

FILED

2007 FEB -2 PM 12:57

RECEIVED  
CENTRAL DISTRICT OF CALIFORNIA  
SECURITIES

1 BRIANE NELSON MITCHELL, Cal. Bar No. 116037  
 E-mail: mitchellbn@sec.gov  
 2 LORRAINE B. ECHAVARRIA, Cal. Bar No. 191860  
 E-mail: echavarria@sec.gov  
 3 DAVID VAN HAVERMAAT, Cal Bar No. 175761  
 E-mail: vanhavermaatd@sec.gov  
 4 WILLIAM G. BERRY, Cal. Bar No. 206348  
 E-mail: berryw@sec.gov

5 Attorneys for Plaintiff  
 6 Securities and Exchange Commission  
 Randall R. Lee, Regional Director  
 7 Michele Wein Layne, Associate Regional Director  
 5670 Wilshire Boulevard, 11th Floor  
 8 Los Angeles, California 90036-3648  
 Telephone: (323) 965-3998  
 9 Facsimile: (323) 965-3908

10  
 11  
 12 UNITED STATES DISTRICT COURT  
 13 CENTRAL DISTRICT OF CALIFORNIA

14 CV-07-2144

15 RGK (AGRx)

16 SECURITIES AND EXCHANGE  
 COMMISSION,

17 Plaintiff,

18 vs.

19 TENET HEALTHCARE  
 20 CORPORATION, a Nevada corporation,  
 21 DAVID L. DENNIS, THOMAS B.  
 22 MACKEY, CHRISTI R. SULZBACH,  
 and RAYMOND L. MATHIASSEN,

23 Defendants.  
 24  
 25  
 26  
 27  
 28

Case No.

COMPLAINT FOR VIOLATIONS  
 OF THE FEDERAL SECURITIES  
 LAWS

1 Plaintiff Securities and Exchange Commission (the “Commission”) alleges  
2 as follows:

3 1. This civil fraud case involves material misrepresentations and  
4 omissions made by defendants Tenet Healthcare Corporation (“Tenet”) and four of  
5 its former senior officers, David L. Dennis (“Dennis”), Thomas B. Mackey  
6 (“Mackey”), Christi R. Sulzbach (“Sulzbach”), and Raymond L. Mathiasen  
7 (“Mathiasen”) (collectively, “defendants”), in Tenet’s filings with the Commission.

8 **I. JURISDICTION AND VENUE**

9 2. This Court has jurisdiction over this action pursuant to Sections 20(b),  
10 20(d)(1), and 22(a) of the Securities Act of 1933 (“Securities Act”), 15 U.S.C. §§  
11 77t(b), 77t(d)(1), and 77v(a), and Sections 21(d)(1), 21(d)(3)(A), 21(e), and 27 of  
12 the Securities Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. §§ 78u(d)(1),  
13 78u(d)(3)(A), 78u(e) and 78aa. Defendants have directly or indirectly made use of  
14 the means or instrumentalities of interstate commerce, of the mails, or of the  
15 facilities of a national securities exchange in connection with the transactions, acts,  
16 practices and courses of business alleged in this Complaint.

17 3. Venue is proper in this district pursuant to Section 22(a) of the  
18 Securities Act, 15 U.S.C. § 77v(a), and Section 27 of the Exchange Act, 15 U.S.C.  
19 § 78aa, because defendants resided within this district during the relevant time  
20 period and certain of the transactions, acts, practices and courses of conduct  
21 constituting violations of the laws alleged in this Complaint occurred within this  
22 district.

23 **II. SUMMARY**

24 4. Tenet is one of the largest publicly traded healthcare companies in the  
25 United States. From 1999 through 2002, Tenet engaged in an unsustainable  
26 strategy to improve its earnings by deliberately exploiting a loophole in Medicare’s  
27 reimbursement system. During this time, Tenet never disclosed its scheme and the  
28 material impact it had on Tenet’s earnings to the investing public in any of its

1 filings with the Commission and, as a result, misled its investors by creating a false  
2 impression of the true reasons behind its financial performance.

3 5. Medicare compensates hospitals for treating extraordinarily sick  
4 Medicare patients with a form of reimbursement known as outlier payments.  
5 Tenet management discovered that it could artificially inflate its revenue from  
6 outlier payments without doing anything more than just simply increasing one of  
7 the numbers used in the formula by Medicare to calculate a hospital's outlier  
8 payment, namely the gross charges listed by a hospital.

