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Harmon Releases Audit of Lawrence County Fiscal Court

FRANKFORT, Ky. – State Auditor Mike Harmon has released the audit of the financial statement of the Lawrence County Fiscal Court for the fiscal year ended June 30, 2022. 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 Lawrence 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 116 of 120 fiscal court audits in Kentucky.

Findings 2 and 5 of the audit report will be referred to the Lawrence County Ethics Commission for further review.

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 findings:

The Lawrence County Fiscal Court did not accurately report debt on the quarterly financial statement: The debt schedule presented with the fourth quarter report (which serves as the year-end financial statement) inaccurately reported debt obligations. The report did not account for the balance of the Kentucky Association of Counties Leasing Trust (KACoLT) – FEMA lease in the amount of \$250,000 or the Justice Center Corporation Refinance, Series 2021, bond issues in the amount of \$9,272,300. In addition to this issue, the fiscal court did not reflect \$64,104 on their financial statement for their short-term debt.

The fiscal court does not have controls in place to ensure that debt obligations are properly reported on the fourth quarter report. By not accurately reporting debt, the county is not in compliance with KRS 68.210. In addition, the fiscal court does not have accurate information on which to base financial decisions.

KRS 68.210 gives the state local finance officer the authority to prescribe a uniform system of accounts. The uniform system of accounts is set forth in the *County Budget Preparation and State Local Finance Officer Policy Manual*, which requires all county debt be reflected properly on the quarterly financial statement.

We recommend the county ensure that the correct amounts are shown on all financial statements presented to the public and the Department for Local Government (DLG). We further recommend the county review all aspects of the quarterly reports before signing and submitting.

County Judge/Executive's Response: This debt was paid off and loan was re-issued during new budget preparation. This was an oversight and has been corrected. We have hired additional help to keep up with the workload. The Assistant Judge or Administrative Assistant will review the reports before signing and submitting.

The Lawrence County Fiscal Court violated the county ethics code: The Lawrence County Fiscal Court violated the county ethics code by engaging in multiple transactions with parties who are related to the county judge/executive, which is a violation of the county's adopted ethics code. A lack of internal controls allowed for the approval and employment of the county judge/executive's brother as the county road foreman, the utilization of a vendor for various projects where the county judge executive's son-in-law is an officer of the entity, and the sale of a personal item by the county judge to the fiscal court. The county judge/executive failed to recuse himself from voting on transactions that involved related party issues in all fiscal court meetings for Fiscal Year 2022. Neither the hiring of the brother nor the payments to a vendor for whom the son-in-law is an officer were submitted to the county's ethics commission as required by the county code of ethics. The total paid per each instance of related party transactions in Fiscal Year 2022 are as follows:

- Road Foreman - \$ 62,108
- Related Party Vendor - \$156,987
- County Judge/Executive - \$1,500

The fiscal court was unaware of the requirements outlined within the county ethics code. Furthermore, the county judge/executive was unaware of the requirement to abstain from voting on all transactions involving related parties. The county is currently in violation of the standards of conduct nepotism clause specified in the county ethics code. This raises concerns that the fiscal court might be showing favoritism towards related parties without implementing appropriate procedures and safeguards. These transactions also violate federal grant requirements. See finding 2022-005.

Implementing internal controls ensures the prevention of conflicts of interest and violations of the county ethics code.

The Lawrence County Ethics Code defines “Member of Immediate family” as a “County Government Official’s spouse, father, mother, grandfather, grandmother, children and spouses, brothers and sisters and spouses, aunts, uncles, bothers-in-law and sisters-in-law, nieces and nephews, or any other person claimed by the individual or individual’s spouse as a dependent for Kentucky income tax purposes.”

Further, the County Ethics Code, Section II Standards of Conduct provides in pertinent part:

- A. No county government officer or employees of member of his immediate family shall have an interest in a business organization or engage in any business, transaction, or professional activity, which is in substantial conflict with the proper discharge of his duties in the public interest.
- B. No county government officer or employee shall use or attempt to use his official position to secure unwarranted privileges or advantages for himself or others.
- C. No county government officer or employee shall act his official capacity in any manner where he, a member of his immediate family, or a business organization in which he has an interest, has a direct or indirect financial or personal involvement that might reasonably be expected to impair his objectivity or independence of judgment.

