Auditor of Public Accounts
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Harmon Releases Audit of Former Green County Clerk's Fee Account

FRANKFORT, Ky. – State Auditor Mike Harmon today released the audit of the 2018 financial statement of former Green County Clerk Billy Joe Lowe. State law requires the auditor to conduct annual audits of county clerks and sheriffs.

Auditing standards require the auditor's letter to communicate whether the financial statement presents fairly the receipts, disbursements and excess fees of the former Green County Clerk in accordance with accounting principles generally accepted in the United States of America. The former clerk's financial statement did not follow this format. However, the former clerk'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 all 120 clerk 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 the internal control over financial operations and reporting.

The audit contains the following comments:

The former Green County Clerk's Office lacked adequate segregation of duties over receipts, disbursements, and reconciliations: This is a repeat finding and was included in the prior year audit report as Finding 2017-001. The former county clerk prepared the daily deposit, prepared and signed checks, and posted to the receipts and disbursements ledger. The former county clerk also prepared all weekly, monthly, and quarterly reports and bank reconciliations for the fee and payroll revolving accounts. The usage tax account was not reconciled.

According to the former county clerk, the condition was a result of a limited budget, which restricted the number of employees the former county clerk could hire or delegate duties to. A lack of segregation of duties increased the former county clerk's risk of misappropriation of assets, errors, and inaccurate financial reporting.

Segregation of duties over receipts, disbursements, and the reconciliation process or implementation of compensating controls, when needed because the number of staff is limited, 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. Monthly bank reconciliations are essential in detecting discrepancies whether caused by fraud or accounting errors on behalf of the entity or the bank.

We recommend the Green County Clerk's Office strengthen internal controls by segregating these duties. If this is not feasible due to a lack of staff, then strong oversight should be implemented. The employee providing this oversight should document his or her review by initialing all source documentation. We also recommend the county clerk's office prepare bank reconciliations on all bank accounts.

Former County Clerk's Response: No response.

The former Green County Clerk lacked adequate internal controls over payroll information processed by a service organization: This is a repeat finding and was included in the prior year audit report as Finding 2017-002. The former county clerk used a Certified Public Accountant (CPA) to process all payroll transactions. The CPA firm is considered to be a service organization. At the end of each payroll period, the CPA received from the former county clerk the necessary information to process payroll including the clerk's salary information, hours for each employee to be paid, hourly rates, and a listing of required and authorized withholdings. The CPA processed this information and generated a payroll report, which the former county clerk relied upon to pay himself and his employees. The CPA also prepared all monthly and quarterly withholding reports which the former county clerk relied upon to pay state, city, and federal withholding amounts due; maintained individual earning records; and prepared W-2 forms for the former county clerk and his employees. If an error occurred, the former county clerk relied on the CPA to determine what caused the error and tell him how to fix it.

The former county clerk relied on the CPA payroll service organization who prepared individual earnings records and sent the county clerk payroll reports for each pay period. The former county clerk did not review these reports and used them to prepare payroll checks for himself and his employees. As a result, there were numerous discrepancies between employee timesheets and the CPA prepared individual earnings records in relation to holidays and vacation/sick leave used as reported in Finding 2018-003.

Without adequate internal controls in place to ensure all information processed by the CPA payroll service organization was accurate, there is a risk that payroll disbursements could be misstated or fraud relating to payroll could occur.

The former county clerk should have implemented internal controls over all information processed by the CPA to ensure all payroll calculations are accurate. This could have been documented on payroll reports. The current county clerk does not use the service organization.

Former County Clerk's Response: No response.

The former Green County Clerk did not maintain proper internal controls over payroll: This is a repeat finding and was included in the prior year audit report as Finding 2017-003. The former county clerk did not maintain proper internal controls over timesheets and leave balances. The following deficiencies were noted:

- Sixteen instances where the payroll check was issued prior to the public officer or employee working all of the hours for which the individual was being paid.
- Ten instances where the hours per the timesheet did not agree to the regular hours per the Individual Earnings Record (IER).
- One timesheet did not reflect any hours worked or leave taken for one day.
- Two instances when holidays were not noted on the timesheet. Holidays were not noted on IERs at all.
- One timesheet was not signed by the county clerk to indicate his review and approval.
- Four timesheets were not signed by the employee.
- One instance where vacation hours per the timesheet did not agree to the vacation hours per the IER.

