



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

FINANCIAL AUDIT DIVISION REPORT

**Minnesota Judicial Branch
Second Judicial District**

Internal Controls and Compliance Audit

July 1, 2009, through March 31, 2011

October 20, 2011

Report 11-23

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

October 20, 2011

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This report presents the results of our internal controls and compliance audit of the Minnesota Judicial Branch's Second Judicial District for the period July 1, 2009, through March 31, 2011.

We discussed the results of the audit with the Second Judicial District's staff at an exit conference on September 26, 2011. This audit was conducted by Michael Hassing, CPA, CISA (Audit Manager) and Joan Haskin, CPA, CISA (Auditor-in-Charge), assisted by auditors David Minch, Blake Schwagel, and Shanda Wilhelmy.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Minnesota Judicial Council, the Office of the State Court Administrator, and the Second Judicial District. This restriction is not intended to limit the distribution of this report, which was released as a public document on October 20, 2011.

We received the full cooperation of the Second Judicial District's staff while performing this audit.

James R. Nobles
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Report Summary

Conclusion

The Second Judicial District, located in Ramsey County, did not have adequate internal controls to ensure that it safeguarded receipts and other assets, accurately paid employees and vendors in accordance with management's authorizations, produced reliable financial information, and complied with finance-related legal requirements.

For the items tested, the Second Judicial District generally complied with finance-related legal requirements over its financial activities. However, the district had some instances of noncompliance related to receipts, payroll, and other administrative expenditures.

Key Findings

- The Second Judicial District did not adequately manage its financial risks or monitor the effectiveness of its internal controls. ([Finding 1, page 7](#))
- The Second Judicial District did not adequately restrict employees' access to its business and data systems. ([Finding 2, page 8](#))
- The Second Judicial District did not review or document its review of some high-risk receipt transactions. ([Finding 3, page 10](#))
- The Second Judicial District did not review key payroll reports. ([Finding 6, page 12](#))
- The Second Judicial District did not have adequate controls over some of its administrative expenditures. ([Finding 7, page 14](#))
- The Second Judicial District did not have adequate controls over gift cards it purchased as incentives for drug and mental health treatment. ([Finding 8, page 16](#))
- The Second Judicial District did not adequately control its capital assets and sensitive items. ([Finding 9, page 18](#))

Audit Objectives and Scope

Objectives

- Internal controls
- Compliance

Period Audited

July 1, 2009, through March 31, 2011

Programs Audited

- Receipts
 - Payroll expenditures
 - Other administrative expenditures
 - Computer system access
-

Overview

Minnesota's Judicial Branch includes the Supreme Court, the Court of Appeals, and the District Courts.¹ Most cases begin in Minnesota's District Courts, which have original jurisdiction in all civil and criminal cases involving Minnesota law. District Courts are located in each of the state's 87 counties and are divided into ten judicial districts for administrative purposes. Minnesota currently has 280 District Court judges. Each district is managed by a chief judge and an assistant chief judge, assisted by a judicial district administrator. There is a court administrator in each county who is responsible for day-to-day operations.

The District Courts use a case management system known as the Minnesota Court Information System (MnCIS) to record court data statewide. The system includes a case management component and a financial management component. Significant aspects of a case are recorded in the system, including fines and fees. Various types of case information is entered into the system including, but not limited to, alleged offenses charged, originating jurisdiction, pleas, dispositions, sentences, hearing dates, documents filed, notices issued, orders and writs issued, judgments, and other court-related events. Financial data from the court information system interfaces with the state's accounting system.

The Second Judicial District and Fourth Judicial District also use a separate automated case management system, known as the Violations Bureau Electronic System (ViBES), to process payable parking, traffic, and criminal violations charged in District Courts in Ramsey and Hennepin counties. Court staff can enter, update, and track citations, enter charges along with the appropriate fines and fees into this system, and record payments received.

Second Judicial District. As of April 2011, the Second Judicial District had 29 judges, five family court referees, and one family court child support magistrate.² The Honorable Kathleen Gearin is the Chief Judge of the Second Judicial District. The main courthouse is located in downtown St. Paul. The district maintains a criminal unit at the Ramsey County law enforcement center in St. Paul and is legislatively mandated to maintain a suburban criminal unit, which is located in the city of Maplewood. The district also operates the Juvenile and Family Justice Center in St. Paul. The Second Judicial District states as its mission, "To provide

¹ The Minnesota Judicial Council is the administrative policy-making authority for the Minnesota Judicial Branch. The purpose of the council is to govern the Judicial Branch through the establishment and monitoring of administrative policies. The Chief Justice of the Supreme Court serves as the chair of the Judicial Council. The State Court Administrator is also a member of the Judicial Council.

² Judges can hear any criminal or civil matter brought before them. Referees can hear certain cases and provide procedural and substantive decisions subject to review and approval by a judge. Magistrates handle child support cases in the expedited child support process.

a fair, impartial, accessible, and open judicial forum for the efficient resolution of criminal, civil, juvenile, family, and probate legal matters.”

The Second Judicial District Court is organized into the following five divisions:

- **Court Administration** oversees the general operation of the court and handles functions, such as human resources, budget and accounting, and information services.
- The **Assignment Office** schedules civil and criminal cases and courtroom assignments.
- The **Civil Division** is responsible for civil lawsuits and cases involving civil commitment, probate, conciliation, and housing.
- The **Criminal and Traffic Division** processes criminal complaints, criminal citations, and traffic tickets. It also provides support staff for criminal-related and traffic-related court sessions. The Violations Bureau is part of the Criminal and Traffic Division.
- The **Special Courts Division** oversees the areas of domestic abuse, family court, guardian ad litem, harassment, and juvenile court.

Table 1 summarizes the Second Judicial District’s receipts and expenditures for the period July 1, 2009, through March 31, 2011.

Table 1 Second Judicial District Receipts and Expenditures July 1, 2009, through March 31, 2011		
	<u>Fiscal Years¹</u>	
	<u>2010</u>	<u>2011</u>
<u>Receipts:</u>		
Fees and Fines	\$23,758,555	\$16,921,672
<u>Expenditures:</u>		
Payroll	\$17,345,776	\$11,588,397
Administrative Expenditures:		
Professional/Technical Contracts	1,208,487	574,348
Purchased Services	799,149	577,879
Equipment	73,584	46,753
Supplies	354,119	342,090
Communications	404,705	202,457
Other Expenditures	<u>728,810</u>	<u>417,920</u>
Total Expenditures	<u>\$20,914,630</u>	<u>\$13,749,844</u>

¹ The state’s fiscal year is July 1 through June 30.