Additionally, Section IV of the County Ethics code states, “[a]fter the effective date of this ordinance, no immediate family member of a County Government Official, as defined in Section 1, paragraph F hereof, shall be employed within Lawrence County by county government or county agencies, except under the following conditions:

1. An Immediate family member of a County Government Official shall not be initially employed or appointed to a position in county government or in a county governmental agency within the same county in which the officer serves unless the spouse or family member is the best qualified, by education and/or experience, to fill such position.
2. In any situation in which a County Government Official desires to employ or appoint an immediate family member (or an immediate family member of another County Government Official) to a position in county government or in a county governmental agency, the Ethics Commission shall make the determination as to whether such family member is best qualified for filling such position, by reviewing the employment applications of all applicants and conducting interviews, if the Commission so desires. Thereafter, the Ethics Commission shall select the most qualified person for the position.”

We recommend the fiscal court adhere to the requirements outlined in the county ethics code by refraining from hiring or engaging vendors who are related parties. If the fiscal court does choose to involve related parties, then the ethics commissions should thoroughly review and assess these

transactions to ensure transparency and ethical compliance. This finding will be referred to the Lawrence County Ethics Commission.

County Judge/Executive's Response: The Fiscal Court hired the County Judge's brother as road foreman because he was the only person who met the requirements for the position and would accept the job, other people were offered the job before the brother, in addition the brother also served in the same position under a previous administration and left on good terms. At the time of the Fiscal Court acceptance of bids from the vendor, the son-in-law of the Judge Executive was not listed as an officer of the entity. The County Judge does not vote on fiscal court matter other than as a tie breaker. All votes cast by the Judge executive are either for tie breaking purposes or purely symbolic to show unity on the Court. All future hiring's and/or vendor purchases that require Ethics Commission approval will be submitted to the Ethics Committee in advance and will be in compliance with all state and federal statutes and guidelines.

The Lawrence County Fiscal Court did not establish and maintain effective internal controls over compliance with coronavirus state and local fiscal recovery fund (SLFRF) requirements:

Federal Program: Assistance Listing #: 21.027 COVID-19 - Coronavirus State and Local Fiscal Recovery Funds

Award Number and Year: 2022

Name of Federal Agency: U.S. Department of the Treasury

Compliance Requirements: Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Reporting

Type of Finding: Significant Deficiency

Amount of Questioned Costs: \$0

COVID Related: Yes

The Lawrence County Fiscal Court transferred federal funds from the American Rescue Plan Act (ARPA) fund to the general, jail, road, Local Government Economic Assistance (LGEA), and E-911 funds without first ensuring sufficient supporting documentation of allowable expenditures during the same period as the funds were reported as expended on the Schedule of Expenditures of Federal Awards (SEFA).

The county was awarded \$2,975,148 in ARPA funds, receiving the first payment of \$1,487,618 into the ARPA fund in May 2021, and their second payment of \$1,487,530 in June 2022. The fiscal court's transfers in total from the ARPA fund to each fund are provided below:

- General - \$714,640
- Road - \$250,000
- Jail - \$40,000
- LGEA - \$25,000
- E-911 - \$10,000
- Payroll - \$217,739

These transfers from the ARPA fund were considered “lost revenue” according to their fiscal court meeting minutes. At the time of these transfers, and until auditors inquired about the supporting documentation, the county did not maintain a list of expenditures that reconciled to the transfer total. After this inquiry, the county gathered documentation and provided auditors a reconciliation of expenditures of eligible costs that supported the amount transferred into the general fund.

An effective internal control system was not in place in Lawrence County to ensure compliance with requirements related to the administration of ARPA funds and the Allowable Costs/Cost Principles compliance requirements. The lack of internal controls was a systemic issue throughout the period.

