

**REPORT OF THE AUDIT OF THE
LEE COUNTY
FISCAL COURT**

**For The Fiscal Year Ended
June 30, 2011**

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To the People of Kentucky
Honorable Steven L. Beshear, Governor
Lori H. Flanery, Secretary
Finance and Administration Cabinet
Honorable Steve Mays, Lee County Judge/Executive
Members of the Lee County Fiscal Court

Independent Auditor's Report

We have audited the accompanying financial statements of the governmental activities and each major fund of Lee County, Kentucky, as of and for the year ended June 30, 2011, which collectively comprise the County's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Lee County Fiscal Court. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with 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, and the Audit Guide for Fiscal Court Audits issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 1, Lee County, Kentucky, prepares its financial statements in accordance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of Lee County, Kentucky, as of June 30, 2011, and the respective changes in financial position, and cash flows, where applicable, thereof for the year then ended in conformity with the basis of accounting described in Note 1.

The county has implemented Governmental Accounting Standards Board Statement 54 as it relates to the modified cash basis of accounting as described in Note 1, which has altered the format and content of the basic financial statements.

In accordance with Government Auditing Standards, we have also issued our report dated April 5, 2012, on our consideration of Lee County, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

To the People of Kentucky
Honorable Steven L. Beshear, Governor
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Members of the Lee County Fiscal Court

Accounting principles generally accepted in the United States of America require that the budgetary comparison information, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

The County omitted the management's discussion and analysis that the Governmental Accounting Standards Board (GASB) requires to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Based on the results of our audit, we present the accompanying comment and recommendation included herein, which discusses the following report comment:

2011-01 The County Should Implement Proper Internal Controls Over Time Sheets

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

April 5, 2012

LEE COUNTY OFFICIALS

For The Year Ended June 30, 2011

Fiscal Court Members:

Steve Mays	County Judge/Executive
Ronnie Paul Begley	Magistrate
Lenard Carl Ross	Magistrate
Bennie Todd	Magistrate
Billy Joe Coomer	Magistrate

Other Elected Officials:

Thomas Hollon	County Attorney
Corbett Dunaway	Jailer
Kim Savage	County Clerk
Emma Adams	Circuit Court Clerk
Wendell Childers	Sheriff
Elizabeth Roach	Property Valuation Administrator
Ray Shuler	Coroner

Appointed Personnel:

Pearl Spencer	County Treasurer
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LEE COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2011

LEE COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2011

	Primary Government Governmental Activities
ASSETS	
Current Assets:	
Cash and Cash Equivalents	\$ 1,168,823
Capital Asset Held for Resale	233,200
Total Current Assets	<u>1,402,023</u>
Noncurrent Assets:	
Capital Assets - Net of Accumulated Depreciation	
Land	319,083
Land Improvements	163,369
Construction in Progress	80,946
Buildings	2,347,445
Other Equipment	170,735
Vehicles and Equipment	1,048,442
Infrastructure	2,860,007
Total Noncurrent Assets	<u>6,990,027</u>
Total Assets	<u>8,392,050</u>
LIABILITIES	
Current Liabilities:	
Financing Obligations Payable	316,738
Noncurrent Liabilities:	
Financing Obligations Payable	262,149
Total Liabilities	<u>578,887</u>
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	6,644,340
Unrestricted	1,168,823
Total Net Assets	<u>\$ 7,813,163</u>

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2011

LEE COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2011

Functions/Programs Reporting Entity	Expenses	Program Revenues Received			Net (Expenses) Revenues and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
Primary Government:					
Governmental Activities:					
General Government	\$ 1,813,463	\$ 81,050	\$ 305,348	\$	\$ (1,427,065)
Protection to Persons and Property	1,410,369	695,765	82,003	70,500	(562,101)
General Health and Sanitation	893,067	369,127	357,288	56,500	(110,152)
Social Services	46,483		17,646		(28,837)
Recreation and Culture	156,305			439,987	283,682
Roads	1,477,122		1,271,282	525,475	319,635
Interest on Long-term Debt	19,691				(19,691)
Capital Projects	23,352				(23,352)
Total Governmental Activities	<u>5,839,852</u>	<u>1,145,942</u>	<u>2,033,567</u>	<u>1,092,462</u>	<u>(1,567,881)</u>
Total Primary Government	<u>\$ 5,839,852</u>	<u>\$ 1,145,942</u>	<u>\$ 2,033,567</u>	<u>\$ 1,092,462</u>	<u>(1,567,881)</u>
General Revenues:					
Taxes:					
					935,042
					261,884
					62,268
					42,569
					30,686
					32,501
					322,904
					2,875
					<u>1,690,729</u>
					122,848
					<u>7,690,315</u>
					<u>\$ 7,813,163</u>

