



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, 2017. 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 Clay County Fiscal Court lacks internal controls over the environment of the county road department: This is a repeat finding and was included in the prior year audit report as Finding 2016-001. The Clay County Fiscal Court lacks internal controls over the environment of the county road department. During most of the fiscal year ending June 30, 2017, the fiscal court did not have internal controls in place to mitigate risks in several areas of the road department including labor, the use of equipment and vehicles, the use of fuel, and the use of materials such as gravel, steel, and pipe. Road department employees were not required to maintain documentation for the type of work performed, location of projects, where work was performed, or materials used in completing projects. Additionally, fuel logs were not maintained to document

the use and addition of fuel. However, auditors performed an onsite review on April 18, 2017, and controls had been implemented to correct this finding for the latter part of the fiscal year.

The fiscal court did not require those charged with management of the road department to implement internal controls. By not having proper controls in place, the county is at risk for misuse and misappropriation of the use of labor, equipment and vehicles, fuel, and materials at the road department.

Strong internal controls would mitigate the risk associated with the use of fiscal court labor and assets.

We recommend the Clay County Fiscal Court continue with the internal controls they have implemented at the road department over the use of equipment, vehicles, fuel, and materials such as gravel, steel, and pipe.

County Judge/Executive's Response: Related information is now being documented by the County Road Foreman.

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 2016-003. 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.

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

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

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 be implemented 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: Two employees are now recording receipts.

The Clay County Fiscal Court lacks internal controls over community center receipts: This is a repeat finding and was included in the prior year audit report as Finding 2016-004. The Clay County Fiscal Court lacks internal controls over community center receipts. No supporting documentation was available for money collected for the reservation of the community center during the fiscal year ended June 30, 2017. Money was either collected in the county judge/executive's office, or by an employee at the community center. Citizens who paid for reservation of the community center at the county judge/executive's office were issued a receipt. However, no receipts were issued to citizens who paid directly to an employee at the community center. Daily checkout sheets were not maintained at either the county judge/executive's office or the community center. Per the receipts ledger, the recorded community center reservation receipts totaled \$11,850 for the fiscal year ending June 30, 2017.

A former county employee was responsible for the collection of funds and scheduling reservations of the community center. The fiscal court did not require supporting documentation to be maintained. Without supporting documentation, the fiscal court cannot determine if the proper amount of receipts were collected from the use of the community center. This could result in undetected misappropriation of assets and incorrect reporting.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The Department for Local Government's *County Budget Preparation and State Local Finance Officer Policy Manual* establishes several procedures to institute a strong internal control environment, including issuing pre-numbered three-part receipts, utilization of daily check-out sheets, and ensuring that deposits are made intact daily.

KRS 64.840(1) states, "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 Clay County Fiscal Court issue a receipt for all money collected for use of the community center.

County Judge/Executive's Response: All receipts for the community Building now come thru the County Judge's Office.

The Clay County Fiscal Court did not properly collect past due ambulance service bills: This is a repeat finding and was included in the prior year audit report as Finding 2016-005. The Clay County Fiscal Court did not attempt to collect past due ambulance service accounts. After six billing statements the county no longer attempts to collect receivables for the ambulance service. The following amounts have been written off as "adjustments" to receivables:

- Fiscal Year Ending June 30, 2013: \$698,531
- Fiscal Year Ending June 30, 2014: \$671,092
- Fiscal Year Ending June 30, 2015: \$394,749
- Fiscal Year Ending June 30, 2016: \$221,721

- Fiscal Year Ending June 30, 2017: \$271,647

The total amount of ambulance service receivables that have been written off from Fiscal Year 2013 to Fiscal Year 2017 is \$2,257,740.

When an ambulance service bill becomes delinquent, the fiscal court sends a letter to the patient stating that the account will be turned over to collections. However, after six billing statements, the patient is not rebilled and the fiscal court does not turn over any accounts to collections.

