

**REPORT OF THE AUDIT OF THE
MARTIN COUNTY
SHERIFF'S SETTLEMENT - 2014 TAXES**

**For The Period
January 1, 2015 Through June 11, 2015**



**MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS
www.auditor.ky.gov**

**209 ST. CLAIR STREET
FRANKFORT, KY 40601-1817
TELEPHONE 502.564.5841
FACSIMILE 502.564.2912**

EXECUTIVE SUMMARY
AUDIT OF THE
MARTIN COUNTY
SHERIFF'S SETTLEMENT - 2014 TAXES

For The Period
January 1, 2015 Through June 11, 2015

The Auditor of Public Accounts has completed the audit of the Sheriff's Settlement - 2014 Taxes for the Martin County Sheriff for the period January 1, 2015 through June 11, 2015. 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 2014 taxes of \$3,117,979 for the districts, retaining commissions of \$118,104 to operate the sheriff's office. The sheriff distributed 2014 taxes of \$3,066,420 to the districts. Refunds of \$102,676 are due to the sheriff from the taxing districts.

Report Comments:

- 2014-001 The Sheriff Did Not Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Did Not Enter Into A Written Agreement To Protect Deposits
- 2014-002 The Sheriff Did Not Have Adequate Controls Over Franchise Bills And Did Not Review Franchise Tax Bills Received From The County Clerk Before Mailing
- 2014-003 The Sheriff Did Not Review The Official Receipt Before Signing

Deposits:

The sheriff's deposits as of March 9, 2015 were exposed to custodial credit risk as follows:

- Uncollateralized and Uninsured \$1,766,521

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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 Kelly Callaham, Martin County Judge/Executive
Honorable John Kirk, Martin County Sheriff
Members of the Martin County Fiscal Court

Independent Auditor's Report

Report on the Financial Statement

We have audited the Martin County Sheriff's Settlement - 2014 Taxes for the period January 1, 2015 through June 11, 2015 - 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.

209 ST. CLAIR STREET
FRANKFORT, KY 40601-1817

TELEPHONE 502.564.5841
FACSIMILE 502.564.2912

WWW.AUDITOR.KY.GOV

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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 Martin County Sheriff on the basis of the 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 Martin County Sheriff, for the period January 1, 2015 through June 11, 2015.

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 January 1, 2015 through June 11, 2015 of the Martin 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 December 6, 2016 on our consideration of the Martin 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 effectiveness of the Martin County Sheriff's 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 Martin 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 Kelly Callaham, Martin County Judge/Executive
Honorable John Kirk, Martin County Sheriff
Members of the Martin 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:

- 2014-001 The Sheriff Did Not Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Did Not Enter Into A Written Agreement To Protect Deposits
- 2014-002 The Sheriff Did Not Have Adequate Controls Over Franchise Bills And Did Not Review Franchise Tax Bills Received From The County Clerk Before Mailing
- 2014-003 The Sheriff Did Not Review The Official Receipt Before Signing

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

December 6, 2016

MARTIN COUNTY
JOHN KIRK, SHERIFF
SHERIFF'S SETTLEMENT - 2014 TAXES

For The Period January 1, 2015 Through June 11, 2015

<u>Charges</u>	County Taxes	Special Taxing Districts	School Taxes	State Taxes
Increases Through Exonerations	\$ 23	\$ 42	\$ 158	\$ 25
Franchise Taxes	110,846	210,102	669,669	
Additional Billings	20	36	137	22
Penalties	2,707	5,523	17,606	2,611
Transferred From Outgoing Sheriff	259,414	508,958	1,692,202	498,018
Gross Chargeable to Sheriff	<u>373,010</u>	<u>724,661</u>	<u>2,379,772</u>	<u>500,676</u>
 <u>Credits</u>				
Exonerations	693	1,298	4,750	762
Discounts	2,419	4,796	15,765	4,469
Delinquents:				
Real Estate	24,196	44,709	165,818	26,618
Tangible Personal Property	43,181	82,711	254,400	154,915
Uncollected Franchise Taxes	3,866	7,094	17,680	
Total Credits	<u>74,355</u>	<u>140,608</u>	<u>458,413</u>	<u>186,764</u>
Taxes Collected	298,655	584,053	1,921,359	313,912
Less: Commissions *	<u>12,693</u>	<u>24,822</u>	<u>67,248</u>	<u>13,341</u>
Taxes Due	285,962	559,231	1,854,111	300,571
Taxes Paid	290,471	600,409	1,886,654	288,886
Refunds (Current and Prior Year)	<u>3,354</u>	<u>6,186</u>	<u>14,906</u>	<u>11,685</u>
(Refunds Due Sheriff) as of Completion of Audit	<u>\$ (7,863)</u>	<u>\$ (47,364)</u>	<u>\$ (47,449)</u>	<u>\$ 0</u>