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2011

LEE COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2011

	General Fund	Road Fund	Solid Waste Fund	Total Governmental Funds
ASSETS				
Cash and Cash Equivalents	\$ 724,806	\$ 141,204	\$ 302,813	\$ 1,168,823
Total Assets	<u>\$ 724,806</u>	<u>\$ 141,204</u>	<u>\$ 302,813</u>	<u>\$ 1,168,823</u>
FUND BALANCES				
Assigned				
Roads		141,204	302,813	444,017
Unassigned	724,806			724,806
Total Fund Balances	<u>\$ 724,806</u>	<u>\$ 141,204</u>	<u>\$ 302,813</u>	<u>\$ 1,168,823</u>

Reconciliation of the Balance Sheet - Governmental Funds to the Statement of Net Assets:

Total Fund Balances	\$ 1,168,823
Amounts Reported for Governmental Activities in the Statement	
Of Net Assets are Different because:	
Capital Assets Used in Governmental Activities are not Financial Resources	
And, Therefore are not Reported in the Funds.	10,177,859
Accumulated Depreciation	(3,187,832)
Capital Asset Held for Resale	233,200
Long-Term and Short-Term Debt is not Due and Payable in the	
Current Period and, Therefore, is not Reported in the Funds.	
Financing Obligations	<u>(578,887)</u>
Net Assets of Governmental Activities	<u>\$ 7,813,163</u>

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2011

LEE COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2011

	General Fund	Road Fund	Solid Waste Fund	Total Governmental Funds
REVENUES				
Taxes	\$ 1,765,583	\$ 24,575	\$	\$ 1,790,158
In Lieu Tax Payments	4,542	26,144		30,686
Excess Fees	32,501			32,501
Licenses and Permits	19,017			19,017
Intergovernmental	887,712	1,336,134	413,788	2,637,634
Charges for Services	695,765		369,127	1,064,892
Miscellaneous	159,512	210,207	15,219	384,938
Interest	1,172	895	808	2,875
Total Revenues	<u>3,565,804</u>	<u>1,597,955</u>	<u>798,942</u>	<u>5,962,701</u>
EXPENDITURES				
General Government	960,122			960,122
Protection to Persons and Property	1,463,188			1,463,188
General Health and Sanitation	44,439		802,178	846,617
Social Services	42,986			42,986
Recreation and Culture	344,503			344,503
Roads	646,301	1,624,022		2,270,323
Debt Service	2,384	82,303	25,214	109,901
Capital Projects	9,899	13,453		23,352
Administration	572,297	185,475	96,502	854,274
Total Expenditures	<u>4,086,119</u>	<u>1,905,253</u>	<u>923,894</u>	<u>6,915,266</u>
Excess (Deficiency) of Revenues Over Expenditures before Other Financing Sources (Uses)	(520,315)	(307,298)	(124,952)	(952,565)
Other Financing Sources (Uses)				
Financing Obligation Proceeds	233,200			233,200
Transfers from Other Funds	150,000	214,442		364,442
Transfers to Other Funds	(214,442)	(150,000)		(364,442)
Total Other Financing Sources (Uses)	<u>168,758</u>	<u>64,442</u>		<u>233,200</u>
Net Change in Fund Balances	(351,557)	(242,856)	(124,952)	(719,365)
Fund Balances - Beginning	1,076,363	384,060	427,765	1,888,188
Fund Balances - Ending	<u>\$ 724,806</u>	<u>\$ 141,204</u>	<u>\$ 302,813</u>	<u>\$ 1,168,823</u>

The accompanying notes are an integral part of the financial statements.

**LEE COUNTY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS**

For The Year Ended June 30, 2011

LEE COUNTY
 RECONCILIATION OF THE STATEMENT OF REVENUES,
 EXPENDITURES, AND CHANGES IN FUND BALANCES OF
 GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2011

Reconciliation to the Statement of Activities:

Net Change in Fund Balances - Total Governmental Funds	\$ (719,365)
<p>Amounts Reported for Governmental Activities in the Statement of Activities are Different because Governmental Funds Report Capital Outlays as Expenditures. However, in the Statement of Activities the Cost of Those Assets are Allocated over Their Estimated Useful Lives and Reported as Depreciation Expense.</p>	
Capital Outlay	1,710,195
Disposal of Capital Assets	(57,837)
Depreciation Expense	(575,354)
Capital Assets Held for Resale	233,200
Construction In Process Completed	(325,000)
<p>The Issuance of Long-term Debt (e.g. Bonds, Financing Obligations) Provides Current Financial Resources to Governmental Funds, While Repayment of Principal on Long-Term Debt Consumes the Current Financial Resources of Governmental Funds. These Transactions, However, Have No Effect on Net Assets.</p>	
Financing Obligation Proceeds	(233,200)
Financing Obligations Principal Payments	90,210
Rounding Difference	(1)
	<hr/>
Change in Net Assets of Governmental Activities	<u><u>\$ 122,848</u></u>

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LEE COUNTY
NOTES TO FINANCIAL STATEMENTS

June 30, 2011

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

The county presents its government-wide and fund financial statements in accordance with a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. This modified cash basis recognizes revenues when received and expenditures when paid. Notes receivable are recognized on the Statement of Net Assets, but notes receivable are not included and recognized on Balance Sheet - Governmental Funds. Property tax receivables, accounts payable, compensated absences, and donated assets are not reflected in the financial statements.