The practice of forgiving delinquent ambulance bills not only results in lost revenue for the ambulance service but results in preferential management of those accounts. Section 52 of the Kentucky Constitution prohibits the fiscal court from forgiving debt in which the amount can be precisely determined and which is not in dispute, as is the case with these ambulance bills.

We recommend the Clay County Fiscal Court implement procedures in order to collect past due ambulance service billings and discontinue the practice of forgiving debts owed.

County Judge/Executive's Response: Clay County Fiscal Court has contracted with a company for collections.

The Clay County Fiscal Court did not have sufficient internal controls over credit card disbursements: This is a repeat finding and was included in the prior year audit report as Finding 2016-006. The Clay County Fiscal Court has not implemented proper internal control procedures over credit card disbursements. The fiscal court approved payment of two invoices for ambulance service fuel purchases that were missing 43 original receipts totaling \$2,051.

The lack of internal controls over credit card disbursements allowed for the payment of invoices without sufficient supporting documentation. According to the county treasurer, receipts for fuel were not always properly maintained by employees who made credit card purchase.

The fiscal court disbursed funds without supporting documentation that the disbursement is valid expense of the county and a proper use of county funds.

Good internal controls require proper supporting documentation to be maintained to support disbursements.

We recommend the Clay County Fiscal Court strengthen internal controls over credit card disbursements to ensure all credit card purchases are supported by original receipts to ensure that disbursements are proper.

County Judge/Executive's Response: County Judge/Executive has notified supervisors and County Jailer, that all receipts are to be turned into the office.

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 2016-008. 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, the following occurred:

- Thirty-nine disbursements were paid without a purchase order
- Three disbursements had a purchase order issued after the date of the invoice
- The encumbrance list was misstated because a list of outstanding purchase orders was not available to compile an accurate listing of encumbrances.

Internal controls over purchase orders were not operating as intended during Fiscal Year 2017. The county treasurer stated that each department has been given 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 deficiencies above occurred. In addition, encumbrances were misstated. These deficiencies could result in inaccurate financial reporting and misappropriation of assets.

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 a 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 supervisors and Jailer 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 2016-009. The Clay County Fiscal Court did not properly bid fuel disbursements totaling \$111,112 to one vendor. Additionally, for Fiscal Year 2017, 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.

Sufficient internal controls were not in place over the bidding process to ensure items were not purchased from vendors without first advertising or receiving bids when necessary on all purchases required to be bid. There were two bidders for road materials and the bids were close. The fiscal court accepted both bids.

By limiting competition or not receiving bids at all, 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) states, “[a]ll bids for the construction or maintenance of county roads and bridges shall be received at the time and placed 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.” KRS 178.140(2) states, “[t]he 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: Fuel was bid for 2017-2018 fiscal year.

The Clay County Fiscal Court paid an employee as a salaried and hourly employee: This is a repeat finding and was included in the prior year audit report as Finding 2016-010. One county employee is receiving wages as a salaried employee while also receiving hourly and overtime pay for another position; however, the time sheet only reflects hours for the position that was considered hourly.

The Clay County Fiscal Court is paying this employee under the same budgeted line item title attributed to the employee’s salary. This line item has the budget to pay for both positions. The fiscal court and employees responsible were unaware of labor laws prohibiting the practice of an employee holding both a salary and hourly position in concurrence.

The Clay County Fiscal Court is not in compliance with U.S. Department of Labor 29 CFR Part 541.

U.S. Department of Labor Fact Sheet #17G states “[b]eing paid on a ‘salary basis’ means an employee regularly receives a predetermined amount of compensation each pay period on a weekly, or less frequent, basis. The predetermined amount cannot be reduced because of variations in the quality or quantity of the employee’s work. Subject to exceptions listed below, an exempt employee must receive the full salary for any week in which the employee performs any work, regardless of the number of days or hours worked.”

