UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 53573 / March 30, 2006

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2405 / March 30, 2006

ADMINISTRATIVE PROCEEDING
File No. 3-12251

In the Matter of
ARON R. CARR, CPA,
Respondent.

ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION’S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that public administrative proceedings be, and hereby are, instituted against Aron R. Carr, CPA (“Carr” or “Respondent”), pursuant to Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.1

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over him and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Public Administrative Proceedings Pursuant to Rule 102(e) of the Commission’s Rules of Practice, Making Findings, and Imposing Remedial Sanctions (“Order”), as set forth below.

1 Rule 102(e)(1)(ii) provides, in pertinent part, that:

The Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct.
III.

On the basis of this Order and Respondent’s Offer, the Commission finds\(^2\) that:

A. **RESPONDENT**

   Aron R. Carr, age 30, was formerly a manager at KPMG. He joined KPMG in 1997 and became a manager in September 2002. He was a senior auditor on the FY 2002 audit of Tenet Healthcare Corporation (“Tenet”). Carr is, and at all relevant times was, a certified public accountant licensed in the State of Texas.

B. **FACTS**

   1. **Tenet Healthcare Corporation**

      Tenet owns and operates acute care hospitals and related health care services. As of May 31, 2002 (Tenet’s fiscal year end), Tenet was the second-largest investor-owned hospital company in the United States, owning or operating 116 hospitals nationwide. Through FY 2002, Tenet’s fiscal year ended on May 31. At the end of the fourth quarter of FY 2002, Tenet announced that the fourth quarter was the tenth straight quarter that its earnings growth had exceeded 20%, the seventh in a row in which earnings growth had exceeded 25%, and the fifth in a row in which earnings growth exceeded 30%.

      Tenet had achieved these results through the use of an undisclosed aggressive charge strategy that it began using in FY 2000. Pursuant to this strategy, Tenet had aggressively increased its gross charges (that is, its listed retail prices) for the purpose of meeting its management-determined earnings targets. Most hospital revenue typically consists of fixed fee payments determined by government payors or by contracts with managed care companies, which are not affected by increases in gross charges. Gross charges, however, have a direct impact on Medicare outlier payments and managed care stop loss payments.\(^3\) Tenet implemented its undisclosed aggressive pricing strategy to trigger substantial increases in revenue from Medicare outlier payments and stop loss payments.

      From April 1999 through April 2002, Tenet hospitals raised charges, on average, over 75%. This resulted in a significant growth in outlier revenue for Tenet from $225 million in FY 1999 to $758 million in FY 2002, and had a dramatic impact on the company’s earnings.

\(^2\) The findings herein are made pursuant to Respondent’s Offer and are not binding on any other person or entity in this or any other proceeding.

\(^3\) Medicare outlier payments are supplemental payments designed to compensate hospitals for treating extraordinarily sick Medicare patients. Calculating outlier payments involves various steps, but the starting point for these calculations is the gross charges set by a hospital. Stop loss payments are analogous to Medicare outlier payments but arise in the managed care context. Stop loss payments typically are a percentage of the gross charges and are triggered after gross charges reach a certain level.
Tenet’s outlier revenue in 1999 represented about 27% of its earnings per share from operations and jumped to 41% when Tenet’s outlier revenue topped $758 million in FY 2002.

From FY 2000 through FY 2002, Tenet’s filings with the Commission contained no reference to Tenet’s aggressive pricing strategy of raising gross charges for the purpose of increasing revenue from Medicare outlier payments. No information was disclosed about the growth trend in outlier payments, the impact of gross charges on Tenet’s revenue, or the sustainability of its aggressive pricing strategy.

On October 28, 2002, an industry analyst from UBS Warburg published two reports disclosing that Tenet’s earnings growth had been driven by dramatically increasing outlier payments (the “UBS Reports”). The industry analyst correctly hypothesized that Tenet fueled the growth in outlier payments by significantly increasing its gross charges. The publication of the UBS Reports and Tenet’s subsequent reaction to it contributed to a loss of market capitalization of more than $11 billion.

2. KPMG’s FY 2002 Audit of Tenet’s Financial Statements

Tenet’s FY 2002 Form 10-K included its FY 2002 financial statements along with KPMG’s audit report containing an unqualified opinion stating that KPMG performed an audit in accordance with Generally Accepted Auditing Standards (“GAAS”). In August 2002, the KPMG audit partner, Clete D. Madden (“Madden”), signed and authorized the release of this audit report. Before issuing the audit report, Madden specifically verified, in the working papers, that the working papers were complete, when in fact the working papers and audit were not substantially complete.

3. The Improper Modification of Working Papers

The working papers of an audit are the principal record of the work done and the conclusions reached during the audit. See AU § 339. Shortly after the publication of the UBS Reports in October 2002, Madden began modifying the working papers by adding comments about outlier payments. He also assembled his audit team and instructed them to “clean up” the working papers. Madden continued to modify working papers, and directed the audit team to modify working papers, even after learning in November 2002 that the Department of Health and Human Services (“DHHS”) and the Commission’s staff were separately investigating Tenet and its outlier payments.4

   a. Improper Changes to Complete the FY 2002 Audit

   The audit team, including Carr, spent over 500 hours changing the working papers in November and December 2002. The audit team modified more than 350 working papers from the FY 2002 audit, including adding nine references to outlier payments. The audit team made these modifications months after Madden signed and authorized the release of the audit report on Tenet’s FY 2002 financial statements. Because of the modifications made by the audit team, it is

4 The Commission has issued a separate order addressing the conduct of the partner and senior manager on the Tenet audit engagement.
impossible to determine the actual condition of all of the working papers at the time that the FY 2002 audit report was issued.

