



Auditor of Public Accounts  
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FOR IMMEDIATE RELEASE

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### **Harmon Releases Audit of Martin County Fiscal Court**

**FRANKFORT, Ky.** – State Auditor Mike Harmon has released the audit of the financial statement of the Martin County Fiscal Court for the fiscal year ended June 30, 2019. 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 Martin 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 Martin County Fiscal Court Did Not Prepare An Accurate Schedule of Expenditures of Federal Awards:** The original Schedule of Expenditures of Federal Awards (SEFA) provided to auditors was materially incorrect and grants were not adequately identified. The SEFA did not contain the Catalog of Federal Domestic Assistance (CFDA) numbers for the Housing and Urban Development (HUD) and American Recovery and Reinvestment (ARRA) grants. In addition, HUD expenditures of \$75,000 were not included on the original SEFA.

The fiscal court did not implement sufficient internal controls to ensure county personnel could prepare an accurate SEFA. As stated in 2 CFR §200.510(b), “the auditee must also prepare a

schedule of expenditures of federal awards for the period covered by the auditee's financial statement which must include the total federal awards expended."

Failure to maintain an accurate SEFA with the required information such as the CFDA numbers could result in a failure to properly obtain a single audit in accordance with Uniform Guidance. This could endanger future federal awards 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 provision of this part."

The auditee shall per 2 CFR §200.510(b) (3), "provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number with the CFDA information is not available."

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

*Former County Judge/Executive's Response: This is specifically related to the 2019-008, and pertains to the previous administration.*

**The Martin County Fiscal Court's overall design and operation of the control environment needs improvement:** This is a repeat finding and was included in the prior year audit report as Finding 2018-001. Internal controls over the accounting process did not operate as designed resulting in procedures not being followed and creating an overall weak internal control environment. These numerous weaknesses significantly increase the risk of fraud, misappropriation of funds, and the fiscal court's ability to ensure that financial data is recorded, processed, and reported in accurate and reliable manner.

The items noted during the audit show the accounting process did not operate as designed due to poor internal controls and are discussed further in detail in the following findings:

- The Martin County Fiscal Court does not have adequate internal controls over disbursements
- The Martin County Fiscal Court does not have adequate internal controls over receipts
- The Martin County Fiscal Court did not have a policy to address reimbursements to the coroner's office for transports
- The Martin County Fiscal Court does not maintain an accurate capital asset schedule or insurance listing
- The Martin County Fiscal Court has \$75,000 of questioned Housing and Urban Development (HUD) funds

Management has a responsibility to implement internal controls that provide reasonable assurance regarding the reliability of financial reporting. Internal control is a management process for keeping an entity on course in achieving its business objectives. These controls should ensure

resources are protected from waste, loss, and misuse and ensure reliable data is obtained, maintained, and fairly disclosed. Entities are required to establish controls to provide reasonable assurance that the recording, processing, and reporting of data is properly performed within the framework of financial management system.

We recommend the fiscal court implement internal controls over the financial accounting system that ensure an adequate internal control structure, that includes management oversight, provides reasonable assurance that assets are safeguarded and transactions are processed in accordance with applicable laws and regulations.

*Former County Judge/Executive's Response: This summarizes 2019-002, -004, -005, -007, and -009. Please refer to the responses provided.*

**The Martin County Fiscal Court does not have adequate internal controls over disbursements:** This is a repeat finding and was included in the prior year audit report as Finding 2018-004. The fiscal court's controls over disbursements were not operating as intended. Based on items tested, disbursements were not properly authorized, supporting documentation was not maintained, and appropriate and proper procedures were not followed.

The deficiencies listed below were able to occur due to lack of monitoring of controls, which diminish the effectiveness of the controls put in place over disbursements by fiscal court. These deficiencies could create errors in recording or allow for the possibility of misappropriation of assets.