Section 13(a)(1) of the Fair Labor Standards Act provides an exemption from both the minimum wage and overtime pay requirements for employees employed as bona fide executive, administrative, and professional employees (including teachers and academic administrative personnel in elementary and secondary schools), outside sales employees, and certain skilled computer professionals (as defined in the Department of Labor's regulations).

U.S. Department of Labor Fact Sheet #17C states

To qualify for the administrative employee exemption, all of the following tests must be met:

- The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than \$455 per week;
- The employee's primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

We recommend the Clay County Fiscal Court seek guidance from the Clay County Attorney to determine if the employee is qualified as an hourly or salaried employee. In addition, we recommend the timesheet reflect actual hours worked in each position.

County Judge/Executive's Response: Additional compensation was given, monthly, when the employee took on the additional duties of the County Treasurer. Change to wages were approved 6/29/17 court meeting.

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 2016-011. The Clay County Fiscal Court does not have proper internal controls over the payroll process. During the fiscal year ending June 30, 2017, the following issues were noted:

- Three employees listed additional hours for on-call and at-home work without specification of when hours were worked.
- Nine timecards were approved without employee signatures.
- Eleven timecards were processed without supervisor approval.
- Three employees were paid without timecard documentation.
- Five employees are paid as salary regardless of the hours worked.
- Leave balances are not maintained for two of the salaried employees

Weak internal controls over payroll have allowed these issues to go undetected.

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) Hours of Work states, “[t]he 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: We have notified salaried employees concerning their documentation of time worked. Supervisors will be notified again concerning the signing and documentation of hours called out. Will begin record of sick and vacation time.

The Clay County Fiscal Court incorrectly amended the budget of the general fund, Local Governmental Economic Assistance Fund, and occupational tax fund: This is a repeat finding and was included in the prior year audit report as Finding 2016-013. The general fund, LGEA fund, and occupational tax fund exceeded the administration line item budget by \$231,150; \$5,081; and \$475,581, respectively. The budget line items should not show a negative balance. Since the amendment created a negative line item, it created the impression that the county did not have funds to transfer although transfers had been made within the available funds. Neither the fiscal court nor the Department for Local Government (DLG) should approve an amendment indicating a negative line item budget.

The fiscal court followed usual protocol and used the account to balance its budget. There was a transfer account also budgeted; however, there were not sufficient funds to make the budgeted transfers and they were not made.

Both the fiscal court and DLG approved the budget amendments. No funds were transferred beyond those available and there was no ending deficit in the fund balance. Although the overall budget variance was not affected, the amendment did affect line items.

The negative budget line item gives the impression that no funds were available for transfer and that the transferred funds were not actually available and the budget was exceeded. The county made the actual cash transfers properly.

The *County Budget Preparation and State Local Officer Policy Manual*, issued by DLG, states, “[t]he fiscal court should be constantly monitoring receipts and expenditures.”

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 Clay County Fiscal Court not approve budget amendments that create negative line items.

County Judge/Executive’s Response: This was the result of over estimating income, not due to over spending of the budget. Will try to estimate more closely.

The Clay County Jail Commissary used a debit card for purchases during Fiscal Year 2017: This is a repeat finding and was included in the prior year report as Finding 2016-015. The Clay County Jail used a debit card to make some purchases for the jail commissary. During Fiscal Year 2017, disbursements totaling \$204 were made using a debit card.

Jail management was unaware that use of a debit card which allows immediate electronic payment of expenses was an unacceptable form of disbursement. The jailer stated that after the prior year exit conference that she stopped using a debit card and applied for a credit card for the jail.

Ineffective internal controls increase the risk of misappropriation of funds from the jail commissary account. The lack of supporting documentation does not permit auditors to confirm funds were used consistent with state law.

The Department for Local Government, under the authority of KRS 68.210, gives the state local finance officer the authority to prescribe minimum requirements for handling public funds. According to the *County Budget Preparation and State Local Finance Officer Policy Manual*, disbursements are to be made by check only.

