



Auditor of Public Accounts
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Harmon Releases Audit of Owsley County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Owsley 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 Owsley 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 Owsley County Fiscal Court lacks adequate segregation of duties and controls over the overall environment of the county: This is a repeat finding and was included in the prior year audit report as Finding 2017-003. The Owsley County Fiscal Court lacks adequate segregation of duties over receipts, disbursements, cash, and payroll. The Owsley County Treasurer was responsible for recording receipts and disbursements in the ledgers, preparing bank reconciliations, and preparing the county’s payroll. Additionally, the Owsley County Treasurer prepared monthly, quarterly, and annual financial reports on behalf of the Owsley County Fiscal Court. The Owsley County Fiscal Court failed to establish adequate management oversight to ensure proper recording of receipts and disbursements, complete and accurate bank reconciliations, and accurate preparation of the Owsley County Fiscal Court’s payroll.

The Owsley County Fiscal Court failed to adequately segregate the duties involved in recording revenues and disbursements, preparing monthly bank reconciliations, and preparing the Owsley County Fiscal Court's payroll. The Owsley County Fiscal Court also failed to provide adequate oversight regarding the Owsley County Treasurer's preparation of financial reports.

The lack of adequate internal controls and segregation of duties, coupled with a lack of adequate management oversight, provides an environment in which an individual could manipulate financial records and misappropriate or misdirect county funds. The following control deficiencies occurred due to the lack of internal controls and segregation of duties over these areas:

- The fiscal court did not approve the treasurer's annual settlement as reported in Finding 2018-002.
- The fiscal court did not properly authorize all cash transfers and intrafund budget transfers as reported in Finding 2018-003.
- The fiscal court did not budget, record, or report funds as reported in Finding 2018-004.
- The fiscal court did not have controls over disbursements as reported in Finding 2018-005.
- The fiscal court's purchase order system did not operate correctly as reported in Finding 2018-006.
- The fiscal court did not have controls over recreation center receipts, did not issue receipts, and did not make daily deposits as reported in Finding 2018-007.
- The fiscal court does not have controls over garbage collections and gravel sale receipts as reported in Finding 2018-008.
- The fiscal court failed to establish internal controls over payroll as reported in Finding 2018-009.
- The fiscal court did not maintain and complete an accurate capital asset schedule in order to comply with regulatory requirements as reported in Finding 2018-010.
- The fiscal court did not properly report encumbrances on the fourth quarter financial report as reported in Finding 2018-011.
- The fiscal court did not prepare an accurate schedule of expenditures of federal awards (SEFA) as reported in Finding 2018-012.
- The fiscal court did not accurately report financial information on the fourth quarter financial report as reported in Finding 2018-013.

The implementation of internal controls and the segregation of duties over various accounting functions such as recording receipts and disbursements, preparing bank reconciliations, and preparing monthly, quarterly, and annual financial reports 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. Appropriate management oversight should be provided to ensure the completion of accurate, timely financial reports.

We recommend the Owsley County Fiscal Court segregate the duties involved in recording receipts and disbursements, preparing bank reconciliations, preparing payroll, and preparing monthly, quarterly, and annual financial reports where possible. If this is not feasible due to a limited budget, appropriate management oversight should be established.

County Judge/Executive's Response: Owsley County does not have funding to adequately segregate duties; however, another employee has been hired to help segregate.

The Owsley County Fiscal Court did not approve the treasurer's annual settlement: The Owsley County Treasurer's annual settlement for Fiscal Year 2018 was not presented and approved by the fiscal court.

The fiscal court did not have controls in place to ensure that staff knew the requirements or did not monitor/review to make sure requirements were followed. Since an annual settlement was not presented and approved, the fiscal court was not aware of the financial condition of the county after ending Fiscal Year 2018. Also, the fiscal court was not in compliance with state regulations.

KRS 68.020(5) states, in part “[t]he county treasurer shall, when required by the fiscal court, settle his accounts as county treasurer, and within thirty (30) days after the close of each fiscal year, he shall, unless his immediate predecessor has done so, make a full and complete settlement for the preceding fiscal year with the fiscal court[.]”

