

Minnesota Supreme Court

Financial Audit

For the Period July 1, 1995, through June 30, 1997

September 1998

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**Financial Audit Division
Office of the Legislative Auditor
State of Minnesota**

98-50



STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Deanna Wiener, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Kathleen Blatz, Chief Justice
Minnesota Supreme Court

We have audited selected areas of the Minnesota Supreme Court (including the Office of the State Court Administrator, the Lawyers Professional Responsibility Board, the Law Examiners Board, the Client Security Board, the Legal Certification Board, the Continuing Legal Education Board, and the State Law Library), the Minnesota Court of Appeals, and the trial courts for the period July 1, 1995, through June 30, 1997, as further explained in Chapter 1. Our audit scope included attorney registration fees, payroll, rent, purchased services, supplies, equipment, and grants. The following Summary highlights the audit objectives and conclusions. We discuss our audit objectives and conclusions more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as 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 require that we design the audit to provide reasonable assurance that Minnesota Supreme Court complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Minnesota Supreme Court is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of Minnesota Supreme Court. This restriction is not intended to limit the distribution of this report, which was released as a public document on September 11, 1998.

A handwritten signature in cursive script, reading "James R. Nobles".

James R. Nobles
Legislative Auditor

A handwritten signature in cursive script, reading "Claudia J. Gudvangen".

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: June 12, 1998

Report Signed On: September 4, 1998

SUMMARY

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Minnesota Supreme Court

Financial Audit

For the Period July 1, 1995, through June 30, 1997

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No. 98-50

Background Information

Article VI of the Minnesota Constitution established the judicial branch. This branch of state government interprets the laws and cases that come before it and must be certain that challenged laws do not violate the constitution. The state judicial branch has several levels of courts. Each court has specific jurisdictions that determine which types of cases it can hear. Our audit focused on three of the courts -- the Supreme Court, the Court of Appeals, and the District Courts. The Honorable Kathleen Blatz is the current Chief Justice of the Minnesota Supreme Court. The Honorable Edward Toussaint is the current Chief Judge of the Court of Appeals. In addition, each of the ten Judicial Districts is served by a chief judge elected by the judges of that district.

Audit Objectives and Conclusions

The objectives of our audit were to gain an understanding of the internal control structure over the accounting and reporting of the Minnesota Supreme Court's financial activities and to determine if the courts complied with material finance-related legal provisions. We reviewed certain operations conducted by the various boards under the Supreme Court. We reviewed the revenues collected by the Lawyers Professional Responsibility Board. The expenditure areas reviewed included payroll, rent, purchased services, supplies, equipment, and grants.

We concluded that the Minnesota Supreme Court designed and implemented internal controls to provide reasonable assurance that transactions were properly authorized and accurately reported in the state's accounting system. However, we did note some separation of duty weaknesses in the payroll area. We also found that the Minnesota Supreme Court generally complied with applicable statutory provisions. However, the Supreme Court advanced rather than reimbursed funds to the Second Judicial District for certain expenditures in violation of Minnesota statute.

The Minnesota Supreme Court agreed with our two findings and have begun to work towards implementing the recommendations.

Minnesota Supreme Court

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Thomas Donahue, CPA	Audit Manager
David Poliseno, CPA, CISA	Auditor-In-Charge
Fubara Dapper, CPA	Auditor
Brad Falteysek	Auditor

Exit Conference

We discussed the findings and recommendations with the following representatives of Minnesota Supreme Court at the exit conference held on August 20, 1998:

Judith Rehak	Director, Court Personnel and Budget Office
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Minnesota Supreme Court

Chapter 1. Introduction

Article VI of the Minnesota Constitution established the judicial branch. This branch of state government interprets the laws and cases that come before it and must be certain that challenged laws do not violate the constitution. The state judicial branch has several levels of courts. Each court has specific jurisdictions that determine which types of cases it can hear. Our audit focused on three of the courts -- the Supreme Court, the Court of Appeals, and the District Courts.

