



Auditor of Public Accounts
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FOR IMMEDIATE RELEASE

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Harmon Releases Audit of McCracken County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the McCracken County Fiscal Court for the fiscal year ended June 30, 2018. State law requires annual audits of county fiscal courts.

Auditing standards require the auditor’s letter to communicate whether the financial statement presents fairly the receipts, disbursements, and changes in fund balances of the McCracken 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 McCracken County Fiscal Court lacks internal controls over cash processes and financial reporting: This is a repeat finding and was included in the prior year audit report as Finding 2017-001. The McCracken County Fiscal Court’s Fourth Quarter Settlement did not agree to the county’s ledgers, and the budget listed on the fourth quarter did not agree to the original budget passed for Fiscal Year 2018. When bank reconciliations were completed, the incorrect numbers were used, which resulted in the road, jail, and sheriff funds having a negative fund balance at year end. The road fund, jail fund, and sheriff fund had negative balances of \$607, \$1,479, and \$4,269, respectively.

The McCracken County Fiscal Court uses a single bank account for its operating fund, and keeps its cash balance on the ledgers in the general fund. During the year, when disbursements were made from the road, jail, and sheriff funds, cash was transferred to those funds on the ledgers to cover the claims. Due to a lack of understanding in the software and a change in treasurers at year end, not enough cash was transferred to those funds.

The McCracken County Fiscal Court's lack of controls over cash transfers resulted in a deficit in three funds, and an overstatement of the general fund. The fiscal court is also not in compliance with KRS 68.210 and KRS 68.110.

Strong internal controls require oversight over the movement of funds in order to decrease risk. The fiscal court is responsible for providing oversight to the treasurer and making the county's financial decisions. KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The Department for Local Government's (DLG) *County Budget Preparation & State Local Finance Officer Policy Manual* requires the treasurer to countersign checks only if the following conditions exist: the claim is reviewed by fiscal court, sufficient fund balance and adequate cash in bank to cover the check, and adequate free balance in a properly budgeted appropriation account to cover the check. Also, KRS 68.110 states "[t]he fiscal court shall not in any year expend any money in excess of the amount annually levied and collected for that year or levied, collected or appropriated for any special purpose."

We recommend the fiscal court approve and document all cash transfers in the fiscal court minutes before the transfers take place, and ensure all financial statements are accurate and in agreement with other financial documentation. We further recommend the fiscal court consider separate checking accounts for each fund in order to ensure the cash balance in each fund is sufficient to pay claims.

Former County Judge/Executive's Response: A clerical error occurred at the end of FY18. A new accounts payable batch was created for July 2018 in order to pay certain items allowable by standing order. However, the checks were inadvertently dated 6/28/18, which made them appear in the wrong year. Accounts payable clerk has been instructed to watch dates carefully.

Material weaknesses exist over the reporting of liabilities and debt: This is a repeat finding and was included in the prior year audit report as Finding 2017-002. Material weaknesses existed over the reporting of liabilities and debt of McCracken County. Due to an oversight and a turnover in the treasurer position at the end of Fiscal Year 2018, no outstanding debt balances were reported on the Fourth Quarter Financial Report as of June 30, 2018.

Strong internal controls over outstanding debt and liabilities are necessary to ensure accurate financial reporting. By not including the outstanding debt balances, the McCracken County Fiscal Court's Fourth Quarter Financial Report was materially misstated.

We recommend the McCracken County Fiscal Court strengthen internal controls over the reporting of debt service payments and outstanding balances. Internal controls, such as comparisons of payment amounts and outstanding balances to amortization and payment schedules should be implemented. We further recommend the county consult with lenders to verify outstanding debt

balances are in agreement with the county's schedule of leases and liabilities. Such practices will strengthen internal controls over liabilities and debt service and ensure that the proper amounts are reported.

Former County Judge/Executive's Response: Current Treasurer will compare payment amounts and outstanding balances to amortization and payment schedules.

The McCracken County Jail lacks adequate internal controls over the inmate fund: This is a repeat finding and was included in the prior year audit report as Finding 2017-004. The McCracken County Jail contracts with a third party commissary company to oversee and maintain the inmate fund. The inmate fund is maintained solely by the commissary company. The commissary company receives cash, makes the deposits, posts transactions to the inmates' accounts, posts to the ledgers, prepares checks, and reconciles the account. Employees of the jail do not have access to any accounting records of the inmate fund, including resident transaction reports and bank statements.

Rather than implement internal controls over the inmate fund, the McCracken County Jail relies on the commissary company to oversee all accounting functions of the fund. A lack of adequate internal controls increases the risk of undetected fraud and errors.

Because the jailer is responsible for the inmates of the county, it is imperative for the jailer to provide sufficient oversight of all accounts associated with the inmates, including the inmate fund.

We recommend the McCracken County Jailer implement internal controls over the inmate fund. These controls should include the jailer or designee reviewing the inmates' accounts to ensure correct fees are being charged, deposits are being posted correctly, and inmate balances are being refunded properly upon release of the inmates.