**

* Commissions:

4.25% on \$1,196,620

3.5% on \$1,921,359

** Special Taxing Districts:

Library District \$ (7,153)

Health District (2,507)

Extension District (4,913)

City of Inez (32,791)

(Refunds Due Sheriff) \$ (47,364)

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

MARTIN COUNTY
NOTES TO FINANCIAL STATEMENT

June 11, 2015

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 Martin 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. These requirements were not met, as the sheriff did not have a written agreement with the bank.

MARTIN COUNTY
NOTES TO FINANCIAL STATEMENT
June 11, 2015
(Continued)

Note 2. Deposits (Continued)

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 Martin 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. On March 9, 2015, the sheriff's bank balance was exposed to custodial credit risk as follows:

- Uncollateralized and Uninsured \$1,766,521

Note 3. Tax Collection Period

The real and personal property tax assessments were levied as of January 1, 2014. Property taxes were billed to finance governmental services for the fiscal year ended June 30, 2015. Liens are effective when the tax bills become delinquent. The collection period for these assessments was January 9, 2015 through June 11, 2015.

Note 4. Interest Income

The Martin County Sheriff earned \$136 as interest income on 2014 taxes. The sheriff distributed the appropriate amount to the school district as required by statute, and the remainder was used to operate the sheriff's office.

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

The Martin County Sheriff collected \$20,737 of 10% add-on fees allowed by KRS 134.119(7). This amount was used to operate the sheriff's office.

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 Kelly Callaham, Martin County Judge/Executive
Honorable John Kirk, Martin County Sheriff
Members of the Martin 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 Martin County Sheriff's Settlement - 2014 Taxes for the period January 1, 2015 through June 11, 2015 - Regulatory Basis and the related notes to the financial statement and have issued our report thereon dated December 6, 2016. The Martin 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 Martin County Sheriff's internal control over financial reporting (internal control) to determine 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 Martin County Sheriff's internal control. Accordingly, we do not express an opinion on the effectiveness of the Martin 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 certain deficiencies in internal control that we consider to be material weaknesses.

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 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 deficiencies described in the accompanying comments and recommendations as items 2014-002 and 2014-003 to be material weaknesses.



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 Martin 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 an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying comments and recommendations as item 2014-001.

Sheriff's Responses to Findings

The Martin County Sheriff's responses to the findings identified in our audit are included in the accompanying comments and recommendations. The Martin County Sheriff's responses were not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on them.

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,



Mike Harmon
Auditor of Public Accounts

December 6, 2016

COMMENTS AND RECOMMENDATIONS

MARTIN COUNTY
JOHN KIRK, SHERIFF
COMMENTS AND RECOMMENDATIONS

For The Period January 1, 2015 Through June 11, 2015

STATE LAWS AND REGULATIONS:

2014-001 The Sheriff Did Not Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Did Not Enter Into A Written Agreement To Protect Deposits

The sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). The sheriff failed to enter into a written agreement with the depository institution to ensure collateralization of deposits until May 31, 2016. On March 9, 2015, the sheriff's deposits of public funds were uninsured and unsecured in the amount of \$1,766,521. According to KRS 66.480(1)(d) and KRS 41.240, financial institutions maintaining deposits of public funds are required to pledge securities or provide surety bonds as collateral to secure these deposits if the amounts on deposit exceed the \$250,000 amount of insurance coverage provided by the FDIC. We recommend the sheriff require the depository institution to pledge or provide collateral in an amount sufficient to secure deposits of public funds at all times. We also recommend the sheriff enter into a written agreement with the depository institution to secure the sheriff's interest in the collateral pledged or provided by the depository institution. According to federal law, 12 U.S.C.A. § 1823(e), this agreement, in order to be recognized as valid by the FDIC, should be (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.

