



## Judicial Council of California

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# REPORT TO THE JUDICIAL COUNCIL

For business meeting on October 28, 2014

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Title	Agenda Item Type
Trial Court Budget: 2 Percent State-Level Reserve Process and Minimum Operating and Emergency Fund Balance Policy	Action Required
Rules, Forms, Standards, or Statutes Affected	Effective Date
None	October 28, 2014
Recommended by	Date of Report
Trial Court Budget Advisory Committee	October 20, 2014
Hon. Laurie M. Earl, Cochair	Contact
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### Executive Summary

The Trial Court Budget Advisory Committee (TCBAC) recommends changes to the current Judicial Council–approved process for the allocation of the 2 percent state-level reserve in the Trial Court Trust Fund, in 2014–2015, to expedite the distribution of the unexpended reserve funds to trial courts earlier in the fiscal year, and to establish a process for courts to apply for funding for emergencies after these funds have been distributed. For 2015–2016, the TCBAC recommends proposing amendments to the statute that establishes the 2 percent state-level reserve. The TCBAC also recommends that the Judicial Council extend the suspension of the minimum operating and emergency fund balance policy for two fiscal years, and requests that the policy be in addition to the 1 percent reserve cap required by statute.

## Recommendation

The Trial Court Budget Advisory Committee (TCBAC) recommends the following:

1. The Judicial Council, starting in 2014–2015, distribute in January, after the council’s December business meeting, 75 percent of the remaining Trial Court Trust Fund (TCTF) 2 percent reserve funds. From January 1 through March 15, the remaining 25 percent of the 2 percent reserve would be available for court requests due to unforeseen emergencies or unanticipated expenses. These court requests would be reviewed and approved by a TCBAC working group. Any remaining funds would be distributed back to the trial courts after March 15. The Judicial Council’s current approved supplemental funding process would need to be updated to reflect these changes.
2. Court requests due to unforeseen emergencies or unanticipated expenses approved after March 15 and until June 30, would be distributed to the court as a cash advance loan<sup>1</sup> until the following fiscal year when the court, if necessary, could apply for supplemental funding from the TCTF 2 percent reserve at the Judicial Council’s October business meeting in order to repay the cash advance loan. These court requests would be reviewed and approved by a TCBAC working group.
3. The TCBAC, working with the Court Executive Advisory Committee, Trial Court Presiding Judges Advisory Committee, and the Policy Coordination and Liaison Committee, would recommend proposed amendments to Government Code section 68502.5(c)(2)(B), the statute that establishes the 2 percent reserve (see Attachment A), to be included as trailer bill language to the 2015 Budget Act. These recommended amendments would be presented at the Judicial Council’s business meeting in either January or February 2015.
4. Extending the suspension of the minimum operating and emergency fund balance policy for two fiscal years until June 30, 2016, and requesting that the minimum operating and emergency fund balance policy be in addition to the 1 percent reserve cap while in the interim seeking the repeal of Government Code section 77203.

## Previous Council Action

### **Trial Court Trust Fund Allocations: 2 Percent State-Level Reserve Process**

On June 27, 2012, the Governor signed into law Senate Bill 1021, which repealed the provisions in Government Code section 77209 related to urgent needs funding from the Trial Court Improvement Fund (TCIF) and added Government Code section 68502.5, which requires that the Judicial Council set aside as a reserve an amount equal to 2 percent of the TCTF appropriation in Program 45.10. In response to this new statute, the Judicial Council, at its August 31, 2012

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<sup>1</sup> Funds made available by Government Code section 68502.6, which authorizes up-to-two-year loan to be made to the TCTF in order to address courts’ cash flow issues (see Attachment D). On June 27, 2014, the Judicial Council approved an updated cash advance process that incorporates use of these funds.

meeting, approved the current policy with regard to the process, criteria, and required information for requesting supplemental funding from the reserve. This process modified what was approved by the council at its October 28, 2011 meeting as it related to requests for supplemental funding for urgent needs from the TCIF. (See Attachment B.)