9 6. Defendant Mackey, Tenet's former chief operating officer and co-  
10 president, was the principal architect of Tenet's scheme to exploit Medicare and  
11 inflate Tenet's outliers. In 1999 and under Mackey's direction, Tenet management  
12 calculated the precise increase to Tenet's gross charges needed to boost its revenue  
13 from outlier payments to a level that would allow Tenet to reach its earnings  
14 targets. Mackey and other members of Tenet's management then directed Tenet's  
15 hospital managers to implement these aggressive gross charge increases.

16 7. For the next three years, Mackey continued to oversee aggressive  
17 gross charge increases by Tenet. Tenet's outlier revenue more than tripled by 2002  
18 and accounted for over 40% of Tenet's earnings per share in fiscal year 2002, as  
19 Tenet's earnings goals were surpassed year after year.

20 8. As Tenet's general counsel and chief compliance officer, defendant  
21 Sulzbach knew, or was reckless in not knowing, about the strategy to aggressively  
22 increase gross charges in order to inflate Tenet's outlier revenues. As early as  
23 1999, Mackey's subordinates and other Tenet managers and employees  
24 approached Sulzbach with questions and concerns regarding the legality of  
25 implementing gross charge increases that triggered outlier payments. By 2002,  
26 Sulzbach had requested, received, and discussed data showing that Tenet's outlier  
27 payments were a significant portion of its Medicare revenue.

28 9. Defendant Mathiasen was Tenet's chief accounting officer and was

1 responsible for Tenet's books and records and for preparing Tenet's annual report.  
2 Mathiasen repeatedly received information reflecting the significant impact  
3 Tenet's strategy to aggressively increase its gross charge was having on its outlier  
4 revenue. He knew, or was reckless in not knowing, that such a strategy was having  
5 a material impact on Tenet's earnings and that it was not sustainable, yet he signed  
6 Tenet's misleading filings. Mathiasen also oversaw the creation of inappropriate  
7 general reserves at Tenet totaling approximately \$107 million by the end of fiscal  
8 year 2002. These inappropriate reserves resulted in material misstatements to  
9 Tenet's financial statements for fiscal years 2000 through 2004.

10 10. As Tenet's chief financial officer, defendant Dennis certified Tenet's  
11 misleading filings even though he knew, or was reckless in not knowing that such  
12 filings were misleading because they omitted material information regarding  
13 Tenet's unsustainable scheme to increase gross charges in order to boost its outlier  
14 revenue and thereby improve its earnings.

15 11. Tenet's scheme likely would have remained a secret from the  
16 investing public but for the research of an analyst from the investment banking  
17 firm of UBS Warburg. In or around October 2002, the analyst discovered Tenet's  
18 exploitation of Medicare and published a report suggesting that Tenet's financial  
19 success was likely fueled by its manipulation of Medicare outliers. Tenet's stock  
20 price immediately dropped about 14% on the news.

21 12. Within about nine days following the UBS Warburg analyst's report,  
22 Mackey was asked to retire and Dennis resigned. Tenet's stock price plummeted  
23 as much as 46%. In total, Tenet's shareholders lost more than \$11 billion in  
24 market capitalization after the outlier scheme was disclosed.

25 13. Dennis, Mackey, Sulzbach, and Mathiasen were substantially  
26 involved in preparing, reviewing and approving of Tenet's public reports with the  
27 Commission, including the Form 10-Q for Tenet's third quarter ending February  
28 28, 2002 ("2002 Third Quarter Form 10-Q"), the Form 10-K for Tenet's fiscal year

1 ended May 31, 2002 ("Tenet's 2002 Form 10-K"), and the Form 10-Q for Tenet's  
2 first quarter ending August 30, 2002 ("Tenet's 2003 First Quarter Form 10-Q").

3 14. Each of these filings omitted material information necessary to make  
4 the statements made not misleading, such as information regarding Tenet's  
5 unsustainable strategy to aggressively increase its gross charges and the impact that  
6 strategy had on Tenet's Medicare outlier revenue, its overall revenues, income,  
7 financial condition, and results of operation.

8 15. Defendants knew, or were reckless in not knowing, that these filings  
9 were misleading because they knew material information regarding Tenet's  
10 unsustainable strategy to increase gross charge to inflate its Medicare outlier  
11 revenue was not disclosed in the filings.

