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One Family's Tale of Tax Shelter Gone Awry

Mark Schiefelbein for The New York Times

The Keeter family, which owns Royal Oak, has sued KPMG.

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Daren M. Keeter, a wiry, sandy-haired property investor in the United States Virgin Islands, received an intriguing invitation six years ago. The big accounting firm KPMG, which had audited the books of his family's charcoal company for two decades, was giving a party for its top Southeast clients in downtown Atlanta. Would Mr. Keeter like to attend?

Today, Mr. Keeter may wish that he never had gone.

The fare at the casual party was pedestrian - raw vegetables and ranch-style dip - but it was there, say papers filed in a lawsuit brought by the Keeter family, that Jeffrey Eischeid, a top KPMG tax partner and a family friend, told him about a certain "specialized financial product" that could be a profitable investment and generate tax savings as well.

Mr. Keeter, then 34, was curious. He was looking to sell his stake in the family's privately held company, Royal Oak Enterprises, and hoped to reduce his tax bill. Mr. Keeter brought the idea to his two older brothers. Seven months later, they and other family members, including Mr. Keeter's father, James, the company's chairman, pooled $188 million into the KPMG financial product.

But the product, according to the Keeters, turned out to be a sham tax shelter.

KPMG is currently in the cross hairs of a criminal investigation over the sale and promotion of bogus tax shelters. The Justice Department is weighing whether to seek an indictment of the firm - a move that would probably lead to its collapse, similar to what happened to its rival, Arthur Andersen, Enron's auditor, in 2002.

While KPMG has been in discussions with prosecutors to try to settle the criminal case, it still faces civil battles in federal and state courts across the country. Dozens of individual investors like the Keeters have filed civil lawsuits against KPMG over sham shelters that have cost them - and the Internal Revenue Service - billions of dollars.

KPMG has argued that investors knew they were taking a risk that the I.R.S. might not accept the claims.

A brief filed on behalf of Mr. Eischeid in January, called the Keeters "extraordinarily wealthy, sophisticated clients" of KPMG "who aggressively sought to minimize their tax obligations." Neither Mr. Eischeid nor KPMG, the brief contends, ever represented "that the I.R.S. would not audit" the shelter.

Among the lawsuits, the Keeter case is significant because of its size - at $188 million, it is one of the largest investor complaints over a tax shelter. It is also a rare example of an entire family buying a bogus tax shelter.

Royal Oak's charcoal is famous among grilling aficionados for its woody flavor and aroma. The company was founded by Daren Keeter's grandfather, Vester, in 1959, in Branson, Mo., when it was known as Keeter Charcoal. The company was sold to an oil company in 1973, but 10 years later Daren's father bought it back and changed the name to Royal Oak.

"When you've got some pretty high-powered firms with letters of opinion - you know, making charcoal is not a high-tech business - we rely on professionals" like KPMG to tell us what investments are legal, said Steven Keeter, who like his brother Daren is a property investor.

Last month, KPMG acknowledged "unlawful conduct" for the first time in the creation and sale of bogus tax shelters. But it is still fighting lawsuits brought by its former clients.

"We haven't received any calls from KPMG saying, 'We acknowledge that we've done wrong by your clients,' " said Gary Mauney, the lawyer for the Keeter family. "Those words are pretty meaningless to some of these families that want to lawfully pay their taxes."

A KPMG spokesman declined to comment on the case.

The tax shelter the Keeters bought was named Blips, for bond linked investment premium strategy. Never valid in the eyes of the Internal Revenue Service, Blips was one of four abusive tax shelters that the Senate Permanent Subcommittee on Investigations in 2003 found that KPMG had sold to at least 350 people from 1997 to 2001, earning fees of $124 million. Those shelters cost the Treasury at least $1.4 billion in unpaid taxes, according to the subcommittee.

According to papers filed in the Keeters lawsuit, family members met over several months in 1999 with Mr. Eischeid and with an executive from Presidio Advisors, a private investment firm that worked with KPMG to create and sell the shelter. A Wall Street law firm, then known as Brown & Wood, vouched for the legitimacy of the shelter, with glowing legal opinion letters.

In late 1999, the Keeters put $188 million into an account at Deutsche Bank. The money, used in tandem with a $500 million loan from the bank, would be used to trade derivatives and options. The Keeters say they thought that they would make an unspecified return on their investment, pay back the loan, as well as generate $188 million in tax savings that could then be legitimately used to offset other gains.

But family members said that they discovered their shelter was not legal only when the I.R.S. began auditing some of their federal tax returns - prepared by KPMG, with the Blips deductions written in - for 2000 and 2001.

The I.R.S. offered amnesty for investors in Blips shelters in 2004, and the Keeters took part in it by coming forward and disclosing their use of the shelter. Still, they face a combined tax bill, plus interest and penalties, of more than $200 million.

The Keeters are suing KPMG, along with Sidley Austin Brown & Wood, the successor to the law firm of Brown & Wood; Deutsche Bank; Presidio Advisors and related Presidio firms, along with Mr. Eischeid and a former KPMG executive who was a co-founder of Presidio, John Larson.

The lawsuit, originally filed in a Georgia court in Fulton County in October 2004, was refiled in federal court in Atlanta in March. The lawsuit, which seeks punitive damages and lawyers' fees and expenses, contends fraud, breach of fiduciary duty and conspiracy, among other charges, and says that the Keeters paid more than $12 million to all the defendants for their shelter.

The lawsuit states that the Keeters were the "unwitting prey of a sophisticated scam" with all the defendants working together to knowingly sell them a bogus tax shelter. "Defendants either knew, or were reckless and negligent in not knowing from the outset, that their Blips product would not pass muster with the I.R.S.," the complaint says.

Mr. Mauney, the lawyer for the Keeters, called the family "salt of the earth," if wealthy.

Royal Oak Enterprises declined to disclose its revenue.

KPMG and the other defendants have moved to have the case dismissed or to compel arbitration. Most of the Keeter defendants signed arbitration agreements with Deutsche Bank and KPMG. Mr. Mauney is now filing papers contending that the arbitration clauses are not valid because the tax shelter was a sham.

The brief filed in January by Mr. Eischeid called the Keeter lawsuit a "shotgun complaint," full of false allegations.

Lawyers for Sidley Austin and Presidio did not return calls for comment. Jeffery D. Horst, a lawyer for Mr. Eischeid, also did not return calls. A spokeswoman for Deutsche Bank declined to comment.

Mr. Eischeid, an architect of the Blips shelter, according to the Senate subcommittee's 2003 report, resigned from KPMG last summer.

The Keeter family members who invested in the Blips shelter include the 19-year-old daughter of James Keeter. Her trust fund assets were put into the shelter.

Daren Keeter, the co-owner of a restaurant in the Virgin Islands, an offshore tax haven, maintains that neither he nor his family knew the shelter was illegal.

"At no point did I ever understand that KPMG was advising my family to enter, with Deutsche Bank's help, an 'abusive' or 'unlawful' tax shelter," he says in a brief filed in March. "We did not agree or give our consent to contracts for an illegal tax shelter."

Mr. Mauney, when asked if Daren and the other Keeters feel betrayed by KPMG and Mr. Eischeid, responded, "When you're claiming you're defrauded, that's lawyer-speak for betrayal." Mr. Keeter bumped into Mr. Eischeid at an airport recently, Mr. Mauney said, describing the exchange between them as "chilly" and "brusque."

Still, Steven Keeter, 46, Daren's brother, said that the huge tax bills and the litigation had not caused tensions within the family. "It hasn't really changed things between us," he said, referring to the tax shelter. "We are business people, and it was a calculated risk."

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