As a result, the following exceptions were noted:

- Sixteen disbursements were not paid within 30 days.
- Fourteen settlement agreements remained unpaid as of the fiscal year end.
- Four transactions totaling \$69,266 were prior year expenditures not paid within 30 days.
- Four transactions did not have adequate documentation.
- The county did not provide proper bid documentation for two transactions that exceed the county's administrative code bid threshold of \$10,000.
- The county issued purchase orders when they did not have the cash balance to cover. The county reported encumbrances for the jail fund of \$301,434 and federal grant fund \$127,306 at June 30, 2019; however, the ending cash balance in these funds was only \$80,970 and \$85,595, respectively.

Proper internal controls over disbursements are important to ensure purchase orders are created with sufficient funds available, include proper supporting documentation, and are paid in a timely manner. KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. Per the Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual*, "purchases shall not be made prior to approval by the County Judge/Executive (or designee) or department head."

In addition, according to the fiscal court's administrative code, "all purchases of items of like or similar nature in excess of \$10,000 in a fiscal year shall be advertised for bids, except otherwise

provided in this administrative code. Items normally supplied as a unit shall not be artificially divided for the purpose of avoiding the competitive bidding procedure of this administrative code.” 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.

*Former County Judge/Executive’s Response: The previous administration left the court with several unpaid invoices from both the current and prior years. The current administration issued a bank franchise tax and doubled the occupational tax. The court updated their purchasing policy which increased the bid threshold from \$10,000 to \$30,000 to match the states guideline.*

**The Martin County Fiscal Court does not have adequate internal controls over receipts:** This is a repeat finding and was included in the prior year audit report as Finding 2018-005. The Martin County Treasurer prepared and deposited receipts, posted receipts to the accounting system, prepared monthly reports for the fiscal court and quarterly reports for the Department for Local Government (DLG), made cash transfers between funds and bank accounts, and performed bank reconciliations. There was no review by another person to ensure daily deposits agree to the receipts ledger.

The lack of adequate segregation of duties and too much control by one individual could result in the undetected misappropriation of assets and errors, and inaccurate financial reporting to occur.

Good internal controls dictate adequate segregation of duties to prevent the same person from having complete control in the receiving, recording, and reporting of funds. A strong internal control structure includes adequate segregation of duties or strong compensating controls to offset the risk caused by the lack of segregation of duties. Without proper segregation or strong compensating controls, the county cannot ensure all receipts are deposited and all bank activity is appropriately documented in the accounting system.

We recommend the fiscal court strengthen internal controls by segregating the duties involved in receiving, recording, reconciling and reporting receipts. If segregation is not possible, we recommend compensating controls, such as a receipt listing prepared by another person to compare to deposit tickets and ledger posting and documentation of oversight and review by a second person.

*Former County Judge/Executive’s Response: This item is related to the previous administration. When the current administration took office in January 2019, changes were implemented. The Judge’s Administrative Assistant opens all incoming mail and receipts all funds. Invoices and funds received are reviewed by either the Judge or Deputy Judge prior to routing to the Finance Office. The invoices are processed by the Finance Officer, Occupational Taxes are routed to the Occupational Tax Director who prepares and makes the deposits, all other receipts are recorded and deposited by the Treasurer. The Finance Officer reconciles the accounts.*

**The Martin County Fiscal Court did not have a policy to address reimbursements to the coroner’s office for transports:** This is a repeat finding and was included in the prior year audit

report as Finding 2018-007. The coroner bills the fiscal court \$300 for reimbursement of expenses to include payments for the transportation of bodies to the chief medical examiner's office in Frankfort. These flat fee transports are performed by either the coroner or one of his deputies and whoever performs the transport receives the \$300 and \$150. All other county employees are reimbursed for actual expenses per the county's administrative code. These \$300 and \$150 lump sum reimbursements totaling \$2,100 are not included on the employees W-2's.