Former Jailer's Response: Tonya Ray Former McCracken County Jailer has no say in continued use of commissary account.

The McCracken County Fiscal Court lacks adequate segregation of duties over the collection of receipts: The county treasurer prepares the deposit, posts the receipts to the ledger, and reconciles the bank statements monthly.

Due to the lack of internal controls in place, the duties associated with the custody, recordkeeping, reconciling, and authorization of receipts are not segregated. A lack of segregation of duties or strong oversight increases the risk of undetected errors and fraud. Segregation of duties or the implementation of compensating controls, when limited by the number of staff, is essential for providing protection against the misappropriation of assets and inaccurate financial reporting. Additionally, proper segregation of duties protects employees in the normal course of performing their daily responsibilities.

To adequately protect against the misappropriation of assets and financial reporting, we recommend that the judge segregate the duties noted above by having an individual independent of the cash receipts process review a daily checkout sheet documenting all receipts for the day and

comparing it to the daily deposit slip. We further recommend that an individual independent of the cash receipts process review postings to the ledgers and monthly bank reconciliations. Documentation, such as the reviewer's initials or signature, should be provided on those items that are reviewed.

Former County Judge/Executive's Response: A daily receipt log is now maintained by the judge's executive secretary. This log will be compared to deposits and receipts posting to the ledger.

Weak internal controls resulted in the misstatement of capital assets on the county's schedule of capital assets: This is a repeat finding and was included in the prior year audit report as Finding 2017-003. The fiscal court failed to periodically conduct physical inspections of all assets to make comparisons to the capital asset list. The fiscal court's schedule of capital assets for the period of audit was misstated by a total of \$107,939. The category of land improvements was misstated by \$52,849 because the fiscal court failed to include an addition, and vehicles and equipment were misstated by \$55,090 because the fiscal court failed to recognize asset retirements that occurred throughout the year. Also, asset additions totaling \$198,445 were not added to the county's insurance, and one asset disposal was not removed from the county's insurance.

Strong internal controls over capital assets are necessary to ensure accurate financial reporting and to protect assets from misappropriation and loss. These errors occurred because the fiscal court failed to emphasize strong internal controls over capital assets and instead relied on a single employee without sufficient supervision. Due to these weak internal controls, capital assets are left vulnerable to misappropriation or misstatement. In this case, assets were not properly insured and a misstatement was able to occur without detection.

In order to strengthen the fiscal court's internal controls over capital assets, we recommend the fiscal court establish a detailed inventory system. This system should include a detailed description of each fiscal court asset, an inventory control number or serial number, the date acquired, purchase price, location, date destroyed or sold as surplus, and a brief description of why the asset was discarded. The inventory of county assets, as well as the county's insurance policy, should be updated throughout the year as new assets are acquired or old assets are retired. This system should be applied consistently in accordance with the county's capitalization policy. Also, all asset additions and retirements should be properly authorized by the fiscal court and documented in the fiscal court minutes. We also recommend the county conduct a physical inspection of the county's assets at the end of each year to make comparisons to the county's inventoried assets.

Former County Judge/Executive's Response: Current Treasurer will update capital asset listing throughout the year. This is being done with a coordinating effort from department heads and elected officials. Annual physical inspections by all departments will be reported to the Finance Office in order to keep records current.

The McCracken County Fiscal Court did not have adequate internal controls over receipts: This is a repeat finding and was included in the prior year audit report as Finding 2017-006. In Fiscal Year 2018, the McCracken County Fiscal Court had internal control deficiencies and

noncompliances regarding the collection of receipts. The following issues were noted with McCracken County Fiscal Court's collection of receipts:

- Triplicate receipts were not issued for applicable receipt transactions, as required by KRS 64.840.
- Pre-numbered, triplicate receipts are not issued for funds collected at Carson Park.
- Receipts collected at Carson Park are not secured in a safe location.
- At Carson Park, collected receipts are not reviewed by someone independent of the collection function.

The findings listed above are due to the lack of effective internal controls, which left receipts vulnerable to misappropriation and loss.

Strong internal controls over the collection of receipts are vital in ensuring that receipts are accounted for properly. Strong internal controls are also important in safeguarding the county's assets and those given the responsibility of accounting for them, as well as helping make certain the county is in compliance with state statutes. 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, if the fine, forfeiture, tax, or fee is paid:

- (a) In cash;
- (b) By a party appearing in person to pay; or
- (c) By check, credit card, or debit card account received through the mail, if the party includes an addressed, postage-paid return envelope and a request for receipt.

(2) One (1) copy of the receipt shall be given to the person paying the fine, forfeiture, tax, or fee and one (1) copy shall be retained by the official for his own records. One (1) copy of the receipt shall be retained by the official to be placed with the daily bank deposit.

To address these issues, we recommend the following:

- Pre-numbered, triplicate receipts should be issued for applicable transactions according to KRS 64.840.
- Carson Park should obtain a bank bag to keep receipts in during the day. This bag should be locked and stored in a safe location during the day.
- An individual independent of receipts collection at Carson Park should create a ledger of all receipts received on each day. This ledger should match the monies received and receipts issued for the day.