Objective, Scope, and Methodology

Our audit of the Second Judicial District (district) included material financial activities (receipts, employee payroll, other administrative expenditures, and computer systems access) for the period July 1, 2009, through March 31, 2011.

Our audit objective was to answer the following questions:

- Were the Second Judicial District's internal controls adequate to ensure it safeguarded its receipts and other assets, accurately paid employees and vendors in accordance with management's authorizations, complied with legal requirements, and produced reliable financial data?
- Did the Second Judicial District comply with selected significant finance-related legal requirements?

To answer these questions, we gained an understanding of the district's financial policies and procedures. We considered the risk of errors in the accounting records and noncompliance with relevant legal requirements. We analyzed accounting data to identify unusual trends or significant changes in financial operations. In addition, we selected a sample of financial transactions and reviewed supporting documentation to test whether the controls were effective and if the transactions complied with laws, regulations, policies, and grant and contract provisions.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

We used the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate the district's internal controls.³ We used

³ The Treadway Commission and its Committee of Sponsoring Organizations were established in 1985 by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organizations should have in place to prevent inappropriate financial activity. The resulting *Internal Control-Integrated Framework* is the accepted accounting and auditing standard for internal control design and assessment.

state and federal laws, regulations, and contracts, as well as policies and procedures established by the judicial branch as evaluation criteria over compliance.⁴

Conclusion

The Second Judicial District's internal controls were not adequate to ensure that it safeguarded receipts and other assets, accurately paid employees and vendors in accordance with management's authorizations, produced reliable financial information, and complied with significant finance-related legal requirements.

For the items tested, the Second Judicial District generally complied with selected finance-related legal requirements over its financial activities. However, the district had some instances of noncompliance related to receipts, payroll, and other administrative expenditures.

The following *Findings and Recommendations* provide further explanation about the exceptions noted above.

⁴ The Judicial Council created bylaws and policies that cover all three levels of the judicial branch. The State Court Administrator's Office developed State Court Finance policies and procedures that provide more specific guidance on cash management, fixed asset management, procurement, contracts, and other financial management functions.

Findings and Recommendations

The Second Judicial District did not adequately manage its financial risks or monitor the effectiveness of its internal controls.

Finding 1

The Second Judicial District did not effectively manage the risks related to several of its key operational and finance-related responsibilities. These risks relate to safeguarding the district's assets, processing unauthorized transactions, accurately recording financial activity, and complying with finance-related legal requirements. The district did not ensure that policies and procedures were being followed or establish sufficient monitoring procedures to assess the effectiveness of several fundamental internal controls specifically related to computer access to its business and data systems, reviewing high-risk receipt transactions, validating certain payroll and administrative expense transactions, and providing sufficient oversight for an incentive gift card program and its capital assets.

The Second Judicial District, along with the State Court Administrator's Office, was aware of certain risks, had identified control activities within its policies to address those risks, and performed selected internal control monitoring functions. While the district had many documented procedures, it did not regularly assess whether these procedures were effective to prevent or detect errors and fraud. In addition, the district had not formally developed a comprehensive risk assessment to monitor its overall control structure.

A comprehensive control structure has all of the following key elements:

- Personnel are trained and knowledgeable about finance-related legal provisions and follow applicable policies and procedures.
- Management identifies risks associated with finance-related legal provisions and develops policies and procedures to effectively address the identified risks.
- Management continuously monitors the effectiveness of the controls, identifies weaknesses and breakdowns in controls, and takes corrective action.
- Management focuses on continual improvement to ensure an acceptable balance between controls and costs.

Findings 2 through 9 identify deficiencies in the district's internal control procedures and specific noncompliance with finance-related legal requirements

that were not prevented or detected by the district's current internal control structure. These deficiencies created an environment that increased the risk for significant errors or noncompliance to occur and not be prevented or detected by the district during the normal course of operations. A key to the ongoing effectiveness of these controls will be how well the district and the State Court Administrator's Office monitor, modify, and update controls when the controls do not work as expected in response to changes in policy, personnel, and regulations.

Recommendations

- *The Second Judicial District should work with the State Court Administrator's Office to develop a comprehensive risk assessment for its critical financial controls and regularly review its risks, internal control activities, and monitoring functions related to its operational and compliance responsibilities.*
- *The State Court Administrator's Office should continue to use system-wide training and reassess its policies and procedures to address similar audit findings reported at several district court offices to provide a more comprehensive control environment for the courts.⁵*

Finding 2

The Second Judicial District did not adequately restrict employees' access to its business and data systems.

The district did not restrict employees' access to the state's accounting system and the court information systems to the access needed for the employees' assigned duties. In addition, employees had access that allowed them to perform incompatible duties. The following deficiencies existed in employees' access to the state's accounting system and the court information systems:

- The district did not promptly terminate the authority of two employees to access the state's accounting system when the employees left the district. Their access authority was not terminated for several months after they resigned. In addition, six district employees retained access authority to the court information system for several months after they were no longer employed by the district.
- The district authorized seven employees unnecessary and incompatible access to the state's accounting system that allowed them to encumber funds for contracts and also enter payments. These duties are incompatible because they may allow one employee to initiate contracts, record transactions, and generate payments to a contractor without sufficient

⁵ See Appendix A on page 20.

authorization or a second review. In addition, these seven employees did not require this access to perform their job duties.

- The district authorized two other employees incompatible access to the state's accounting system. These employees could encumber funds, enter purchase orders, receive goods, and make payments. Generally, the functions of purchasing, receiving, and payment processing should be segregated to provide an appropriate level of control over expenditures. The district stated it had some monitoring processes in place for incompatible access to the state's accounting system but did not retain documentation of these reviews.
- The district authorized sixteen court clerks within the criminal division incompatible access to the computer system used for parking, traffic, and criminal violations. These employees could access cash, post receipts to an account, adjust amounts due, and void transactions.
- The district's accounting manager did not periodically review security access reports and did not detect that requested deletions and changes to some employees' access within the state's accounting system had not been made.

