

CITY OF COVINGTON
Covington, Kentucky



SINGLE AUDIT REPORTS
June 30, 2017

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CITY OF COVINGTON, KENTUCKY
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2017

Federal Grantor/ Pass-Through Grantor/ Program Title	Federal CFDA Number	Grantor's Number	Revenues	Expenditures
<u>U.S Department of Housing and Urban Development</u>				
Section 8 Housing Choice Voucher	14.871	KY-133-VO-0054-0F04	\$ 5,884,891	\$ 5,999,987
Community Development Block Grants/ Entitlement Grants	14.218	B-16-MC-21-0001	1,400,561	1,403,835
HOME Investment Partnership Programs	14.239	M-15-DC-21-0200 Loans outstanding	738,038 -	728,809 128,717
			<u>738,038</u>	<u>857,526</u>
Total U.S. Department of Housing and Urban Development			<u>8,023,490</u>	<u>8,261,348</u>
<u>DEPARTMENT OF JUSTICE</u>				
Bulletproof Vest Partnership Program	16.607	N/A	9,695	9,695
Equitable sharing program	16.922	N/A	146,649	170,398
Pass through from Kenton County				
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2013-DJ-BX-0159	46,311	46,311
Total Department of Justice			<u>202,655</u>	<u>226,404</u>
<u>Department of Transportation</u>				
Pass through from Kentucky Transportation Cabinet				
Highway Planning and Construction - Streetscape Phase III	20.205	PO2 1200005121	61,738	61,738
Highway Planning and Construction - 3rd and Johnson	20.205	PO2 6251500001640	3,542	3,542
Highway Planning and Construction - River Center Boulevard	20.205	PO2 6251500001640	44,201	44,201
Highway Planning and Construction - Latonia Avenue Project	20.205	PO2 6251500001640	20,580	20,580
Highway Planning and Construction - River Front Commons	20.205	059 0008 004-008	268,575	252,990
Highway Planning and Construction - Covington 6th Street Restoration	20.205	PO2 6251400003076	856	856
Highway Planning and Construction - Electric Alley	20.205	PO2 6251400003076	37,340	37,340
State and Community Highway Safety	20.600	1600002702	28,908	28,908
Total Department of Transportation			<u>465,740</u>	<u>450,155</u>
<u>Department of the Interior</u>				
Pass through from Kentucky Heritage Council				
Historic Preservation Fund Grants-In-Aid	15.904	N/A	9,038	9,038
Total Department of the Interior			<u>9,038</u>	<u>9,038</u>
<u>Department of Homeland Security</u>				
Staffing for Adequate Fire and Emergency Response	97.083	N/A	169,071	169,071
Total Department of Homeland Security			<u>169,071</u>	<u>169,071</u>
Total Federal Financial Assistance			<u>\$ 8,869,994</u>	<u>\$ 9,116,016</u>

The City did not pass through any funds to subrecipients.

CITY OF COVINGTON, KENTUCKY
SCHEDULE OF EXPENDITURE OF FEDERAL AWARDS - NOTES
for the year ended June 30, 2017

Note 1 - Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the City of Covington, Kentucky and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Therefore, some amounts presented in, or used in the preparation of, the basic financial statements may differ from those numbers.

Note 2 - Indirect Cost Rates

The City did not elect to use the 10 percent de minimis cost rate as allowed under the Uniform Guidance.

Note 3 - Passthrough entity numbers were presented when available.



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH
MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE**

To the Mayor and City Commissioners
City of Covington, Kentucky

Report on Compliance for Each Major Federal Program

We have audited the City of Covington, Kentucky's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the City of Covington, Kentucky's major federal programs for the year ended June 30, 2017. The City of Covington, Kentucky's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the City of Covington, Kentucky's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Covington, Kentucky's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the City of Covington, Kentucky's compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Covington, Kentucky, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2017.

Report on Internal Control over Compliance

Management of the City of Covington, Kentucky, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City of Covington, Kentucky's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Covington, Kentucky's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Covington, Kentucky as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the City's basic financial statements. We have issued our report thereon dated January 25, 2018, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Covington, Kentucky's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

RHF

RHF, PLLC
Lexington, Kentucky
January 25, 2018



**INDEPENDENT AUDITORS' REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON
AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

To the Mayor and City Commissioners
City of Covington, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Covington, Kentucky, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the City of Covington, Kentucky's basic financial statements and have issued our report thereon dated January 25, 2018, wherein we noted that the financial statements of Devou Properties, Inc. were audited by other auditors.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Covington, Kentucky's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Covington, Kentucky's internal control. Accordingly, we do not express an opinion on the effectiveness of the City of Covington, Kentucky's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider findings 2017-001, 2017-002 and 2017-003 described in the accompanying schedule of findings and questioned costs to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider findings 2017-004 and 2017-005 as described in the accompany schedule of findings and questioned costs to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Covington, Kentucky's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* (2017-005).