KRS 68.030 states, in part, “[e]ach settlement made by the county treasurer shall be approved by the fiscal court in open court, and shall, by order of the fiscal court, be recorded by the county clerk in a book kept for that purpose. The original shall be filed in the county clerk's office, and preserved as a record of the court.”

Strong internal controls over financial reporting are vital in ensuring the fiscal court is aware of requirements as stated in KRS 68.020(5) and KRS 68.030 and ensuring compliance with all state regulations.

We recommend the fiscal court implement internal controls to ensure compliance with all state regulations. We also recommend that the fiscal court require the treasurer to present an annual settlement for approval within 30 days after the end of the fiscal year.

County Judge/Executive's Response: The county treasurer has prepared an annual settlement and [it] will be approved at the next fiscal court meeting.

The Owsley County Fiscal Court did not properly authorize all cash transfers and intrafund budget transfers: The Owsley County Fiscal Court did not properly authorize all cash transfers between county funds. Furthermore, the Owsley County Fiscal Court did not properly authorize intrafund budget transfers of appropriations from one line item to another in the same fund. As a result, the following cash transfers and intrafund budget transfers were not properly authorized:

- Eighteen of the 42 cash transfers processed, totaling \$286,050, were not documented in the minutes of the fiscal court meetings.
- Intrafund budget transfers totaling \$22,321 for the general fund.
- Intrafund budget transfers totaling \$130,235 for the road fund.
- Intrafund budget transfers totaling \$6,099 for the jail fund.

- Intrafund budget transfers totaling \$3,240 for the Local Government Economic Assistance (LGEA) fund.
- Intrafund budget transfers totaling \$13,000 for the solid waste fund.
- Intrafund budget transfers totaling \$1,097 for the parks and recreation fund.
- Intrafund budget transfers totaling \$8,164 for the Local Government Economic Development (LGED) fund.

This was due to the fiscal court believing that approving the cash transfers as needed was sufficient. The fiscal court did not have controls in place to ensure compliance with state law regarding the uniform system of accounts which requires all cash transfers and intrafund budget transfers to be properly authorized. By not properly authorizing cash transfers, the risk of misappropriation of assets is increased as cash could be transferred to non-county funds. Furthermore, failure to approve intrafund budget transfers prevents the fiscal court from making fully informed decisions on budgetary matters.

Strong internal controls over cash transfers are vital in ensuring the fiscal court's financial reports accurately reflect the financial activity of the fiscal court. In addition, KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. This 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 states, "[a]ll transfers require a court order."

We recommend the fiscal court implement stronger internal controls over the cash transfer process to ensure all cash transfers are approved by the fiscal court. We also recommend that all cash transfers and intrafund budget transfers be voted on specifically and clearly documented in the fiscal court minutes.

County Judge/Executive's Response: The fiscal court has been authorizing all transfers for years. Transfers will be properly authorized beginning immediately.

The Owsley County Fiscal Court did not budget, record or report three federal grants: This is a repeat finding and was included in the prior year audit report as Finding 2017-002. The fiscal court did not budget, record, or report three federal grant funds with expenditures totaling \$82,337. The grant funds not reported were the U.S. Department of Agriculture (USDA) Community Facilities Grant program, the USDA Teleworks Grant Fund, and the Appalachian Regional Commission (ARC) Wolf Creek Metal Equipment Fund. The fiscal court maintained separate bank accounts for these funds, but did not include them in the original budget, or any amendment to the budget. In addition, the receipts and disbursements of the funds were not recorded on the ledgers or reported on the fourth quarter financial statement.

The county treasurer was new during Fiscal Year 2018 and did not realize these funds should be reported on the fourth quarter financial report. The fiscal court did not have controls in place to ensure all funds were reported. Failure to record the activity in these accounts on the fourth quarter financial report resulted in a materially inaccurate financial statement. Furthermore, the fiscal court was not in compliance with the uniform system of accounts.