Limiting access to the needs of assigned duties and separating incompatible duties are fundamental internal controls designed to prevent error and fraud. These weaknesses, combined with the lack of effective mitigating controls to detect inappropriate or unauthorized transactions, created an unacceptable risk of error or fraud occurring without detection.

Recommendations

- *The Second Judicial District should limit employee access to the state's accounting system and the court information systems to the minimal level necessary for employees to complete job responsibilities.*
 - *The Second Judicial District should eliminate incompatible system access. In instances when that is not possible, it should develop and document effective mitigating controls, such as periodic, independent, and documented reviews of the employees' work.*
 - *The Second Judicial District should periodically review and validate that employees' access to the state's accounting system and court information systems is appropriate.*
-

Finding 3

The Second Judicial District did not review or document its review of some high-risk receipt transactions.

The Second Judicial District's criminal division did not review high-risk transactions entered into the computer system it used for parking, traffic, and criminal violations. Transactions, such as court dismissals or waivers, fine reductions, and error corrections, are high-risk because these transactions could provide an opportunity for fraud; a cashier could conceal the theft of receipts by eliminating or reducing the related revenue and receivables. District personnel stated that they could not generate a report from this system to identify or review these types of transactions. Without review of these high-risk transactions, errors or irregularities could occur without detection.

In addition, the district did not document its review of similar high-risk transactions entered directly into the court information system. The district generated reports from this system that identified high-risk receipt transactions; however, the district did not document its review of the reports.

Judicial branch policy states that supervisory staff should routinely review clerical dismissals of nonmandatory court cases, no proof of insurance charges, financial adjustments, credits, reductions, reversals, and void transactions.⁶ The policy also requires that the transaction review process be properly documented.

Recommendations

- *The Second Judicial District's criminal division should identify and review high-risk transactions recorded in the computer system used for parking, traffic, and criminal violations. Staff performing these reviews should be independent of the receipt process and should retain evidence of the review.*
- *The Second Judicial District's criminal and civil divisions should document their review of the court information system transaction listing report of high-risk transactions.*

Finding 4

The Second Judicial District did not promptly deposit some receipts.

The Second Judicial District's criminal division did not deposit all receipts of \$250 or more daily.⁷ Employees told us that they held some receipts until local law enforcement offices submitted the corresponding citation, and they had entered it into the computer system used for parking, traffic, and criminal

⁶ Minnesota Judicial Branch Policy 209(h) Section IV.

⁷ Minnesota Judicial Branch Policy 207(a) Section V, part 5.1.1 (3) requires daily deposit of receipts totaling \$250 or more. This is a lower threshold than Minnesota Statutes 2011, Chapter 16A.275, which requires daily deposit when receipts total \$1,000 or more.

violations. On June 22, 2011, the Traffic Violations Bureau in St. Paul had undeposited receipts of \$6,775. On May 26, 2011, the Law Enforcement Center in St. Paul had \$2,000 in bail money that was not promptly deposited. District personnel stated that they had held bail money for about three days, waiting for the court information system to be updated before depositing the funds.

In addition, the Second Judicial District did not promptly deposit receipts from several local government entities. On January 14, 2010, the district deposited \$34,836 that it had received as reimbursements for 2009 costs for printing citation books for local government entities. Checks in the deposit were dated from December 15, 2009, to January 6, 2010. Similarly, on March 3, 2011, the district deposited \$30,304 for reimbursement of 2010 printing costs; the checks in this deposit were dated from December 8, 2010, to January 4, 2011.

Judicial branch policy requires court employees to deposit receipts of \$250 or more daily.⁸ Not promptly depositing receipts increased the risk of loss or theft.

Recommendation

- *The Second Judicial District should deposit receipts totaling \$250 or more on a daily basis.*

The Second Judicial District did not have adequate separation of incompatible duties over its local bank account.

Finding 5

A criminal division accountant had incompatible duties related to the district's local bank account. The accountant could both sign checks and also reconcile the account to the bank statements. These duties are incompatible because they allow the accountant to write unauthorized or inappropriate checks without detection through the bank reconciliation. The district used its local bank account for refunds, trust fund disbursements, and restitution payments. The authorized amount of the bank account was \$200,000. Adequate separation of these incompatible duties would have a person not involved in the account's daily processing performing the bank reconciliation to verify that all checks written were authorized and recorded accurately.

Recommendation

- *The Second Judicial District should have someone not involved in the operations of the local bank account perform the reconciliation to the monthly bank statement.*

⁸ Minnesota Judicial Branch Policy 207(a) Section V, part 5.1.1 (3).

Finding 6

The Second Judicial District did not review key payroll reports.

District payroll staff did not review key payroll reports to ensure the accuracy of wages and verify that staff posted payroll expenditures to correct accounts on the state's accounting system. Payroll is the largest expense of the district, totaling over \$17 million during fiscal year 2010, approximately 83 percent of the district's total expenditures. The district paid most employees through the state's payroll system; those employees entered hours worked and created timesheets using the state's self-service time entry system. The district paid some employees through Ramsey County's payroll system because those employees elected to continue to receive county benefits when the court transitioned from county to state funding.⁹ Without regular reviews of key payroll reports, there is an increased risk of undetected errors, inappropriate transactions, or exposure of not public data.

The district had weaknesses in its reviews of the following payroll reports:

- **Self-Service Time Entry Audit Report** - None of the self-service time entry audit reports for the ten pay periods we tested had any indication of district review, such as comments, edits, dates, or signatures. Review of the self service time entry audit report is an important control to ensure the accuracy of the office's payroll. The best control over the integrity of employees' payroll information is achieved when employees prepare their own timesheets and supervisors, who have direct knowledge of employees' work, review and approve timesheets. The self service time entry audit report identifies exceptions related to these controls, e.g., timesheets completed by someone other than the employee and timesheets approved by a backup supervisor or other employee who may not have direct knowledge of an employee's work schedule and may inadvertently authorize inappropriate payroll transactions, rather than the employee's primary supervisor. The reports we tested included 100 instances where supervisors completed timesheets for employees and 52 instances in our tests where a back-up supervisor approved the timesheets. In addition, the district did not have controls in place to ensure the appropriateness and accuracy of timesheets completed, submitted, reviewed, or approved by a payroll employee for other district employees.