The State Local Finance Officer does not require the county to report capital assets and infrastructure; however the value of these assets is included in the Statement of Net Assets and the corresponding depreciation expense is included on the Statement of Activities.

B. Reporting Entity

The financial statements of Lee County include the funds, agencies, boards, and entities for which the fiscal court is financially accountable. Financial accountability, as defined by Section 2100 of the Governmental Accounting Standards Board (GASB) Codification of Governmental Accounting and Financial Reporting Standards, as amended by GASB 14 and GASB 39, was determined on the basis of the government's ability to significantly influence operations, select the governing authority, participate in fiscal management and the scope of public service. Consequently, the reporting entity includes organizations that are legally separate from the primary government. Legally separate organizations are reported as component units if either the county is financially accountable or the organization's exclusion would cause the county's financial statements to be misleading or incomplete. Component units may be blended or discretely presented. Blended component units either provide their services exclusively or almost entirely to the primary government, or their governing bodies are substantively the same as the primary government. All other component units are discretely presented. The County has no discretely presented component units.

Blended Component Units

The following legally separate organization provides its services exclusively to the primary government, and the fiscal court is able to impose its will on this organization. This organization's balances and transactions are reported as though they are part of the county's primary government using the blending method.

Public Service Corporation

The Public Service Corporation is a legally separate entity established to provide debt service for the purchase of real estate property from the Kentucky Mountains Farm Cooperative. The Public Service Corporation's governing body consists entirely of Fiscal Court members. Therefore, management should include the Public Service Corporation as a component unit, and its financial activity should be blended with that of the fiscal court. However, the Public Service Corporation had no financial activity during the year to blend with the fiscal court.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

C. Lee County Elected Officials

Kentucky law provides for election of the officials below from the geographic area constituting Lee County. Pursuant to state statute, these officials perform various services for the Commonwealth of Kentucky, its judicial courts, the fiscal court, various cities and special districts within the county, and the board of education. In exercising these responsibilities, however, they are required to comply with state laws. Audits of their financial statements are issued separately and individually and can be obtained from their respective administrative offices. These financial statements are not required to be included in the financial statements of Lee County, Kentucky.

- Circuit Court Clerk
- County Attorney
- Property Valuation Administrator
- County Clerk
- County Sheriff

D. Government-wide and Fund Financial Statements

In March 2009, the Governmental Accounting Standard Board (GASB) issued Statement No. 54 – *Fund Balance Reporting and Government Fund Type Definitions*. This Statement established fund balance classifications based primarily on the extent to which the County is bound to honor constraints on the use of the resources reported in each governmental fund as well as establishes additional note disclosures regarding fund balance classification policies and procedures. The County implemented this standard effective July 1, 2010. As a result, the following previously reported funds are now included in the General Fund: LGEA, Ambulance, Jail and Handicap Funds.

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its non-fiduciary component units. For the most part, the effect of interfund activities has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on sales, fees, and charges for support. Business-type revenues come mostly from fees charged to external parties for goods or services. Fiduciary funds are not included in these financial statements due to the unavailability of fiduciary funds to aid in the support of government programs.

The government-wide statements are reported using the economic resources measurement focus and the modified cash basis of accounting. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. Property tax receivables, accounts payable, compensated absences, and donated assets are not reflected in the financial statements.

The statement of net assets presents the reporting entity's non-fiduciary assets and liabilities, the difference between the two being reported as net assets. Net assets are reported in three categories: 1) invested in capital assets, net of related debt - consisting of capital assets, net of accumulated depreciation and reduced by outstanding balances for debt related to the acquisition, construction, or improvement of those assets; 2) restricted net assets - resulting from constraints placed on net assets by creditors, grantors, contributors, and other external parties, including those constraints imposed by law through constitutional provisions or enabling legislation; and 3) unrestricted net assets - those assets that do not meet the definition of restricted net assets or invested in capital assets.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
 June 30, 2011
 (Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

D. Government-wide and Fund Financial Statements (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function; 2) operating grants and contributions; and 3) capital grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Internally dedicated resources such as taxes and unrestricted state funds are reported as general revenues.

Funds are characterized as either major or non-major. Major funds are those whose assets, liabilities, revenues, or expenditures/expenses are at least ten percent of the corresponding total (assets, liabilities, etc.) for all funds or type (governmental or proprietary) and whose total assets, liabilities, revenues, or expenditures/expenses are at least five percent of the corresponding total for all governmental and enterprise funds combined. The fiscal court may also designate any fund as major. Major individual governmental funds are reported as separate columns in the financial statements.

Governmental Funds

The primary government reports the following major governmental funds:

General Fund - This is the primary operating fund of the fiscal court. It accounts for all financial resources of the general government, except where the Department for Local Government requires a separate fund or where management requires that a separate fund be used for some function.

Road Fund - This fund is for road and bridge construction and repair. The primary source of revenue for this fund is state payments for truck licenses distribution, municipal road aid, and transportation grants. The Department for Local Government requires the fiscal court to maintain these receipts and expenditures separately from the General Fund.