Strong internal controls over the budgeting, recording, and reporting of funds is vital in ensuring that the fiscal court's financial reports accurately reflect the financial activity of the fiscal court. In addition, the uniform system of accounts, as prescribed pursuant to KRS 68.210, requires counties to submit quarterly reports to their regulatory agency, the Department for Local Government (DLG). These reports should include all funds of the fiscal court, should include all activity within the funds, and should agree to the fiscal court's reconciled cash balances. The DLG's *County Budget Preparation and State Local Finance Officer Policy Manual* states, "[i]t is necessary to amend the budget to reflect the receipt and expenditure of funds received through a state or federal grant if that grant was not part of the original budget document."

We recommend the fiscal court implement strong internal controls over the budgeting, recording, and reporting of funds to ensure financial reports accurately reflect the financial activity of the fiscal court. We further recommend the fourth quarter financial report prepared by the Owsley County Treasurer include all financial activity of the Owsley County Fiscal Court including any grant funds received and disbursed during the fiscal year.

County Judge/Executive's Response: The county did not budget any pass-thru agency funds but will do so in the future.

The Owsley County Fiscal Court did not have controls over disbursements: The Owsley County Fiscal Court did not have sufficient controls over disbursements which allowed the following deficiencies to occur:

- Twelve disbursements tested, totaling \$399,708, did not have adequate supporting documentation.
- One project exceeding the county's bid threshold of \$20,000 was not advertised for bids.
- Three disbursements tested were not presented to the fiscal court.
- Sixteen of 72 disbursements tested were copies from vendors. Original invoices could not be located.
- Four disbursements tested were not paid within thirty days (KRS 65.140).
- One disbursement was paid by the statement balance.
- Two disbursements tested included finance charges due to being paid late.
- Two items were purchased using a debit card without any supporting documentation.
- Debt payments were not paid according to the amortization schedule: \$666 was not paid in 2018.
- There were overdraft charges totaling \$60 for the Local Government Economic Assistance (LGEA) Fund bank account.
- There were negative balance fees of \$110 for the Appalachian Regional Commission (ARC) Wolf Creek Metal Equipment Fund.
- There were overdraft fees of \$60 for the Parks and Recreation Fund.

The fiscal court failed to ensure procedures were in place to properly support disbursements paid from county funds. By not having good controls in place, errors were allowed to occur and were not detected. Weak controls also increase the risk of misappropriation of county funds. These conditions also lead to noncompliance with the regulations noted below.

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.”

KRS 65.140(2) states, “[u]nless the purchaser and vendor otherwise contract, all bills for goods or services shall be paid within thirty (30) working days of receipt of a vendor's invoice except when payment is delayed because the purchaser has made a written disapproval of improper performances or improper invoicing by the vendor or by the vendor's subcontractor.”

Under the authority of KRS 68.210, the state local finance officer is to prescribe minimum requirements for handling public funds. According to the Department for Local Government’s (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*, disbursements are to be made by check only. Strong internal controls dictate policies and procedures be in place and working effectively to ensure county funds are expended on items to efficiently operate the county; operating disbursements have appropriate supporting documentation; and disbursements are properly coded prior to inclusion on the monthly claims list.

We recommend the fiscal court improve internal controls over disbursements to prevent these deficiencies from occurring. Such procedures should include ensuring all claims against the county are adequately supported, properly recorded, allowable, paid timely, and reviewed prior to payment. We also recommend the fiscal court follow proper bid laws and regulations by ensuring all applicable purchases and contracts be made in compliance with KRS 424.260.

County Judge/Executive’s Response: The county has employed an additional finance officer to control disbursements as needed.

The Owsley County Fiscal Court’s purchase order system did not operate correctly: The Owsley County Fiscal Court’s purchasing procedures were not operating correctly. Seventy-two disbursements tested totaling \$749,848 did not have a properly executed purchase order.

The county treasurer stated she was aware that purchase orders were not properly prepared or executed. By having weak internal controls over the purchase order system, the fiscal court assumes a higher risk of misstatement and fraud. In addition, purchases could be made that exceed available cash or the amount available in the budget for a line item. Furthermore, encumbrances are reported incorrectly on the quarter financial reports.

Strong internal controls over disbursements are essential in ensuring disbursements are properly approved and recorded.