The Minnesota judicial branch's payroll policies and procedures require authorized agency payroll or accounting staff to review the self-service time entry audit report.¹⁰ Judicial branch policy requires that

⁹ As district courts transitioned from county to state funding, county court employees became state court employees. Statutory provisions allowed these employees to retain the benefits provided by the county (county-benefited employees) or elect the benefits provided by the state. Employees who chose to retain the county benefits stayed on the county payroll system; the courts reimbursed the counties for these costs.

¹⁰ Minnesota Judicial Branch Policy 206(a) III.F.

documentation be retained when timesheets are completed by a supervisor or approved by a back up supervisor.¹¹

- **Self-Service Managers Report** - The district did not review the self-service managers report. This report shows the review and approval structure established for the automated timesheet system. It identifies employees in each payroll “department” and the departments’ primary and backup supervisors. Human resources staff indicated that they had not reviewed this report since they established the original review and approval structure in April 2005. Our review of the May 24, 2011, report identified an employee who retired in November 2009 listed as a primary approver for a department. The Minnesota judicial branch’s payroll policies require the district to review the assignment of backup approvers and the payroll approval structure at the beginning of each fiscal year.¹²
- **Payroll Register Report** - The payroll register report shows the current pay period’s earnings codes, hours, pay rates, adjustments, lump-sum payments, and expense reimbursements for each employee paid through the state’s payroll system. None of the ten pay periods we tested had any indication of district review, such as comments, edits, dates, or signatures for the payroll register. While the district printed and filed the reports, district staff stated that they did not review the reports. The Minnesota judicial branch’s payroll policies and procedures require authorized agency payroll or accounting staff to review the payroll register report.¹³
- **County Reports** - The district had no documentation to show that payroll staff reviewed the county generated payroll register report or the funding report for the employees paid through the county payroll system.¹⁴ The payroll register report shows the current pay period’s earnings type descriptions, hours, deductions, and gross and net pay for each employee. The funding report lists the current pay period’s total earnings by fund, department, and account for each employee. Although district staff printed both reports and told us they recalculated totals on the funding report, none of the payroll registers or funding reports for the ten pay periods tested had any indication of review, such as comments, edits, dates, or signatures. In addition, supervisors had not signed 10 of 630 timesheets we tested for employees paid through the county payroll system. Supervisory signatures provide validation and accountability for the actual hours worked and leave taken.

¹¹ Minnesota Judicial Branch Policy 206(a) III.E.

¹² Minnesota Judicial Branch Policy 206(a) III.E.

¹³ Minnesota Judicial Branch Policy 206(a) III.F.

¹⁴ As district courts transitioned from county to state funding, county court employees became state court employees. Statutory provisions allowed these employees to retain the benefits provided by the county (county-benefited employees) or elect a new set of benefits provided by the state. Employees who chose to retain the county benefits stayed on the county payroll system; the courts reimbursed the counties for these costs.

The district also did not obtain annual reports from Ramsey County identifying county employees who have access to private data of state employees paid through the county's payroll system. Judicial Branch Policy states that districts should obtain these reports from the counties to ensure that the counties appropriately limit access of state employees' private data.¹⁵

The Minnesota judicial branch's payroll policies require that employees review and monitor county reports to verify the accuracy of payroll reimbursed to the county and leave activity for county-benefited employees.¹⁶

Recommendations

- *The Second Judicial District should review key payroll reports to verify the accuracy of payroll transactions and show the resolution of exceptions noted. The district should sign and date the reports to document its reviews.*
- *The Second Judicial District should retain documentation to support the accuracy of changes supervisors make of employee timesheets and timesheets approved by backup supervisors.*
- *The Second Judicial District should ensure that supervisors authorize timesheets for payments, and someone independent of the payroll process review data entry of employee hours worked.*

Finding 7

The Second Judicial District did not have adequate controls over some of its administrative expenditures.

The district did not have adequate supporting documentation on file for some of its expenditures, initiated some purchases without sufficient authorization, and did not properly identify the liability date for many of its expenditures. The district had the following exceptions:

- **Lack of Documentation** - The district did not have any documentation on file to support 3 of 28 supplies and equipment transactions tested (totaling \$12,470).¹⁷ The district also did not have documentation, such as receipts, packing slips, or bids, for another 8 of the 28 supplies and equipment

¹⁵ Minnesota Judicial Branch Policy 206(a) III.F.2.

¹⁶ Minnesota Judicial Branch Policy 206(a) III.F.2.

¹⁷ Although the district lacked documentation to support that these transactions adhered to purchasing policies and to show proper authorization, the transactions appeared to be reasonable and appropriate for the district's operations.

transactions tested. Due to the lack of receipts and packing slips, we were unable to determine if the district received goods or services prior to making payments for transactions totaling \$77,445. The district did not have written offers, price quotes, or approved sole source request forms on file for 4 of 5 transactions that required them. Payments for these transactions totaled \$75,548. Judicial branch policy requires documented evidence of competitive bid procurement procedures.¹⁸ Finally, the district did not have invoices to support payments for 5 of 16 professional and technical services transactions tested. These payments totaled \$13,370. Judicial branch policy requires appropriate documentation before payments are made.¹⁹

- **Lack of Authorization** - The district initiated two of the eight supply and equipment purchases that exceeded the courts established \$10,000 procurement limit without sufficient authorization, as required by judicial branch policy.²⁰ The district processed transactions of \$15,314 and \$17,384 without obtaining the approval of the district administrator. In addition, the district entered into a contract for \$23,274 of technology-related services without having the State Court Administrator's Office chief information officer/information technology division director sign the contract, as required by the policy.
- **Inaccurate Liability Dates** - The district did not properly identify the liability date for most of the expenditures we tested. The district entered the incorrect record date in the state's accounting system for 33 of 51 transactions tested. For 27 of these transactions, district staff allowed the accounting system to default to the date of the transaction (rather than enter the date they actually received the goods or services) either because they did not document the date of receipt (no dates or signatures on the packing slips) or there was not evidence of receipt. The Department of Management and Budget uses the record date to determine the state's outstanding liabilities at year-end for financial reporting purposes.