On June 27, 2014, the Judicial Council approved a 2015–2016 Budget Change Proposal (BCP) for changes to the statutory language regarding the 2 percent TCTF reserve. The TCBAC was to reevaluate the entire 2 percent TCTF reserve and allocation process. If the result of the evaluation was to recommend to the council that the process should be changed—for example, a change in the date for allocating the remaining funding to the courts—a BCP to change the language of the statute would need to be submitted to the Department of Finance (DOF).

### **Trial Court Budget: Minimum Operating and Emergency Fund Balance Policy**

On August 31, 2012, effective immediately, the council suspended the minimum operating and emergency fund balance policy, which required courts to maintain a fund balance or reserve that was roughly equal to between 3 percent and 5 percent of their prior year general fund expenditures. The council’s action was taken in the context of two statutory changes. First, the policy became at least somewhat redundant when Government Code section 68502.5 required, starting in 2012–2013, the establishment of the 2 percent reserve in the TCTF that would be funded from courts’ allocations. Each court contributes towards the reserve, which by statute is equal to 2 percent of the total TCTF Program 45.10 (Support for Operation of the Trial Courts) appropriation. Any monies that are not allocated by the council through the supplemental funding process are distributed back to each court in the same proportion to their contribution to the reserve. Second, Government Code section 77203 imposed, effective June 30, 2014, a 1 percent cap on fund balances that courts can carry forward from one fiscal year to the next. In view of the efforts to either eliminate or increase the 1 percent cap before it went into effect, the council suspended, instead of eliminated, the minimum operating and emergency fund balance policy.

### **Recent Actions on 2 Percent Process and Fund Balance Policy**

On July 29, 2014, the TCBAC presented recommendations to the Judicial Council for changes to the process for the allocation of the 2 percent state-level reserve and the minimum operating and emergency fund balance policy. The Judicial Council deferred the TCBAC recommendations presented for changes to the process for the allocation of the 2 percent state-level reserve and the committee’s recommendation that the Judicial Council terminate the minimum operating and emergency fund balance policy until their October meeting, and requested the TCBAC work with other advisory bodies to provide further input to the council on the issues and recommendations presented in those items.

### **Rationale for Recommendations**

At its July 7, 2014 meeting, the TCBAC discussed options and recommendations brought forward by its 2 Percent Reserve Process Working Group to change the current Judicial Council–approved process for the allocation of the 2 percent state-level reserve in the TCTF. The TCBAC

also considered options on the minimum operating and emergency fund balance policy, which was suspended by the council for two years on August 31, 2012. At the council's business meeting on July 29, 2014, the committee recommended that the Judicial Council:

- In January, after the Judicial Council's December business meeting, distribute 100 percent of the remaining TCTF 2 percent reserve funds. Courts would have two opportunities per fiscal year instead of four to request supplemental funding from the 2 percent reserve.
- Seek the repeal of Government Code section 68502.5(c)(2)(B), which requires that the Judicial Council set aside as a reserve an amount equal to 2 percent of the Trial Court Trust Fund appropriation in Program 45.10.
- Terminate the minimum operating and emergency fund balance policy.

The first recommendation from the TCBAC, to distribute 100 percent of the remaining TCTF 2 percent reserve funds in January after the council's December business meeting, originated from its working group. Courts would have two opportunities per fiscal year instead of four to request supplemental funding from the 2 percent reserve. The Judicial Council's current approved process would need to be updated to reflect this recommended change. The second recommendation was from TCBAC which was for the Judicial Council to seek the repeal of Government Code section 68502.5(c)(2)(B), which requires that the council set aside as a reserve an amount equal to 2 percent of the TCTF appropriation. This recommendation by the committee was made primarily because the statute that establishes the 2 percent reserve became law prior to the development and application of the Workload Allocation Funding Methodology and is inconsistent with the workload-based funding model adopted by the Judicial Council.

The Judicial Council deferred the TCBAC recommendations for changes to the process for the allocation of the 2 percent state-level reserve and the committee's recommendation that the Judicial Council terminate the minimum operating and emergency fund balance policy until their October meeting. The council requested the TCBAC work with other advisory bodies to provide further input to the council on the issues and recommendations presented in those items.

