



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial-Related Audit

Minnesota Supreme Court
July 1, 1997, through June 30, 2001



Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Kathleen Blatz, Chief Justice
Minnesota Supreme Court

We have audited the Supreme Court for the period July 1, 1997, through June 30, 2001, as further explained in Chapter 1. Our audit scope included attorney registration fees, payroll, grants, rent, purchased services, supplies, equipment, travel, and other operating costs. The audit objectives and conclusions are highlighted in the individual chapters of this report.

We conducted our audit in accordance with standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the Supreme Court complied with the provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Supreme Court is responsible for establishing and maintaining the internal control structure and for compliance with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Supreme Court. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 1, 2002.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: January 31, 2002

Report Signed On: February 25, 2002

Minnesota Supreme Court

Table of Contents

	Page
Report Summary	1
Chapter 1. Introduction	2
Chapter 2. Revenues	4
Chapter 3. Payroll	6
Chapter 4. Other Expenditures	9
Status of Prior Audit Issues	11
Supreme Court Response	12

Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Cecile Ferkul, CPA, CISA	Audit Manager
Tony Toscano	Audit Director
April Snyder	Auditor
Theresa Hahn	Auditor
Marisa Zenk	Auditor

Exit Conference

The following staff from the Supreme Court participated in the exit conference held on February 15, 2002:

Natha Horbach	Finance Director
Roger Volk	Accounting Supervisor
Diana Williams	Human Resources Director

Report Summary

Current Findings and Recommendations

- The Supreme Court needs to improve controls over receipts. The court did not adequately safeguard or promptly deposit attorney registration fee receipts, which totaled about \$4 million annually. We recommended that the court keep receipts in a secure place and make deposits in a timely manner. (Finding 1, page 5)
- The Supreme Court did not document its approval for employees to exceed vacation leave maximums. We recommended that the Supreme Court require employees to reduce their balances to the maximum allowable accrual or document its agreement with the employees it allowed to exceed vacation accrual maximums. (Finding 2, page 7)
- The Supreme Court did not complete a physical inventory of fixed assets and did not conduct periodic spot checks to verify their existence and location. Although the court has procedures for adding and deleting items from an automated fixed asset module, without a periodic, complete physical inventory, the court cannot ensure the records are accurate. Without an adequate system of accounting for fixed assets, theft or misuse of fixed assets could go undetected. We recommended that the court complete a physical inventory, conduct periodic spot checks of fixed assets, and update inventory records as appropriate. (Finding 3, page 10)

Financial-Related Audit Reports address internal control weaknesses and noncompliance issues noted during our audits of state departments and agencies. The scope of our audit work at the Supreme Court included attorney registration receipts, payroll, travel, and other administrative expenditures for rent, jury costs, purchased services, supplies, and equipment. The court's response is included in the report.

Minnesota Supreme Court

Chapter 1. Introduction

Article VI of the Minnesota Constitution established the judicial branch of state government to interpret laws and cases and to ensure that challenged laws do not violate the constitution. The judicial branch has several levels of courts, each with specific jurisdictions that determine the types of cases to be heard. Our audit focused on the district courts, the Court of Appeals, and the Supreme Court.

District Courts

The district courts in Minnesota are the trial courts of general jurisdiction. In each of the state's ten judicial districts, made up of one to seventeen counties, the district court hears all civil, criminal, family, juvenile, traffic, and ordinance violation cases. The Governor initially appoints judges to vacant seats. The judges then stand for election by the voters of the respective districts, for six-year terms. As of January 2002, there were 257 district judges. Each district has at least three judges. Every two years, judges of each district elect a chief judge and an assistant chief judge, who have administrative responsibility for coordinating the business of the court in that district.

The state pays all judicial salaries; however, the funding of other district court operational costs evolved from total county funding to a shared funding arrangement between the state and counties. This process began in 1990 as a pilot project in the Eighth Judicial District. At that time, the state assumed a larger financial responsibility for court operations. The 1999 Legislature expanded the scope of state funded operations in the Eighth Judicial District effective July 1999 and extended the funding to the Fifth, Seventh, and Ninth Judicial Districts effective July 2000.