Supreme Court

The Supreme Court is the highest court in the state. The Supreme Court's main function is to hear appeals, along with administering the court system and regulating the practice of law. The Court hears appeals of cases from the Court of Appeals and other agencies, including the Minnesota Workers' Compensation Court of Appeals and the Minnesota Tax Court. It also has jurisdiction over defendants convicted of first-degree murder, and discretionary review of decisions of the Court of Appeals. The Court also has jurisdiction over legislative contests and may issue writs of mandamus, prohibition, and habeas corpus.

There are no witnesses, no juries, no evidence, and no trials in the handling of a case before the Supreme Court. Instead of one judge, there are seven justices. The Supreme Court issues all of its decisions in writing. One justice writes the opinion of the court, explaining the legal bases, and the other justices review it and make revisions. The opinions are then released and printed immediately in a legal newspaper and later bound in books for law libraries.

The Governor appointed the Honorable Kathleen Blatz Chief Justice on January 29, 1998. The Honorable A.M. Keith served as Chief Justice throughout the audit period and retired on January 29, 1998. Voters elect the justices to six-year terms on a non-partisan ballot. The Governor fills any vacancies during a term on the court.

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 in the areas of budget, facilities management, legislation, caseload management, personnel, continuing education, operations research, records management, information systems, planning and research. Each judicial district has a district administrator working in conjunction with the Office of the State Court Administrator. The Supreme Court also oversees various boards and other organizations related to the judicial process. Following is a summary of these organizations' responsibilities and funding sources:

Minnesota Supreme Court

Board of Law Examiners

<u>Composition</u>	The Supreme Court appoints two public members and seven attorneys to the board to serve for a term of three years.
<u>Funding</u>	Bar application fees.
<u>Responsibilities</u>	To administer the Bar exam and to conduct background investigations of all applicants for admission to the practice of law.

Board of Continuing Legal Education

<u>Composition</u>	The Supreme Court appoints the 13-member board, of which the Minnesota Bar Association nominates 6 members. The chairperson serves at the pleasure of the Court. One member of the board is a District Judge. Three members, excluding the chairperson, are not required to be members of the Bar. With the exception of the District Judge, the remaining members are required to be members of the Bar. No member may serve more than two three-year terms.
<u>Funding</u>	Licensing fees paid by Minnesota licensed lawyers and legal corporations.
<u>Responsibilities</u>	To accredit programs for continuing legal education, keep records of attorney hours for continuing education, and to assure that attorneys comply with continuing legal education requirements.

Board of Legal Certification

<u>Composition</u>	The Supreme Court appoints twelve members consisting of nine lawyers licensed in this state and three public members. No member may serve more than two three-year terms.
<u>Funding</u>	Registration fees paid by certified agencies.
<u>Responsibilities</u>	To approve and regulate agencies that certify lawyers as specialists practicing in this state. It also adopts standards required by the certifying agency.

Lawyers Professional Responsibilities Board

<u>Composition</u>	The Supreme Court appoints fourteen lawyers and nine nonlawyers to the board. The Minnesota State Bar Association may nominate six lawyers to the Court. No member may serve more than two three-year terms.
<u>Funding</u>	Licensing fees paid by Minnesota licensed lawyers and legal corporations.
<u>Responsibilities</u>	To review and investigate complaints of unprofessional conduct against Minnesota lawyers.

Minnesota Supreme Court

Law Library

- Composition No Board. The Law Library Committee of the Supreme Court is the governing body for the library. The committee recommends the appointment for the state law librarian, who administers daily operations. The law librarian supervises a professional staff of ten full-time and four part-time employees.
- Funding Supreme Court appropriations.
- Responsibilities The library provides research and information services to users of legal data through both traditional and electronic sources.

Client Security Board

- Composition The Supreme Court appoints seven members to the board. Members include five lawyers, of whom the Bar Association nominates three, and two public members. No member may serve more than two three-year terms.
- Funding Licensing fees paid by Minnesota lawyers.
- Responsibilities The board reviews claims by clients who believe their lawyers defrauded them and compensates victims accordingly. The board can sue on behalf of the client security fund to recover payments made, whenever possible.