12 16. Also, in June 2002, Tenet filed a prospectus supplement in connection  
13 with a \$400 million debt offering. The prospectus supplement incorporated  
14 Tenet's 2001 fiscal year-end filing, as well as all subsequent quarterly filings in  
15 fiscal year 2002. These filings also omitted material information regarding Tenet's  
16 gross charge increases and their impact on Tenet's Medicare outlier revenue,  
17 financial condition, and results of operation, thereby rendering the prospectus  
18 misleading.

19 17. Dennis, Mackey, Sulzbach, and Mathiasen were substantially  
20 involved in the preparation, review and approval of the filings incorporated in the  
21 June 2002 prospectus supplement and each of them knew, or was reckless in not  
22 knowing, that these filings were misleading.

23 18. Mackey and others in Tenet's management participated and made  
24 statements regarding Tenet's financial performance and operations in earnings  
25 calls and presentations made by Tenet to Wall Street analysts and investors.  
26 During these earnings calls and presentations, Mackey and others in Tenet's  
27 management misled the investing public by failing to reveal material information  
28 regarding Tenet's gross charge increases and their impact on Tenet's Medicare

1 outlier revenue.

2 19. Accordingly, Tenet violated Section 17(a) of the Securities Act and  
3 Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act and Rules 10b-5, 12b-  
4 20, 13a-1, and 13a-13 thereunder.

5 20. Dennis, Mackey, Sulzbach, and Mathiasen violated Section 17(a) of  
6 the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5  
7 thereunder, and aided and abetted Tenet's violations of Section 13(a) of the  
8 Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

9 21. Mathiasen also violated Rule 13b2-1 under the Exchange Act and  
10 aided and abetted Tenet's violations of Section 13(b)(2)(A) of the Exchange Act.

### 11 **III. DEFENDANTS**

12 22. Tenet Healthcare Corporation is a Nevada corporation with its  
13 principal executive offices in Dallas, Texas. From 1999 through 2002, Tenet  
14 maintained its principal executive offices in Santa Barbara, California and its  
15 common stock was registered with the Commission pursuant to Section 12(b) of  
16 the Exchange Act and listed on the New York and Pacific Stock Exchanges. From  
17 at least 1999 through at least November 2002, Tenet's fiscal year ended on May  
18 31st of each calendar year.

19 23. Defendant David L. Dennis is a resident of Los Angeles, California.  
20 Dennis was the chief financial officer and co-president of Tenet from February  
21 2000 until November 2002.

22 24. Defendant Thomas B. Mackey is a resident of Keswick, Virginia.  
23 Mackey was the chief operating officer and co-president of Tenet from January  
24 1999 until November 2002. From 1999 through 2002, Mackey was a resident of  
25 Montecito, California.

26 25. Defendant Christi R. Sulzbach is a resident of Santa Barbara,  
27 California. Sulzbach joined Tenet in 1983 as an assistant general counsel and  
28 served as the chief compliance officer, executive vice president, and general

1 counsel of Tenet from February 1999 until September 2003. Sulzbach has been  
2 licensed with the California State Bar since 1980.

3 26. Defendant Raymond L. Mathiasen is a resident of Los Angeles,  
4 California. Mathiasen was the chief accounting officer of Tenet from March 1996  
5 until November 2002. Mathiasen retired from Tenet in April 2004. Mathiasen  
6 joined Tenet (then known as National Medical Enterprises) in 1985 as a vice  
7 president in its accounting department. Mathiasen has been licensed as a CPA in  
8 California since 1969. His license is currently inactive.

9 **IV. TENET'S PRIOR HISTORY**

10 27. Tenet was formerly known as National Medical Enterprises ("NME").  
11 In or around July 1994, NME consented to the entry of a permanent injunction  
12 against future violations of the antifraud and reporting provisions of the federal  
13 securities laws, following a complaint filed by the Commission in federal district  
14 court alleging improper and fraudulent revenue recognition practices by NME in  
15 its psychiatric and substance abuse treatment facilities.

16 28. At about the same time, NME also entered into a settlement  
17 agreement with the United States Department of Justice ("DOJ") and the  
18 Department of Health and Human Services ("HHS") related to civil and criminal  
19 charges against NME in connection with its improper psychiatric billing practice.