Without complete documentation and accurate recording of procurement, contract, and disbursement transactions, the district cannot support that it paid vendors in accordance with management's authorizations, complied with legal requirements, and produced reliable financial data. The district had an unacceptable risk that errors and unauthorized and inappropriate transactions could occur and not be detected.

¹⁸ Minnesota Judicial Branch Policy 202(a) Attachment 4.

¹⁹ Minnesota Judicial Branch Policy 202(a) section V.D.3.

²⁰ Minnesota Judicial Branch Policy 202(a) Attachment 1.

Recommendations

- *The Second Judicial District should retain adequate documentation to support its administrative expenditure transactions.*
- *The Second Judicial District should ensure that it properly authorizes and approves all transactions.*
- *The Second Judicial District should record on packing slips or receiving documents the actual date the goods are received or services rendered to ensure it can correctly code the liability date for expenditure transactions in the state's accounting system.*

Finding 8**The Second Judicial District did not have adequate controls over gift cards it purchased as incentives for drug and mental health treatment.**

The Second Judicial District did not maintain an adequate inventory of incentive gift cards and did not adequately track or safeguard the cards. The district did not have a policy regarding the use of gift cards for incentives or program expenses within some of its programs.

The drug court coordinator and the mental health court coordinator purchased a variety of retail gift cards to distribute to people participating in drug court or mental health court as incentives for them to reach specific milestones in their treatment programs.²¹ The coordinators also used the cards to pay for program expenses, such as cakes for participants upon graduation from the program and for books given to participants as incentives. In addition, participants in these court programs who completed all requirements and responsibilities for the week could win gift cards during weekly courtroom “fishbowl” drawings. The denominations of the gift cards ranged from \$10 to \$300 and included \$10 and \$20 discount department store cards, \$25 movie theater cards, \$50 restaurant cards, and \$300 grocery store cards.²² The district funded the incentive program through various department budgets or interagency agreements with the Department of Human Services. The coordinators either received a check to purchase the cards or paid with their own resources and received reimbursement from the district.

The district had the following weaknesses related to accounting for these incentive gift cards:

²¹ Based on the gift cards on hand or other evidence, the district purchased gift cards from Target, Walmart, Cub Foods, Rainbow Foods, Erbert and Gerbert's Sandwich Shop, and movie theaters.

²² The coordinators used \$300 gift cards to pay for program expenses, such as cakes and paper products. These large valued cards were not given to participants.

- The drug court coordinator did not maintain an inventory of gift cards and did not have records of when or to whom they distributed the gift cards. On June 1, 2011, the drug court had unredeemed gift cards totaling \$1,290 on hand; the district had gift cards totaling \$990 in unlocked file drawers, and the drug court coordinator had a \$300 grocery gift card in her purse that she stated she was going to use for purchasing graduation cakes for clients.
- On June 2, 2011, the mental health coordinator had eight cards totaling \$130 in a locked drawer. The mental health coordinator maintained an inventory of the cards purchased and dates used; however, the list did not include the purchase dates or exactly what some of the cards were used for. According to the tracking sheet for the period April 2010 through May 2011, the coordinator gave \$600 worth of cards to clients/participants as incentives, spent \$430 on program expenses, and provided gift cards totaling \$590 to a person working in a local mental health clinic to distribute to clients. There was no documentation on file from the mental health clinic regarding the status of those cards.
- The district had no receipts to support two separate purchases of \$200 worth of incentive gift cards. In those instances, the district generated checks through the state's accounting system to the vendor.²³ The program coordinator stated that she took the checks to the vendor to purchase gift cards. However, there was no evidence that the division court administrator authorized these transactions prior to the purchase or how the program coordinator actually used the funds.

Without adequate physical safeguarding of the gift cards, an accurate inventory of the gift cards purchased and used, and documentation to support appropriate authorization for the gift card purchases and uses, there is an unacceptably high risk that gift cards could be lost, stolen, or used for inappropriate and unauthorized purposes.

Recommendations

- *The Second Judicial District should develop a policy for the use of gift cards as incentives within certain court ordered programs.*

²³ The district used the state's warrant special handling process, also referred to as the pull warrant process, to obtain the printed state warrant so the program coordinator could purchase the incentive cards directly from the vendor. See Department of Management and Budget's Policy 0803-02, *Warrant Special Handling Request*.

- *The Second Judicial District should maintain an inventory of gift cards and track the purchase and use of all cards. The district should periodically verify that the gift cards on hand reconcile to the inventory records.*
- *The Second Judicial District should maintain documentation to support the authorization of all gift cards purchased and their use or distribution.*
- *The Second Judicial District should adequately safeguard gift cards.*

Finding 9

The Second Judicial District did not adequately control its capital assets and sensitive items.

The district did not maintain a comprehensive capital asset listing or perform a periodic physical inventory for its capital assets or sensitive items, as required by judicial branch policy.²⁴ The judicial branch policy states that a district asset coordinator needs to maintain a current and accurate capital asset inventory and asset tracking file, conduct physical inventory count of all capital assets, including sensitive items, at least once every two years, and implement procedures for disposing of surplus property and for removing retired assets from its capital asset records, as needed. The district court's equipment purchases from July 2009 through March 2011 totaled \$200,576. Without an accurate inventory list, the district could not maintain appropriate accountability for equipment and sensitive assets, increasing the risk of assets being lost or stolen without detection.

Recommendations

- *The Second Judicial District should maintain a comprehensive capital asset listing, including sensitive items.*
- *The Second Judicial District should ensure that it records all current year additions and deletions to its comprehensive list of capital assets.*
- *The Second Judicial District should perform a physical inventory of its capital assets and sensitive items at least once every two years.*

²⁴ Minnesota Judicial branch Policy 208(a), III.B.3.