In addition, a Supreme Court order created the Lawyer Trust Account Board on July 1, 1983, to administer the Minnesota Interest on Lawyer Trust Account Program (IOLTA). The court appoints the nine-member board consisting of six lawyers and three public members. The Minnesota Code of Professional Responsibility requires Minnesota attorneys to place certain client funds in pooled interest-bearing trust accounts. Interest earned on these accounts, net of any transaction costs, is remitted directly to the board by the financial institutions. The board grants funds to nonprofit organizations to provide legal services for the poor, law-related education programs, and other programs.

We did not audit the Lawyer Trust Account Board. An independent accounting firm audited the board for the two-year period through June 30, 1997. For the two fiscal years ended June 30, 1997, the board received approximately \$1.6 million. The board granted out approximately \$1 million during this same period.

Minnesota Court of Appeals

The Court of Appeals has jurisdiction over all appeals from trial courts, except conciliation court and individuals convicted of first-degree murder. The Court of Appeals also hears appeals from the Commissioner of Economic Security and various administrative agencies. A rotating panel of three judges hears all appeals. Litigants bring cases to the Court of Appeals from lower court rulings. Cases never originate at this level. There must be a legal basis for an appeal, such as judicial error, failure to follow proper procedure, or that the law violates the constitution. Voters elect judges of the court statewide to six-year terms. Eight of the sixteen judges must be a resident of each of the eight congressional districts. The other judges serve at-large. The Honorable Edward Toussaint is the current Chief Judge.

Minnesota Supreme Court

Minnesota District Courts

The District Courts in Minnesota are the trial courts of general jurisdiction. Minnesota has ten separate judicial districts. Each district may consist of one to seventeen counties. The District Courts hear all civil, criminal, family, juvenile, traffic, and ordinance violation matters. Voters elect judges in their respective districts for six-year terms. The Governor appoints judges to vacant seats. 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 the administrative responsibility for coordinating the business of their district court. Each district also has a district administrator who handles managerial functions, such as developing budgets, handling personnel matters, and overseeing the processing of cases, and planning and implementing judicial policies.

In 1990, the Legislature mandated a state funded pilot project for court operations in the Eighth Judicial District located in west central Minnesota. The Legislature established the project to resolve the administrative issues arising out of state funding of the courts at this level. Each of the 13 county court administrators oversees the operations of the district court within that county. The Legislature also set December 31, 1999, as the date the pilot project would sunset.

Funding for the courts is primarily through General Fund appropriations. Each court receives its own appropriation. For fiscal year 1997, the legislature appropriated \$19,434,000 to the Supreme Court. The legislature also appropriated \$5,832,000 and \$67,020,000 to the Court of Appeals and the District Courts respectively. The following Table 1-1 provides a summary of the Supreme Court's financial activity for the fiscal year ended June 30, 1997.

Table 1-1
Minnesota Court System
Summary of Revenues and Expenditures
For the Fiscal Year Ended June 30, 1997

	District Courts	Court of Appeals	Supreme Court	Total
Revenues:				
Attorney Registration Fees	\$ 0	\$ 0	\$ 1,822,649	\$ 1,822,649
Other Revenues (Note 1)	946,409	0	2,742,615	3,689,024
Total Revenues	<u>\$ 946,409</u>	<u>\$ 0</u>	<u>\$ 4,565,264</u>	<u>\$ 5,511,673</u>
Expenditures:				
Payroll	\$56,317,029	\$4,584,334	\$ 9,184,747	\$70,086,110
Purchased Services	6,568,747	53,198	1,828,120	8,450,065
Grants	0	0	6,471,332	6,471,332
Equipment	2,617,485	21,313	2,079,663	4,718,461
Rent	159,416	1,018,751	2,818,140	3,996,307
Other Expenditures	1,616,094	104,903	1,153,141	2,874,138
Materials and Supplies	1,132,080	77,881	844,769	2,054,730
Total Expenditures	<u>\$68,410,851</u>	<u>\$5,860,380</u>	<u>\$24,379,912</u>	<u>\$98,651,143</u>

Note 1: The other revenues under District Courts reflect only the amount collected in the Eighth Judicial District. The other nine Judicial Districts deposit their receipts directly with the State Treasurer.