Solid Waste Fund - This fund accounts for all revenues from users of the Solid Waste Services.

Special Revenue Funds

The Road Fund and Solid Waste Fund are presented as special revenue funds. Special revenue funds are used to account for the proceeds of specific revenue sources and expenditures that are legally restricted for specific purposes.

E. Deposits and Investments

The government's cash and cash equivalents are considered to be cash on hand, demand deposits, certificates of deposit, and short-term investments with original maturities of three months or less from the date of acquisition.

KRS 66.480 authorizes the county to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

F. Capital Assets

Capital assets, which include land, land improvements, buildings, furniture and office equipment, building improvements, machinery, equipment, and infrastructure assets (roads and bridges) that have a useful life of more than one reporting period based on the government's capitalization policy, are reported in the applicable governmental or business-type activities of the government-wide financial statements. Such assets are recorded at historical cost or estimated historical cost when purchased or constructed.

Cost of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life are not capitalized. Land and Construction In Progress are not depreciated. Interest incurred during construction is not capitalized. Capital assets and infrastructure are depreciated using the straight-line method of depreciation over the estimated useful life of the asset.

	Capitalization Threshold	Useful Life (Years)
Land Improvements	\$ 12,500	10-60
Buildings and Building Improvements	\$ 25,000	10-75
Machinery and Equipment	\$ 2,500	3-25
Vehicles	\$ 2,500	3-25
Infrastructure	\$ 20,000	10-50

G. Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, long term debt and other long-term obligations are reported as liabilities in the applicable financial statements. The principal amount of bonds, notes and financing obligations are reported.

In the fund financial statements, governmental fund types recognize bond interest, as well as bond issuance costs when received or when paid, during the current period. The principal amount of the debt and interest are reported as expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures. Debt proceeds are reported as other financing sources.

H. Fund Equity

In the fund financial statements, governmental funds report aggregate amounts for five classifications of fund balances based on the constraints imposed on the use of these resources. The nonspendable fund balance classification includes amounts that cannot be spent because they are either (a) not in spendable form – prepaid items or inventories; or (b) legally or contractually required to be maintained intact.

The spendable portion of the fund balance comprises the remaining four classifications: restricted, committed, assigned, and unassigned.

Restricted fund balance. This classification reflects the constraints imposed on resources either (a) externally by creditors, grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions or enabling legislation.

LEE COUNTY
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2011
 (Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

H. Fund Equity (Continued)

Committed fund balance. These amounts can only be used for specific purposes pursuant to constraints imposed by formal resolutions or ordinances of the fiscal court – the government's highest level of decision making authority. Those committed amounts cannot be used for any other purpose unless the fiscal court removes the specified use by taking the same type of action imposing the commitment. This classification also includes contractual obligations to the extent that existing resources in the fund have been specifically committed for use in satisfying those contractual requirements.

Assigned fund balance. This classification reflects the amounts constrained by the county's "intent" to be used for specific purposes, but are neither restricted nor committed. The fiscal court and Judge/Executive have authority to assign amounts to be used for specific purposes. Assigned fund balances include all remaining amounts (except negative balances) that are reported in governmental funds, other than the General Fund, that are not classified as nonspendable and are neither restricted nor committed.

Unassigned fund balance. This fund balance is the residual classification for the General Fund. It is also used to report negative fund balances in other governmental funds.

When both restricted and unrestricted resources are available for use, it is the county's policy to use externally restricted resources first, then unrestricted revenues – committed, assigned, and unassigned - in order as needed.

I. Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

J. Joint Venture

A legal entity or other organization that results from a contractual agreement and that is owned, operated, or governed by two or more participants as a separate activity subject to joint control, in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility is a joint venture. Based upon these criteria, the following is considered a joint venture of the Wolfe County Fiscal Court:

Three Forks Regional Jail

On October 6, 2000, the Counties of Lee, Owsley and Wolfe (the participating counties) entered into an Interlocal Cooperation Agreement in order to provide for joint and cooperative action in the acquisition, construction, installation, maintenance and financing of the Three Forks Regional Jail. Pursuant to this interlocal agreement, Lee County (the lead county) established the Three Forks Public Properties Corporation,

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

J. Joint Venture (Continued)

a legally separate organization, to act as an agency and instrumentality of the participating counties in financing the acquisition and construction of the Three Forks Regional Jail. On December 1, 2000 the corporation issued \$6,295,000 of first mortgage revenue bonds.

The only source of funds expected by the Three Forks Public Properties Corporation to meet the debt service requirements on the bonds are the rental payments from the participating counties, as stipulated in the lease and sublease agreements dated October 1, 2000. Pursuant to the lease and sublease, each participating county covenants to meet its proportionate share of the debt service requirements on the bond as follows (the "proportionate share" or "use allowance"): 40% for Lee County, 22% for Owsley County, and 38% for Wolfe County.