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 a purchase order system for all fiscal courts and each fiscal court is responsible for ensuring their purchase order system is executed and working properly. Furthermore, this manual requires purchase requests to indicate the proper appropriation account number to which the claim will be posted.

DLG also highly recommends that fiscal courts accept the practice of issuing purchase orders for payroll and utility claims. Issuing purchase orders allows the county to actually see the cash requirements needed to cover a particular bill.

The *Owsley County Administrative Code* section 425.3 states, "[f]our copies of purchase order are prepared: one for the vendor, one for the agency requesting the items, and two for the Judge/Executive." In addition, section 425.5 states, "[a]fter payment is made, Judge/Executive files one copy of the purchase order in numerical sequence and the other copy alphabetically by vendor's name along with vendor's invoice."

We recommend the fiscal court strengthen controls over purchasing procedures by requiring disbursements to have purchase orders submitted prior to approval. We recommend the fiscal court comply with KRS 68.210 by requiring purchase orders to be completed for all disbursements. Purchase orders should include dates, amounts, account codes, and department head approvals to ensure sufficient appropriations are available within the amount of line items in the fiscal court's budget.

County Judge/Executive's Response: The purchase order system has operated functionally for the past years. The fiscal court will make the necessary adjustments.

The Owsley County Fiscal Court did not have controls over recreation center receipts, did not issue receipts, and did not make daily deposits: The fiscal court receives cash at the recreation center for events, room rentals, and concessions. Cash is maintained in cash drawers and turned over to the county judge/executive once per week. Receipts are not issued for transactions and money is only turned over to the fiscal court once per week.

The fiscal court did not have controls in place to ensure all recreation receipts have been accounted for and reported properly. Without a proper way to account for cash receipts, receipts could be collected and not be recorded or deposited intact with the fiscal court.

Good internal controls dictate that adequate controls exist over recreation center receipts and disbursements to ensure they are properly reported. In addition, 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 the Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*. This manual states, "[d]aily deposits intact into a federally insured banking institution." It also states, "[p]re-numbered three-part receipt forms should be issued for all receipts. Original to be given to payer, copy to be attached in sequential order to daily cash check-

out sheet or daily deposit record, and copy to remain in file.” Also, good internal controls dictate receipts are accounted for daily and all collections are deposited daily. Any discrepancies between the deposit and daily checkout sheet should be documented.

KRS 64.840(1) states, in part, “all county officials shall, upon the receipt of any fine, forfeiture, tax, or fee, prepare a receipt that meets the specifications of the state local finance officer[.]”

We recommend the fiscal court implement internal controls to ensure compliance with KRS 64.840(1) and the DLG’s *County Budget Preparation and State Local Finance Officer Policy Manual* by ensuring pre-numbered receipts are issued for all transactions and all receipts are deposited daily.

County Judge/Executive’s Response: Deposits will be made bi-weekly. Many days there is less than \$5 received.

Auditor’s Reply: As cited in the finding, the Department for Local Government’s *County Budget Preparation and State Local Finance Officer Policy Manual* requires daily deposits. This requirement is not dependent upon the amount collected.

The Owsley County Fiscal Court does not have controls over garbage collections and gravel sale receipts: The fiscal court receives payments for garbage collections and gravel sales. Collections can be received by the county treasurer, finance officer, or janitor. Manual receipts are issued to customers. Solid waste receipts are posted to customer accounts by the treasurer through solid waste collection software. Gravel sale receipts are issued to customers in order for them to pick up gravel from the county road garage. During the month of June 2018, there was a shortage in cash receipts of \$480 when comparing solid waste collection reports to bank deposits. Further testing for the month of March 2018 showed a variance of \$18. The amount could not be detailed due to the fiscal court not maintaining all collection records. The county treasurer is also responsible for performing bank reconciliations.

The fiscal court did not have controls in place to ensure collections were being properly recorded. Receipts could not be accounted for or recorded properly.

Good internal controls dictate that adequate controls exist over receipts to ensure they are recorded and deposited properly.