The 2 Percent Reserve Process Working Group met twice to consider options to address issues that were raised at the July 29 council meeting on the TCBAC recommendations. One issue raised was that if the council was to distribute 100 percent of the remaining TCTF 2 percent reserve funds in January, there would be no funds available for trial courts to request emergency funding in the second half of the fiscal year (January–June). Additionally, a policy would be needed to deal with court funding emergencies for courts, prior to requesting the repeal of the statute and the Judicial Council policy on court-held minimum operating and emergency reserve. The working group brought options and recommendations for the full committee to consider at its September 26, 2014 meeting. At the TCBAC meeting on September 26, the committee made

four recommendations, all of which originated from its working group, to be presented at the Judicial Council's October 28 business meeting. Three of the recommendations made were for changes to the supplemental funding process and one recommendation was to the operating and emergency reserve fund balance policy.

## **Recommendations on Supplemental Funding Process**

### **Recommendation 1: Allocation Process**

The recommendation from the TCBAC is for the Judicial Council, starting in 2014–2015, to distribute 75 percent of the remaining TCTF 2 percent reserve funds in January, after the council's December business meeting. The remaining 25 percent of the 2 percent reserve would be available for court requests due to unforeseen emergencies or unanticipated expenses from January 1 through March 15. These court requests would be reviewed and approved by a TCBAC working group. Any remaining funds would be distributed back to the trial courts after March 15. The Judicial Council's current approved supplemental funding process would need to be updated to reflect this change. (See Attachment C.)

*Discussion.* The committee voted unanimously to recommend this option to the Judicial Council. The main reason the committee recommends this option is that it accomplishes two goals. This recommendation expedites the distribution of 75 percent of the remaining 2 percent reserves to the courts by two months and leaves a 25 percent reserve to address emergency requests submitted from January through March 15. It also addresses the issue raised at the July 29, 2014 council meeting on the TCBAC's previous recommendation for the council to distribute 100 percent of the remaining TCTF 2 percent reserve funds in January, leaving no funds available for trial courts to request emergency funding in January or February as is the case with the current process. The TCBAC made an amendment to this option to include that court requests submitted during this period would be reviewed and approved by a TCBAC working group.

### **Recommendation 2: Extension of Process Timeline**

The recommendation from the TCBAC is to establish a process for the period after March 15, when the remaining 2 percent reserves have been distributed pursuant to statute and the Judicial Council–approved process. The committee recommends, starting in 2014–2015, that after March 15 and until June 30, approved court requests due to unforeseen emergencies or unanticipated expenses would be distributed to the court as a cash advance loan, until the following fiscal year when the court, if necessary, could apply for supplemental funding from the TCTF 2 percent reserve at the Judicial Council's October business meeting in order to repay the cash advance loan. These court requests would be reviewed and approved by a TCBAC working group.

*Discussion.* The committee voted unanimously to recommend this option to the Judicial Council. The decision by TCBAC members to recommend this option was made primarily to address the period of time after March 15 to June 30, when the remaining 2 percent reserves have been distributed pursuant to statute and there's no funding process in place for courts that are faced with an emergency funding need during this period of time. There was agreement by the

committee members that a TCBAC working group would review and approve these requests that would only constitute a preapproval until the following fiscal year when the Judicial Council could allocate funds from the next fiscal year's 2 percent allocation, if the court's request was approved. The application process and criteria would be the same as the current supplemental funding process. There was discussion by the committee as to whether using the cash advance funds made available by Government Code section 68502.6, which states that a court should have a balanced budget, would be allowable. Judicial Council staff informed the committee that Department of Finance staff is aware of the issue of a "dark period" in the statute that established the 2 percent reserve, when no funding for court emergencies is available, and acknowledges that this change is a solution to address this concern for now until statute changes are made.

### **Recommendation 3: Proposed Amendments to Statute**

The recommendation from the TCBAC is for the committee, working with the Court Executive Advisory Committee, Trial Court Presiding Judges Advisory Committee, and the Policy Coordination and Liaison Committee, to recommend that proposed amendments to Government Code section 68502.5(c)(2)(B) be included as trailer bill language to the 2015 Budget Act. These recommended amendments would be presented at the Judicial Council's business meeting in either January or February 2015.