Appendix A

In Finding 1 on page 7, we noted that several of the internal control weaknesses identified in this report for the Second Judicial District (Findings 2, 3, 4, and 6) have also been issues reported in our audits of other district court offices. The following table identifies those other district court audit reports with similar types of internal control weaknesses:

Audit Report Number²⁵	11-23	09-34	06-16	05-34	04-35	04-35
Issue Date	Oct. 2011	Oct. 2009	June 2006	June 2005	Aug. 2004	Aug. 2004
Audited District or Office	District 2	District 1	District 3	State Court Administrator's Office	District 4	District 7
Finding	Finding Number	Finding Number	Finding Number	Finding Number	Finding Number	Finding Number
The district did not restrict access to its business and data systems.	2	10	1			3
The district did not review high risk receipt transactions.	3	1				
The district did not promptly deposit some receipts.	4	2			2	2
The district did not review key payroll reports.	6	7		1	7	8

²⁵ See the Office of the Legislative Auditor's website for these specific audit reports related to various Judicial District Courts or the State Court Administrator's Office. The audit reports include the Judicial Branch responses to the audit findings.

<http://www.auditor.leg.state.mn.us/fad/fadrpts.htm>

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STATE COURT ADMINISTRATOR

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October 11, 2011

Mr. James R. Nobles
Minnesota Legislative Auditor
140 Centennial Building
658 Cedar Street
St. Paul, MN 55155

Dear Auditor Nobles:

I write in response to the internal control and compliance audit of the Second Judicial District for the period July 1, 2009, through March 31, 2011. Judicial Branch financial transactions are included in the State of Minnesota's Comprehensive Annual Financial Report on which you issued unqualified opinions for the years ended June 30, 2009, and June 30, 2010.

We note in your transmittal letter that *"For the items tested, the Second Judicial District generally complied with selected finance-related legal requirements over its financial activities."* We also note that there was no loss of public funds related to any of the audit findings.

All of your recommendations have been given careful attention and corrective action has either already been implemented or is well underway. Our internal audit unit will also conduct continuous follow-up until each finding is fully resolved. Periodic progress reports will be provided to the Judicial Branch Audit Committee, and we will work to implement a longer-term strategy to better gauge risk.

Sincerely yours,



Sue K. Dosal
State Court Administrator

cc: The Honorable Chief Justice Lorie Skjerven Gildea, Chair
Minnesota Judicial Council

The Honorable Kathleen Gearin, Chief Judge, Second Judicial District

Finding 1: The Second Judicial District did not adequately manage its financial risks or monitor the effectiveness of its internal controls.

Response:

The Second Judicial District agrees that it did not ensure that certain policies and procedures were being followed. Please note that no loss of funds was uncovered. Effective immediately, the district will implement reinforcement training in the areas of procurement, capital assets, and payroll. The district administration office will monitor compliance by developing a series of self-assessment checklists. These reviews will be conducted by district administration and reported back to the district administrator regularly. In addition, the internal audit unit will independently conduct continuous follow-up until each finding is fully resolved.

The State Court Administrator's Office and the Second Judicial District agree that continued development of a comprehensive risk assessment to monitor its overall control structure could more effectively prevent and detect errors and ensure conformance to policy.

The concept of risk assessment is integrated into the management process. Judicial Branch managers analyze and manage risks informally through day-to-day activities. Every manager thinks about risk in every decision they make even though they may not use formal risk terminology or document assessment and management of those risks.

Managers are made aware of emerging risks through several forums. Often times, simple discussions in divisional or unit meetings will identify a risk that needs management. Front line court clerks deal with critical operating issues every day and are often in the best position to recognize problems as they arise. Ongoing monitoring of budget reports, payroll reports, expenditure reports, and information system reports will often times identify a risk. Unusual trends in receipts and expenditures may identify a risk. District managers routinely network with counterparts in other districts to benchmark and to exchange information and strategies on emerging risks. When necessary, the appropriate division at the State Court Administrator's office is consulted to determine the best course of action to manage a particular risk. Once a risk is identified, the manager brainstorms the worst case scenario, analyzes the significance of the risk, and then decides on a cost effective corrective action, often times on the spot.

Most emerging risks at the district level are related to new legislation, budget and staff reductions, increased complexity of case and financial management processes, changing customer expectations, increased volume of transactions, future handoff of certain responsibilities to the centralized court payment center, and information system changes such as the recent conversion to a new state accounting system and periodic upgrades to the court information system.

Risk responsive actions at the district level generally include monitoring of a troubling situation, implementation of a new policy, creation of additional training, or improvement

of exception reports. The State Court Administrator's Finance and Court Services Divisions have created branch wide policies and procedures that manage many of the financial and operational risks faced by the judicial districts. For instance, the internal web site contains a court information system resource center site that provides guidance and training on such key financial processes as accurate fee assessment, daily balancing and depositing, manual receipts, monitoring of high risk transactions, auto referral of overdue accounts, payment plans, auto assessment of fines and fees, and document imaging. Various branch wide work groups such as the accounting workgroup, the financial management workgroup, the court administrator team, the court collections workgroup, the data quality workgroup, and the human resource management team, create and communicate applicable policies, procedures, and best practices. Key policies include the employee code of ethics, confidentiality, conflicts of interest, procurement, contracting, capital assets, and payroll. Training and WebEx sessions are available for such financial and case related transactions as adjustments and credits and monitoring and collections. The State Court Administrator's Information Technology Division provides a branch wide information technology infrastructure that includes system configuration, virus protection software, restricted access, central database management, a back-up plan, firewalls, and input controls.

The Judicial Council and State Court Administration are aware of its responsibilities to maintain an effective internal control structure. The Judicial Branch is also aware that executive branch agencies are required to design an internal control framework that is consistent with the Treadway Commission's Committee of Sponsoring Organizations' (COSO) *Internal Control – Integrated Framework*. Over the next year, the chief financial officer in consultation with the internal audit manager will examine and evaluate formalized risk assessment strategies and determine capability.

Persons responsible for resolving: Diane Carlson, Assistant District Administrator; Dawn Torgerson, Chief Financial Officer

Estimated implementation date: Checklists will be used effective immediately. Risk assessment will be ongoing.

Finding 2: The Second Judicial district did not adequately restrict employees' access to its business and data systems.

Response:

The Second Judicial District agrees that it did not promptly terminate the access authority of two employees to the state's previous accounting system when the employees left the district. Please note that the first employee's logon ID had been disabled and the password expired long before the employee left the district. This was due to system inactivity. Access has been fully terminated from the previous accounting system and no access has been carried over to the new accounting system. The second employee transferred to another district but has subsequently returned. Access authority in the new accounting system will be restricted to necessary functions only.