Sheriff's Response: We were assured by the bank that this was being done. We were unaware that there were inadequate pledges and will follow up with the bank regarding this matter.

INTERNAL CONTROL - MATERIAL WEAKNESSES:

2014-002 The Sheriff Did Not Have Adequate Controls Over Franchise Bills And Did Not Review Franchise Tax Bills Received From The County Clerk Before Mailing

The sheriff did not review all franchise tax bills before mailing to the taxpayer and any tax bills that are found with errors should be given back to the county clerk to correct and reissue. A lack of adequate controls over franchise billing caused three franchise tax bills to have the following issues:

- One amended franchise tax bill was calculated using the full assessment amounts instead of the amended tax assessment.
- One franchise tax bill charged real estate taxes when the assessment was for tangible only.
- One franchise tax bill overcharged penalties.

These errors resulted in taxpayer refunds totaling \$71,748.

Good internal controls dictate the sheriff implement procedures to ensure the accuracy of franchise bills. In order to review and recalculate franchise tax bills, the sheriff should do the following:

1. Obtain a copy of the certification from the Department of Revenue (from the county clerk's office). If the certification has been amended, obtain both the original certification and the amended certification to determine the correct amount to be billed.
2. Review the certification.

MARTIN COUNTY
 JOHN KIRK, SHERIFF
 COMMENTS AND RECOMMENDATIONS
 For The Period January 1, 2015 Through June 11, 2015

INTERNAL CONTROL - MATERIAL WEAKNESSES: (Continued)

2014-002 The Sheriff Did Not Have Adequate Controls Over Franchise Bills And Did Not Review Franchise Tax Bills Received From The County Clerk Before Mailing (Continued)

3. Review the tax bill to determine if all districts have been included with the proper assessments for both real estate and tangible. It is important that the correct assessments are applied to either real estate or tangible because tax rates are different for each.
4. Determine if tax rates are accurate based on the appropriate tax year.
5. After determining if tax rates are correct and assessments are correct, recalculate the tax bill.
6. If an amended bill is issued, determine the amounts due the districts for the amended amount collected by calculating the difference between the original certification and the amended certification. Recalculate the bill.
7. After collecting the taxes, include these amounts on the monthly report and distribute to the taxing districts.

We recommend the sheriff review each franchise bill for accuracy before mailing to the taxpayer. The sheriff should notify the county clerk when an error is noted so that the bill can be corrected before being sent out.

Sheriff's Response: We will validate the accuracy of the clerk's calculations and follow recommended procedures.

2014-003 The Sheriff Did Not Review The Official Receipt Before Signing

During the audit we found that 235 tax bills included tangible tax for the City of Inez that should not have been charged to taxpayers. When the data was interpreted by the tax software, there was an error in coding which caused taxpayers to be overcharged for tangible taxes for the City of Inez. This error resulted in taxpayer refunds totaling \$32,791.

According to the Kentucky Department of Revenue, Office of Property Valuations *Property Tax Duties of the Sheriff's Office* handbook, "...since the receipt is the basis for charges of property taxes to the sheriff's office for the collection year, the sheriff also needs to be sure that the amounts on the receipt are correct." Good internal controls dictate the sheriff implement procedures to review the official receipt for accuracy before signing it.

We recommend the sheriff work with the PVA and review the official receipt before signing, comparing prior official receipts and discuss any large or unusual variances with the PVA. The sheriff should also recalculate a sample of bills and compare them to the tax roll to verify that tax assessments and districts are correct.

Sheriff's Response: These bills were sent out before we took office and thus were beyond our control; however we will follow these recommendations for future years.