The county did not follow their administrative code which states, "(1) Officials and employees of the Court may be reimbursed for personal expenses incurred while performing their duties as an employee of the Court. Personal expenses shall include food, lodging and travel. (3) Receipts shall be required for hotel bills, airline tickets, and automobile expense where travel is by court-owned vehicle. The use of court owned vehicles is encouraged while on court business. Employees shall be reimbursed \$4.00 for breakfast, \$5.00 for lunch, and \$12.00 for dinner without a receipt. Request for reimbursements in excess of these amounts shall be accompanied by a receipt." The coroner and his deputies are receiving lump sum payments as a fee for services provided, instead of a reimbursement of actual expenses for the coroner's office. Also since the reimbursements are for flat rate and not actual expenses the amounts are taxable; however, they were not included on their W-2's.

KRS 64.410(2) states, in part, "[n]o officer shall demand or receive any fee for his services:...(b) any fee for services rendered when the law has not fixed compensation therefor[.]" Furthermore, KRS 64.530(4) allows the fiscal court to provide a salary for county officers and their deputies and assistants to be fixed no later than the first Monday in May in the officer was elected. The elected officer's compensation may not be changed but the deputies or assistants may be reviewed and adjusted by the fiscal court no later than the first Monday in May in any successive year upon written request by the officer.

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 specially appropriated by the General Assembly."

KRS 64.185 addresses monthly coroner and deputy coroner salaries based on county population as well allows for a per month expense allowance up to \$300/month.

We recommend the fiscal court follow their county's adopted policies and procedures, applicable statutes, and IRS regulations.

*Former County Judge/Executive's Response: The previous administration paid the Coroner and Deputy Coroner in this manner. When this concern was pointed out, the current administration immediately stopped the payments (April 2020).*

**The Martin County Fiscal Court does not maintain an accurate capital asset schedule or insurance listing:** This is a repeat finding and was included in the prior year audit report as Finding 2018-008. The county's capital asset listing and insurance listing are inaccurate. The capital asset listing did not include all items that meet the county's capital asset threshold. Controls are not in

place to ensure that capital assets are being added and removed from the capital asset listing and/or insurance listing.

Not maintaining an accurate list of capital assets or insurance policy could cause capital assets to be uninsured or result in paying for insurance for an asset the county no longer owns. It also leaves capital assets vulnerable to misappropriation and misstatement.

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*, capital asset records are necessary for proper valuation, adequate and accurate insurance coverage, internal control, and long range planning for property replacement. Additionally, good internal controls dictate management oversight of capital assets to prevent misappropriation or theft.

We recommend insurance policies must be updated timely in order for the county to avoid unnecessary costs associated with insurance coverage on assets no longer owned by the county and to ensure that all county assets are properly insured in the event of loss. The county should also conduct a physical inspection of county assets at the end of each year and make comparisons to the county's list of inventoried assets and insurance policy.

*Former County Judge/Executive's Response: The previous administration did not maintain an accurate Capital Assets Schedule. Currently, we have an accurate insurance listing that is confirmed for the insurance company annually in January. The Capital Assets Schedule is currently being updated. We will have an accurate Capital Assets Schedule by March 31, 2022.*

**The Martin County Fiscal Court did not have effective internal controls over federal expenditures:**

Federal Program: CFDA 12.127 Southern and Eastern Environmental Infrastructure

Award Number and Year: 2016

Name of Federal Agency and Pass-Through Agency: U.S. Department of Defense and Kentucky Department of Military Affairs

Compliance Requirements: Procurement, Suspension, and Debarment

Type of Finding: Material Weakness

Amount of Questioned Costs: \$0

The Martin County Fiscal Court failed to implement effective internal controls over federal expenditures. Program expenditures totaling \$1,195,338 were tested giving 100% coverage. Numerous weaknesses were noted which significantly increase the risk of fraud, misappropriation of funds, and noncompliance with federal funds.

During testing the following was noted:

- The fiscal court used restricted federal funds to operate the county. (See Finding 2019-008)
- No purchase orders were maintained for federal expenditures for the 14 transactions that were tested.