We recommend the fiscal court separate the duties of receiving payments, posting to customer accounts, preparing deposits, and preparing bank reconciliations. If segregation of duties is not feasible due to lack of funds, the county should implement and document compensating controls to offset this control weakness.

County Judge/Executive’s Response: The fiscal court has hired an additional employee to better control all collections and receipts.

The Owsley County Fiscal Court failed to establish internal controls over payroll: The lack of internal controls over payroll resulted in the following issues:

- Five of the 16 employees tested had withholdings treated as pre-tax deductions that should have been after-tax deductions, which resulted in underreported W-2 wages.
- Personnel files could not be found for six of the 16 employees tested.
- The test of employee withholdings resulted in six authorizations not being located.
- Eleven of 23 employees tested had vacation leave balances that exceeded the limit set by the County Administrative Code of 240 hours.
- Two employees were issued two W-2s with differing social security numbers.
- The Department of Emergency Services (DES) Director receives a \$50 expense allowance per month.
- The DES Director and the 911 Coordinator were not required to maintain timesheets in any capacity.
- The treasurer and finance officer's timesheets could not be located when initially requested. The treasurer did provide timesheets at a later date, but it could not be confirmed that these had been completed during the specified pay period tested.
- Employees holding two jobs within the county, generally as a Road Laborer and a Solid Waste Worker, are not maintaining adequate timesheets showing hours worked for each position.
- None of the employees' timesheets tested were reviewed or signed by supervisors of departments.
- Employees with two different job titles are accruing double leave balances (including sick and vacation leave) in the payroll system for both positions each month.

The lack of internal controls and adequate oversight have allowed issues with the payroll process to go unnoticed. The lack of controls over payroll have allowed numerous errors to occur. Additionally, sufficient supporting documentation for payroll has not been maintained and numerous issues of non-compliance were noted with regard to the Owsley County Administrative Code and Kentucky Revised Statutes (KRS). Strong internal controls over payroll are vital in ensuring the payroll amounts are calculated and accounted for properly.

The Owsley County Administrative Code, Section 350.2 states, “[e]ach employee will receive one day annual leave for each complete month worked and may accumulate to a maximum of thirty days.”

The Owsley County Administrative Code, Section 350.3 states, “[e]ach employee will receive one sick day per month with no maximum on days each could accumulate.”

KRS 337.320(1) states, “[e]very employer shall keep a record of: (a) [t]he amount paid each pay period of 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.”

Good internal controls dictate that timesheets be kept for payroll verification and 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.

KRS 64.710 states, “[n]o public officer or employee shall receive or be allowed or paid any lump sum expense allowance, or contingent fund for personal or official expenses, except where such allowance or fund either is expressly provided for by statute or is specifically appropriated by the General Assembly.”

We recommend the fiscal court:

- Strengthen internal controls over the payroll process.
- Comply with KRS 337.320 by requiring timesheets or timecards be maintained for all employees; these should be signed by the employees and then reviewed and signed by the employees’ immediate supervisors.
- Ensure employees holding two positions within the county accrue leave at the rate listed in the Owsley County Administrative Code.
- Ensure all forms for withholdings or any other personnel documents be maintained in the employees’ file.
- Ensure all employees’ vacation leave balances are in compliance with the Owsley County Administrative Code.
- Discontinue the use of the expense allowance for the DES Director per KRS 64.710.

County Judge/Executive’s Response: Will be corrected.

The Owsley County Fiscal Court did not maintain and complete an accurate capital asset schedule in order to comply with regulatory requirements: The schedule of capital assets and infrastructure for the audit period did not recognize all asset purchases that occurred throughout the year. The county treasurer is responsible for maintaining the schedule. She makes additions and deletions based on the time of purchase or when item is taken out of the county’s name. The fiscal court’s schedule of capital assets was materially misstated by \$131,982. The fiscal court’s schedule of capital assets for June 30, 2018, was understated/overstated as follows:

- \$113,482 for three roads that were resurfaced and not added to infrastructure.
- Vehicle valued at \$18,500 that was reported stolen in Fiscal Year 2018 was not deleted.