Court of Appeals

The Court of Appeals has jurisdiction over all appeals from the district courts except conciliation court and from the Commissioner of Economic Security and various administrative agencies. Any appeal must have a legal basis, such as judicial error, failure to follow proper procedure, or violation of the constitution. Voters elect the 15 judges and the chief justice to six-year terms. A rotating panel of three judges hears each appeal. The Honorable Edward Toussaint has served as the Chief Judge since 1995.

Supreme Court

The Supreme Court is the highest court in the state. The Supreme Court's main functions are to hear appeals, administer the court system, and regulate the practice of law. The court hears appeals of cases from the Court of Appeals, the Minnesota Workers' Compensation Court of Appeals, and the Minnesota Tax Court. It also has jurisdiction over defendants convicted of

Minnesota Supreme Court

first-degree murder and discretionary review of decisions of the Court of Appeals. The Supreme Court has six judges and a chief justice. Voters elect justices to six-year terms on a non-partisan ballot. The Governor fills any vacancies that occur during a term on the court. The Honorable Kathleen Blatz has served as the Supreme Court's Chief Justice since January 1998.

The Supreme Court supervises and coordinates the work of the state's courts through the Office of the State Court Administrator. The office has administrative responsibilities for the budget, facility management, legislation, caseload management, personnel, continuing education, record management, information systems, planning, and research. The office also collaborates and consults with the ten district court administrators who have similar responsibilities at the district court level.

Table 1-1 provides a summary of the financial activity of the courts for the fiscal year ended June 30, 2001.

Table 1-1			
Minnesota Court System			
Sources and Uses of Funds			
Fiscal Year 2001			
	<u>Supreme Court</u>	<u>Court of Appeals</u>	<u>District Courts</u>
Sources:			
State Appropriations	\$28,990,000	\$6,749,000	\$100,834,000
Attorney Registration Fees	3,826,123	0	0
Interagency Agreement with the Department of Human Services for Child Support Enforcement	3,441,176	0	0
Other	2,027,330	0	238,941
Balance Forward In	7,710,213	96,558	1,442,938
Total Sources	<u>\$45,994,842</u>	<u>\$6,845,558</u>	<u>\$102,515,879</u>
Uses:			
Salaries	\$14,695,649	\$5,276,430	\$ 82,309,125
Grants	7,787,323	0	0
Rent	2,822,742	957,868	291,315
Other Operating Costs/Juries	438,386	16,664	5,766,662
Equipment	2,339,749	176,114	2,916,668
Purchased Services	6,370,781	4,258	5,986,175
Supplies	1,263,114	102,856	1,700,945
Travel	204,141	34,158	938,684
Other	3,439,051	180,472	2,381,615
Total Expenditures	<u>\$39,360,936</u>	<u>\$6,748,820</u>	<u>\$102,291,189</u>
Balance Forward Out	6,087,700	0	18,335
Appropriations Cancellations	546,206	96,738	205,549
Net Transfers	0	0	806
Total Uses	<u>\$45,994,842</u>	<u>\$6,845,558</u>	<u>\$102,515,879</u>

Source: Minnesota Accounting and Procurement System through December 31, 2001.

Chapter 2. Revenues

Chapter Conclusions

The Supreme Court accurately recorded attorney registration fees, interagency agreements, and district court fines and fees as revenue in the accounting records. For the items tested, the court properly allocated attorney registration fee receipts in accordance with court rules. However, the Supreme Court did not adequately safeguard and timely deposit attorney registration fees.