On December 1, 2000, the three participating counties established the Three Forks Regional Jail Authority pursuant to the provisions of KRS 441.800 and KRS 441.810 to act as the constituted authority of the participating counties in the acquisition, construction, equipping, and operation of the Three Forks Regional Jail.

The Three Forks Regional Jail Authority and the Three Forks Public Property Corporation are comprised of an eight-member board of directors. Lee County appoints three of the eight members. Wolfe and Owsley counties appoint two members each. In addition the Lee County Jailer is a required member of the board.

A copy of the Three Forks Regional Jail Audit Report may be obtained by writing the management at 2475 Center Street, Beattyville, KY 41311.

K. Property Tax Calendar

Generally and except as otherwise provided by law, property taxes are assessed as of January 1, levied (mailed) November 1, due at discount November 30, due at face value December 31, delinquent January 1 following the assessment, and subject to sale ninety days following April 15.

Note 2. Deposits

The primary government maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(D). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. These requirements were met.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the government's deposits may not be returned. The government does not have a deposit policy for custodial credit risk, but rather follows the requirements of KRS 41.240 (4). As of June 30, 2011, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 3. Capital Assets

Capital asset activity for the year ended June 30, 2011 was as follows:

	Reporting Entity			
	Beginning Balance	Increases	Decreases	Ending Balance
Primary Government:				
Governmental Activities:				
Capital Assets Not Being Depreciated:				
Land and Land Improvements	\$ 319,083	\$	\$	\$ 319,083
Construction in Progress (Restated)	266,946	139,000	(325,000)	80,946
Total Capital Assets Not Being Depreciated	586,029	139,000	(325,000)	400,029
Capital Assets, Being Depreciated:				
Land Improvements	196,068			196,068
Buildings (Restated)	2,692,178	407,212		3,099,390
Other Equipment (Restated)	468,918	48,843		517,761
Vehicles and Equipment	1,941,007	277,455	(150,510)	2,067,952
Infrastructure	3,058,974	837,685		3,896,659
Total Capital Assets Being Depreciated	8,357,145	1,571,195	(150,510)	9,777,830
Less Accumulated Depreciation for:				
Land Improvements	(24,525)	(8,174)		(32,699)
Buildings (Restated)	(685,285)	(66,660)		(751,945)
Other Equipment (Restated)	(283,439)	(63,587)		(347,026)
Vehicles and Equipment	(942,111)	(170,072)	92,673	(1,019,510)
Infrastructure	(769,793)	(266,859)		(1,036,652)
Total Accumulated Depreciation	(2,705,153)	(575,352)	92,673	(3,187,832)
Total Capital Assets, Being Depreciated, Net	5,651,992	995,843	(57,837)	6,589,998
Governmental Activities Capital Assets, Net	\$ 6,238,021	\$ 1,134,843	\$ (382,837)	\$ 6,990,027

Depreciation expense was charged to functions of the primary government as follows:

<u>Governmental Activities:</u>	
General Government	\$ 47,910
Protection to Persons and Property	84,276
Social Services	3,497
Recreation and Culture	56,986
General Health and Sanitation	51,338
Roads, Including Depreciation of General Infrastructure Assets	331,345
Total Depreciation Expense - Governmental Activities	<u>\$ 575,352</u>

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 4. Short-term Debt

Mack Trucks

In March 2011, Lee County Fiscal Court entered into a financing obligation agreement for \$233,200 with People's Exchange Bank to purchase Mack trucks. The county purchased heavy trucks to use for one year; then the trucks are to be sold at auction. The terms of the agreement stipulate a one-year repayment schedule, with principal and interest due on March 18, 2012 with an interest rate of 4.0 percent. The outstanding principal as of June 30, 2011 was \$233,200.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
<u>Governmental Activities</u>					
Financing Obligations	\$	\$ 233,200	\$	\$ 233,200	\$ 233,200
Governmental Activities Short-term Liabilities	\$ 0	\$ 233,200	\$ 0	\$ 233,200	\$ 233,200

Note 5. Long-term Debt

A. Road Paving

In May 2002, Lee County Fiscal Court entered into a financing obligation agreement for \$300,000 with the Kentucky Association of Counties Leasing Trust Program, for road paving. The terms of the agreement stipulate a ten-year repayment schedule, with variable monthly payments and variable annual principal payments. The principal amount is due on January 20 of each year to end on January 20, 2012 with an interest rate of 2.75 percent. The outstanding principal as of June 30, 2011 was \$35,000. Future lease principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Principal	Interest
2012	\$ 35,000	\$ 995
Totals	\$ 35,000	\$ 995

B. Solid Waste Equipment

In July 2003, Lee County Fiscal Court entered into a financing obligation agreement for \$325,000 with the Kentucky Association of Counties Leasing Trust Program, for a multipurpose agreement for the purpose of solid waste equipment. However, the county only used \$250,241 of the proceeds to purchase equipment. During December 2003, the county judge/executive requested the balance of the agreement be applied towards the principal thereby reducing monthly payments. The terms of the agreement stipulate a ten-year repayment schedule, with variable monthly payments and variable monthly principal payments to end on October 20, 2010 an interest rate of 2.175 percent. This debt was paid in full as of June 30, 2011.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 5.

