

**Office of
The City Attorney
City of San Diego**

**MEMORANDUM
MS 59**

(619) 533-5800

DATE: November 13, 2012
TO: Eduardo Luna, City Auditor
FROM: City Attorney
SUBJECT: Conducting Fraud Hotline Investigation on Matters that are Subject of Pending Legal Proceeding or Investigation

QUESTION PRESENTED

May the San Diego City Auditor (Auditor) investigate a fraud hotline complaint when the allegations of such complaint are the subject of pending City litigation, investigation, or other legal proceeding?

SHORT ANSWER

When the Auditor receives a matter through the Fraud Hotline, where such matter is subject of pending litigation or where legal proceedings or investigations are initiated or in process, the Auditor should evaluate the impact on the legal proceeding or investigation. In some cases, it may be appropriate for the Auditor to work with legal authorities to investigate; in other cases it may be appropriate for Auditor to defer or withdraw from the Auditor investigation to avoid interfering with an ongoing investigation or legal proceeding.

ANALYSIS

I. CITY CHARTER AND GAGAS REQUIREMENTS

Charter section 39.2 states that the Auditor “may investigate any material claim of financial fraud, waste or impropriety within any City Department.” The Auditor maintains a Fraud Hotline pursuant to California Government Code section 53087.6, that allows anyone to submit complaints of possible fraud, waste or abuse of City resources. Charter section 39.2 also requires the Auditor to follow the Government Auditing Standards (GAGAS) in the performance of his responsibilities. (See, Charter section 39.2, providing that the City Auditor “shall follow Government Auditing Standards” in connection with performance audits, and other duties as

may be required by ordinance or as provided by the Constitution and general laws of the State.) Occasionally, the Auditor receives a Fraud Hotline complaint concerning a matter that is the subject of a pending criminal, civil, or administrative proceeding. In those cases, GAGAS recommends that an auditor evaluate the impact of an auditor investigation to determine whether the auditor should defer or withdraw from investigations to avoid interfering with the legal proceedings.

Specifically, GAGAS provides guidance for auditors with respect to pending litigation as follows:

Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud, noncompliance with provisions of laws, regulations, contracts or grant agreements, or abuse. Laws, regulations, and policies may require auditors to report indications of certain types of fraud, noncompliance with provisions of laws, regulations, contracts or grant agreements, or abuse to law enforcement or investigatory authorities before performing additional audit procedures. *When investigations or legal proceedings are initiated or in process, auditors should evaluate the impact on the current audit. In some cases, it may be appropriate for the auditors to work with investigators or legal authorities, or withdraw from or defer further work on the audit or a portion of the audit to avoid interfering with an ongoing investigation or legal proceeding.* (Emphasis added)

Gov't Auditing Standards, §6.35

GAGAS section 6.35 applies specifically to "Field Work Standards for Performance Audits." However, San Diego Charter section 39.2 states, without limitation, that the Auditor "shall follow Government Auditing Standards."

Turning to the Auditor's own "Audit Handbook", it provides: "[i]n fraud-related situations, our policy will be not to interfere with legal proceedings or investigations." San Diego City Auditor's Audit Handbook at 49, 72. Although this language is located in the "Audit Standards" and the "Audit Process" sections of the handbook (Sections 3 and 5 respectively), the language in Section 9, "Fraud Hotline", states: "[t]he Fieldwork Standards, Audit Planning, and Reporting of Audit Results described in Sections 4 through 7 of this manual will be followed for all audits of internal controls resulting from Hotline referrals." *Id.* at 115.

Consistent with GAGAS, the Audit Handbook also provides that "Auditors will exercise professional judgment in pursuing indications of possible fraud, illegal acts, violations of provision of contracts and grant agreements, or abuse in order not to interfere with potential investigations, legal proceedings, or both." Accordingly, both GAGAS and the Auditor's policies recognize the importance of evaluating the impact of the Auditor's work when a Fraud

Hotline complaint is potentially related to the same subject matter as a legal proceeding or investigation.¹

II. PRACTICAL CONSIDERATIONS

In addition to the standards enumerated by the GAGAS, there are practical reasons the Auditor should consider when he wishes to investigate a matter in litigation. First, the Auditor and his staff may become witnesses in the litigation if they conduct a concurrent investigation and interview witnesses. Although generally the hotline investigations are confidential, the law is unclear whether information obtained in a Fraud Hotline investigation can remain confidential if such information also is the subject of a pending legal proceeding.² The Auditor could inadvertently “open the door” to a confidential whistleblower complaint.

Second, a common tactic by opposing counsel is to look for inconsistencies in prior statements of witnesses. Even minor inconsistencies or statements taken out of context could jeopardize the City’s efforts in the legal proceeding and potentially create liability for the City.

Finally, an investigation by the Auditor could result in a duplication of efforts and be an inefficient use of City resources. For example, it would be inefficient to have City staff be interviewed by the Auditor in connection with the Fraud Hotline, interviewed by the City Attorney in preparing for litigation, and deposed by the opposing party. In each case, the attorney handling the matter would need to be present with City staff to ensure that confidential information related to the litigation is not disclosed. When a matter is in litigation, the City devotes substantial resources to the case. It could be inefficient to devote Auditor resources to duplicate investigative efforts and risk interfering with ongoing legal proceedings.

III. SUGGESTED PROTOCOL FOR EVALUATING IMPACT ON PENDING LEGAL PROCEEDING

In order to comply with the GAGAS and take into account the practical applications relevant to evaluating the impact of an Auditor investigation on a legal proceeding that is pending or initiated, the following steps are recommended:

1. Auditor defines work plan with specific scope of the proposed investigation (i.e. who Auditor will interview, what questions Auditor intends to ask, etc.).
2. Auditor consults in writing with the Assistant City Attorney assigned to litigation.

¹ The City of San Diego Fraud Hotline Procedures Manual is currently being revised, and procedures for how to handle a Fraud Hotline Complaint whose allegations are subject of pending litigation will be included in the revised manual.

² Nothing in the Whistleblower Statute provides that an investigative audit conducted pursuant to the statute may be kept confidential if such information, or witness is subpoenaed in a legal proceeding.

3. Auditor asks for input from Assistant City Attorney on the impact of Auditor's investigative plan on current legal proceeding.
4. Auditor exercises professional judgment to evaluate the impact of pursuing an investigation on matters which are subject of a pending, or initiated legal proceeding. In some cases, it may be appropriate to work with legal authorities, and in some cases it may be appropriate to defer further work, or withdraw from the investigation, to avoid interfering with, or compromising the litigation.

If the Auditor and Assistant City Attorney cannot come to an agreement as to the scope and evaluation of the impact on the legal proceeding, such matter should be presented to Audit Committee for further direction.

CONCLUSION

The Auditor plays an important role in investigating fraud, waste and abuse of City resources. However, when such matters are the subject of a legal proceeding or pending investigation, the Auditor should evaluate the impact of an investigation on a legal proceeding prior to pursuing its own investigation. In some cases, it may be appropriate to cooperate or conduct concurrent investigation; in other cases, the Auditor should defer or withdraw from the investigation to avoid interfering with the legal proceeding.

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cc: Audit Committee

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