Failure to establish and maintain effective internal controls over compliance with federal program requirements could subject the county to the risk of reporting ineligible expenditures on the SEFA and using grant funds for unallowable purposes.

2 CFR 200.303 states in part, “[t]he 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.”

2 CFR §200.302(b) states, “[t]he financial management system of each non-Federal entity must provide for the following ...:(2) [a]ccurate, current and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements set for in §200.328 and 200.329.”

In addition, 2 CFR §200.502(a) states, “[t]he determination of when a Federal award is expended must be based on when the activity related to the Federal award occurs.” Therefore, the county should only include expenditures on the Schedule of Expenditures of Federal Awards (SEFA) for which there is sufficient supporting documentation.

We recommend the county establish and maintain internal controls over compliance for all federal program expenditures to ensure accurate use and reporting of federal awards, including maintaining sufficient supporting documentation of expenditures that reconciles to any transfer from a federal program fund into other county funds.

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County Judge/Executive’s Response: The fiscal court would like to point out that ARPA funds were properly distributed. During this time there was little guidance on how to manage the reporting. All reporting has been corrected.

The Lawrence County Fiscal Court failed to implement effective internal controls over federally reimbursed expenditures and circumvented internal controls by performing a split purchase:

Federal Program: Assistance Listing #: 21.027 COVID-19 - Coronavirus State and Local Fiscal Recovery Funds

Award Number and Year - 2022

Name of Federal Agency: U.S. Department of the Treasury

Compliance Requirements; Procurement, Suspension, and Debarment

Type of Finding: Material Weakness and Noncompliance

Amount of Questioned Costs: \$64,999

Opinion Modification: Yes, Qualified

COVID Related: Yes

The Lawrence County Fiscal Court paid \$29,999 to a vendor for inflatables and associated items for the Lawrence County Cove project. This vendor was paid an additional \$5,000 on the same day for other items applicable to the cove project for a total of \$34,999. In addition, the fiscal court also made a payment of \$30,000 to another vendor for the renting of equipment which is also a violation of the ethics code as discussed in Findings 2022-002 and 2022-005. There was a total of \$64,999 in purchases with federal funds that were not advertised or opened for bid in accordance with KRS 424.260. Additionally, vendors were not checked to see if they were debarred or suspended.

The fiscal court circumvented internal controls by making split payments to the vendor for less than \$30,000. The county issued separate payments to the vendor so that bidding would not be required. The county also failed to advertise or open a bid for the inflatables cove project and the rental of the dozer. The county failed to follow proper procurement procedures which results in a noncompliance with state laws and federal regulations and is at risk for extensive federal oversight and repayment of questioned costs.

The version of KRS 424.260(1) in effect at the time of the subject expenditures stated, “[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 agreement for: (a) Materials; (b) Supplies, except perishable foods such as meat, poultry, fish, egg products, fresh vegetables, and fresh fruits; (c) Equipment; or (d) Contractual services other than professional; involving an expenditure of more than thirty thousand dollars (\$30,000) without first making newspaper advertisement for bids.”

2 CFR §200.318(a) requires, “[t]he non-Federal entity must have and use documented procurement procedures, consistent with State, local, and tribal laws and regulations and the standards of this section, for the acquisition of property or services required under a Federal award or subaward. The non-Federal entity's documented procurement procedures must conform to the procurement standards identified in § 200.317 through 200.327.”

We recommend all expenditures of \$30,000 or more be bid in accordance with KRS 424.260(1). Purchases should not be split in order to avoid bid requirements. The fiscal court and management should also abide by the requirements of 2 CFR §200.318(a) by adhering to their own policies and procedures for procurement of projects.

County Judge/Executive's Response: The two purchases made by the county were made at different times for different items. Although both purchases were paid for at the same time, due to the fiscal court approval needed to pay the bills, neither of them separately required a bid process.

