

Prosecutors Urge Dismissal Of KPMG Indictments

**Government Cites Flaw
In Tax-Shelter Action;
Tactic to Save Case Seen**

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Federal prosecutors are urging a judge to dismiss indictments against a dozen former KPMG LLP executives on charges they sold illegal tax shelters, the latest twist in what the government has billed as the biggest criminal-tax case in U.S. history.

The government's case has fared poorly since indictments were handed up in the fall of 2005, after a years-long investigation into sales of tax shelters that cost the government billions of dollars in lost tax revenue.

REVERSAL OF FORTUNE?

- **The Motion:** Prosecutors want charges dismissed against a dozen of the 18 defendants in the KPMG tax-shelter case.
- **The Backdrop:** The move comes after a ruling last year that the government violated the rights of the defendants during its investigation.
- **What's Next:** The motion could mean the 12 will never be tried. But if the judge dismisses the charges against them, the door could then open for an appeal on his initial ruling.

Last year, U.S. District Judge Lewis A. Kaplan ruled that the government had overreached in its investigation, violating the defendants' constitutional rights to counsel and due process. He also slammed prosecutors for acting improperly.

Judge Kaplan has since tried, but failed, to find a way to fix the constitutional violation without dismissing the indictments. In response to a recent suggestion for the government and defense attorneys to suggest further remedies, prosecutors argued in a filing late Friday in federal court in Manhattan that the judge's decision showed that there is a fundamental flaw in the proceedings and that he must dismiss the indictments. The upshot is that 12 of the 18 defendants may now never stand trial, including the accounting giant's former vice chairman.

"They're just giving up on everything," said David Spears, attorney for Jeffrey Stein, the former KPMG vice chairman who is the highest-ranking firm executive charged in the case. "It's just stunning and very ungovernment-like."

Some legal experts said the move actually was aimed at allowing prosecutors to appeal last year's ruling by Judge Kaplan, a tactic that may let the government resume its case against all of the defendants. "It seems they are challenging the judge," said Steven Peikin, a former federal prosecutor who is now a defense

attorney at Sullivan & Cromwell LLP. "I don't see the government going down easy."

Judge Kaplan's 2006 ruling turned on the matter of legal fees for the defendants. He ruled that prosecutors can't pressure companies to stop paying legal bills for indicted employees, and that such pressure is a violation of due-process rights.

After the ruling, the Justice Department repudiated a policy which had called for prosecutors to consider a company's willingness to stop paying legal fees for executives under investigation as a sign of cooperation that could help the organization avoid charges. Because the original ruling didn't prescribe a remedy, legal experts said, it wasn't appealable.

On Friday, consequently, prosecutors recommended that Judge Kaplan dismiss indictments against 12 of 18 defendants currently slated to stand trial in September on charges they sold and marketed tax shelters that created sham investments designed to generate paper losses so wealthy individuals could evade taxes. Prosecutors said the remaining six defendants shouldn't be affected by such a decision because they weren't involved in the wrangle over the payment of legal fees. The defendants all have pleaded not guilty.

A dismissal of the indictments based on the earlier ruling could constitute an action that would give the government grounds to appeal that groundbreaking decision. "I think it makes a lot of tactical sense," said Stephen Gillers, a New York University law school professor who has followed the case. "This gives the government an opportunity for immediate review" by the appeals court.

An appellate decision overturning Judge Kaplan's finding of a violation of the KPMG defendants' constitutional rights would let prosecutors continue with the criminal case against all 18 defendants without having to worry that a conviction could be overturned later on appeal because of the question of constitutional violations.

In arguing for a dismissal of some of the indictments of former KPMG executives, prosecutors are echoing advice recently given to Judge Kaplan by an appeals court. That court suggested that Judge Kaplan could dismiss the indictments as it quashed a plan by the judge aimed at remedying the constitutional violations by allowing the defendants to sue KPMG for their legal fees.

The next move is up to Judge Kaplan. He has scheduled a July 2 hearing to hear arguments on how to proceed in the criminal case. A decision regarding the government's argument, as well as motions to dismiss the indictments from the defendants, could be issued sometime this summer.

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