G. Bevin, Governor

William M. Landrum III, Secretary

Finance and Administration Cabinet

Honorable Wallace C. Taylor, Estill County Judge/Executive

Honorable Gary Freeman, Estill County Sheriff

Members of the Estill County Fiscal Court

Other Reporting Required by *Government Auditing Standards* (Continued)

Based on the results of our audit, we have presented the accompanying comments and recommendations, included herein, which discusses the following report comments:

- 2015-001 The Sheriff Did Not Distribute Tax Collections By The Tenth Of Each Month
- 2015-002 The Sheriff Did Not Make Daily Deposits
- 2015-003 The Sheriff's Office Lacks Adequate Segregation Of Duties

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Mike Harmon", with a long horizontal flourish extending to the right.

Mike Harmon
Auditor of Public Accounts

June 13, 2017

ESTILL COUNTY
GARY FREEMAN, SHERIFF
SHERIFF'S SETTLEMENT - 2015 TAXES

For The Period April 16, 2015 Through April 15, 2016

<u>Charges</u>	<u>County Taxes</u>	<u>Special Taxing Districts</u>	<u>School Taxes</u>	<u>State Taxes</u>
Real Estate	\$ 321,334	\$ 1,474,150	\$ 1,696,344	\$ 455,846
Tangible Personal Property	18,352	85,522	79,352	57,865
Fire Protection	2,763			
Increases Through Exonerations	273	1,246	1,439	387
Franchise Taxes	65,157	303,948	298,257	
Additional Billings	283	1,283	1,482	400
Oil Property Taxes	4,165	19,035	21,990	5,909
Limestone, Sand, and Gravel Reserves	53	242	280	75
Penalties	2,233	10,201	11,675	3,206
Adjusted to Sheriff's Receipt	3	15	(4)	(1)
Gross Chargeable to Sheriff	<u>414,616</u>	<u>1,895,642</u>	<u>2,110,815</u>	<u>523,687</u>
 <u>Credits</u>				
Exonerations	1,753	7,998	9,240	2,483
Discounts	4,997	22,759	25,864	7,570
Delinquents:				
Real Estate	14,897	67,903	78,339	21,052
Tangible Personal Property	161	752	698	630
Franchise Taxes	<u>5,300</u>	<u>24,216</u>	<u>21,862</u>	
Total Credits	<u>27,108</u>	<u>123,628</u>	<u>136,003</u>	<u>31,735</u>
Taxes Collected	387,508	1,772,014	1,974,812	491,952
Less: Commissions *	<u>16,469</u>	<u>74,223</u>	<u>74,055</u>	<u>20,908</u>
Taxes Due	371,039	1,697,791	1,900,757	471,044
Taxes Paid	368,368	1,685,203	1,886,759	469,868
Refunds (Current and Prior Year)	<u>2,587</u>	<u>12,412</u>	<u>13,562</u>	<u>1,048</u>
Due Districts as of Completion of Audit	<u>\$ 84</u>	<u>\$ 176</u>	<u>\$ 436</u>	<u>\$ 128</u>

**

* and ** See next page.

The accompanying notes are an integral part of this financial statement.

ESTILL COUNTY
GARY FREEMAN, SHERIFF
SHERIFF'S SETTLEMENT - 2015 TAXES
For The Period April 16, 2015 Through April 15, 2016
(Continued)

* Commissions:

4.25% on \$ 2,216,353

4% on \$ 435,121

3.75% on \$ 1,974,812

** Special Taxing Districts:

Library District	\$	124
Health District		86
Extension District		55
Soil Conservation		15
Ambulance		(104)
		<hr/>

Due Districts or
(Refund Due Sheriff)

\$ 176

ESTILL COUNTY
NOTES TO FINANCIAL STATEMENT

April 15, 2016

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a regulatory basis of accounting, which demonstrates compliance with the laws of Kentucky and is a special purpose framework. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

KRS 66.480 authorizes the sheriff's office to invest in obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The Estill County Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240, the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the sheriff's deposits may not be returned. The Estill County Sheriff does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 66.480(1)(d) and KRS 41.240. As of April 15, 2016, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

ESTILL COUNTY
NOTES TO FINANCIAL STATEMENT
April 15, 2016
(Continued)

Note 3. Tax Collection Period

A. Property Taxes

The real and personal property tax assessments were levied as of January 1, 2015. Property taxes were billed to finance governmental services for the fiscal year ended June 30, 2016. Liens are effective when the tax bills become delinquent. The collection period for these assessments was September 11, 2015 through April 15, 2016.

B. Oil Property Taxes

The tangible property tax assessments were levied as of January 1, 2015. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was November 13, 2015 through May 16, 2016.

C. Limestone, Sand, And Gravel Property Taxes

The tangible property tax assessments were levied as of January 1, 2015. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was November 13, 2015 through May 16, 2016.

D. Franchise Taxes

The franchise tax assessments were levied by the Kentucky Department of Revenue for various tax years. Franchise taxes are billed to finance governmental services. The collection period for these assessments was April 16, 2015 through April 15, 2016.

Note 4. Interest Income

The Estill County Sheriff earned \$24 as interest income on 2015 taxes. The sheriff was in substantial compliance with his statutory responsibilities.

