



Auditor of Public Accounts
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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, 2017. 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 fiscal court has \$254,994 in liabilities as of June 30, 2017 for disbursements relating to the government building: The fiscal court received \$8,143,894 in bond proceeds, \$1,998,965 in state grant funds, and \$560,000 from the Economic Development Authority totaling \$10,702,859 of funds that were received for the government building. The fiscal court spent \$10,756,315 as of June 30, 2017, which resulted in an overrun of \$53,456. This does not include the liabilities of \$254,994 that are still owed contractors as of June 30, 2017, leaving this project \$308,450 over budget.

The fiscal court failed to implement proper internal control procedures to prevent the overspending of this project. As of January 2017, the fiscal court owed contractors \$772,066. The fiscal court

enter into settlement agreement with the contractors to pay the remaining funds. The first payment was due on February 15, 2017, and the remaining balance is to be paid in two semiannual payments over the next 48 months. The Economic Development Authority gave the fiscal court \$560,000 of recaptured coal severance funds. These funds were used to pay the first initial payment to the contractors and the first semiannual payment. Without the Economic Development Authority giving the fiscal court these funds, the fiscal court did not have the cash flow to pay these bills.

KRS 65.140 requires “all bills for goods or services shall be paid within thirty (30) working days of receipt of a vendor's invoice except when payment is delayed because the purchaser has made a written disapproval of improper performances or improper invoicing by the vendor or by the vendor's subcontractor.”

We recommend the fiscal court implement procedures to comply with KRS 65.140 and pay bills within 30 working days. In addition, we recommend the fiscal court implement procedures to ensure that projects are overseen and stay within budget.

County Judge/Executive's Response: This occurred under the previous administration. We have properly budgeted and tracked this liability and are making payments accordingly.

The fiscal court had \$596,562 of prior year disbursements paid in the current fiscal year: Auditors found that \$596,562 of disbursements tested were from prior fiscal years. Disbursements in the amount of \$10,000 should have been paid in Fiscal Year 2014, and \$586,562 should have been paid in Fiscal Year 2015. These invoices were not listed on the prior year encumbrance list, therefore leaving the fiscal court with no knowledge these invoices were outstanding. In addition, these invoices were not taken into account toward their ending cash balance. The prior year ending cash balance in the road fund was \$56,320, two invoices totaling \$577,372 should have been paid in the prior year. However, the fiscal court did not have the funds to pay these two invoices, which would have left the road fund in a deficit of \$521,052.

The fiscal court failed to implement proper internal control procedures to detect that these prior year disbursements were outstanding. These purchases should have been listed on the encumbrance list as an outstanding purchase order at the end of each year, therefore alerting the fiscal court that these expenditures were outstanding.

Without implementing proper internal control procedures, the fiscal court is making decisions without a true financial picture of the county's finances. If these expenditures would have been listed on the encumbrance list, the fiscal court would have been aware that there were a cash flow problems.

KRS 65.140 requires “all bills for goods or services shall be paid within thirty (30) working days of receipt of a vendor's invoice except when payment is delayed because the purchaser has made a written disapproval of improper performances or improper invoicing by the vendor or by the vendor's subcontractor.”

We recommend the fiscal court implement procedures to comply with KRS 65.140 and pay bills with 30 working days. In addition, we recommend the fiscal court implement procedures to ensure that all expenditures are accounted.

County Judge/Executive's Response: This occurred under the previous administration. The current administration inputs invoices as received and has properly budgeted for prior year claims.

The fiscal court has not implemented internal controls over disbursements: Internal controls associated 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 a 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:

- The fiscal court is paying vendors in advance.
- Thirty-one disbursements totaling \$1,429,354 were not paid within 30 days.
- Eleven instances was noted where sufficient supporting documentation was not maintained to determine what was purchased.
- Four transactions were prior year expenditures that were paid in Fiscal Year 2018 totaling \$596,562.

Proper internal controls over expenditures 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 *County Budget Preparation and State Local Finance Officer Policy Manual*, issued by the Department for Local Government (DLG), “purchases shall not be made prior to approval by the county judge/executive (or designee) or department head.” 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 expenditures and ensure they are operating effectively.

County Judge/Executive's Response: This occurred under the previous administration. The current administration follows the KRS.

The fiscal court did not follow proper bid laws and regulations: The fiscal court did not maintain bid documentation for any of the vendors tested during expenditures over the bid threshold. The fiscal court lacks sufficient internal controls over the bidding process to ensure items were not purchased from vendors without first advertising or receiving bids when necessary on all purchases requiring bids.

As a result, eight disbursements totaling \$1,139,944 were not bid in Fiscal Year 2017. By limiting competition or not receiving bids at all, the fiscal court may not get the benefits of the best price available. Competitive bidding ensures the fiscal court procures equipment and services at the best

price available. Maintaining proper bid documentation also ensures all bids are considered on an equal basis and ensures all bids meet the minimum specifications of the fiscal court.

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."

We recommend the fiscal court follow the requirements of the administrative code and properly advertise and award bids for all purchases over \$10,000. We further recommend the fiscal court implement internal controls over the bidding process to ensure all required bid documentation are maintained and approved by the fiscal court.

County Judge/Executive's Response: This occurred under the previous administration. The current administration passed an ordinance to update the bid amount to match the state's requirement which will keep us in compliance. Bid documentation is maintained by the court recorder.

The fiscal court did not properly report encumbrances: The encumbrance list was not inclusive. Auditors found that the fiscal court entered into settlement agreements for the government building due to the overspending of funds acquired. These settlement agreements totaled \$772,066. After the first initial payments were made in February, the remaining balance of these agreements totaled \$254,994. This remaining balance of these agreements were not listed on the encumbrance list. Based upon these expenditures not being listed on the encumbrance list auditors could not determine if the fiscal court had more encumbrances not listed.

The fiscal court failed to implement proper internal control procedures to detect that these prior year expenditures were outstanding. These purchases should have been listed on the encumbrance list as an outstanding purchase order at the end of each year, therefore alerting the fiscal court that these expenditures were outstanding. Without implementing proper internal control procedures, the fiscal court is making decisions without a true financial picture of the county's finances. If these expenditures would have been listed on the encumbrance list, the fiscal court would have been aware that there were cash flow problems.

KRS 68.210 requires the state local finance officer create system of uniform accounts for all accounts for all counties and county officials. The *County Budget Preparation and State Local Finance Officer Policy Manual* requires the county to disclose encumbrances of the face of the fourth quarter financial report. Inaccurate reporting of encumbrances does not show the accurate cash balances, and cannot inform management of cash flow problems. We recommend the fiscal court maintain an accurate listing of outstanding purchase orders and include all outstanding purchase orders on the fourth quarter financial statement.

County Judge/Executive's Response: This occurred under the previous administration. The current administration is tracking the encumbrances properly.

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

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