



## Memorandum

**TO:** Making Government Work  
Better Committee

**FROM:** Gerald A. Silva  
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Mark Danaj

**SUBJECT:** *Workers' Compensation Claims Liability*    **DATE:** October 13, 2005

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During the City's annual 2003-04 financial audit, the City's external auditors, Macias Gini & Company LLP made a recommendation that the City review its methodology in developing workers' compensation claims liability estimates. This recommendation was discussed during the presentation of the Auditor's Report to the Making Government Work Better Committee (MGWB) on March 17, 2005. MGWB subsequently referred a recommendation to the Rules Committee requesting that a review of the City's method of calculating its workers' compensation reserves be added to the City Auditor's work plan.

In 1994, the City Auditor issued a report entitled "*An Audit of the City Of San Jose's Workers' Compensation Program Claims Database*". In that report, the City Auditor recommended and the City Council subsequently adopted a policy to "*annually calculate the estimated liability for workers' compensation using current information in the workers' compensation claims database...*" The City Auditor verified that the City had implemented the City Auditor's recommendation when calculating the estimated liability for workers' compensation claims as of June 30, 1994. Subsequent to 1994, the City had reverted to using an actuarial study to estimate its workers' compensation claims liability.

During the course of the 2003-04 financial audit, staff recognized an inconsistency in the method the City was determining the estimated liabilities for workers' compensation claims. Since an actuarial study had been performed as a method of determining the workers' compensation estimated claims, absent an alternative method being conducted, the amount booked for the estimated claims as of June 30, 2004 was determined through the use of the actuarial study.


Recognizing the inconsistency in following the previous direction from Council in 1994, staff requested the City Auditor to help calculate the financial statement implications of the City using the claims based methodology as previously directed. Accordingly, the City Auditor reviewed the City's workers' compensation actuarial study, the procedures for estimating the reserves in the City's workers' compensation database, a recent independent study of the reliability of reserves in the workers' compensation database, two database reserve reports, and held several discussions with the City's independent external auditors.

Based upon the review noted above, the City Auditor, the Departments of Finance and Employee Services, and the City's external auditors concur that it is permissible and acceptable for the City to comply with the City Council's 1994 policy to annually calculate the estimated liability for

workers' compensation using current information in the workers' compensation claims database. By so doing, the City's outstanding liability for workers' compensation claims has been reduced by \$20.8 million as of June 30, 2005. This fiscal impact has been recorded in the City's 2004-05 audited financial statements and the change in accounting method has been reflected in the City's 2004-05 Comprehensive Annual Financial Report (CAFR).

  
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