Source: Minnesota Accounting and Procurement System (MAPS) through close of fiscal year 1997.

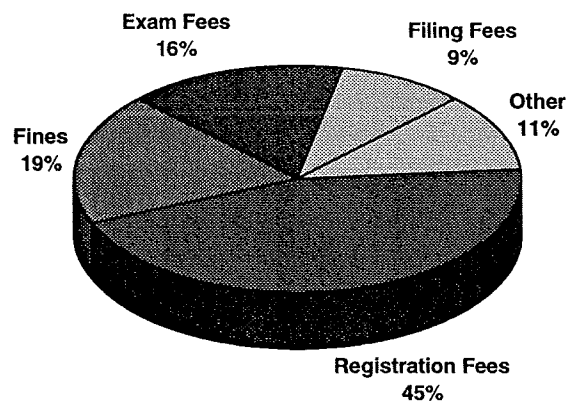
Chapter 2. Revenue

Chapter Conclusions

The Supreme Court designed and implemented internal controls to provide reasonable assurance that attorney registration fees were adequately safeguarded and accurately reported in the accounting records. For the items tested, the Supreme Court complied with applicable legal provisions and management's authorization.

The Supreme Court collects revenue for administering the Minnesota Bar exam through the Board of Law Examiners. It also collects revenue for attorney and legal corporation licenses and registrations through the Lawyers Professional Responsibility Board. These receipts are deposited to the state treasury as dedicated revenue and are available to fund court designated activities. In addition, the Eighth Judicial District collects revenue through filing fees and court assessed fines and deposits these receipts into the state treasury as non-dedicated revenue. Figure 2-1 shows the breakdown of revenue collections for the two years ended June 30, 1997.

Figure 2-1
Minnesota Court System
Summary of Revenue Collections
For the Two Years Ended June 30, 1997



Source: Minnesota Accounting and Procurement System (MAPS) Reports.

Minnesota Supreme Court

Audit Objective and Methodology

Our review of the Supreme Court's revenue focused on attorney registration fees and addressed the following question:

- Did the Supreme Court design and implement internal controls to provide reasonable assurance that attorney registration fees were adequately safeguarded, accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization?

To answer this question, we interviewed Minnesota Supreme Court employees to gain an understanding of controls over the revenue process. We tested selected attorney registration fees and supporting documentation to determine that the appropriate receipts were collected, deposited, and accurately posted to the accounting records.

Conclusion

The Supreme Court designed and implemented internal controls to provide reasonable assurance that attorney registration fees were adequately safeguarded and accurately reported in the accounting records. For the items tested, the Supreme Court complied with applicable legal provisions and management's authorization.

Chapter 3. Payroll

Chapter Conclusions

The Supreme Court designed and implemented internal controls to provide reasonable assurance that payroll expenditures were properly authorized, processed, and accurately reported in the accounting records. In addition, for the items tested, the Supreme Court processed payroll and personnel transactions in accordance with its Judicial Personnel Plan and applicable state policies and procedures. However, the Supreme Court did not adequately segregate certain payroll duties.

The Supreme Court's payroll costs reflect both payments to state employees and reimbursements to various counties for county payroll charges. For state employees, the Supreme Court processes payroll data through the state's personnel/payroll system. The Court began using the state's new system, the State Employee Management (SEMA4) system, in December 1995. Except for the Eighth Judicial, the districts send payroll information, including timesheets, to the Supreme Court for input into SEMA4. The Eighth District enters its own payroll information into SEMA4. However, the Supreme Court staff enters all personnel information into SEMA4.