Note 5. Sheriff's 10% Add-On Fee

The Estill County Sheriff collected \$21,756 of 10% add-on fees allowed by KRS 134.119(7). This amount was used to operate the sheriff's office.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Wallace C. Taylor, Estill County Judge/Executive
Honorable Gary Freeman, Estill County Sheriff
Members of the Estill County Fiscal Court

**Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With *Government Auditing Standards***

Independent Auditor's Report

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Estill County Sheriff's Settlement - 2015 Taxes for the period April 16, 2015 through April 15, 2016 - Regulatory Basis and the related notes to the financial statement and have issued our report thereon dated June 13, 2017. The Estill County Sheriff's financial statement is prepared on a regulatory basis of accounting, which demonstrates compliance with the Commonwealth of Kentucky's regulatory basis of accounting and budget laws, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statement, we considered the Estill County Sheriff's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of the Estill County Sheriff's internal control. Accordingly, we do not express an opinion on the effectiveness of the Estill County Sheriff's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying comments and recommendations, we identified a certain deficiency in internal control that we consider to be a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statement will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying comments and recommendations as item 2015-003 to be a material weakness.

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Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With *Government Auditing Standards*
(Continued)

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Estill County Sheriff's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying comments and recommendations as items 2015-001 and 2015-002.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Mike Harmon", with a long horizontal line extending to the right.

Mike Harmon
Auditor of Public Accounts

June 13, 2017

COMMENTS AND RECOMMENDATIONS

ESTILL COUNTY
GARY FREEMAN, SHERIFF
COMMENTS AND RECOMMENDATIONS

For The Period April 16, 2015 Through April 15, 2016

STATE LAWS AND REGULATIONS:

2015-001 The Sheriff Did Not Distribute Tax Collections By The Tenth Of Each Month

The sheriff did not distribute franchise tax collections in a timely manner. The sheriff received a franchise tax collection in April 2016, but did not distribute the collection until June 2016. Payments were not made timely due to an oversight of the sheriff and his bookkeeper. Failure to make timely tax distributions is an issue of noncompliance that prevents taxing districts from receiving revenues timely and may cause cash flow issues for the taxing districts.

KRS 134.191(1) requires the sheriff to “provide monthly reports by the tenth day of each month to the chief executive of the county, the department, and any other district for which the sheriff collects taxes.” Furthermore, KRS 134.191(3) states, “[a]t the time of making the report, the sheriff shall pay to the county treasurer. . .to the department, and to any other districts for which the sheriff collects taxes, all funds belonging to the county, the state, or the district that were collected during the period covered by the report.” We recommend the sheriff provide monthly reports and distribute tax payments by the tenth of each month as required by KRS 134.191.

Sheriff's Response: The sheriff did not provide a response.

2015-002 The Sheriff Did Not Make Daily Deposits

The sheriff did not make daily deposits as required. The auditor randomly selected one week of February 2016 to test. There were two deposits made for receipts received during this week. The first deposit was dated February 2, 2016, and included receipts ranging from January 29, 2016 through February 2, 2016. This deposit did not clear the bank until February 11, 2016. The second deposit was dated February 11, 2016, and included receipts ranging from February 3, 2016 through February 11, 2016. This deposit did not clear the bank until February 18, 2016.

Daily deposits were not made because the sheriff has not adopted a policy requiring daily deposits. Failure to make daily deposits increases the risk of undetected errors and misappropriation of assets. The Department for Local Government, under the authority of KRS 68.210, established minimum requirements for all local officials with regard to handling public funds and one of these requirements is “daily deposits intact into a federally insured banking institution.” We recommend the sheriff start making daily deposits intact into a federally insured banking institution in order to comply with the Department for Local Government requirements and to reduce the risk of undetected errors and misappropriation of assets.

Sheriff's Response: The sheriff did not provide a response.

INTERNAL CONTROL - MATERIAL WEAKNESS:

2015-003 The Sheriff's Office Lacks Adequate Segregation Of Duties

The sheriff's office lacks adequate segregation of duties over receipts, disbursements, and reconciliations. The sheriff's bookkeeper receives payments for taxes, records receipts in the ledger, prepares bank deposits, and performs monthly bank reconciliations. Additionally, the same employee prepares checks for payments from the tax account, records disbursements in the ledger, and prepares monthly reports reflecting amounts to be paid to each taxing district.

ESTILL COUNTY
GARY FREEMAN, SHERIFF
COMMENTS AND RECOMMENDATIONS
For The Period April 16, 2015 Through April 15, 2016
(Continued)

INTERNAL CONTROL - MATERIAL WEAKNESS: (Continued)

2015-003 The Sheriff's Office Lacks Adequate Segregation Of Duties (Continued)

The sheriff said the lack of adequate segregation of duties is a result of a limited budget, which restricts the number of employees the sheriff can hire or delegate these duties to, which could result in the undetected misappropriation of assets and inaccurate financial reporting. Good internal controls dictate the same employee should not handle, record, and reconcile receipts. Further, the same employee should not be responsible for preparing, recording, and reconciling disbursements. The segregation of duties over various accounting functions such as opening mail, preparing deposits, recording receipts and disbursements, and preparing monthly reports, or the implementation of compensating controls 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 sheriff segregate these duties, or implement steps to strengthen internal controls through compensating controls such as:

- The sheriff should periodically compare the daily bank deposit to the daily checkout sheet, and then compare the daily checkout sheet to the receipts ledger.
- The sheriff should compare the monthly financial reports to the receipts and disbursements ledgers for accuracy.
- The sheriff should periodically compare the amounts due districts per the monthly reports to the payments to the taxing districts.
- The sheriff should periodically compare the monthly bank reconciliation to the balance in the checkbook.
- All disbursement checks should be signed by two people, with one being the sheriff.
- The sheriff should personally mail or deliver tax payments to the taxing districts.

All of the compensating controls should be documented by the sheriff initialing and dating the documents used to perform the comparisons.

Sheriff's Response: The sheriff did not provide a response.