Attorney registration fees are one of the Supreme Court's largest revenue sources. An attorney pays this fee to obtain a license after passing the bar exam and to renew the license annually. Through the Rules of the Supreme Court for Registration of Attorneys, the state Bar Association sets the attorney registration fees. The Supreme Court collects the fees and allocates them to the following entities as prescribed by court rules:

- State Board of Law Examiners
- State Board of Continuing Legal Education
- Lawyers Professional Responsibility Board
- Minnesota Client Security Fund
- Legal Services Advisory Committee

The Supreme Court also received funding through two interagency agreements. Beginning in fiscal year 2000, the court received federal and state funds through the Department of Human Services to allow the court to administer the child support contested hearing process. This process became the court's responsibility after a determination that having it in the executive branch violated the separation of powers doctrine. The court received \$3,416,550 and \$3,441,176 in fiscal years 2000 and 2001, respectively. Expenditures included payroll, repairs and alterations, professional/technical contracts, travel, supplies, and equipment. In fiscal year 1999, the court received \$490,000 from the Department of Public Safety for enhancements to the criminal justice computer systems.

Since fiscal year 1999, as part of a pilot project to have the state assume a larger share of district court operating costs, the Eighth Judicial District deposited fines and fees in the state treasury as non-dedicated receipts. In fiscal year 2001, the state expanded the pilot project to the Fifth, Seventh, and Ninth Judicial Districts. Consequently, those districts also deposited fines and fees into the state treasury.

Minnesota Supreme Court

Audit Objectives and Methodology

Our audit of revenue focused on the following objectives:

- Did the Supreme Court adequately safeguard its receipts?
- Did the Supreme and district courts timely and properly deposit receipts?
- Did the Supreme Court properly allocate and record its attorney registration fee receipts?
- Did the Supreme Court receive the correct amount from the interagency agreements?

To address these objectives, we interviewed office personnel to gain an understanding of the internal control structure for revenue transactions. We analyzed and tested these revenues to ensure compliance with the terms of the court orders, statutes, and interagency agreements.

Conclusions

The Supreme Court accurately recorded attorney registration fees, the interagency agreements, and district court fines and fees in the accounting records. For the items tested, the court properly allocated attorney registration fee receipts. However, the Supreme Court did not adequately safeguard and timely deposit attorney registration fees.

1. The Supreme Court needs to improve controls over receipts.

The Supreme Court did not adequately safeguard or promptly deposit attorney registration fee receipts. Court staff kept checks in a file cabinet or in a bin on top of a filing cabinet and did not promptly deposit five of the nine deposits initially tested. Testing of the first two weeks in June 2001 found that the court held receipts from two to six days before making a deposit. Failure to properly secure or promptly deposit receipts increases the risk of theft or loss. Attorney registration fees totaled about \$4 million annually.

Recommendation

- *The Supreme Court needs to adequately secure receipts and make deposits in a timely manner.*