Long Term Debt (Continued)

C. Rear Loader

In February 2008, Lee County Fiscal Court entered into a financing obligation agreement for \$111,800 with the Kentucky Association of Counties Leasing Trust Program, to purchase a rear loader. The terms of the agreement stipulate an eight-year repayment schedule, with variable monthly payments and variable monthly principal payments to end on March 20, 2016 an interest rate of 5.227 percent. The outstanding principal as of June 30, 2011 was \$71,228. Future lease principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Principal	Interest
2012	\$ 13,599	\$ 2,880
2013	14,457	2,310
2014	15,370	1,706
2015	16,340	1,063
2016	11,462	332
Totals	<u>\$ 71,228</u>	<u>\$ 8,291</u>

D. Blacktop Project

In August 2009, Lee County Fiscal Court entered into a financing obligation agreement for \$300,000 with the Kentucky Association of Counties Leasing Trust Program, to pave county roads. The terms of the agreement stipulate an eight-year repayment schedule, with variable monthly payments and variable monthly principal payments to end on August 20, 2017 an interest rate of 4.217 percent. The outstanding principal as of June 30, 2011 was \$239,458. Future lease principal and interest requirements are:

Fiscal Year Ended June 30	Governmental Activities	
	Principal	Interest
2012	\$ 34,939	\$ 9,413
2013	36,362	7,965
2014	37,844	6,455
2015	39,386	4,882
2016	40,990	3,248
2017-2018	49,937	1,635
Totals	<u>\$ 239,458</u>	<u>\$ 33,598</u>

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 5.

Long Term Debt (Continued)

E. Changes In Long-term Liabilities

Long-term liability activity for the year ended June 30, 2011, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Primary Government:					
<u>Governmental Activities:</u>					
Financing Obligations	\$ 435,897		\$ 90,210	\$ 345,687	\$ 83,538
Governmental Activities					
Long-term Liabilities	\$ 435,897	\$ 0	\$ 90,210	\$ 345,687	\$ 83,538

Note 6. Employee Retirement System

The fiscal court has elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost sharing, multiple employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability and death benefits to plan members. Benefit contributions and provisions are established by statute.

Nonhazardous covered employees are required to contribute 5 percent of their salary to the plan. Nonhazardous covered employees who begin participation on or after September 1, 2008 are required to contribute 6 percent of their salary to be allocated as follows: 5% will go to the member's account and 1% will go to the KRS insurance fund. The county's contribution rate for nonhazardous employees was 16.93 percent.

Hazardous covered employees are required to contribute 8 percent of their salary to the plan. Hazardous covered employees who begin participation on or after September 1, 2008 are required to contribute 9 percent of their salary to be allocated as follows: 8% will go to the member's account and 1% will go to the KRS insurance fund. The county's contribution rate for hazardous employees was 33.25 percent.

The county's contribution for FY 2010 was \$253,088 and FY 2011 was \$253,512.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Nonhazardous employees who begin participation on or after September 1, 2008 must meet the rule of 87 (members age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months service credit.

Aspects of benefits for hazardous employees include retirement after 20 years of service or age 55. For hazardous employees who begin participation on or after September 1, 2008 aspects of benefits include retirement after 25 years of service or the member is age 60, with a minimum of 60 months of service credit.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 6. Employment Retirement System (Continued)

CERS also provides post retirement health care coverage as follows:

For member participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

<u>Years of Service</u>	<u>% Paid by Insurance Fund</u>	<u>% Paid by Member through Payroll Deduction</u>
20 or more	100%	0%
15-19	75%	25%
10-14	50%	50%
4-9	25%	75%
Less than 4	0%	100%

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, non-hazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount.

Hazardous employees whose participation began on or after July 1, 2003, earn fifteen dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount. Upon the death of a hazardous employee, such employee's spouse receives ten dollars per month for insurance benefits for each year of the deceased employee's hazardous service. This dollar amount is subject to adjustment annually based on the retiree cost of living adjustment, which is updated annually due to changes in the Consumer Price Index.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report. This report may be obtained by writing the Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, KY 40601-6124, or

Note 7. Insurance

For the fiscal year ended June 30, 2011, Lee County was a member of the Kentucky Association of Counties' All Lines Fund (KALF). KALF is a self-insurance fund and was organized to obtain lower cost coverage for general liability, property damage, public officials' errors and omissions, public liability, and other damages. The basic nature of a self-insurance program is that of a collectively shared risk by its members. If losses incurred for covered claims exceed the resources contributed by the members, the members are responsible for payment of the excess losses.

Note 8. Prior Period Adjustment

The beginning net asset balance as of June 30, 2011 for governmental activities of Lee County Fiscal Court has been restated. We have made adjustments to correct prior year capital asset errors. The beginning net asset balance was decreased by \$50,601.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2011
(Continued)

Note 9. Construction In Progress

Construction In Progress consisted of the following project as of June 30, 2011:

Emergency Service Building	\$34,446
Skate Park	<u>46,500</u>
	<u>\$80,946</u>

Note 10. Subsequent Events

Subsequent events have been evaluated through April 5, 2012, which is the date the financial statements were available to be issued.