Former County Judge/Executive's Response: Carson Park now has pre-numbered triplicate receipts. Carson Park now has a fire proof lock box to hold payments until they are delivered daily to finance. All receipts received daily by Judge/Executive Secretary are now being logged.

The McCracken County Fiscal Court lacks adequate controls over their bid process: The McCracken County Fiscal Court did not follow the bid process before entering into a monthly service agreement that over the course of the year was above the \$20,000 threshold set by KRS 424.260. Also, during Fiscal Year 2018, the county purchased a vehicle using a state pricing contract, but the incorrect price was used by the dealership.

Due to an oversight by the McCracken County Fiscal Court, the fiscal court failed to bid this monthly service contract, and did not notice that the incorrect price was being used for the vehicle purchased. Since bidding procedures were not followed, it is possible that the county did not get the best value for services provided. This also puts the county at higher risk for potential fraudulent purchases.

Strong internal controls require management to monitor disbursements and purchase orders to ensure compliance with bid laws, and to keep good records of all bid transactions. KRS 424.260 states, “[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 agreements 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 monitor all disbursements to ensure that bidding procedures are followed for all qualifying disbursements. We further recommend the fiscal court document these procedures in the fiscal court minutes.

Former County Judge/Executive’s Response: Current Treasurer is aware of procurement process outlined in the Administrative Code and is taking corrective action.

The McCracken County Fiscal Court has deficiencies with their purchase order system and reporting encumbrances: This is a repeat comment and was included in the prior year audit report as Finding 2017-007. The McCracken County Fiscal Court’s purchase order system does not work as designed. Throughout the fiscal year, purchase orders were created after invoices were received, as opposed to before the purchase was made. The county uses the purchase order system’s outstanding list as their list of encumbrances. According to the treasurer, that list is not accurate as there are often encumbrances listed that have already been paid.

Department heads are allowed to make orders and purchases without obtaining a purchase order from the finance office. Due to the system not working as designed, the risk of misappropriation is elevated, and control over expenditures is reduced. Encumbrances are also misstated on the McCracken County Fiscal Court’s Fourth Quarter Financial Statement, and are not tracked properly.

A purchase order system that is designed and works effectively creates strong internal controls over expenditures, and will aid in correctly reporting encumbrances.

We recommend the fiscal court strengthen internal controls over the purchase order system. Purchase orders should be acquired from the finance office before making any order or purchase. Invoices should then be matched to purchase orders and then claims can be made. Once fiscal court approves the claims, payment can be made.

Former County Judge/Executive's Response: Current Treasurer is working on enforcing a Purchase Order System county wide. Our goal is to have this accomplished by the end of FY 18/19.

The McCracken County Fiscal Court did not approve cash transfers prior to making them: This is a repeat finding and was included in prior year audit report as Finding 2017-008. Throughout Fiscal Year 2018, cash transfers were made prior to being approved by the fiscal court. Some were then later recognized by the fiscal court in future fiscal court meetings, while some were not recognized in the fiscal court meetings at all.

The former treasurer was responsible for all cash transfers and the fiscal court did not require prior approval for them to be made. Due to the lack of controls over cash transfers, the county's funds were at an increased risk of misappropriation.

Strong internal controls require oversight over the movement of funds in order to decrease risk. The fiscal court is responsible for providing oversight of the treasurer and making the county's financial decisions.

We recommend that all cash transfers be approved and documented in the fiscal court minutes before the transfers take place.

Former County Judge/Executive's Response: Current Treasurer is working on a process where cash transfers are approved by fiscal court prior to those cash transfers being made.

The McCracken County Fiscal Court lacks internal controls over a third party administrator: During Fiscal Year 2018, the McCracken County Fiscal Court approved health plans elected by employees, including plans that contained an employer funded Health Reimbursement Account (HRA). Each health insurance plan details the annual contribution to the HRA from the county. The McCracken County Fiscal Court has contracted with a third party administrator to administer the HRA accounts. During the year, the third party administrator was allowing the employees more than the annual contribution approved by fiscal court. Of the seven employees tested, three employees' total elections in their HRA account was more than the annual contribution from the county.

Due to the lack of internal controls and the fact reports are not provided by the third party administrator, the account balances for employees were not being reviewed nor reconciled to the county's records. Because of the lack of internal controls, this error went undetected. Furthermore, the county was overcharged, and employees received benefits not approved by the fiscal court.

Strong internal controls are vital in ensuring that employees' HRA amounts are calculated and accounted for properly. Strong internal controls are also important in safeguarding the county's

assets and those given the responsibility of accounting for them, as well as, helping make certain the county is in compliance with state statutes.

We recommend the McCracken County Fiscal Court implement internal controls over the third party administrator and HRA accounts. Reports from the third party administrator should be generated on a monthly basis, and the McCracken County Fiscal Court should review and reconcile the account balances to the county's records to ensure accuracy and that the county is paying for benefits approved by the fiscal court.

Former County Judge/Executive's Response: Monthly reports will be requested from the third party administrator to be reviewed and reconciled.

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

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