*Discussion.* The committee voted unanimously to recommend this option to the Judicial Council. The TCBAC considered another option which was to seek the repeal of Government Code section 68502.5 and recommend a more appropriate percentage to be held in reserve at the state level for urgent needs. No motion was made to recommend the option for repealing the statute. There was, though, a brief discussion by committee members on the importance of working on proposing structural changes to amend the statute—which could be permanent—instead of repealing it.

### **Recommendation on Fund Balance Policy**

#### **Recommendation 4: Operating and Emergency Reserve Policy**

The recommendation from the TCBAC is to extend the suspension of the minimum operating and emergency fund balance policy for two fiscal years until June 30, 2016, and request that the minimum operating and emergency fund balance policy be in addition to the 1 percent reserve cap while in the interim seeking the repeal of Government Code section 77203.

*Discussion.* The committee voted unanimously to recommend this option to the Judicial Council. Several TCBAC members briefly discussed that it was important to continue pursuing the repeal of Government Code section 77203.

### **Comments, Alternatives Considered, and Policy Implications**

This item was not circulated for comment. Options were considered by the TCBAC and are discussed in the Rationale for Recommendations section of the report.

## **Implementation Requirements, Costs, and Operational Impacts**

Not applicable.

## **Relevant Strategic Plan Goals and Operational Plan Objectives**

The recommended changes to the process for the allocation of the 2 percent reserve in the TCTF will address the strategic plan goals of Access, Fairness, and Diversity (Goal I); Independence and Accountability (Goal II); Modernization of Management and Administration (Goal III); Quality of Justice and Service to the Public (Goal IV); and Branchwide Infrastructure for Service Excellence (Goal VI).

## **Attachments**

1. Attachment A: Government Code, § 68502.5(c)(2)(B)
2. Attachment B: Judicial Council–Approved Process for Supplemental Funding
3. Attachment C: Summary of Recommended Changes to Judicial Council–Approved Process
4. Attachment D: Government Code, § 68502.6

**Government Code section 68502.5(c)(2)(B)**

(B) Upon preliminary determination of the allocations to trial courts pursuant to subparagraph (A), the Judicial Council shall set aside 2 percent of the total funds appropriated in Program 45.10 of Item 0250-101-0932 of the annual Budget Act and these funds shall remain in the Trial Court Trust Fund. These funds shall be administered by the Judicial Council and be allocated to trial courts for unforeseen emergencies, unanticipated expenses for existing programs, or unavoidable funding shortfalls. Unavoidable funding shortfall requests for up to 1.5 percent of these funds shall be submitted by the trial courts to the Judicial Council no later than October 1 of each year. The Judicial Council shall, by October 31 of each year, review and evaluate all requests submitted, select trial courts to receive funds, and notify those selected trial courts. By March 15 of each year, the Judicial Council shall distribute the remaining funds if there has been a request from a trial court for unforeseen emergencies or unanticipated expenses that has been reviewed, evaluated, and approved. Any unexpended funds shall be distributed to the trial courts on a prorated basis.

## Judicial Council-Approved Process for Supplemental Funding

Below is the process for supplemental funding that was approved by the Judicial Council at its August 31, 2012, meeting.