LEE COUNTY
BUDGETARY COMPARISON SCHEDULES
Required Supplementary Information - Modified Cash Basis

For The Year Ended June 30, 2011

LEE COUNTY
BUDGETARY COMPARISON SCHEDULES
 Required Supplementary Information - Modified Cash Basis

For The Year Ended June 30, 2011

	GENERAL FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes	\$ 1,480,818	\$ 1,532,818	\$ 1,741,714	\$ 208,896
In Lieu Tax Payments	7,600	7,600	4,542	(3,058)
Excess Fees	28,629	28,629	32,501	3,872
Licenses and Permits	18,000	18,000	19,017	1,017
Intergovernmental Revenue	317,450	317,450	329,878	12,428
Charges for Services	8,000	8,000	6,537	(1,463)
Miscellaneous	78,100	127,601	152,807	25,206
Interest	1,500	1,500	798	(702)
Total Revenues	1,940,097	2,041,598	2,287,794	246,196
EXPENDITURES				
General Government	911,995	1,000,796	960,122	40,674
Protection to Persons and Property	244,196	278,569	266,060	12,509
General Health and Sanitation	1,500	1,142	595	547
Social Services	51,150	50,960	42,986	7,974
Recreation and Culture	142,480	355,886	332,503	23,383
Roads	200,000	285,664	285,050	614
Debt Service		2,450	2,384	66
Capital Projects	260,000	9,900	9,899	1
Administration	341,276	286,284	275,035	11,249
Total Expenditures	2,152,597	2,271,651	2,174,634	97,017
Excess (Deficiency) of Revenues over Expenditures Before Other Financing Sources (Uses)	(212,500)	(230,053)	113,160	343,213
OTHER FINANCING SOURCES (USES)				
Transfers from Other Funds			150,000	150,000
Transfers to Other Funds	(254,391)	(334,391)	(548,833)	(214,442)
Total Other Financing Sources (Uses)	(254,391)	(334,391)	(398,833)	(64,442)
Net Changes in Fund Balance	(466,891)	(564,444)	(285,673)	278,771
Fund Balance - Beginning	469,391	569,391	902,804	333,413
Fund Balance - Ending	\$ 2,500	\$ 4,947	\$ 617,131	\$ 612,184

LEE COUNTY
 BUDGETARY COMPARISON SCHEDULES
 Required Supplementary Information - Modified Cash Basis
 For The Year Ended June 30, 2011
 (Continued)

ROAD FUND				
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes		\$ 24,574	\$ 24,575	\$ 1
In Lieu Tax Payments	32,490	32,490	26,144	(6,346)
Intergovernmental Revenue	798,855	1,338,529	1,336,134	(2,395)
Miscellaneous	182,876	182,876	210,207	27,331
Interest	700	700	895	195
Total Revenues	1,014,921	1,579,169	1,597,955	18,786
EXPENDITURES				
Roads	680,828	1,629,896	1,624,022	5,874
Debt	308,642	82,543	82,303	240
Capital Projects	10,000	13,453	13,453	0
Administration	181,451	187,973	185,475	2,498
Total Expenditures	1,180,921	1,913,865	1,905,253	8,612
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	(166,000)	(334,696)	(307,298)	27,398
OTHER FINANCING SOURCES (USES)				
Transfers from Other Funds			214,442	214,442
Transfers to Other Funds			(150,000)	(150,000)
Total Other Financing Sources (Uses)			64,442	64,442
Net Changes in Fund Balance	(166,000)	(334,696)	(242,856)	91,840
Fund Balance - Beginning	166,000	334,696	384,060	49,364
Fund Balance - Ending	\$ 0	\$ 0	\$ 141,204	\$ 141,204

LEE COUNTY
 BUDGETARY COMPARISON SCHEDULES
 Required Supplementary Information - Modified Cash Basis
 For The Year Ended June 30, 2011
 (Continued)

SOLID WASTE FUND				
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Intergovernmental	\$	\$ 323,001	\$ 413,788	\$ 90,787
Charges for Services	401,000	401,000	369,127	(31,873)
Miscellaneous	100	100	15,219	15,119
Interest	500	500	808	308
Total Revenues	401,600	724,601	798,942	74,341
EXPENDITURES				
General Health and Sanitation	554,528	871,458	802,178	69,280
Debt Service	42,972	25,526	25,214	312
Administration	74,100	97,617	96,502	1,115
Total Expenditures	671,600	994,601	923,894	70,707
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	(270,000)	(270,000)	(124,952)	145,048
Net Changes in Fund Balances	(270,000)	(270,000)	(124,952)	145,048
Fund Balances - Beginning	270,000	270,000	427,765	157,765
Fund Balances - Ending	\$ 0	\$ 0	\$ 302,813	\$ 302,813