The fiscal court lacks adequate controls over reporting of capital assets. The county treasurer also stated she compared her listing to the insurance listing but did not perform an actual inventory of equipment. By having weak internal controls over capital assets, assets are left vulnerable to misappropriation or misstatement. In this case, misstatements were able to occur without detection resulting in an understatement in infrastructure of \$113,482 and an overstatement of vehicles of \$18,500.

Strong internal controls over capital assets are necessary to ensure accurate financial reporting, to protect assets from misappropriation, and to ensure accurate insurance coverage. 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 states, “[f]ixed asset records are necessary for proper asset valuation, adequate and accurate insurance coverage, internal control, and long range planning for property replacement. An annual physical inventory

of property and equipment shall be conducted on or before June 30. Physical counts must be compared to the master asset inventory listing. Resulting differences must be reconciled, explained and documented.” Furthermore, the manual states “[a] fixed asset record should be prepared for each acquisition that meets the useful life and threshold limits. Deletion, sale, or disposal of fixed assets must be approved by the authorized personnel and documented accordingly.”

We recommend the fiscal court maintain a complete and accurate capital asset schedule to comply with DLG requirements. Procedures should be implemented that will identify and track additions and deletions for the purpose of the schedule of capital assets with adequate supporting documentation and any additions or deletions should be reconciled to the department inventory records annually for insurance coverage.

County Judge/Executive’s Response: Capital asset schedule will be maintained regularly.

The Owsley County Fiscal Court did not properly report encumbrances on the fourth quarter financial report: Encumbrances were not properly reported by the Owsley County Fiscal Court on the fourth quarter financial report. Encumbrances are funds the fiscal court has committed prior to the actual disbursements. The amounts reported as encumbrances did not include all amounts committed as of June 30, 2018, since purchase orders are not properly issued for all funds committed.

The county treasurer stated she was aware that purchase orders were not being prepared correctly or entered into the computer. The fourth quarter financial report misstated the unencumbered cash balance as of June 30, 2018, which helps management and other users determine the financial position of the fiscal court.

Strong internal controls are vital to ensure compliance with requirements governing fiscal court disbursement procedures and to ensure the fourth quarter financial report contains all of the required information. In addition, according to KRS 68.360(2), “[t]he county judge/executive shall, within (15) days after the end of each quarter of each fiscal year, prepare a statement showing for the current fiscal year to date actual receipts from each county revenue source, the totals of all encumbrances and expenditures charged against each budget fund, the unencumbered balance of the fund, and any transfers made to or from the fund.” Additionally, 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 this information to be presented on the quarterly financial reports.

We recommend the fiscal court add controls to ensure encumbrances are reported properly on the front page of the fourth quarter financial report in order to accurately disclose unencumbered cash balances for each fund. In addition, purchase orders should be issued for all funds committed so all encumbrances are reported on the quarterly financial report.

County Judge/Executive’s Response: Will be corrected.

The Owsley County Fiscal Court did not prepare an accurate schedule of expenditures of federal awards (SEFA): The Owsley County Fiscal Court prepared a Schedule of Expenditures of Federal Awards (SEFA) for Fiscal Year 2018, as required by the Department for Local Government (DLG) and Uniform Guidance. Total federal disbursements per the SEFA totaled \$30,360. However, the SEFA did not include the Wolf Creek Metal Expansion Program federal disbursements of \$24,659, the Community Facilities Grant Program federal disbursements of \$50,000, and the Disaster and Emergency Services Grant federal disbursements of \$7,678. In addition, the fiscal court does not have policies and procedures in place for SEFA preparation.

The county treasurer did not include these disbursements when preparing the SEFA. Because the fiscal court did not include the federal disbursements for the Wolf Creek Metal Expansion Program, the Community Facilities Grant Program, and the Disaster and Emergency Services Grant on the SEFA, the SEFA was inaccurate.

Good internal controls dictate the fiscal court prepare an accurate SEFA and include total federal awards expended for each individual federal program. Completeness and accuracy are critical to the SEFA preparation. In addition, Uniform Guidance states that the auditee must prepare a SEFA for the period covered by the auditee's financial statements, which must include the total federal awards expended as determined by 2 CFR 200.502.