- a. Supplemental funding for urgent needs is defined as unavoidable funding shortfalls, unforeseen emergencies, or unanticipated expenses for existing programs.
  - i. A request can be for either a loan or one-time funding that is not repaid, but not for ongoing funding.
- b. The submission, review, and approval process is:
  - i. All requests will be submitted to the Judicial Council for consideration;
  - ii. Requests will be submitted to the Administrative Director of the Courts by either the court's presiding judge or court executive officer;
  - iii. The Administrative Director of the Courts will forward the request to the AOC Director of Finance [now Fiscal Services Office].
  - iv. AOC Finance Division [Fiscal Services Office] budget staff will review the request, ask the court to provide any missing or incomplete information, draft a preliminary report, share the preliminary report with the court for its comments, revise as necessary, and issue a final report for the council;
  - v. The final report will be provided to the requesting court prior to the report being made publicly available on the California Courts website; and
  - vi. The court may send a representative to the Judicial Council meeting to present its request and respond to questions from the council.
- c. Beginning in 2012–2013, court requests for supplemental funding for urgent needs due to unavoidable budget shortfalls, must be submitted to the Administrative Director of the Courts, by no later than October 1. Courts are encouraged to submit supplemental funding requests for urgent needs before the October 1 deadline, but no earlier than 60 days after the Budget Act is enacted into law.
- d. Beginning in 2012–2013, the Judicial Council shall allocate up to 75 percent of the 2 percent state-level reserve fund by October 31 of each year to courts requesting supplemental funding for urgent needs due to unavoidable funding shortfalls.
- e. Beginning in 2012–2013, after October 31 and by March 15 of each fiscal year, the Judicial Council shall allocate the remaining funds if there has been an approved request from a trial court(s) requesting supplemental funding for urgent needs due to unforeseen emergencies or unanticipated expenses for existing programs. Any unexpended funds shall be distributed to the trial courts on a prorated basis.

- f. To be considered at a scheduled Judicial Council business meeting, requests submitted after October 31 for supplemental funding due to unforeseen emergencies and unanticipated expenses must be submitted to the Administrative Director of the Courts at least 25 business days prior to that business meeting.
- g. The Judicial Council would consider appropriate terms and conditions that courts must accept in order to receive supplemental funding for urgent needs.

***Judicial Council-Approved Criteria for Eligibility for and Allocation of Supplemental Funding***

Below are the criteria for eligibility for and allocation of supplemental funding for trial courts' urgent needs that were approved by the Judicial Council at its August 31, 2012, meeting.

- a. Only trial courts that are projecting a current-year negative fund balance can apply for supplemental funding related to urgent needs.
- b. Generally, no court may receive supplemental funding for urgent needs in successive fiscal years absent a clear and convincing showing.
- c. Courts submitting on or before October 1 can only receive up to the amount the court contributed to the 2 percent state-level reserve fund. If the requested amount is beyond the court's contribution to the 2 percent state-level reserve fund, the Judicial Council may distribute more funding to the court, after October 31 and prior to March 15 of the fiscal year.

More specifically, courts that submit by October 1 a request for an unavoidable funding shortfall, may apply with updated financial information for unforeseen emergencies or unanticipated expenses for existing programs distribution at a future Judicial Council business meeting prior to March 15.

- d. Allocate to all courts after March 15 a proportionate share of any unexpended funds from the 2 percent state-level reserve, regardless of whether the Judicial Council has allocated to a court supplemental funding for an urgent need in the current fiscal year, using courts' current year Trial Court Trust Fund and General Fund base allocation.
- e. If a court that is allocated supplemental funding determines during the fiscal year that some or all of the allocation is no longer needed due to changes in revenues and/or expenditures, [it] is required to return the amount that is not needed.

***Judicial Council-Approved Information Required to be Provided by Trial Courts for Supplemental Funding***

Below is the information required to be provided by trial courts for supplemental funding for urgent needs that were approved by the Judicial Council at its August 31, 2012, meeting.

- a. A description of what factors caused or are causing the need for funding;
- b. If requesting a one-time distribution, an explanation of why a loan would not be appropriate;
- c. Current status of court fund balance;
- d. Three-year history of year-end fund balances, revenues, and expenditures;
- e. Current detailed budget projections for the current fiscal year (e.g., FY 2012–2013), budget year (e.g., FY 2013–2014), and budget year plus 1 (e.g., FY 2014–2015);
- f. Measures the court has taken in the last three years regarding revenue enhancement and/or expenditure reduction, including layoffs, furloughs, reduced hours, and court closures;
- g. Employee compensation practices (e.g., cost-of-living adjustments) and staffing levels in the past five years;
- h. Description of the consequences to the court’s operations if the court does not receive funding;
- i. Description of the consequences to the public and access to justice if the court does not receive funding;
- j. What measures the court will take to mitigate the consequences to court operations, the public, and access to justice if funding is not approved;
- k. Five years of filing and termination numbers;
- l. Most recent audit history and remediation measures;
- m. If supplemental funding was received in prior year, please identify amount received and explain why additional funding is again needed in the current fiscal year; and

- n. If the request for supplemental funding is not for a one-time concern, the court must include an expenditure/revenue enhancement plan that identifies how the court will resolve its ongoing funding issue.