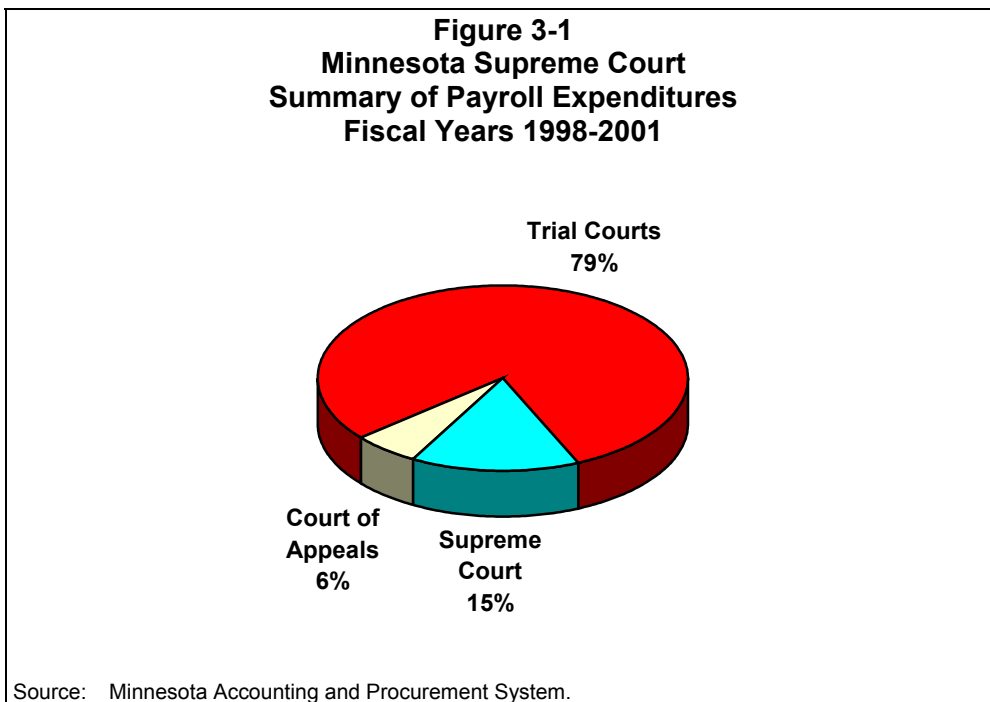
Chapter 3. Payroll

Chapter Conclusions

The Supreme Court properly authorized, processed, and accurately reported payroll expenditures in the accounting records. Except for the court's lack of documentation of approval for certain vacation leave balances, the Supreme Court complied with the Judicial Personnel Plan and applicable state policies and procedures.

The Supreme Court's payroll costs included payments to state employees and payments to judicial districts for county payroll charges. The Supreme Court processed state employee payroll data through the state's payroll/personnel system and paid judicial districts for employees who elected to retain their status as county employees for purposes of county benefits. For fiscal years 1998 through 2001, payroll payments to counties totaled about \$30 million.

The court's payroll expenditures totaled about \$339,300,000 for the four fiscal years ended June 30, 2001. Figure 3-1 shows the percentage of payroll expenditures by each court.



Minnesota Supreme Court

Audit Objectives and Methodology

Our review of the Supreme Court's payroll focused on the following questions:

- Did the Supreme Court properly authorize, process, and record payroll transactions in the accounting records?
- Did the Supreme Court process payroll in accordance with the Judicial Personnel Plan and applicable state policies and procedures?

To answer these questions we interviewed Supreme Court employees to gain an understanding of the payroll process. We performed analytical procedures on the payroll population to detect unusual trends or irregularities. We tested pay rates for judges and a sample of the reimbursements to counties.

Conclusion

The Supreme Court properly authorized, processed, and accurately reported payroll expenditures in the accounting records. Except for the court's lack of documentation of approval for certain vacation leave balances, as explained in Finding 2, the Supreme Court complied with the Judicial Personnel Plan and applicable state policies and procedures.

2. The Supreme Court did not document its approval for employees to exceed vacation leave maximums.

The Supreme Court allowed some employees to accrue vacation leave exceeding the maximum balances allowed by the Judicial Personnel Plan. As of June 30, 2001, five employees had vacation balances ranging from 346.5 to 955.5 hours. The court did not document approval for these exceptions to the leave accrual policy and did not document its understanding with the employees about how and when leave balances would be reduced to the maximum amounts. Without written documentation, employees may believe they are entitled to payment for their entire vacation balance upon leaving state service, or the employee may take an extended vacation and disrupt the office's operations. We raised this same concern in our audit report issued in September 1994.

The Judicial Personnel Plan allows employees to accumulate vacation leave to a maximum of 260 hours and allows directors to accumulate vacation leave to any amount as long as they reduce the balance once a year to at least 275 hours. None of the five employees reduced their leave balances to the allowable levels during the audit period. The plan also provides that in "emergency situations" the court may temporarily suspend the maximum number of hours. The plan restricts employees' vacation accruals to limit the state's liability to employees upon termination and to ensure that employees take reasonable periods of time-off at regular intervals.

Recommendation

- *The Supreme Court should require employees to reduce their balances to the maximum allowable accrual or document its agreement with employees it has allowed to exceed vacation accrual maximums.*

Chapter 4. Other Expenditures

Chapter Conclusions

The Supreme Court, Court of Appeals, and district courts properly recorded its administrative expenditures in the state's accounting system in compliance with legal provisions and management's authorizations. However, the Supreme Court did not complete a physical inventory of its fixed assets.

