



**OFFICE OF THE LEGISLATIVE AUDITOR**  
STATE OF MINNESOTA

**FINANCIAL AUDIT DIVISION REPORT**

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# **Minnesota Judicial Branch Fifth Judicial District**

## **Internal Controls and Compliance Audit**

**July 1, 2011, through May 31, 2013**

**October 31, 2013**

**Report 13-26**

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## OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

October 31, 2013

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Fifth Judicial District

Mr. Jeff Shorba, State Court Administrator  
Minnesota Judicial Branch

Mr. Richard Fasnacht, District Administrator  
Fifth Judicial District

This report presents the results of our internal controls and compliance audit of the Minnesota Judicial Branch – Fifth Judicial District for the period from July 1, 2011, through May 31, 2013. The objectives of this audit were to determine if the district had adequate internal controls, as of May 2013, to ensure that the district safeguarded its financial resources, accurately paid employees and vendors in accordance with management’s authorizations, complied with finance-related legal requirements, and created reliable financial information.

We discussed the results of the audit with the Fifth Judicial District’s staff at an exit conference on October 16, 2013. This audit was conducted by Michael Hassing, CPA, CISA (Audit Manager), Zach Yzermans, CPA (Auditor-in-Charge), and auditors Pat Ryan, Heather Varez, CPA, and Lori Leysen.

We received the full cooperation of the staff from the Fifth Judicial District and the State Court Administrator’s Office while performing this audit.

Handwritten signature of James R. Nobles in black ink.

James R. Nobles  
Legislative Auditor

Handwritten signature of Cecile M. Ferkul in black ink.

Cecile M. Ferkul, CPA, CISA  
Deputy Legislative Auditor



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# Report Summary

## Conclusion

The Fifth Judicial District (district) generally had adequate internal controls to ensure that it safeguarded its financial resources, accurately paid employees and vendors in accordance with management's authorizations, complied with finance-related legal requirements, and produced reliable financial information. For the items we tested, the district generally complied with finance-related legal requirements over its receipts, payroll, and other administrative expenditures. However, the district had some internal control weaknesses and instances of noncompliance.

## Findings

- The Fifth Judicial District did not always have accurate account balances in the court information system for money held on behalf of others by court order. ([Finding 1, page 7](#))
- The Fifth Judicial District had not complied with some documentation requirements related to certain high-risk manual receipt transactions. ([Finding 2, page 8](#))
- The Fifth Judicial District did not have required documentation to support its month-end revenue verifications. ([Finding 3, page 9](#))
- The Fifth Judicial District had not complied with some contract and purchasing policies. ([Finding 4, page 10](#))

## Audit Objectives and Scope

### Objectives

- Internal controls
- Compliance

### Period Audited

July 1, 2011, through May 31, 2013

### Audited Areas

- Receipts of fines, fees, and surcharges
  - Payroll expenditures
  - Selected administrative expenditures
  - System security access
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# Minnesota Judicial Branch