We recommend the Clay County Jailer ensure that disbursements are made by check only, in accordance with the *County Budget Preparation and State Local Finance Officer Policy Manual*.

County Judge/Executive’s Response: Jailer to respond.

County Jailer's Response: The use of debit card was a prior year finding in the 2016-2015 audit. After the prior year exit conference we stopped using debit card and applied for a credit card. The issue was resolved.

The Clay County Fiscal Court did not adequately identify federal grants or maintain an accurate Schedule of Expenditures of Federal Awards (SEFA): This is a repeat finding and was included in the prior year audit report as Finding 2016-016. The Clay County Fiscal Court did not adequately identify federal grants or accurately maintain a Schedule of Expenditures of Federal Awards (SEFA). The original SEFA provided to auditors was incorrect. Several adjustments totaling \$82,071 were made to correctly document federal expenditures for Fiscal Year 2017.

The accounting personnel are not always informed of federal expenditures and do not appear to have been properly trained to maintain an accurate SEFA with the required information such as the Catalog of Federal Domestic Assistance (CFDA) numbers. Inadequate controls over properly maintaining the SEFA form has contributed to inaccurate reporting.

Failure to maintain an accurate SEFA could result in a failure to properly obtain a single audit in accordance with Uniform Guidance. This could endanger future federal funding.

Per 2 CFR 200.501(a), “[a] non-Federal entity that expends \$750,000 or more during the non-Federal entity’s fiscal year in Federal awards must have a single or program-specific audit conducted for that year in accordance with the provisions of this part.” Good internal controls dictate the fiscal court prepare a materially accurate SEFA and include total federal awards expended for each individual federal program. Completeness and accuracy are critical to the SEFA preparation.

We recommend the Clay County Fiscal Court implement internal controls to immediately recognize all federal awards and keep track of the federal grant information including the identifying CFDA number. An employee should be assigned to track federal expenditures while maintaining an accurate SEFA.

County Judge/Executive's Response: Working with DES Coordinator and County Treasurer to try and maintain better Schedule of Expenditures.

An emergency budget amendment was declared for a nonemergency situation: On June 21, 2017, the Clay County Fiscal Court accepted an emergency budget amendment for a nonemergency situation. The budget for Fiscal Year 2016-2017 was amended to increase occupational tax and water line funds by \$236,536.

An emergency budget amendment was declared because there was not time to publish and advertise before the end of the fiscal year. Time constraints do not meet the definition of a legitimate emergency.

By declaring an emergency for a nonemergency situation, proper procedures for amendments to the county budget were not followed

The *County Budget Preparation and State Local Finance Officer Policy Manual* states, “[a] budget amendment is an ordinance and must be approved by the fiscal court in the statutorily prescribed manner including advertising and publishing requirements. All amendments to a county budget must be approved by the State Local Finance Officer as mandated by KRS 68.280.” It further states, “[a]ny amendments to a county budget submitted to the State Local Finance Officer on an emergency basis must strictly adhere to the provisions of KRS 67.078 and a photocopy of the fiscal court order naming and describing the emergency must accompany the budget amendment pursuant to KRS 68.280.”

We recommend the Clay County Fiscal Court follow proper procedures for adopting budget amendments. If an emergency budget amendment is to be adopted, the Clay County Fiscal Court must first declare an emergency and describe the nature of the emergency. We further recommend the Clay County Fiscal Court submit all budget amendments to the State Local Finance Officer.

County Judge/Executive’s Response: The meeting was identified as an emergency meeting in order to get the funds amended into the 2016-17 budget. This was the procedure we were advised to do by the Department of Local Government. DLG was sent a copy of the amendment after the first reading, however they are not required to sign off on the amendment, since there is no second reading.

Auditor’s Reply: Emergency budget amendments are intended to be for true emergencies and not for modification to a fiscal court’s budget.

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

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