LEE COUNTY
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

June 30, 2011

Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

	<u>Revenues</u>	<u>Expenditures</u>	<u>Transfers & Other Financing Sources (Uses)</u>	<u>Fund Balances - Beginning</u>
General Fund				
Budgetary Comparison Schedule	\$ 2,287,794	\$ 2,174,634	\$ (398,833)	\$ 902,804
Debt Issued for the Purchase of Mack Trucks		233,200	233,200	
Prior Year Audit Adjustments Not Recorded On Books				(558)
Amounts Budgeted in Separate Funds By the County that do not Meet the Definition of a Special Revenue Fund As Defined by GASB 54	<u>1,278,010</u>	<u>1,678,285</u>	<u>334,391</u>	<u>174,117</u>
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	<u>\$ 3,565,804</u>	<u>\$ 4,086,119</u>	<u>\$ 168,758</u>	<u>\$ 1,076,363</u>

**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**

Morgan-Franklin, LLC
Certified Public Accountants

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Brenda K. Morgan, CPA
Jody B. Franklin, CPA

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The Honorable Steve Mays, Lee County Judge/Executive
Members of the Lee County Fiscal Court

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

We have audited the financial statements of the governmental activities and each major fund of Lee County, Kentucky, as of and for the year ended June 30, 2011, which collectively comprise the County's basic financial statements and have issued our report thereon dated April 5, 2012. Lee County presents its financial statements on the modified cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with 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.

Internal Control Over Financial Reporting

Management of Lee County Fiscal Court is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the County's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control 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 *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.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be

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
(Continued)

material weaknesses, as defined above. However, we identified a deficiency in internal control over financial reporting, described in the accompanying comment and recommendation as item 2011-1 that we consider to be a significant deficiency in internal control over financial reporting. 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.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the County's financial statements are free of 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 no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The Lee County Judge/Executive's response to the finding identified in our audit is included in the accompanying comment and recommendation. We did not audit the County Judge/Executive response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, others within the entity, and the Department for Local Government and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

April 5, 2012

COMMENT AND RECOMMENDATION

FISCAL YEAR ENDED JUNE 30, 2011

**LEE COUNTY
COMMENT AND RECOMMENDATION**

Fiscal Year Ended June 30, 2011

SIGNIFICANT DEFICIENCY:

2011-1 The County Should Implement Proper Internal Controls Over Time Sheets

Condition: During our payroll testing we noted the following:

- Two instances where employees were paid for more time than was indicated on their timesheets. It appears one EMT was paid for four hours of overtime that he did not actually work and a paramedic chosen for testing was paid .5 hours of overtime that he did not actually work.
- One instance in which an EMT was paid for two hours for being called in for unscheduled work hours when his time sheet indicated less than two hours were worked. It appears that in practice when EMTs are called in for unscheduled work hours; they are paid for a minimum of two hours regardless of actual hours worked.
- One instance where a supervisor did not sign a timesheet.

Criteria:

- The County should establish adequate internal controls over timesheets to ensure employees receive proper payment.
- Absent a policy regarding paying employees for time worked, the County should only pay employees for actual hours worked. If the County chooses to pay a minimum amount for individuals who are called in for unscheduled work hours, the personnel policies and procedures should reflect this practice.
- Supervisors should sign off on timesheets.

Cause: There is a lack of internal controls over timesheets. There are no written policies in place when EMTs are called in for unscheduled work hours.

Effect: Lack of proper internal controls for payroll increase the risk that incorrect payroll information will be processed by the County and that these errors will not be identified and corrected.

Recommendation: We recommend the Fiscal Court reevaluate their controls over payroll to determine the controls that would best address the findings listed under the condition section above. The Fiscal Court may determine the controls listed above under the criteria section are adequate or may decide to implement other controls to eliminate such internal control weaknesses in the future.

County's Response: In response to the Exit Conference –

- *Condition: The two instances where employees were paid for more time than was indicated on their timesheets was clearly an error in addition of hours.*
- *One instance where an employee was paid for two hours for being called in: I agree the Policy for the 2 hr call in should have been a written policy.*
- *One instance where a supervisor did not sign a timesheet- We will check better to insure we have a signed timesheet by the supervisors.*

**CERTIFICATION OF COMPLIANCE -
LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM**

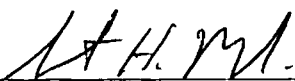
LEE COUNTY FISCAL COURT

**For The Fiscal Year Ended
June 30, 2011**

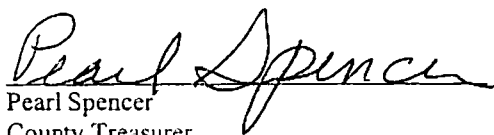
CERTIFICATION OF COMPLIANCE
LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAMS
LEE COUNTY FISCAL COURT

Fiscal Year Ended June 30, 2011

The Lee County Fiscal Court hereby certifies that assistance received from the Local Government Economic Assistance Program was expended for the purposes intended as dictated by the applicable Kentucky Revised Statutes.



Steve Mays
County Judge/Executive



Pearl Spencer
County Treasurer