The County does acknowledge the \$29,999.00 price tag being close to the allowable amount to spend without bidding, however, the county would state that the purchase price was agreed upon out of good faith and with no attempt to circumvent the bidding requirements. The final \$30,000.00 accounted for in this section was for the rental of a dozer. The anticipated rental time and need far exceeded initial estimates. During the initial rental period, the dozer was rented to level the new soccer field, during the work on the soccer field the adjacent land was given to the county and the work on that field exceeded the initial estimates, leading to the overage. Upon realizing the amount was getting close to the \$30,000.00 bid requirement the county contacted the owner of the dozer and explained the situation. At that point the owner of the dozer made an offer to sell the dozer to the county at a discounted price which would include a portion of the balance the county already owed. The county bid the purchase of a new dozer. The only bid received by the county for a dozer was from the rented dozer's owner. The county has put into place controls that will require opening of bids no matter the anticipated and/or expected outcomes in adherence to all statutory authority.

The Lawrence County Fiscal Court did not abide by 2 CFR 200.318(c)(1):

Federal Program: Assistance Listing #: 21.027 COVID-19- Coronavirus State and Local Fiscal Recovery Funds and 97.036 Disaster Grants Public Assistance

Award Number and Year: 2022

Name of Federal Agency and Pass-Through Agency (if applicable): U.S. Department of the Treasury and U.S Department of Disaster Emergency Management passed through Kentucky Department of Military Affairs

Compliance Requirements: Activities Allowed/Allowable Costs

Type of Finding: Material Weakness and Noncompliance

Amount of Questioned Costs: ALN 21.027 \$4,160 (excludes \$30,000 included in Finding 2022-004) and ALN 97.036 \$92,984

Opinion Modification: Yes, Qualified

COVID Related: Yes- ALN 21.027

During testing of Assistance Listing Number (ALN) 97.036 and ALN 21.027, it was discovered that the Lawrence County Fiscal Court did not have internal controls over disbursements of federal funds. Federal funds were disbursed to a vendor of which the Judge/Executive's son-in-law is a member and the judge's brother who is the road foreman for premium pay and as a FEMA applicant agent. Provided below are the totals spent for each ALN:

- ALN 97.036 Vendor Total - \$78,961
- ALN 97.036 Road Foreman Total - \$14,023
- ALN 21.027 Vendor Total - \$30,000 (See finding 2022-004)
- ALN 21.027 Road Foreman Total - \$4,160

The fiscal court disbursed federal funds to parties with a known relation to the Lawrence County Judge/Executive. The fiscal court is noncompliant with the 2 CFR 200.318(c)(1) and the Lawrence County Ethics Code and is at risk for extensive federal oversight and repayment of questioned costs.

2 CFR 200.318(c)(1) states, “[t]he Non-Federal entity must maintain written standards of conduct covering conflicts of interest and governing the actions of its employees engaged in the selection, award and administration of contracts. No employee, officer, or agent may participate in the selection, award, or administration of a contract supported by a Federal award if he or she has a real or apparent conflict of interest. Such a conflict of interest would arise when the employee, officer, or agent, any member of his or her immediate family, his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in or a tangible personal benefit from a firm considered for a contract. The officers, employees, and agents of the non-Federal entity may neither solicit nor accept gratuities, favors, or anything of monetary value from contractors or parties to subcontracts. However, non-Federal entities may set standards for situations in which the financial interest is not substantial, or the gift is an unsolicited item of nominal value. The standards of conduct must provide for disciplinary actions to be applied for violations of such standards by officers, employees, or agents of the non-Federal entity.”

County Ethics Code - Section III Standards of Conduct states, “C. No county government officer or employee shall act his official capacity in any manner where he a member of his immediate family. or a business organization in which he has an Interest. has a direct or indirect financial or personal Involvement that might reasonably be expected to Impair his objectivity or independence of Judgment.”

We recommend the fiscal court adhere to the requirements set by federal standards. The fiscal court should refrain from using vendors and employees that could potentially create conflicts of interest when using federal funds. If the fiscal court does choose to involve related parties, it is imperative that the ethics commissions thoroughly review and assess these transactions to ensure transparency and ethical compliance. This finding will be referred to the Lawrence County Ethics Commission.

County Judge/Executive’s Response: See answer to 2022-002.

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

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