City of Covington, Kentucky's Response to Findings

City of Covington, Kentucky's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The City of Covington, Kentucky's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

RFH

RFH, PLLC
Lexington, Kentucky
January 25, 2018

CITY OF COVINGTON, KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
for the year ended June 30, 2017

I. SUMMARY OF AUDITORS' RESULTS

Financial Statements:

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

Material weaknesses identified X Yes No
 Significant deficiencies identified that are not
 considered to be material weaknesses X Yes None reported

Non-compliance material to financial statements noted X Yes No

Federal Awards:

Internal control over major programs:

Material weaknesses identified Yes X No
 Significant deficiencies identified that are not
 considered to be material weaknesses Yes X None reported

Type of auditors' report issued on compliance for major programs:

Unmodified for all major programs.

Any audit findings disclosed that are required to be
 reported in accordance with 2 CFR 200.516(a)? Yes X No

Major Program:

CFDA Numbers	Name of Federal Program or Cluster
20.205	Highway Planning and Construction
14.871	Section 8 Housing Choice Vouchers

Dollar threshold used to distinguish between type A
 and type B programs: \$ 750,000

Auditee qualified as a low-risk auditee? Yes X No

II. FINDINGS RELATED TO FINANCIAL STATEMENTS

Finding 2017-001 – Material Weakness – Audit Adjustments (Recurring)

Condition: During the course of our audit, we identified material misstatements that were not identified by the City's internal controls over financial reporting. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A deficiency in operation exists when a properly designed control does not operate as designed. In this case, the internal controls over the preparation and review of the City's financial statements did not operate as designed and we consider this a material weakness.

Effect: Audit adjustments were necessary to properly record receivables, payables, accrued liabilities, debt transactions and interfund activity.

Recommendation: We recommend the City enhance its internal controls over financial reporting with steps such as management review of account reconciliations and listings, analysis of the financials compared to prior years and improved internal communication to ensure the preparation of reliable financial statements in conformity with generally accepted accounting principles.

CITY OF COVINGTON, KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS, Continued
for the year ended June 30, 2017

Management's Response: *We agree with the auditors' comments, and the following actions have been taken or will be taken to improve the situation. We have deemed it necessary to review the suite of internal controls, and will make necessary adjustments to enhance the effectiveness of the control environment. We will initiate more thorough management review of account reconciliations and listings, which will be part of a larger effort to increase the magnitude and effectiveness of internal communication. We plan on performing analyses of the year-over-year financial data. We plan to have remediated this issue prior to Q4 FY18.*

Finding 2017-002 – Material Weakness – Fixed Asset Recording (Recurring)

Condition: Numerous issues were noted with fixed asset tracking and recording. It was determined that multiple fixed assets purchased during the current fiscal year were not added to the depreciation schedule prepared by the client. In addition, multiple fixed assets that were sold during the current fiscal year had not been removed from the depreciation schedule. Finally, a physical inventory of fixed assets owned by the City was not completed during the current year.

Effect: Audit adjustments were necessary to capitalize current year capital additions and record current year disposals.

Recommendation: We recommend the City utilize their third party software to properly track and record capital assets. In addition, we recommend that management improve the closing process to properly account for capital assets and minimize audit adjustments. The City should also reconcile the capital asset listing to a physical inventory of the City's assets on at least an annual basis.

Management's Response: *We agree with the auditors' comments, and the following actions have been taken or will be taken to improve the situation. A more thorough review of fixed asset accounting will be incorporated into normal accounting procedures, especially during the closing process. With FY 2017 being the first full year that our new Fixed Asset software tool is available and in use, we will be using our third party software more extensively to better track and maintain fixed asset accounting. A review of the capitalization policy will be performed, with modifications made after consideration of current practices, to better ensure that our policy is realistic and attainable allowing for compliance with all relevant accounting principle. This will be followed by a wide distribution of the policy to those involved in accounting for fixed assets. In addition, additional temporary staff has been hired and are currently updating our Fixed Asset software to make this tool more functional in the future.*

Finding 2017-003 – Material Weakness – Lack of Adequate Segregation of Duties

Condition: During our audit, we noted that the City lacks adequate segregation of duties within the finance department, primarily due to turnover and staff departures that occurred during the current fiscal year.

Criteria: The basic premise of segregation of duties is that no one employee should have access to both physical assets and the related accounting records or to all phases of a transaction. In addition, proper segregation of duties should include oversight of finance department activity by individuals with knowledge of internal controls and accounting regulations, who were not involved in the original transaction.

Effect: The City's finance department was not staffed at the level that is necessary to ensure proper segregation of duties. As a result, internal control and oversight responsibilities that would normally be segregated among multiple staff members were the responsibility of single individuals.

Recommendation: We recommend that the City review and modify finance department activity and staffing levels to ensure that adequate segregation of duties can be achieved.