Each pay period the former county clerk provided a payroll summary to the service organization who prepared the IERs which tracked hours worked, holiday hours, overtime hours worked, vacation leave, and sick leave. The former county clerk relied on reports he received from his payroll service organization without reviewing the reports. As a result of inaccurate timesheets, employees could be paid for more or less hours than actually worked. In addition, without accurate tracking of vacation and sick leave balances, there is an increased risk that employees could be paid for leave not earned.

KRS 337.320(1) requires that "[e]very employer shall keep a record of: (a) The amount paid each pay period to each employee; (b) The hours worked each day and each week by each employee; and (c) Such other information as the commissioner requires." Additionally, KRS 45.340 and OAG 79-448 state that checks shall be tendered to an officer or employee only after he/she has completed the work for which he/she is being paid.

We recommend the county clerk's office strengthen internal controls over the payroll process to ensure timesheets are accurately prepared and signed by all employees for each pay period, and are reviewed, approved, and signed by the county clerk or his designee. We also recommend the county clerk review payroll reports and compare them to timesheets each pay period to ensure they are accurate. Finally, checks should not be dated before the end of the pay period to ensure employees are paid for the actual hours worked.

Former County Clerk's Response: No response.

The former Green County Clerk's fourth quarter financial report was materially inaccurate: The former Green County Clerk's fourth quarter financial report submitted to the Department for Local Government (DLG) was materially inaccurate. The book balance on Part One – Summary and Reconciliation of All Accounts on the fourth quarterly report shows $(54,433), which does not reconcile to the bank. In addition, total receipts were understated by $93,769 and disbursements were overstated by $16,200, which exceeds the threshold of materiality for receipts, causing the fourth quarterly report to be materially misstated.

Receipts and disbursements for the first quarter were erroneously posted to the previous fee account in the computer software. The former county clerk did not properly reconcile the fee account financial quarterly reports to the bank which would have revealed the error. When financial statements contain material errors, they do not provide accurate results of the operations, financial position, and cash flows of the entity needed to make future decisions regarding the amount and timing of future cash flows. Reconciling financial records to the bank is essential for identifying errors in financial reporting due to accounting errors or fraud. Any discrepancies should be investigated and corrected timely.

We recommend the county clerk's office implement controls to ensure accurate financial reporting and submit amended financial reports to DLG when necessary.

Former County Clerk's Response: No response.

The former Green County Clerk did not require third-party purchasers of delinquent tax bills to make deposits and payments in accordance with 103 KAR 5:180: The former Green County Clerk did not require third-party purchasers of delinquent tax bills to make deposits at the time of registration as required by 103 KAR 5:180 for priority tax bills and current tax bills. This is a repeat finding and was included in the prior year audit report as Finding 2017-004.

According the former Green County Clerk, this occurred because he did not agree with the requirements set forth in 103 KAR 5:180 and chose to not make the deposits prior to the tax sale date.

Failure to collect deposits could result in the county clerk not being able to cover any additional costs and expenses associated with any purchaser who fails to make full payment at the time of the tax sale. In addition, this resulted in non-compliance with 103 KAR 5:180.

103 KAR 5:180 Section 4 requires third party purchasers make a deposit with county clerk for tax bills they wish to purchase at the tax sale. Purchasers are required to provide a deposit of 100% of tax bills listed on the purchaser's priority tax bill list and a deposit 25% of the tax bills listed on the purchaser's current tax bill list. The deposits should be applied to the payment of the tax bills the purchaser purchases at the tax sale and any balances refunded to the third party purchasers.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. Pursuant to KRS 68.210, the state local finance officer has prescribed minimum accounting and reporting standards in the Department for Local Government's (DLG) *County Budget Preparation and State Local Finance Officer Policy Manual.* It requires daily deposits be made intact to a federally insured financial institution, so those deposits paid by the third party purchasers should be deposited to an official bank account when received.

We recommend the county clerk's office require third party purchasers make deposits for tax bills they wish to purchase as required by 103 KAR 5:180.

Former County Clerk's Response: Uncalled for.

The county clerk's responsibilities include collecting certain taxes, issuing licenses, maintaining county records and providing other services. The clerk's office is funded through statutory fees collected in conjunction with these duties.

The audit report can be found on the auditor's website.

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