System security reports with the previous accounting system had to be obtained from Minnesota Management and Budget. Access reviews were limited to annual evaluations. The district accounting manager had been reviewing these reports but did not fully document the examination. With the new accounting system, the State Court Administrator's Office Finance Division can now generate access reports upon demand. The district accounting manager will conduct access evaluations quarterly. These evaluations will be thoroughly documented and will include applicable comments or check marks, date reviewed, and reviewer initials.

The Second Judicial District agrees that six employees retained access to the court information system after they left employment or transferred. Supervisors have already been reminded to promptly submit the required exit forms to the Information Technology Division upon an employee's resignation or transfer. To ensure compliance with exit procedures, the district's human resources staff will begin monthly resignation and transfer notifications to the business systems analyst to ensure access is deleted.

The Second Judicial District agrees that seven employees had incompatible access to the state's accounting system. Although some access was not required for the employees to perform their primary duties, they were allowed clearance in the event a back-up was needed. Although we have removed the ability for backups to initiate contracts, some overlap has been retained. As a mitigating control, the assistant district administrator and/or the district accounting manager will document their examination of the monthly budget reporting package. Detailed payment transactions will be reviewed for unusual vendor names or amounts and a comparison made with budgeted amounts. Documentation will include applicable comments or check marks, date reviewed, and reviewer initials.

The Second Judicial District agrees that sixteen court clerks had incompatible access to the payable citations system. Incompatible access is necessary to efficiently service customers. As a mitigating control, an exception report that lists high risk transactions is currently being developed and tested. An independent clerk or supervisor who does not access cash or post payments will examine a sample of high risk transactions and verify accuracy. These evaluations will be thoroughly documented and will include applicable comments or check marks, date reviewed, and reviewer initials.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager; Diane Carlson; Assistant District Administrator, and Karen Mareck, Criminal Division Manager

Estimated implementation date: December 31, 2011

Finding 3: The Second Judicial District did not review or document its review of some high-risk receipt transactions.

Response:

The Second Judicial District agrees that the criminal division did not review high-risk transactions entered into the payable citations system. As stated in our response to

finding 2, an exception report that lists high risk transactions is currently being developed and tested. A court clerk or supervisor who is independent of the receipting process will examine a sample of high risk transactions and verify accuracy. These evaluations will be thoroughly documented and will include applicable comments or check marks, date reviewed, and reviewer initials.

The Second Judicial District agrees that review of similar high-risk transactions entered into the court information system were not fully documented. The district has already implemented this recommendation and has supplemented its reviews with applicable comments or check marks, date reviewed, and reviewer initials.

Persons responsible for resolving: Karen Mareck, Criminal Division Manager; Vicki Petry, Criminal Division Accountant; Elizabeth Lundgren, Civil Division Accountant

Estimated implementation date: December 31, 2011

Finding 4: The Second Judicial district did not promptly deposit some receipts.

Response:

The Second Judicial District agrees that the Violations Bureau did not always promptly deposit all receipts of \$250 or more. Please note that the criminal division processes approximately \$16 million of receipts each year. All receipts have been properly accounted for, and no discrepancies have occurred. None of the idle receipts involved cash but were limited to a small number of customer checks for citations awaiting transmittal from the issuing municipalities. These checks were adequately safeguarded and promptly processed and deposited as soon as the citations were transmitted.

We will continue to review our business processes and work with the municipalities to transmit paper citations at the earliest opportunity. If necessary to delay processing and depositing, we will seek a waiver from the Minnesota Management and Budget or seek exempting legislation during the next legislative session. At the branch wide level, the State Court Administrator's Office is in the process of raising the daily deposit threshold to \$1,000 to more closely align with state statute and executive branch policy.

The Second Judicial District agrees that on at least one occasion, a small amount of bail funds were not promptly deposited. However, all funds were properly safeguarded. This issue has been addressed with appropriate staff. All bail funds are currently being deposited promptly.

The Second Judicial District agrees that the criminal division did not always promptly deposit disbursement checks from local government entities for citation books. Although the checks were not deposited promptly, they were adequately safeguarded in the interim. It was believed that retention of checks until all had been received contributed to better record keeping. This practice has now been modified, and all disbursement checks will be deposited promptly.

Persons responsible for resolving: Karen Mareck, Criminal Division Manager

Estimated implementation date: November 30, 2011

Finding 5: The Second Judicial District did not have adequate separation of incompatible duties over its local bank account.

Response:

The Second Judicial District agrees that the accountant could both sign checks and also reconcile the bank account. Please note that the ability to sign checks and reconcile the bank account was formally combined as the same “right” in the court information system. Nevertheless, two individuals traded the reconciliation of the bank statement each month. The Second Judicial District is working with the State Court Administrator’s Office Finance Division to separate these abilities into two individual rights. An independent employee who does not sign checks is now performing the bank reconciliations. Thus, duties are now adequately segregated.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager; Vicki Petry, Criminal Division Accountant

Estimated implementation date: Recommendation is already implemented

Finding 6: The Second Judicial District did not review key payroll reports.

Response:

The Second Judicial District agrees that some employees were not completing their own timesheets and that some back-ups were approving time sheets on behalf of the supervisor. Please note that most of the instances cited in the report where supervisors completed timesheets on behalf of the employee were due to the employee’s absence or the need to correct errors.

Employees have already been reminded to complete their own timesheets prior to an anticipated absence. An automated e-mail from the payroll department is delivered to each district employee on the last day of the pay period as a reminder to complete time entry. Supervisors have already been reminded that employees themselves must make any necessary corrections to time sheets and mark it as complete before the supervisor reviews and marks it as approved. In rare circumstances where an employee is suddenly unavailable, the supervisor may complete and approve the employee’s time sheet but will add justification in the system comments field. In addition, the supervisor will seek subsequent verification from the employee through e-mail exchanges or other documentation that time recorded was accurate. This documentation will be forwarded to the payroll department to be attached to the Self Service Time Entry Audit Report to demonstrate actions taken and compliance with policy.