- Seven of the 14 transactions tested were not paid within 30 working days.
- The fiscal court was advanced funds; however, waited 18 months to make full payment to the vendor. (See Finding 2019-009)
- The fiscal court did not monitor the contractor for Davis Bacon requirements. (See Finding 2019-010)
- The fiscal court did not monitor for the suspension and debarment requirement.

The fiscal court has not sufficiently overseen the expenditure of federal funds and did not prioritize implementation of an effective internal control system.

An inaccurate implementation of controls and lack of management oversight and involvement can cause noncompliance with federal requirements and jeopardize the fiscal court's future funding.

Uniform Guidance 2 CFR §200.303 states "the non-Federal entity must: (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award."

We recommend the fiscal court implement adequate internal controls to ensure federal compliance requirements are met.

*Former County Judge/Executive's Response: This addresses 2019-004, 2019-008, 2019-009, 2019-010. Please refer to the detailed responses for these items.*

### **The Martin County Fiscal Court Has \$75,000 Of Questioned Housing and Urban Development (HUD) Funds:**

Federal Program: CFDA 12.127 Southern and Eastern Environmental Infrastructure

Award Number and Year: 2016

Name of Federal Agency and Pass-Through Agency: U.S. Department of Defense and Kentucky Department of Military Affairs

Compliance Requirements: Activities Allowed/Unallowed

Type of Finding: Material Weakness

Amount of Questioned Costs: \$75,000

On July 10, 2018, the fiscal court wrote a check from the Housing and Urban Development (HUD) escrow account to the Martin County Sheriff's office in the amount of \$75,000 for a police contract. The funds that are deposited into the HUD escrow account are the rental payments from tenants that have received housing. The CFDA number for this federal program was not provided by the fiscal court. Additional time and research from the auditors was done to obtain the CFDA number.

The fiscal court has cash flow issues and decided to use restricted federal funds to operate the county.

The sheriff's fund owes the HUD fund \$75,000 increasing the deficit fund balance to \$267,951 as of June 30, 2019.

According to Section 3 of the HUD grant agreement, these funds are to be spent on replacing existing roofing material and sheathing, installation of permanent block foundation, doors and windows, exterior siding, insulation, replacement of damaged sheetrock, heating and cooling systems, replacement of existing plumbing and electrical system, installation of a potable drinking water supply and septic system, and renovations for handicapped accessibility.

We recommend the fiscal court not spend restricted funds to operate the county. In addition, we recommend the fiscal court immediately transfer these funds back to the HUD fund.

*Former County Judge/Executive's Response: This action was taken by the previous administration. After the exit for this audit, an emergency court meeting was called to transfer the funds back to the HUD account. The meeting was held on December 7, 2021, and the transfer was completed on December 8, 2021.*

**The Martin County Fiscal Court failed to implement adequate internal controls over cash management of federal funds:**

Federal Program: CFDA 12.127

Award Number and Year: 2016

Name of Federal Agency and Pass-Through Agency: U.S. Department of Defense and Kentucky Department of Military Affairs

Compliance Requirements: Cash Management

Type of Finding: Material Weakness, Noncompliance

Amount of Questioned Cost: \$0

Opinion Modification: Qualified

During the test of federal awards, we found that an invoice was reimbursed before the contractor was paid. The invoice was dated February 28, 2017, in the amount of \$92,750. On October 26, 2017, the fiscal court approved a payment to the vendor in the amount of \$92,750. The fiscal court made the first payment for this invoice on May 31, 2018, in the amount of \$63,049.89, leaving an unpaid balance of \$29,700.11, which was paid on September 6, 2018. The check stub is dated October 26, 2017; however, the check isn't dated until May 31, 2018, which shows the check was originally dated the day of the fiscal court meeting approved payment for the invoice.

The first reimbursement from the federal agency was received and deposited in August 2017, in the amount of \$63,049.89. Therefore, according to documentation, the fiscal court received reimbursement for an expenditure 18 months before the vendor was paid in full.