## Fifth Judicial District Overview

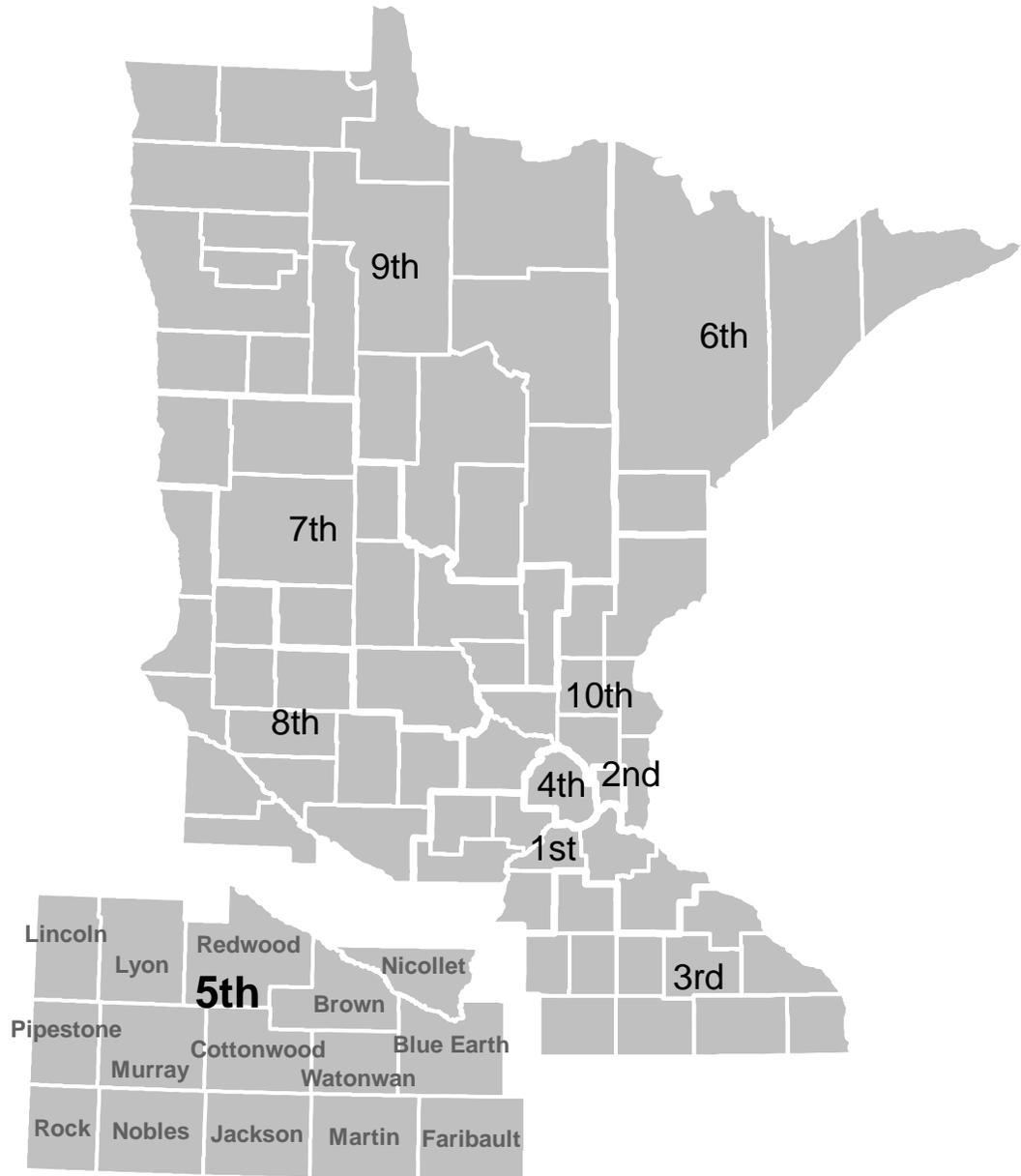
Minnesota's Judicial Branch includes the Supreme Court, Court of Appeals, and district courts. All civil and criminal cases involving Minnesota law originate within the district courts, which consist of approximately 289 judges who preside over trials and hearings throughout the state. While the district courts are part of the state court system, they generally operate from county courthouses and are organized by county boundaries into ten judicial districts.

Our audit focused on selected financial activities related to the Fifth Judicial District. As of August 2013, the Fifth Judicial District had 16 judges and served approximately 283,000 citizens in the southwestern Minnesota counties of Blue Earth, Brown, Cottonwood, Faribault, Jackson, Lincoln, Lyon, Martin, Murray, Nicollet, Nobles, Pipestone, Redwood, Rock, and Watonwan, as shown in Figure 1 on the following page. The district's administrative office, located in Mankato, processed payroll transactions and other administrative expenditures. The Fifth Judicial District had court administrative offices in each of the 15 counties that make up the district. Those offices collected and processed court fees, fines, and surcharges.