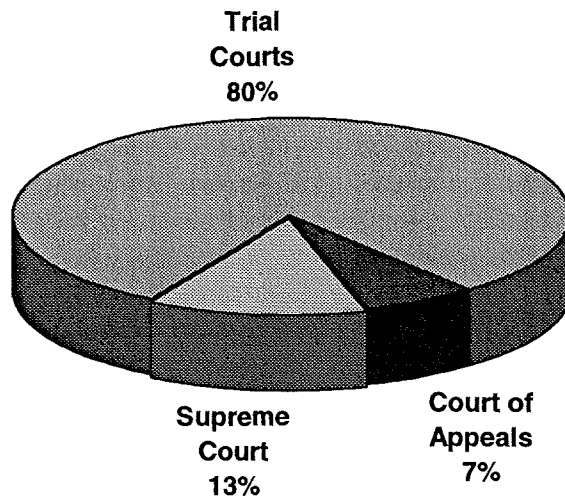
The Court also employs individuals in the various counties that have been elected under the judicial branch plan to maintain their status as county employees for purposes of county benefits. Minn. Stat. Section 480.181 allowed county court employees the option of becoming state employees and receiving state benefits or remaining county employees with county benefits. Each month, the District Court offices collect the payroll information from their respective counties and submit a report to the Supreme Court. The Supreme Court reimburses the counties for their payroll expenditures. For fiscal years 1996 and 1997, the reimbursement totaled about \$15,600,000.

The Judicial Branch adopted a Judicial Branch Personnel Plan that is followed by the courts. This plan is very similar to other bargaining agreements representing state employees. For example, instead of merit increases permitted under traditional bargaining agreements, the Judicial Plan offers stability payments. Employees who have worked at least five years and have reached the top of their salary range may receive a stability payment instead of a merit increase.

The court's payroll expenditures totaled about \$140,000,000 during the two fiscal years ended June 30, 1997. Figure 3-1 shows the percentage of payroll expenditures by each court.

Minnesota Supreme Court

Figure 3-1
Minnesota Court System
Summary of Payroll Expenditures
For the Two Years Ended June 30, 1997



Source: Minnesota Accounting and Procurement System (MAPS) as of the close for fiscal 1996 and 1997.

Audit Objectives and Methodology

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

- Did the Supreme Court design and implement internal controls to provide reasonable assurance that payroll expenditures were properly authorized, processed, and accurately reported in the accounting records?
- Did the Supreme Court process payroll and personnel transactions in accordance with the Judicial Personnel Plan and applicable state policies and procedures?

To answer these questions, we interviewed the Supreme Court's 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 samples of payroll expenditures to determine if the Supreme Court properly authorized, processed, and recorded the expenditures in the accounting records. We also tested the samples of payroll expenditures to determine if the Supreme Court complied with the Judicial Personnel Plan and other applicable legal provisions.

Conclusions

The Supreme Court designed and implemented internal controls to provide reasonable assurance that payroll expenditures were properly authorized, processed, and accurately reported in the accounting records. In addition, for the items tested, the Supreme Court processed payroll and personnel transactions in accordance with its Judicial Personnel Plan and applicable state policies and procedures. However, as discussed in Finding 1, the Supreme Court did not adequately segregate certain payroll duties.

Minnesota Supreme Court

1. Prior Finding Not Resolved: The Supreme Court did not adequately segregate certain payroll functions.

The Supreme Court did not adequately segregate the entering of the payroll transactions from verifying the payroll transactions. Except for the Eighth Judicial District, which directly entered its payroll information into SEMA4, the districts submitted employee timesheets to the Supreme Court. One Supreme Court employee entered the payroll transactions into SEMA4 and subsequently verified the entries made. The same employee also entered the stability payments into SEMA4 and verified them. The lack of segregation of duties increases the risk that errors or irregularities could occur and not be detected by the Court.

Recommendation

- *The Supreme Court should segregate the payroll-input function from the verification function.*

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Chapter 4. Other Expenditures

Chapter Conclusion

The Supreme Court designed and implemented internal controls to provide reasonable assurance that expenditures were properly authorized and accurately reported in the accounting records. In addition, for the items tested, the Supreme Court complied with applicable legal provisions and management's authorization. However, the Supreme Court inappropriately advanced funds to one judicial district for certain expenditures in violation of Minnesota statute.