The modifications include documenting procedures that the audit team performed in November 2002 giving the impression that additional work was done before the issuance of the audit report. For example, in November 2002, a staff member created a working paper documenting an assessment of the risk of material financial statement misstatement due to fraud. GAAS required that this assessment and documentation be done before the issuance of the audit report. See AU § 316 (2000). Carr (as well as Madden and the senior manager) then backdated his signatures on this document, giving the false impression that he had reviewed and signed this document before the issuance of the audit report.

b. **After-the-fact Creation of the FY 2001 Audit Compliance Binder**

During November 2002, Carr also improperly created eight documents that together comprise what the auditors referred to as the Compliance Binder, and that related to the FY 2001 audit. Carr was a manager when he improperly created the Compliance Binder. The purpose of the Compliance Binder was to document the procedures that tested Tenet’s healthcare compliance function. The audit team purportedly relied on the fact that Tenet was closely monitoring its compliance policies to conclude that the risk of financial statement misstatement due to fraud was mitigated.

Carr created the FY 2001 Compliance Binder by copying certain working papers from either the FY 2000 or the FY 2002 Compliance Binder and placing the copies in the FY 2001 Compliance Binder. Carr did not do any of the substantive work detailed in the FY 2001 Compliance Binder and did not know what work, if any, was performed. Carr also misleadingly created an altered “ethics” document and placed it in the FY 2001 Compliance Binder. Tenet provided a “FY 2002 Ethics Program Attendance Sheet” to the audit team during the FY 2002 Audit. In November 2002, Carr copied the sheet and placed it in the FY 2001 Compliance Binder. However, because Tenet’s document was titled “FY 2002 Ethics Program Attendance Sheet,” Carr covered up that title and pasted the title “FY 2001 Ethics Program Attendance Sheet” onto the document before he copied it. Even though Carr created the Compliance Binder in November 2002, he placed the date of July 2001 on each working paper that made up the binder.

C. **THE RESPONDENT ENGAGED IN IMPROPER PROFESSIONAL CONDUCT WITHIN THE MEANING OF RULE 102(e) OF THE COMMISSION’S RULES OF PRACTICE**

Rule 102(e)(1)(ii) of the Commission’s Rules of Practice provides, in part, that the Commission may censure or deny, temporarily or permanently, the privilege of appearing or practicing before it to any person who is found by the Commission to be lacking in character or integrity, or to have engaged in improper professional conduct. Rule 102(e)(1)(iv) defines improper professional conduct with respect to persons licensed as accountants.

As applicable here, improper professional conduct means a “single instance of highly unreasonable conduct that results in a violation of applicable professional standards in
circumstances in which an accountant knows, or should know, that heightened scrutiny is warranted.” Rule 102(e)(1)(iv)(B)(1). As explained herein, Carr acted highly unreasonably in failing to comply with GAAS by improperly modifying and creating working papers.

GAAS states that the working papers are the principal record of the work done and the conclusions reached during an audit. AU § 339. The working papers should document that the auditor has adequately planned and supervised the work, gained a sufficient understanding of internal controls, and obtained sufficient competent evidential matter to afford a reasonable basis for an opinion. AU § 339.05 (2000). It follows from the AU § 339 requirements on working papers “that any addition, deletion, or modification to the working papers after they have been finalized in connection with the completion of the audit may be made only with appropriate supplemental documentation, including an explanation of the justification for the addition, deletion or modification.”

The Commission has previously stated, “Working papers prepared or collected by auditors in the course of an audit provide the single most important support for their representation regarding compliance with [GAAS]. They serve as the repository for the competent evidential matter necessary to afford the auditors with a reasonable basis for opining on an issuer’s financial position…. It is therefore imperative that auditors preserve their working papers in a complete and unaltered form.”

As a result of the conduct described above, Carr violated applicable professional standards by inappropriately modifying working papers and improperly creating the FY 2001 Compliance Binder to evidence audit procedures that Carr knew or reasonably should have known were not performed. Carr also violated these applicable professional standards by misleadingly creating a document and placing it in the working papers.

**D. FINDINGS**

Based on the foregoing, the Commission finds that the Respondent engaged in improper professional conduct within the meaning of Rule 102(e)(1)(ii) of the Commission’s Rules of Practice. Specifically, by altering the working papers after the issuance of the audit report, after the publication of the UBS Reports, and after government investigators began looking at Tenet, Respondent engaged in highly unreasonable conduct that resulted in a violation of applicable professional standards in circumstances in which he knew, or should have known, that heightened scrutiny was warranted.

**IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in the Offer made by Respondent.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Carr is denied the privilege of appearing or practicing before the Commission as an accountant.

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B. After three years from the date of this Order, Carr may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company’s financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent’s work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

   a. Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board (“Board”) in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

   b. Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in Respondent’s or the firm’s quality control system that would indicate that Respondent will not receive appropriate supervision;

   c. Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

   d. Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.
C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission’s review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent’s character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Nancy M. Morris
Secretary