



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

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Knox County Fiscal Court for the fiscal year ended June 30, 2015. 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 Knox 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 non-compliance with laws, regulations, contracts and grants. The auditor must also comment on material weaknesses involving the internal control over financial operations and reporting.

The audit contains the following comments:

The Knox County Fiscal Court lacks adequate segregation of duties over disbursements.

The county treasurer posts the disbursements to the ledgers, prepares and signs the checks, and reconciles the bank account monthly. In addition, the county treasurer prepares the financial report. The condition is a result of a limited budget, which restricts the number of employees the fiscal court can hire or delegate duties to. Lack of segregation of duties increases the fiscal court's risk of misappropriation of assets, errors and inaccurate financial reporting. Segregation of duties over disbursements or implementation of compensating controls due to a limited number of staff, is essential for providing protection to employees in the normal course of performing their duties and can also prevent inaccurate financial reporting and misappropriation of assets. We recommend the fiscal court strengthen internal controls by segregating these

duties. If segregation is not possible due to a limited number of staff, strong oversight should be implemented. The employee providing this oversight should document his or her review by initialing all source documentation.

County Judge/Executive J.M. Hall's response: In the future one employee will complete reconciliations monthly, another employee will review the reconciliations and initial that they have reviewed the reconciliations.

The Knox County Fiscal Court did not have strong internal controls over disbursements. Internal controls over disbursements were not operating as intended during Fiscal Year 2015. Disbursements were not properly authorized, supporting documentation was not maintained and appropriate, and proper procedures were not followed. As a result of not monitoring controls, the below deficiencies occurred, and could result in inaccurate reporting and misappropriation of assets. The following exceptions were noted:

- The fiscal court approved one claim in the amount of \$269,804. However, the available line item for "New Machinery and Equipment" was \$264,853, leaving a negative balance of \$4,951 when payment was approved and paid.
- Eight instances were noted where disbursements were made and not presented to the fiscal court prior to payment or included on the annual standing order to pre-approve certain recurring expenses. Subsequent to payment, they were presented to the fiscal court and approved.
- Two disbursements were not presented to the fiscal court. One was for asphalt in the amount of \$224,159, and the other was \$82 for affidavit on deed tax.
- Two disbursements were not paid within 30 days. No late fees or interest were incurred.
- Four instances of no documentation to support contributions made to the hospital and one for the sheriff's office. In addition, the hospital contributions were incorrectly posted as capital assets.
- Three credit card disbursements totaling \$248 did not have receipts, and two totaling \$330 were missing invoices. Two purchase orders were dated after invoice and interest of \$0.15 was charged for a \$15 balance not paid in prior month.
- Hauling tickets were not signed by road department personnel for gravel documenting the delivery date and quantity.
- Ten out of 115 gas receipts tested were not maintained to support the monthly statement.
- Four instances were noted where disbursements did not have purchase orders attached to the invoice.
- Twelve out of 69 invoices tested had purchase orders dated after the date of the invoices or receipts. Therefore items could have been ordered or services rendered without prior approval to ensure adequate funds were available in each account.
- Purchase orders attached to four gravel invoices tested totaling \$183,736 did not agree to the purchase order number on the haul tickets.

Proper internal controls over disbursements are important to ensure purchase orders are created when sufficient funds are available, are presented to the fiscal court, include proper supporting documentation, and are paid within 30 days. KRS 68.210 gives the State Local Finance Officer the authority to prescribe a uniform system of accounts. Per the *County Budget Preparation and*

State Local Finance Officer Policy Manual, issued by the Department for Local Government (DLG) “purchases shall not be made without approval by the judge/executive (or designee), and/or a department head. ... Purchase requests shall not be approved in an amount that exceeds the available line item appropriation unless the necessary and appropriate transfers have been made.”

KRS 68.300 states, in part, “[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.” KRS 68.275 requires claims within budget line items and authorized by the fiscal court be paid by the county judge/executive and co-signed by the county treasurer. In addition, KRS 68.275 requires the county judge/executive to present all claims to the fiscal court for review prior to payment unless the expenses are included on a standing order adopted by the fiscal court to preapprove the payment of certain claims such as monthly payroll and utility expenses. Furthermore, KRS 65.140 requires invoices to be paid within 30 days of being received. We recommend the fiscal court implement proper internal controls over disbursements and ensure they are operating effectively.