The court administrative offices at the counties use the Minnesota court information system to record case management and related financial activity. One of the system's many components is financial management. District court employees enter all aspects of a case into the court information system, including the related fines and fees. Case information includes the details of the violation or court order, originating jurisdiction, and court dates. Financial data from the court information system interfaces daily with the state's accounting system.

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**Figure 1**  
**Fifth Judicial District**  
**Boundaries and Counties**



Source: Minnesota Office of the Legislative Auditor.

Table 1 summarizes the Fifth Judicial District's receipts and expenditures for the period July 1, 2011, through June 30, 2013.

**Table 1**  
**Fifth Judicial District**  
**Receipts and Expenditures**  
**July 1, 2011, through June 30, 2013<sup>1</sup>**

	Fiscal Years	
	2012	2013
<u>Receipts:</u>		
Fees and Fines	\$10,438,121	\$10,218,712
<u>Expenditures:</u>		
Payroll	\$ 8,769,202	\$ 8,681,460
Administrative Expenditures:		
Professional/Technical Contracts	517,241	794,785
Purchased Services	280,647	349,820
Supplies	138,809	219,332
Other Expenditures <sup>2</sup>	274,969	352,620
Total Expenditures	<u>\$9,980,868</u>	<u>\$10,398,017</u>

<sup>1</sup> Our audit scope included fiscal year 2013 activity through May 31, 2013.

<sup>2</sup> Other expenditures include travel, employee development, space rental and utilities, printing and advertising, computer and system services, communication, claims, equipment, repairs and maintenance, and state agency services.

Source: The state's accounting system.

## Objectives, Scope, and Methodology

Our audit of the Fifth Judicial District included material financial activities (receipts, payroll, and selected administrative expenditures) and system security access for the period July 1, 2011, through May 31, 2013. The audit objectives were to answer the following questions:

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

To meet the audit objectives, 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 to the district administrative office, we also

conducted audit work at court administrative offices in six counties.<sup>1</sup> 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.<sup>2</sup>

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.<sup>3</sup> We used state and federal laws, regulations, and contracts, as well as policies and procedures established by the judicial branch as evaluation criteria over compliance.<sup>4</sup>

## Conclusion

The Fifth Judicial District generally had adequate internal controls to ensure that it safeguarded its financial resources, accurately paid employees and vendors in accordance with management's authorizations, complied with finance-related legal requirements, and produced reliable financial information. For the items we tested, the district generally complied with finance-related legal requirements over its receipts, payroll, and other administrative expenditures. However, the district had some internal control weaknesses and instances of noncompliance.

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

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<sup>1</sup> We conducted detailed audit work at court administrative offices in the following counties: Blue Earth, Brown, Faribault, Lincoln, Nicollet, and Nobles.

<sup>2</sup> We also considered our prior audit reports from other District Courts as part of our understanding (See Office of the Legislative Auditor's Financial Audit Division, Report 09-34, *Minnesota Judicial Branch – First Judicial District*, issued October 23, 2009, and Report 11-23, *Minnesota Judicial Branch – Second Judicial District*, issued October 20, 2011).

<sup>3</sup> 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.

<sup>4</sup> 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.

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## Findings and Recommendations

**The Fifth Judicial District did not always have accurate account balances in the court information system for money held on behalf of others by court order.**

### Finding 1

In two of the six court administrative offices we tested, the court information system's record of money held in local bank accounts on behalf of minor or incompetent persons by court order did not always agree with the offices' documentation related to those accounts. Court staff had not consistently updated the accounts in the court information system to reflect documented authorizations allowing for release of some of the money. The state court administrator's office told us that they expected court administrative offices in the counties to maintain accounts on the court information system consistent with their records of court orders, investments, and authorized releases of money in these accounts. In addition, the court information system's Month-end Participation Guide provided instructions on how to produce a report to review this financial activity.<sup>5</sup>