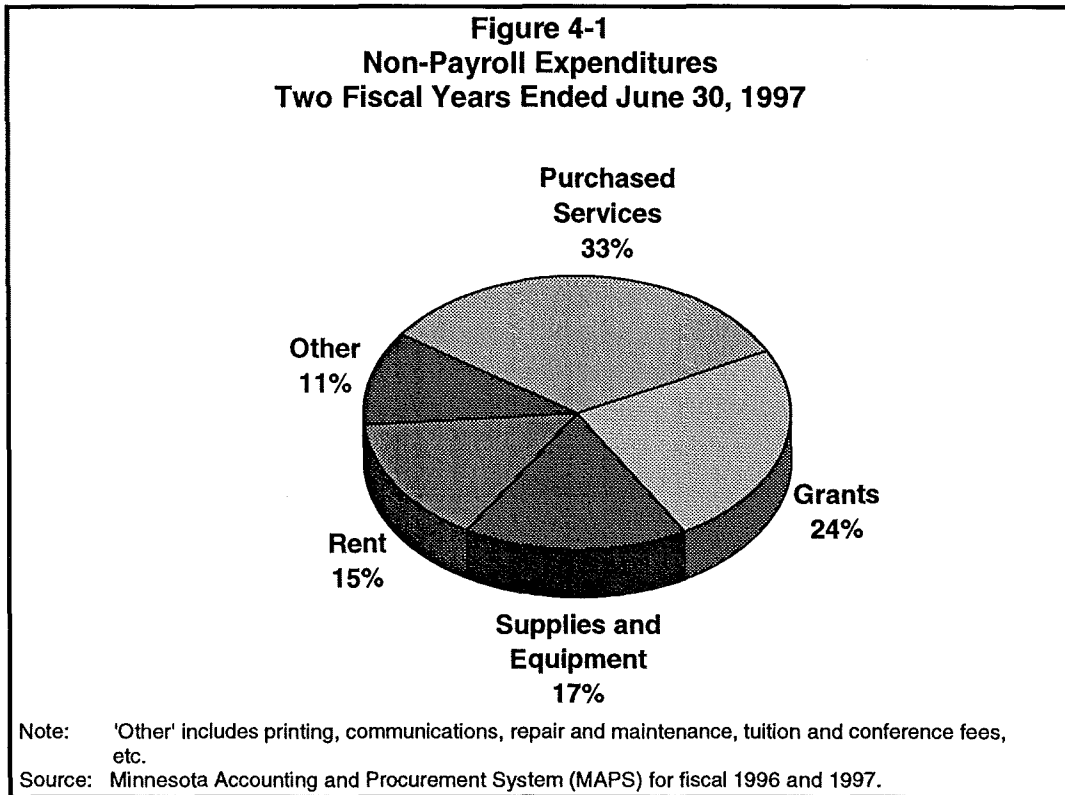
The Court's non-payroll expenditures included grant disbursements, rent, purchased services, supplies, equipment, and other expenditures. Each of the judicial boards is responsible for its purchasing decisions. The district courts and Court of Appeals also make purchasing decisions and enter into contracts for goods or services. The administrative service section of the Supreme Court receives the payment documentation from the boards and the courts for review and approval and enters the payment transaction into MAPS.

Purchased services expenditures included reimbursements to the judicial districts for jury related expenses such as jury fees, lodging, meals, and childcare. The counties pay the jury costs directly and submit monthly billing statements to the district offices. The district offices review the statements and forward them to the Supreme Court for payment. The Supreme Court reimburses the counties on a monthly basis.

The Supreme Court grants 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 selects six organizations throughout the state to administer the assistance to qualified individuals. The Supreme Court also grants out money under its community dispute resolution program. The program operates to bring disputed parties together voluntarily and resolves their differences through mediation or arbitration.

Figure 4-1 shows expenditure categories for the two fiscal years ended June 30, 1997, and the percentages of each category to total expenditures.

Minnesota Supreme Court



Audit Objectives and Methodology

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

- Did the Supreme Court design internal controls to provide reasonable assurance that expenditures were properly authorized and accurately reported in the accounting records?
- Did the Supreme Court comply with applicable legal provisions and management's authorization?