County Judge/Executive J.M. Hall’s response: In the future we will try to have all disbursements pre-approved and the fiscal court has implemented more internal controls over disbursements in that the County Treasurer is reviewing the disbursements made by the Finance Officer to assure disbursements are with the approved amounts.

The Knox County Fiscal Court did not have adequate internal controls over gravel inventory. The Knox County Fiscal Court does not have adequate internal controls over gravel purchased and stored at the county’s road department. The road materials are contained within a fenced area to deter unauthorized access, and the county maintains a log for gravel that lists the date and location of job sites. However, the log does not document the gravel hauled to the road department from the rock quarry, making it impossible to estimate how much gravel should be in the stockpile. The fiscal court’s lack of controls has created an opportunity for misappropriation of the county’s assets to occur. When controls are not in place to protect the county’s resources, the risk of fraud increases. Good internal controls dictate the fiscal court have better recordkeeping over the gravel stockpile and log gravel activity. We recommend the county maintain a log to track the gravel hauled to the road department, and also track the gravel hauled from the road department to jobsites. This would allow an estimate of gravel to be on hand and help determine if a shortage exists.

County Judge/Executive J.M. Hall’s response: The Fiscal Court has now assigned an employee to monitor and log all incoming and outgoing materials including gravel.

The Knox County Fiscal Court did not follow proper bid laws and regulations. The Knox County Fiscal Court did not properly bid and made payments to three vendors for purchases over \$20,000 in fiscal year 2015. These expenditures were for a jail van purchased for \$23,220, election machines for \$110,000, and two Mack trucks purchased for the road department for \$269,804. The election machines were bid and a vendor was awarded, but the county purchased from a different vendor than the one that was awarded the bid.

The fiscal court bid some purchases over \$20,000, but sufficient internal controls were not in place over the procurement process to ensure items were not purchased from vendors without first advertising or receiving bids when necessary. By limiting competition or not receiving bids at all, the fiscal court may not get the benefit 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, "Except 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." We recommend the 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 J.M. Hall's response: If an emergency has not been declared, the Fiscal Court will bid all purchases required by KRS 424.260.

The Knox County Fiscal Court did not ensure the same level of health insurance benefits are provided to all county employees as stated in Kentucky Attorney General Opinion (OAG) 94-15. County employees are not receiving the same level of health insurance benefits. Elected officials are receiving county paid family coverage while others are paying for the extra cost for family coverage. During the fiscal year ended June 30, 2015, the county paid as much as \$986 per month per employee for additional costs for the family plan over the single plan. The fiscal court believes they can separate elected officials and county employees. According to the County Administrative Code, "The County pays the premium for all individual health insurance policies offered by the county; except, however, the county will pay the premium for family health insurance plans for all elected county officials." As a result of different levels of health insurance benefits among the employees, it appears to be discrimination among the employees. In addition, county funds are being spent for the personal benefit of some employees which could have been expended on other necessary items for the benefit of the county. OAG 94-15 states, "The basic statute providing for governmentally funded health coverage (KRS 79.080) for public employees does not provide for one level of coverage for officers, and another level for employees. Accordingly, we believe such differing coverage would not be lawful as not authorized by statute." We recommend the fiscal court follow the direction expressed in OAG 94-15 and ensure the same level of health insurance coverage for all employees. The fiscal court should update the County Administrative Code to comply with KRS 79.080 and OAG 94-15.

County Judge/Executive's J.M. Hall's response: All county employees are equal and all county elected officials are equal.

The Knox County Jail commissary lacks adequate segregation of duties over receipts and disbursements. Due to the limited number of employees, the jail has a lack of segregation of duties over receipts and disbursements. The bookkeeper prepares deposits and posts these deposits to the receipts ledger. The bookkeeper also prepares and signs checks and posts these disbursements to the disbursements ledger. This condition is a result of a limited budget, which restricts the number of employees the county can hire or delegate duties to. Lack of segregation

of duties increases the risk of misappropriation of assets, errors, and inaccurate financial reporting. Adequate segregation of duties would prevent the same person from having a significant role in these incompatible functions. In addition, proper segregation of duties protects employees in the normal course of performing their daily responsibilities. Segregation of duties, or the implementation of compensating controls, is essential for providing protection to employees in the normal course of business. We recommend the jailer implement strong oversight in these areas, either by having an employee independent of those functions or the jailer review transactions and initial the documentation.

County Judge/Executive J.M. Hall's response: See Jailer's Response.

County Jailer Mary Hammons' response: We will be working on segregation of duties.

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

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