The two court administrative offices had the following discrepancies between the account balances on the court information system and the offices' other documentation:

- The court information system for four of the five accounts we tested in one court administrative office had balances that totaled \$310,829; however, the office's documentation (including the initial court orders, new investments held, and authorized releases of money) supported balances totaling \$41,873, a difference of nearly \$270,000.
- The court information system for one of the five accounts we tested in the other court administrative office had a balance of \$165,689; however, the office's documentation included a note that, as of October 2009, all of the money had been released. Court staff were unable to fully reconcile the amount recorded in the court information system with its file documentation or provide a complete record of formal court orders authorizing the release of all the money recorded on the court information system.<sup>6</sup>

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<sup>5</sup> Detailed instructions about how to record trust account financial transactions were included in the court information system's Trust Accounts Training Manual (Pilot) dated May 8, 2009. The State Court Administrator's Office distributed this manual to certain district court administrative offices as part of a pilot project but, by October 2013, it had not established it as official Judicial Branch guidance.

<sup>6</sup> In this case, the conservator had filed annual reports and account summaries with the court administrative office, as required by *Minnesota Statutes* 2012, 524-5.420, which supported the full release of money from the court to the conservator in 2009. The state court administrative office also has other processes, such as a conservator audit function, to monitor the actions of conservators to review how money under conservator control is used.

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Without accurate accounting records, the district cannot effectively use the court information system as part of its process to monitor these accounts.

*Recommendation*

- *The Fifth Judicial District should ensure that the court information system is an accurate record of the money held in local bank accounts on behalf of others per court order.*

## **Finding 2**

**The Fifth Judicial District had not complied with some documentation requirements related to certain high-risk manual receipt transactions.**

The district did not consistently record complete or accurate information for receipts they manually processed when the court information system was unavailable. In addition, four of the six court administrative offices we tested failed to review manually processed receipts to ensure the court clerks subsequently posted these receipts correctly in the court information system. Court clerks provided customers with hand-written receipts for payments when they could not generate an electronic receipt, either because the related citation was not yet in the court information system or the court had closed its cash registers at the end of the day for balancing.

Judicial branch policy requires that the court administrative offices include specific information on the manually processed receipt documents to ensure the accuracy of these transactions.<sup>7</sup> The 60 manual receipt transactions we tested at the six court administrative offices had numerous incidences where the documentation of manual receipt transactions did not comply with the policy because of missing and/or inaccurate information. The documentation supporting the 60 manual receipt transactions we tested had the following deficiencies:

- For 2 transactions, the manual receipt did not state the amount received and, therefore, did not agree to the amount recorded in the court information system.
- For 5 transactions, the transaction number on the manual receipt did not tie to the correct transaction in the court information system.
- For 21 transactions, the manual receipt number was not recorded in the court information system.
- For 22 transactions, the manual receipt did not include a case number, or the case number recorded did not tie to the correct case in the court information system.

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<sup>7</sup> Minnesota Judicial Branch Policy 209(e), Manual Receipts.

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- For 13 transactions, the manual receipt did not explain why the receipt was processed manually, rather than electronically through the court information system.
- For 32 transactions, the manual receipt document lacked evidence of a daily review required by the court's manual receipt policy to ensure the amount of the manual receipt is included in the total system receipts for the day.

The use of manual receipts heightens the risk that the district may not have properly recorded cash collections in the court information system or deposited all the cash collected. Additionally, failure to complete the daily reviews of manual receipts could allow erroneous or inappropriate entries to go undetected.