To answer these questions, we interviewed the Supreme Court's employees to gain an understanding of the procurement and disbursement process. We performed analytical procedures to detect unusual trends or irregularities. We tested samples of expenditures to determine if the Supreme Court properly authorized, processed, and recorded the expenditures in the accounting records. We also tested the samples of expenditures to determine if the Supreme Court complied with the applicable legal provisions.

Minnesota Supreme Court

Conclusions

The Supreme Court designed and implemented internal controls to provide reasonable assurance that expenditures were properly authorized and accurately reported in the accounting records. In addition, for the items tested, the Supreme Court complied with applicable legal provisions and management's authorizations. However, as discussed in Finding 2, the Supreme Court inappropriately advanced funds to the Second Judicial District for certain expenditures.

2. Prior Finding Not Resolved: The Supreme Court inappropriately advanced funds to the Second Judicial District for certain expenditures.

The Supreme Court advanced, rather than reimbursed, the Second Judicial District for compensation and travel costs of jurors. Each month the Second Judicial District requested advances from the Supreme Court for anticipated juror costs. The Supreme Court processed the advance based on the receipt of the request. However, Minn. Stat. Section 593.48, states that, "...except for the eighth judicial district where the state shall pay directly, payments shall be paid out of the county treasury upon receipt of authorization to pay from the jury commissioner. The jury cost shall be reimbursed monthly by the Supreme Court upon submission of an invoice by the county treasurer." The Supreme Court also advanced the Second Judicial District payroll costs for employees electing to receive county benefits. This practice results in inequities to the other districts.

Recommendation

- *The Supreme Court should reimburse, rather than advance, the districts for jury costs as required by Minnesota statute.*

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Minnesota Supreme Court

Status of Prior Audit Issues As of June 12, 1998

Most Recent Audits

Legislative Audit Report 94-41, issued in September 1994 covered the two fiscal years ended June 30, 1993. The report contained eight findings. The first three findings pertained to receipt collection operations in the Eighth District. We did not audit the Eighth District's receipt collection process this year and, therefore, we did not determine the status of these findings. Finding 4 addressed the lack of monitoring payroll reimbursements made to the counties. The Supreme Court resolved this finding. Finding 5 addressed control weaknesses over stability payments. The Court did not resolve this finding and the audit report addresses this issue in Finding 1. Finding 6 dealt with timesheets not signed by both the employees and supervisors. The Court resolved this finding. Finding 7 disclosed several Court employees exceeding their accumulative vacation leave balances. The Court resolved this finding. Finding 8 disclosed that the Court advanced, rather than reimbursed one judicial district for certain expenditures. The Court did not resolve this finding and the current audit report addresses this issue in Finding 2.

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THE SUPREME COURT OF MINNESOTA
MINNESOTA JUDICIAL CENTER
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CHAMBERS OF
KATHLEEN A. BLATZ
CHIEF JUSTICE

(612) 296-3380

September 2, 1998

Mr. James Nobles
Legislative Auditor
First Floor South, Centennial Building
658 Cedar Street
Saint Paul, Minnesota 55155

Dear Mr. Nobles:

Following completion of the most recent audit of the Judicial Branch for Fiscal Years 1994-1997 by members of your staff, two recommendations were made for improving internal controls.

1. The Supreme Court should separate the payroll input function from the verification function.

While we have segregated aspects of the payroll and verification function, that separation has not been completed. We agree that further segregation is desirable. We have received funding from the 1998 Legislature for one additional fiscal staff and are in the process of hiring. This new position will allow the court to implement this recommendation.

2. The Supreme Court should reimburse, rather than advance, the districts for jury costs as required by Minnesota Statutes.

Funding is advanced to only one of our ten districts (Second Judicial District, Ramsey County) upon its representation that it would not finance these costs in the first instance. Court representatives will discuss with Ramsey County representatives the concerns raised about non-compliance with statutory provisions and will work to facilitate a change by the county in the current reimbursement process.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Kathleen A. Blatz".

Kathleen Blatz
Chief Justice