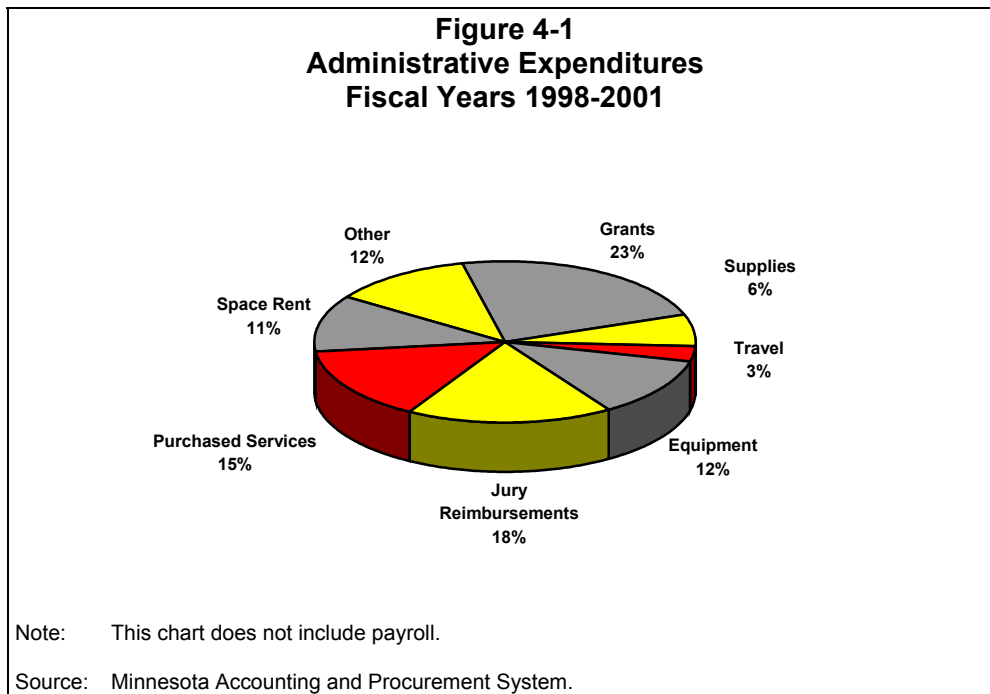
The Supreme Court's non-payroll expenditures, including grants, rent, purchased services, supplies, equipment, travel, and other operating costs totaled approximately \$140 million during fiscal years 1998-2001. Each of the various boards within the Supreme Court had responsibility for purchasing decisions within its budgetary limits. The district courts and Court of Appeals also made purchasing decisions and contracted for goods and services. The administrative services section of the Supreme Court received the payment documentation from the boards and the other courts, reviewed and approved them, and entered the payments into the state's accounting system.

The Supreme Court granted funds to various non-profit organizations to provide legal assistance for low-income individuals through its legal services and family law programs. An advisory committee selected six organizations throughout the state to administer the assistance to qualified individuals. The Supreme Court also granted money under its community dispute resolution program. The program operated to bring disputed parties together voluntarily to resolve their differences through mediation or arbitration. Although many of the grant agreements for fiscal year 2000 were not signed until August 1999, the Supreme Court reimbursed most grantees for services provided since July 1, 1999. The standard grant contract used by the court stated that the grantee should not begin work until the court fully executed the grant agreement. Fiscal year 2001 grant agreements were timely prepared and signed.

The Supreme Court's purchased services included reimbursements to the judicial districts for jury related expenses such as the daily fee paid to the jurors, lodging, meals, and childcare. The counties directly paid the jury costs and then submitted the payment information to the district offices. The district offices reviewed the information and forwarded it to the Supreme Court for reimbursement. Except as noted in Finding 3, the Supreme Court reimbursed the district offices on a monthly basis.

Figure 4-1 shows non-payroll expenditures for the four fiscal years ended June 30, 2001, and the percentage of each category to total expenditures.

Minnesota Supreme Court



Audit Objectives and Methodology

Our review of other expenditures focused on the following questions:

- Did the Supreme Court accurately record non-payroll expenditures in the accounting records in compliance with legal provisions and management’s authorizations?
- Did the Supreme Court comply with material finance-related legal provisions?