#### *Recommendations*

- *The Fifth Judicial District should ensure that all required information is included on manual receipts and accurately entered into the court information system. The district should also ensure that it documents reviews of manual receipts according to judicial policy.*
- *The Fifth Judicial District should ensure that staff at all of the court administrative offices are sufficiently trained on the judicial policy requirements for processing, documenting, and reviewing manual receipts.*

### **The Fifth Judicial District did not have required documentation to support its month-end revenue verifications.**

### **Finding 3**

The district did not consistently retain month-end revenue reports for the completion of its month-end review process to ensure that receipts were appropriately and accurately deposited and recorded, as required by judicial branch policy.<sup>8</sup> We selected a sample of five months and examined the documentation supporting the month-end reviews for those months at the six court administrative offices we visited. The following reports were missing:

- For seven of the month-end reviews we tested, the district had not retained the bank reconciliation report. The bank reconciliation report documents the court administrative offices' comparisons between its recorded receipt transactions and the deposits recorded on the monthly bank statements to confirm the accuracy of the recorded transactions.

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<sup>8</sup> Minnesota Judicial Branch Policy 209(a), Section I and Section V, Part I, #21.

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- For eleven of the month-end reviews we tested, the district had not retained the account balances report. As part of the month-end review process, the court administrative offices must clear or transfer their account balances from the court information system to the state treasury. The court administrative offices generate the account balances report from the court information system to verify that all court accounts have been transferred to the state treasury and have a zero balance. Accounts with remaining balances may indicate that the disbursement to the state treasury was not correctly generated or a refund was not issued.

Reviews of these reports as part of the month-end review process are fundamental internal controls to ensure the accuracy of the accounting records and to detect errors or unauthorized transactions.

*Recommendation*

- *The Fifth Judicial District should retain all reports required by judicial branch policy to support that the district accurately and timely completed the month-end review process.*

## **Finding 4**

**The Fifth Judicial District had not complied with some contract and purchasing policies.**

The district did not always comply with judicial branch policies for establishing and administering contracts, including obtaining required bids. The district's administrative office is responsible for all contracting activity for the district. The district had the following exceptions:

- For all five contracts we tested that were greater than \$50,000, the district did not prepare risk assessments prior to the final execution of the contracts. Judicial branch policy requires that a formal risk assessment be completed on all contracts in excess of \$50,000 before the contract is signed.<sup>9</sup> The risk assessment is used to identify and minimize financial exposure and avoid unnecessary liability to the courts.
- For three of fifteen contracts tested, the district allowed the contractor to begin providing services before the contract was executed. In addition, for five of the fifteen contracts, the district had not encumbered funds in the accounting system before the contractor started performing services. Judicial branch policy requires that contracts are signed by all parties, and funds are encumbered before contractors begin to provide billable services.<sup>10</sup>

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<sup>9</sup> Minnesota Judicial Branch Policy 203(a), Attachment 5.

<sup>10</sup> Minnesota Judicial Branch Policy 203(a), Section IV.

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- The district made payments on two contracts we tested for invoices that covered eight months and eleven months of services, respectively; the contracts required, however, that the contractors submit monthly invoices for billable costs. In addition, the district paid an invoice from one of these contractors that included \$8,400 in employee benefit charges without confirming or verifying the nature of those charges and whether they were accurate and identified as allowable under the terms of the contract.
- For three of the five purchases we tested that required bids because they exceeded \$2,500, the district could not show that it had solicited bids from vendors. Judicial branch policy requires the district to solicit and document a minimum of two bids for purchases between \$2,501 and \$10,000 and at least three written solicitations for purchases greater than \$10,000 for purchases not under state contract.<sup>11</sup> Obtaining bids ensures the district receives a competitive price for goods and services and provides vendors equal access to state purchases.

Without complete documentation and accurate verification of procurement, contract, and disbursement transactions, there is an increased risk that errors and unauthorized or inappropriate transactions could occur and not be detected.

#### *Recommendations*

- *The Fifth Judicial District should comply with judicial branch policy when it enters into and administers contracts for professional and technical services.*
- *The Fifth Judicial District should obtain and document vendor bids for purchases, in compliance with judicial branch policy.*

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<sup>11</sup> Minnesota Judicial Branch Policy 202(a) Procurement Procedures, Attachment 4.

