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Former auditor grilled by ex-Met executive's lawyer

Questionable real estate deal at heart of fraud case

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"You have a motive to lie in this trial and make Mr. Turner a scapegoat" – defense attorney David Marshall

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Metropolitan Mortgage

SEATTLE – Metropolitan Mortgage & Securities Co.'s former auditor Jack Behrens once told the U.S. Securities and Exchange Commission that he thought just about everyone in the defunct Spokane company was untrustworthy.

Lawyers defending former Metropolitan Mortgage executive Thomas G. Turner seized upon Behrens' statements from 2004 to tell a jury that he was trying to deflect all blame for a major accounting scandal from his firm, Ernst & Young LLP.

"You believe Metropolitan in Spokane is full of a whole bunch of crooks," Turner's attorney, David Marshall, said of Behrens, pointing out to the jury that Ernst & Young is defending itself in at least four major lawsuits and arbitration hearings related to Met with a potential price tag in the tens of millions of dollars or more. "You have a stake in this case."

Turner is accused of lying to Behrens and other Ernst & Young auditors about a complicated real estate deal that helped Metropolitan post a $10 million gain on its books and thus report to investors and regulators that it operated as a profitable company in 2002.

The case is about more than whether one man lied to another. By misleading auditors, Turner was trying to trick the SEC, brokers and investors, alleged federal prosecutors with the fraud section of the U.S. Attorney's Office. Metropolitan had lost money in 2000 and 2001, the first red-ink years in the firm's 50-year history. More important, the company was running out of cash to pay the interest owed to bondholders and dividends due to preferred stockholders.

To solve the cash crunch, Metropolitan was seeking the OK from the SEC to issue new unsecured debenture bonds and stock.

The SEC, however, was balking, partly because Metropolitan had changed its business strategy away from seller-financed residential mortgages to subprime commercial lending and was losing money. And Washington state financial regulators relayed long-held concerns about Metropolitan's unusual business practice of relying on unsecured debenture bonds sold to unsophisticated investors as a primary means of repaying interest on older notes. Furthermore, the state, which had tightly regulated Metropolitan for decades, lost much of its authority due to new federal rules.

With pressure mounting to turn a profit in 2002, Turner struck what is now considered a notorious deal with Trillium Corp., a Bellingham timber and property development company.

Prosecutors and Ernst & Young accused Turner of lying about the true nature of the deal and hiding information. It's a crime for company executives to lie to their outside auditors.

Behrens gave tough testimony, recounting with authority how he was stunned by Turner's alleged deceit more than a year after the real estate deal went through. Ernst & Young was so troubled by the affair that it resigned and withdrew two years' worth of audit opinions.

Marshall had a different take.

He said Ernst & Young reaped more than $1 million a year auditing Metropolitan, and still more offering tax and business advice.

But when it looked like Metropolitan would struggle to get SEC approval to sell more bonds and stocks, and when regulators and others began looking more closely at the questionable real estate deal Behrens signed off on, Ernst & Young needed an exit.

"You approved the deal and told (Tom Turner) it was OK," Marshall said to Behrens. "And when trouble started you started looking for the door. Isn't that right?"

Retorted Behrens: "Absolutely not."

Marshall then continued.

"You have a motive to lie in this trial and make Mr. Turner a scapegoat," he said.

In his parting shot, Marshall looked at him and said, mockingly: "They're all liars. Everyone but you, Mr. Behrens."

Prosecutors next called on William Smith, Metropolitan's former chief financial officer, to bolster its case by testifying about his suspicions of Turner.

Metropolitan owner C. Paul Sandifur Jr., who has not been charged with crimes, hired Smith in August 2003 to better manage the company's finances. His hiring came more than a year after the firm's last CFO left.

Smith focused on complying with the SEC requests for financial information relating to Metropolitan's attempt to sell new stocks and bonds.

He also delved into a now-disallowed offshore tax shelter Metropolitan used in 1999 and 2000. As part of his efforts, he learned of an odd series of business transactions of one of Metropolitan's larger real estate and loan customers, Trillium Corp.

Smith soon learned that Trillium was paying the debts of another, supposedly independent company.

When Smith inquired why, he didn't receive a satisfactory answer, he told the jury late Friday afternoon.

His curiosity grew as he continued having conversations with Turner, who Smith said gave him information in small increments.

The conversations between the new CFO and Turner, a 19-year company veteran who had climbed his way to the No. 2 position in the Metropolitan group of companies, grew more heated, with Smith recalling one October meeting in Turner's office where both men were standing across a desk speaking at each other with "raised voices."

Smith told the jury about seeking an internal audit committee investigation of the Trillium deal when he couldn't get an answer to one critical question: Why was Trillium paying on a loan supposedly taken out by another company?

By this time Metropolitan was in financial chaos.

Smith recalled talking to Behrens on Nov. 14, 2003, about the audit investigation in an airport while returning from a meeting in New York City with potential restructuring partners Skadden Arps and Rothschild Investment.

By December, Metropolitan was in default. It filed for Chapter 11 bankruptcy in early February.