## Summary of Recommended Changes to Judicial Council–Approved Process

Judicial Council–Approved Process for Supplemental Funding	Trial Court Budget Advisory Committee Recommendation 1
<p><u>Page 1(e)</u></p> <p>e. Beginning in 2012–2013, after October 31 and by March 15 of each fiscal year, the Judicial Council shall allocate the remaining funds if there has been an approved request from a trial court(s) requesting supplemental funding for urgent needs due to unforeseen emergencies or unanticipated expenses for existing programs. Any unexpended funds shall be distributed to the trial courts on a prorated basis.</p> <p><u>Page 2(d)</u></p> <p>c. Allocate to all courts after March 15 a proportionate share of any unexpended funds from the 2% state-level reserve, regardless of whether the Judicial Council has allocated to a court supplemental funding for an urgent need in the current fiscal year, using courts’ current year Trial Court Trust Fund and General Fund base allocation.</p>	<p><u>Page 1(e)</u></p> <p>Beginning in <del>2012–2013</del> 2014-2015, after October 31 and by March 15 of each fiscal year, the Judicial Council shall allocate <b>25 percent</b> of the remaining funds if there has been an approved request from a trial court(s) requesting supplemental funding for urgent needs due to unforeseen emergencies or unanticipated expenses for existing programs. Any unexpended funds shall be distributed to the trial courts on a prorated basis. <b>After March 15 and until June 30, requests due to unforeseen emergencies or unanticipated expenses approved, will be distributed to the court as a cash advance loan, until the following fiscal year when the court, if necessary, could apply for supplemental funding from the TCTF 2 percent reserve at the Judicial Council’s October business meeting in order to repay the cash advance loan. These requests will be reviewed and approved by the Trial Court Budget Advisory Committee’s working group.</b></p> <p><u>Page 2(d)</u></p> <p>c. Allocate to all courts <del>after March 15</del> <b>in January</b>, 75 percent of any unexpended funds from the 2% state-level reserve, regardless of whether the Judicial Council has allocated to a court supplemental funding for an urgent need in the current fiscal year, using courts’ current year Trial Court Trust Fund and General Fund base allocation.</p>

**Government Code section 68502.6.**

(a) If the cash balance of the Trial Court Trust Fund is insufficient to support trial court operations during the fiscal year, the Administrative Office of the Courts may transfer funds from any fund identified in subdivision (c) as a loan to the Trial Court Trust Fund. The total amount of outstanding loans shall not exceed one hundred fifty million dollars (\$150,000,000) at any time during the fiscal year. The Administrative Office of the Courts shall not authorize a loan pursuant to this section to provide cash resources to any court that has not first provided a balanced budget approved by the Judicial Council.

(b) The Administrative Office of the Courts may transfer funds from the Trial Court Trust Fund for the repayment of the loan described in subdivision (a). Interest shall not be charged or paid on any loan authorized pursuant to this section and all loans shall be repaid within two years from the date on which the loan originated. The authority to transfer funds provided by this section shall not interfere with the objectives for which the funds identified in subdivision (c) were created. This section shall not be construed to provide additional expenditure authority to the Trial Court Trust Fund.

(c) Moneys in the following funds shall be available for transfer to the Trial Court Trust Fund as a loan for cash flow purposes:

- (1) The State Court Facilities Construction Fund.
- (2) The Immediate and Critical Needs Account of the State Court Facilities Construction Fund.
- (3) The Judicial Branch Workers' Compensation Fund.

(d) For each loan executed pursuant to this section, the Administrative Office of the Courts shall, no later than August 30 of each year, report the following information to the Joint Legislative Budget Committee and the Department of Finance:

- (1) The date of the loan.
- (2) The amount loaned to each court.
- (3) The funding source of the loan.
- (4) The repayment date or proposed repayment date of the loan.

*(Added by Stats. 2013, Ch. 31, Sec. 5. Effective June 27, 2013.)*