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**Jeffrey Shorba**  
STATE COURT ADMINISTRATOR

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October 25, 2013

Mr. James R. Nobles  
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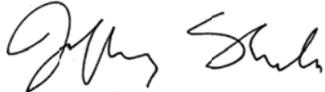
Dear Mr. Nobles:

This letter conveys the Minnesota Judicial Branch's responses to the Office of the Legislative Auditor's (OLA) Internal Control and Compliance report, findings, and recommendations. We view the audits performed by your office as valuable opportunities for an independent assessment of our financial processes and a means to assist our branch to improve processes in financial activities.

We appreciate the opportunity to respond. We found the information in your report and in the exit conference to be informative and helpful.

Listed below are your findings and the Judicial Branch's plan to implement the recommendations. All of your recommendations have been given careful attention and corrective action has either already been implemented or is 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 Council.

Sincerely yours,



Jeffrey Shorba  
State Court Administrator

cc: The Honorable Chief Justice Lorie Skjerven Gildea, Chair  
Minnesota Judicial Council  
The Honorable Bradley Walker, Chief Judge, Fifth Judicial District  
Richard Fasnacht, Fifth Judicial District Administrator

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**Finding 1: The Fifth Judicial District did not always have accurate account balances in the courts information system for money held on behalf of others by court order.**

Recommendation:

- The Fifth Judicial District should ensure that the court information system is an accurate record of the money held in local bank accounts on behalf of others per court order.

*Response:*

The Fifth Judicial District agrees that the counties had not always properly entered the financial transactions relating to monies and/or trust accounts ordered by the courts to be held on behalf of an external party. The counties are responsible for tracking the accounts until the release of the funds directed by judicial rules and court order. The certificate of deposits or other types of non-cash records are held by an external financial institution. Please note that the funds are not state money or taxpayer funds; the court is not holding any money and/or funds; and, there are no reporting requirements to the treasury at the Minnesota Office of Management and Budget. (This is record keeping for the courts benefit.)

This is an area the Branch knows is a complicated area to track and has been working to improve. The State Court Administrator's Office (SCAO) currently is working on developing a procedure that further provides instructions on these types of accounts. SCAO will be providing training to all districts prior to the implementation of the procedure. Until that time, the district will better track and monitor the financial activity of these external trust accounts. The district plans to review all non-cash trust accounts and to make the necessary financial transactions to ensure the records are appropriately reflected in the courts information system.

*Persons responsible for resolving:* Barb Worrell, Assistant District Administrator; Dan Ostdiek, Chief Financial Officer

*Estimated implementation date:*

Track, monitor, and update records – June 30, 2014

Non-Cash Trust Procedure implementation – October 1, 2014

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**Finding 2: The Fifth Judicial District had not complied with some documentation requirements related to certain high-risk manual receipt transactions.**

Recommendation:

- The Fifth Judicial District should ensure that all required information is included on the manual receipts and accurately entered into the court information system.

The district should also ensure that it documents reviews of manual receipts according to the judicial policy.

- The Fifth Judicial district should ensure that staff at all of the court administrative offices are sufficiently trained on the judicial policy requirements for processing, documenting, and reviewing manual receipts.

*Response:*

The Fifth Judicial District agrees that the counties did not consistently record complete or accurate information for receipts that are manually processed when the court information system is unavailable or properly review the manual receipts to ensure clerks entered the receipt correctly.

The court administrator or employee who is independent of the manual receipting process will examine and review all manual receipt transactions and verify accuracy daily. These evaluations will ensure manual receipts are properly documented and accurately entered into the court information system. Evaluations will be thoroughly documented and will include applicable comments or check marks, date reviewed, and reviewer initials.

The Fifth Judicial District will conduct training to all employees responsible for completing manual receipts and performing the review of manual receipts to ensure understanding of the procedures.