Supervisors have already been reminded that they are primarily responsible for approving the times sheets of their designated departments. In rare situations when a supervisor is

absent or in travel status, a backup approver may have to be relied upon. Supervisors have been reminded to document the accuracy of a backup's approvals through e-mail exchanges or other documentation. The documentation will be forwarded to the payroll department to be attached to the Self Service Time Entry Audit Report to demonstrate actions taken and compliance with policy.

The payroll department will document its review of the Self Service Time Entry Audit Report by including comments, dispositions, date reviewed, and reviewer initials. Supporting documents such as e-mail exchanges between employee, supervisor, and backups will be reviewed for reasonableness and attached to the report to demonstrate actions taken and compliance with policy. A sample of exceptions will be reviewed each period followed by a comprehensive review each quarter. Troubling patterns or overuse of backup approvers will be highlighted and addressed with the appropriate employee or supervisor so that awareness levels are raised and effective solutions including additional training explored. The payroll office will work with employees and supervisors across the district so that the number of exceptions appearing on the report can be reduced to the bare minimum.

The Second Judicial District agrees that the self-service manager report was not being reviewed. The primary, backup, and department ID structure has now been reviewed to ensure employee/supervisor relationships are properly reflected in the system. The structure will be revisited at the beginning of each fiscal year. This will ensure that employees are assigned to primary approvers who have the most direct knowledge of the employee's work schedule. Please note that the retired employee mentioned in the report was still listed as a primary approver, but no employees were connected to the department.

The Second Judicial District agrees that the payroll register was not being regularly reviewed. The bulk of earning codes and hours are verified by the supervisor during the self service time entry process. However, the district recognizes that this process does not ensure accuracy of pay rates or supplemental earnings codes, adjustments, severance, and lump-sum payments entered directly by the payroll department. Effective immediately, the accounting manager or an employee independent of payroll entry will review the payroll register at the end of each period to ensure pay rates, and any supplemental earnings codes, adjustments, severance, and lump-sum payments are accurate. These reviews will be thoroughly documented and will include applicable comments or check marks, date reviewed, and reviewer initials.

The Second Judicial District agrees that reimbursement recalculations of the county payroll register and comparison of county funding reports to the budget for county-benefited employees was not adequately documented. The payroll department has already implemented this recommendation and has supplemented its reimbursement calculations and budget comparisons with applicable comments or check marks, date reviewed, and reviewer initials. In addition, supervisors of county-benefited employees have been reminded to review, validate, and sign timesheets prior to submitting to the county payroll system for processing.

The Second Judicial District agrees that annual reports identifying county employees with access to the private data of court employees has not been obtained. Effective immediately, the district has obtained a suitable report from the county and will review it annually to ensure the private data of court employees is not inappropriately available to county employees who have no business purpose. We will request that the county restrict access as appropriate.

In response to these findings, the State Court Administrator's Office Finance Division will be reviewing procedures, conducting reinforcement training, and working on controls to minimize these instances in the future.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager; Sharon Harper, Human Resources Manager; Dawn Torgerson, Chief Financial Officer

Estimated implementation date: Recommendation is already implemented

Finding 7: The Second Judicial District did not have adequate controls over some of its administrative expenditures.

Response:

The Second Judicial District agrees that it could not locate some of the supporting documentation for certain payments made. Departmental managers who order supplies and equipment have already been reminded to retain the packing slips or similar documentation and forward to the district accounting office to demonstrate that goods or services were received prior to payment. In addition, the district accounting office will ensure that all written offers, price quotes, approved sole source request forms, and other evidence of competitive bid are retained in a proper procurement and contract file.

The Second Judicial District agrees that certain supply and equipment purchases and contracts were authorized by officials who did not have authority at that threshold. The district accounting office will ensure that all future procurements and contracts are authorized at the appropriate threshold by the designated official.

The Second Judicial District agrees that for certain payments, the liability date was allowed to default to the system entry date. In many instances, the ordering department had not indicated the date goods or services were received on the packing slip or invoice. Please note that the district accounting office was careful to ensure that all transactions were recorded in the correct fiscal year so that the state's financial statements would be correct. In the future, the district accounting office will ensure the correct liability date is entered prior to processing the payment. Departmental managers who order supplies and equipment have already been reminded to indicate the date that goods and services were received on the packing slip or invoice before forwarding to the accounting division.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager

Estimated Implementation date: November 30, 2011

Finding 8: The Second Judicial District did not have adequate controls over gift cards it purchased as incentives for drug and mental health treatment.

Response:

The Second Judicial District agrees that it did not have a policy for use of incentive gift cards in court ordered programs. A branch wide policy of the State Court Administrator's Office Finance Division is forthcoming. Effective immediately, the district has developed a process to ensure that gift cards are accurately inventoried, secured, and tracked. Gift cards will only be purchased for use by individual participants in court ordered programs. Gift cards will no longer be used to pay for program expenses. In addition, gift cards will no longer be purchased through the state's warrant special handling process but via an invoice or expense reimbursement.

Gift cards are now entered into a log when purchased. This log includes the retail vendor, the date purchased, the serial number, and amount. Gift cards are secured in a safe until the day they are presented to a participant. Gift card inventories will only be allowed to accumulate to a reasonable estimate of what may be needed for a 30 day period. Upon distribution, an entry will be made of the specific participant who received the gift card. Cards will no longer be distributed to local clinics.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager; Dawn Torgerson, Chief Financial Officer

Estimated implementation date: April, 30, 2012, for development of a statewide policy and training

Finding 9: The Second Judicial District did not adequately control its capital assets and sensitive items.

Response:

The Second Judicial District agrees that the district's capital asset and sensitive item listings were not current. Effective immediately, capital asset and sensitive item listings will be made current with physical inventories taking place in each division every two years. Please note that the district's capital assets are typically limited to items such as network servers, network applications, and audio visual equipment for courtrooms. Sensitive items are typically limited to laptop computers.

The State Court Administrator's Office Finance Division plans to create reinforcement training for all capital asset coordinators. The training will not only reinforce the procedures, but will speak to the importance of this issue from an internal control perspective.

Persons responsible for resolving: Jeremy Olson, District Accounting Manager; Dawn Torgerson, Chief Financial Officer

Estimated Implementation date: April 30, 2012