2 CFR 200.302(b)(1) states, "[i]dentification, in its accounts, of all Federal awards received and expended and the Federal programs under which they were received. Federal program and Federal award identification must include, as applicable, the CFDA title and number, Federal award identification number and year, name of the Federal agency, and the name of the pass-through entity, if any." This information enables the auditee to reconcile amounts presented in the financial statement to related amounts in the SEFA.

2 CFR 200.508 states, "[t]he auditee must: (b) Prepare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with §200.510 Financial statements."

2 CFR 200.510(b) states, in part, "Schedule of expenditures of Federal awards. The auditee must also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements which must include the total Federal awards expended as determined in accordance with §200.502 Basis for determining Federal awards expended."

We recommend the Owsley County Fiscal Court develop policies and procedures for SEFA preparation, as well as strengthen internal controls over the preparation in order to ensure its completeness and accuracy and compliance with reporting compliance requirements.

County Judge/Executive's Response: An accurate SEFA will be prepared.

The Owsley County Fiscal Court did not accurately report financial information on the fourth quarter financial report: The fiscal court's fourth quarter financial report did not accurately reflect the approved budget amounts and did not include all payroll disbursements for the solid waste fund and the parks and recreation fund. The following errors occurred:

- The fourth quarter financial report included a budgeted receipt of \$50,000 for a U.S. Department of Agriculture (USDA) grant for the solid waste fund. The fiscal court's approved budget did not have a budget line item for the \$50,000 receipt for the solid waste fund.
- The fourth quarter financial report did not include disbursements totaling \$6,440 for salaries for the solid waste fund and \$1,121 for payroll disbursements for the county's portion of social security for the parks and recreation fund.

These misstatements are a result of not having internal controls over the financial reporting process. The fiscal court failed to recognize the importance of strong internal controls over reporting financial information, and instead relied on a single employee without sufficient oversight. The errors were not detected because the fourth quarter financial report was not reviewed by another employee to ensure accuracy.

Because of not having internal controls in place, the amounts reported on the quarterly financial report were misstated and did not agree with the actual budgeted amounts and the actual transaction amounts. Also, not having internal controls in place resulted in disbursements not being included on the financial report reducing the usefulness of the financial reports to the public as well as to the fiscal court. The fiscal court needs accurate financial information to oversee the financial condition of the government as well as to prepare future budgets.

KRS 68.020(4) states the county treasurer, "shall keep an accurate detailed account of all money received and disbursed by him for the county, and shall keep books of accounts 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 68.210 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 treasurer to, "[p]repare a quarterly financial statement for the State Local Finance Officer." The manual provides a format to be used when preparing the quarterly financial statement. This format includes reporting original budget estimates, budget amendments, actual receipts and disbursements and total available in each line item. In addition, the manual provides a chart of accounts and states, "[a]ll counties must use the account numbers from the chart of accounts." Strong internal controls over financial reporting are vital in ensuring the fiscal court's financial reports accurately reflect the financial activity of the fiscal court. These controls should include an individual independent of the accounting function reviewing the financial reports for compliance with DLG reporting requirements.

We recommend the fiscal court implement internal controls over the financial reporting process. Internal controls such as a thorough review of quarterly financial reports by someone independent of the accounting function can help detect misstatements and errors that have occurred. This review should include tracing budgeted amounts reported to the original budget and budget amendments approved by DLG. This review should also include tracing transactions posted to the receipts and disbursements ledgers to actual bank statement transactions. It should also include agreeing fund balances between the quarterly financial reports and bank reconciliations, agreeing bank balances per the bank statements to the quarterly financial reports and bank reconciliations,

checking for mathematical accuracy, and verification of bank reconciliation amounts. Ledgers should also be reviewed to verify transactions have been recorded and posted to the correct account codes. Once the ledgers and reconciliations are deemed accurate, the reviewer should document that fact and submit the review to the fiscal court for approval. By implementing these procedures, the fiscal court can implement its internal control system, and help ensure accurate financial reporting.

County Judge/Executive's Response: Will be corrected.

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

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