To address these objectives, we interviewed personnel to gain an understanding of the controls over expenditures. We tested a sample of transactions to determine whether the courts properly authorized, processed, and recorded expenditure transactions. We also reviewed expenditures to determine if the courts complied with material finance-related legal provisions. Finally, we reviewed the courts’ process to record and control fixed assets.

Conclusions

The Supreme Court properly recorded its non-payroll expenditures in the state’s accounting system in compliance with legal provisions and management’s authorizations. However as discussed in Finding 3, the court did not complete a physical inventory of its fixed assets.

Minnesota Supreme Court

3. The Supreme Court did not complete a physical inventory of fixed assets.

The Supreme Court did not complete a physical inventory of all fixed assets. In addition, the court did not conduct periodic spot checks to verify the existence and location of these assets. The court used an automated fixed asset inventory module to record its fixed assets additions. The court's inventory list included computers for several districts acquired in 1991 and a fax machine acquired in 1989. It seems unlikely that the court still has or is currently using these assets. Although the court has procedures for adding and deleting items from the state's fixed asset module, without a periodic, complete physical inventory, the court cannot ensure the records are accurate.

Financial management responsibilities include maintaining an accurate record of the location of fixed assets, identifying the employees accountable for the physical security of the assets, and conducting periodic physical counts and/or spot checks. A physical count of the fixed asset inventory also helps to ensure that the amount stated on the financial statements is accurate. Without an adequate system of accounting for fixed assets, theft or misuse of fixed assets could go undetected. The court's management of its fixed asset inventory becomes more challenging as more districts fall under the court's jurisdiction.

Recommendation

- *The court should complete a physical inventory, conduct periodic spot checks of fixed assets, and update inventory records as appropriate.*

Minnesota Supreme Court

Status of Prior Audit Issues As of January 31, 2002

Most Recent Audit

Legislative Audit Report 98-50, issued in September 1998, focused on selected operations of the Supreme Court, Court of Appeals, and district courts. The report contained two findings, both of which were implemented.



**THE SUPREME COURT OF MINNESOTA
MINNESOTA JUDICIAL CENTER
25 CONSTITUTION AVENUE
SAINT PAUL, MINNESOTA 55155**

CHAMBERS OF
KATHLEEN A. BLATZ
CHIEF JUSTICE

(651) 296-3380

February 22, 2002

Mr. James Nobles
Legislative Auditor
First Floor South, Centennial Building
658 Cedar Street
Saint Paul, MN 55115

Dear Mr. Nobles:

Following the completion of the most recent audit of the Judicial Branch for Fiscal Years 1998 – 2001 by members of your staff, three recommendations were made for improving internal controls.

1. Improve controls over safeguarding and prompt deposit of Attorney Registration Fee Receipts:

Finance staff will meet with the Attorney Registration Clerk and walk through the procedures used to handle fee receipts. Finance staff will design improved procedures in order to ensure safeguarding and prompt deposit of receipts. Improved procedures will be in place by March 31, 2002.

2. Document approval when employees have to exceed vacation maximums.

During the past several years, the extraordinary workload of State Court Administration has made it impossible for a few key employees to take sufficient vacation time to reduce their accruals to the limits set by the Judicial Branch Personnel Policy. Our Human Resources staff will be examining these policies and recommending changes. In addition, Human Resources staff have implemented procedures to document in the employee's file any exceptions granted under the existing policy.

3. Complete a physical inventory and improve tracking for fixed assets.

Historically, the Courts have not had sufficient staff time to conduct a physical inventory of fixed assets. However, this biennium we have received funding to add additional staff to our Finance Department. Responsibility for monitoring and control of fixed assets, including coordination of the physical inventory, has been assigned to our Accounting Lead Worker position. During FY 03, Court staff will take a complete inventory of fixed assets, and we will reconcile the inventory with our assets listing. We expect to complete this work by June 30, 2003.

Sincerely yours,

/s/ Kathleen A. Blatz

Kathleen A. Blatz
Chief Justice