Management's Response: *We agree with the auditors' comments, and the following actions have been taken or will be taken to improve the situation. Current City Policy ensures proper segregation of*

CITY OF COVINGTON, KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS, Continued
for the year ended June 30, 2017

duties within the Finance Department. Finance staff continues to implement dual authorization for all finance department functions. When staffing levels in the Finance Department return to budgeted levels, there will be adequate staff to ensure segregation of duties for all finance functions and to meet current city policy.

Finding 2017-004 – Significant Deficiency – Accounting Procedures (Recurring)

Condition: During our audit, we noted that the City does not have a current comprehensive accounting procedures manual.

Effect: An effectively designed comprehensive accounting procedures manual can reduce errors, inefficiencies, miscommunications, omitted procedures and wasted efforts that can result in inaccurate or untimely accounting records. An effective accounting manual can also help define responsibilities, improve consistency, allow for easier review of accounting principles, train new employees and ensure that records are produced in the form designed by management.

Recommendation: We recommend that the City develop and implement a comprehensive accounting procedures manual.

Management's Response: We agree with the auditors' comments, however, the City has continued to document procedures via memos from the Finance Director. In June of 2015, the City implemented Phase I of its new financial systems software to include the following modules: A/R, A/P, G/L, Purchasing, Bank Reconciliation, and Cash Receipts. In October of 2015, the City implemented a Fixed Assets software module. In March of 2016, the City implemented a Business Tax software module. The City anticipates completing the remaining portions of its systems upgrades by the end of FY17. Once staffing levels in Finance return to budgeted levels the City will formalize its accounting procedures into a new desk manual. The City's desk manual will be subject to an annual management review and all department personnel will be required to acknowledge their review of managerial updates to the policy manual.

Finding 2017-005 – Significant Deficiency – Budgetary Noncompliance (Recurring)

Condition: As of June 30, 2017, we noted that multiple funds have expenditures in excess of their budget ordinance appropriations. In addition, the City's original budget ordinance was passed on a detailed line item basis; however, amendments to the budget were made on a summarized basis without reference to the line items of the original budget ordinance.

Criteria: Kentucky Revised Statute (KRS) 91A.030 prohibits the expenditure of moneys except in accordance with a budget ordinance.

Effect: The City was not in compliance with Kentucky statutes.

Recommendation: We recommend that the City monitor budgeted expenditures and amend when the City expects to incur expenditures in excess of appropriations. We also recommend that the City amend future budgets on the same level of detail as the original budget ordinance.

Management's Response: We agree with the auditors' comments and have implemented remedial efforts to prevent future non-compliance to KRS 91A.030. During 2015, the City implemented Phase I of its new financial systems software which was expressly designed to ensure proper tracking of expenditures and amendments to appropriations. During FY 2016, the City's Finance Director implemented a new work flow process using a Budget Re-appropriation form that requires detailed descriptions for re-appropriation of expenditures. This form is initiated by Department Directors and signed by the City Manager prior to an adjustment being made to budget line items in the City's financial system. Electronic, as well as paper records, for all adjustments are kept on an ongoing basis. This process has been improved as feedback has been received during its initial rollout, and the

CITY OF COVINGTON, KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS, Continued
for the year ended June 30, 2017

City believes that the budget re-appropriation process is now sufficient for the purpose of budgetary compliance. Furthermore, quarterly budget status reviews are performed by management and department heads in order to address areas of concern within the budget.

Finally, development of the FY 2017-2018 budget for all funds was accomplished using the City's new automated software tool, Extended Budgeting. This software module is integrated into the City's core financial system enabling development of the City's budget with direct input by Department Heads. This new process provides a closed-loop solution to budgeting by placing ownership for budget development, as well as ongoing budgetary compliance, into the hands of Department Heads. We deem this finding to be appropriately re-mediated and no further action is necessary.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

NONE

IV. PRIOR AUDIT FINDINGS

Finding 2016-001 – Material Weakness – Audit Adjustments

Audit adjustments were necessary to properly record receivables, payables, unearned revenue, accrued liabilities and interfund activity and to restate beginning fund balance.

Status: Repeated as Finding 2017-001

Finding 2017-002 – Material Weakness – Fixed Asset Recording

Audit adjustments were necessary to restate net position, capitalize prior year additions and reclassify current year capital additions.

Status: Repeated as Finding 2017-002

Finding 2016-003 – Significant Deficiency – Accounting Procedures

The City lacked a comprehensive accounting procedures manual.

Status: Repeated as Finding 2017-004

Finding 2016-004 – Budgetary Noncompliance

The City was not in compliance with Kentucky statutes related to budgeting.

Status: Repeated as Finding 2017-005

Finding 2016-005 – CFDA 14.871 Section 8 Housing Choice Vouchers

The City did not submit its unaudited financial information, for the fiscal year ended June 30, 2015, until March 2016. The City's audited submission was in the IPA disagrees status.

Status: The City submitted its unaudited financial information for the fiscal year ended June 30, 2016 by the required due date.