*Persons responsible for resolving:* Fifth Judicial District Court Administrators, Kathy Gronewald, Business Systems Coordinator

*Estimated implementation date:* December 31, 2013

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**Finding 3: The Fifth Judicial District did not have required documentation to support its month-end revenue verifications.**

*Recommendations:*

- The Fifth Judicial District should retain all reports required by judicial branch policy to support that the district accurately and timely completed the month end review process.

*Response:*

The Fifth Judicial District agrees and understands the importance of retaining documentation to verify and support its month-end processes. The district notes the following in regards to this finding:

- The District went through risk assessment training in August 2012. Since this training, the district has completed multiple risk assessments that identify risks, control activities to mitigate those risks, and any compensating controls that are needed. The district has an understanding and increased awareness of where the risks are in the month-end process and understands the areas in need of improvement, i.e. additional controls. Since that process, the district would like to note of the 18 exceptions in the report, only 3 are current fiscal years

exceptions. The district believes it has greatly improved in the month end process at the counties through their extensive work in risk assessment.

- For 5 of the 18 exceptions, a system error had occurred that month and the reports were unavailable to print during the month-end process. These reports were available only during that time and the district is unable to re-create these reports due to the system error that took place.
- Even though the district was missing the reports noted, it was able to verify the month ends were completed timely and accurately in the court information system.
- The reports noted show transactions were performed properly. If transactions were not performed properly this would be discovered when comparing the monthly remittance report from the court information system to the group disbursement check. The monthly remittance report provides a breakdown of all the fees included in the group disbursement (month end remittance to the state), which is generated from the court information system. If the missing account balance report shows anything other than a zero balance in liabilities after the group disbursement, the total on the monthly remittance report will not match the amount of the group disbursement check. The error will be found through this process and corrected.

The district believes it has already properly addressed this issue and will continue to improve processes as needed moving forward.

*Persons responsible for resolving the finding: Barb Worrell, Assistant District Administrator and Court Administrators*

*Estimated Implementation date: Resolved*

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**Finding 4: The Fifth Judicial District had not complied with some contract and purchasing policies.**

**Recommendations:**

- The Fifth Judicial District should comply with judicial branch policy when it enters into and administers contracts for professional and technical services.
- The Fifth Judicial District should obtain and document vendor bids for purchases, in compliance with judicial branch policy.

*Response:*

The Fifth Judicial District agrees with the exceptions noted in the audit report. The exceptions noted are in a new court area, and it took some time to coordinate all the different parties related to purchasing and contracts.

The contract and procurement procedure is currently being revised by SCAO to ensure better understanding by staff and more efficient processes in contracts and purchasing of goods and services. The risk assessment requirement in the procedure was removed in 2012 due to inefficiencies in the process; subsequently, the district created a contracts and

procurement risk assessment that sufficiently identifies the risks in these areas as well as the controls to mitigate those risks for all purchasing and contracts.

Managers and drug court coordinators who order supplies and equipment and/or who enter into contracts on behalf of the branch have been reminded to execute contracts prior to contractors beginning work; to monitor the contract thoroughly during the contract period to ensure invoicing by contractors is done timely and have all the supporting documentation to ensure services and/or goods were received prior to payment; and, to retain written offers, price quotes, approved sole source request forms, and other evidence of competitive bids and forward to the district accounting office to demonstrate that goods or services were properly bid prior to the order.

*Persons responsible for future training:* Bridget Nusser, District Accounting Manager, Barb Worrell, Assistant District Administrator, Brenda Pautsch, District Drug Court Manager, Dan Ostdiek, Finance Director

*Estimated Implementation date:* Resolved for current contract and purchasing policies.

Contracts and Procurement Procedure implementation - February 1, 2014

Additional training will be conducted for managers, court administrators and drug court coordinators on the revised policies within 2 months of the effective date of the revisions.

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