After the fiscal court approved the payment, the treasurer chose to withhold the payment to the vendor for seven months and did not pay the invoice in full at that time. However, reimbursement for the payment to the vendor was requested and received from the federal agency. It is not clear why the payment was withheld.



The county was not in compliance with federal cash management requirements. These delays in payment of invoices could create errors in recording or allow for the possibility of misappropriation of assets. In addition, internal control weaknesses and noncompliance with grant agreements could affect the county receiving federal funds in the future.

Per the grant agreement for the county to receive reimbursement of funds, they must submit a “sufficient invoice”. A “sufficient invoice” per the agreement must contain the following (1) a written certification by the Non-Federal Sponsor (county) to the Government that it has made specified payments to contractors, suppliers, or employees for performance of work in accordance with this Agreement, or a written certification by the Non-Federal Sponsor (county) to the Government that it has received bills from contractors, suppliers, or employees for performance of work in accordance with this Agreement; (2) copies of all relevant invoices and evidence of such payments or bills received; (3) written identification of such costs that have been paid with Federal program funds and a copy of the written verification from the Federal agency that provided the funds; and (4) a written request for reimbursement for the amount of such specified payments or bills received.

Uniform Guidance 2 CFR §200.303 states “the non-Federal entity must: (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.”

We recommend the fiscal court implement procedures to comply with all federal compliance requirements and all Federal and State laws regarding grant agreements.

*Former County Judge/Executive’s Response: The concern happened under the previous administration. When the new administration took office, the concern was found, the new treasurer documented the concern. The Corp of Engineers was contacted and informed of the issue (undocumented).*

*Currently, projects are tracked on spreadsheets that show the date work was completed/invoice date, date paid, cancelled check received, and the request for reimbursement date.*

**The Martin County Fiscal Court failed to implement adequate internal controls over special tests and provisions - Davis Bacon requirements:**

Federal Program: CFDA 12.127

Award Number and Year: 2016

Name of Federal Agency and Pass-Through Agency: U.S. Department of Defense and Kentucky Department of Military Affairs

Compliance Requirements: Special Tests and Provisions

Type of Finding: Material Weakness, Noncompliance

Amount of Questioned Cost: None

Opinion Modification: Qualified

The fiscal court failed to implement adequate internal controls over the special tests and provisions - Davis Bacon requirements. The fiscal court contracted with a third party that oversaw the planning, design, inspection services, environmental services, and construction administration for the project. The agreement with this third party does not state the construction of this project is subject to the wage rate requirements and the U.S. Department of Labor (DOL) regulations. These items are federal government requirements. In addition, the contractor did not submit weekly, when work was performed, a copy of the payroll and a statement of compliance to the fiscal court. When payrolls were recalculated, immaterial discrepancies were found.

The fiscal court did not monitor the third party contractor as required to ensure that the federal requirement was met and did not ensure the contract contained the required Davis Bacon provision. When grantees do not follow federal requirements, they cannot ensure that charges to the federal grant are accurate and federal compliance requirements are adhered to.

Without good internal controls, the fiscal court cannot ensure that resources are protected from waste, loss, and misuse. These deficiencies could create errors in recording or allow for the possibility of misappropriation of assets. In addition, internal control weaknesses and noncompliance with grant agreements could affect the county's ability to receive federal funds.

Uniform Guidance 2 CFR §200.303 states “the non-Federal entity must: (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.”

It is the fiscal court's responsibility to monitor the third party contractor to ensure that the federal requirement was being met.

According to 29 CFR part 5 “non-federal entities shall include in their construction contracts subject to the Wage Rate Requirements a provision that the contractor or subcontractor comply with those requirements and the DOL regulations. This includes a requirement for the contractor or subcontractor to submit to the non-federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payroll).”

We recommend the fiscal court implement adequate internal controls over federal programs to ensure compliance with applicable federal, state, and local laws.

*Former County Judge/Executive's Response: A procedure will be developed a procedure to ensure the provisions of Davis Bacon are met. The procedure will be written and in place by March 31, 2022 and will also include the Suspension and Debarment requirement.*

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

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