20 29. As part of NME's settlement agreement with DOJ and HHS, NME  
21 agreed to pay a then record \$379 million (including a \$33 million criminal fine)  
22 and to enter into a five-year "Corporate Integrity Agreement," which required,  
23 among other things, that NME implement a corporate integrity program and retain  
24 an independent third party to audit its billing practices.

25 30. NME's Corporate Integrity Agreement expired on June 13, 1999, at  
26 approximately the same time that Tenet first began to implement the outlier  
27 scheme.

28 31. Sulzbach was primarily responsible for overseeing Tenet's

1 compliance with the provisions of the Corporate Integrity Agreement.

2 **V. DEFENDANTS' FRAUDULENT CONDUCT**

3 **A. Background: Tenet's Financial Struggles In 1999**

4 32. Tenet was struggling financially in 1999. By May 31, 1999 (the end  
5 of its fiscal year), Tenet's year-end filings showed a drop in its earnings per share  
6 to about \$1.65 from about \$1.73 the previous year. Tenet was also experiencing  
7 "anemic" cash flow by 1999. Tenet management pointed to the Balanced Budget  
8 Act, passed by Congress in 1997, which had dramatically reduced Medicare  
9 reimbursement, as a cause of Tenet's financial problems.

10 33. In or around June 1999, Mackey (who had just been appointed as the  
11 chief operating officer and co-president) and others in Tenet management decided  
12 that Tenet must "reestablish[] credibility" with investors and industry analysts.  
13 Mackey and others in Tenet's management agreed to set an earnings per share  
14 target of \$1.95 to \$2.00 for fiscal year 2000. This target represented an almost  
15 20% increase from 1999.

16 34. Mackey, along with other members of Tenet management, concluded  
17 that in order to reach the target they had set for fiscal year 2000, Tenet needed to  
18 aggressively increase its gross charges. Mackey understood that increasing gross  
19 charges would result in an increase in Tenet's Medicare outlier payments.

20 35. In the healthcare industry, gross charges are the listed retail prices for  
21 a hospital's services, but gross charges are not the same as prices. In other words,  
22 gross charges typically do not reflect what the hospital ultimately gets paid for its  
23 services. In fact, the majority of hospital reimbursement consists of fixed fee  
24 payments and is not impacted by the hospital's gross charges. In general, private  
25 insurance companies pay for hospital services based on prices negotiated between  
26 the insurance company and a hospital. In the Medicare context, the substantial  
27 majority of reimbursement consists of fixed fee payments set by the Center for  
28 Medicare & Medicaid Services ("CMMS"), the agency responsible for

1 administering the Medicare program. Such payments are generally not impacted  
2 by the gross charges of a hospital.

3 36. There are two significant components of hospital revenue that are  
4 impacted by gross charge increases: Medicare outlier payments and private insurer  
5 stop loss payments.

6 37. Medicare outlier payments are supplemental payments to hospitals  
7 that are designed to compensate hospitals for treating extraordinarily sick Medicare  
8 patients. Literally, such patients are considered statistical “outliers” in the  
9 Medicare outlier formulation because, when treating these patients, hospitals  
10 typically incur treatment costs exceeding the fixed fee payment determined by  
11 Medicare.

12 38. The Medicare formula used from at least 1999 through November  
13 2002 to calculate outlier payments included a hospital’s gross charges in  
14 determining the reimbursement paid to hospitals for providing treatment to  
15 Medicare patients.

16 **B. The Loophole in the Medicare Outlier Formula**

17 39. From at least 1999 through November 2002, the Medicare outlier  
18 calculation contained multiple steps, including thresholds designed to prevent  
19 increases in gross charges from artificially inflating the calculated outlier payment.  
20 However, Mackey and others in Tenet management identified a loophole in the  
21 outlier calculus that, in practice, allowed arbitrary increases in gross charges to  
22 cause substantial increases to the calculated outlier payment.

23 40. The loophole in the Medicare outlier calculus involved at least two  
24 components: the cost-to-charge ratio and the statewide average ratio

25 **1. The Cost-to-Charge Ratio**

26 41. The cost-to-charge ratio was intended to offset increases in gross  
27 charges so that the computed outlier amount could not be inflated by arbitrary  
28 increases to gross charges. Mackey, along with others, recognized the cost-to-

