Auditors Of Lincoln On the Spot

Top Ernst Officials Will Testify Today

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WASHINGTON, Nov. 13 — As the story of the failure of the Lincoln Savings and Loan Association unfolds, Congressional investigators and regulators are beginning to focus more and more on the role of the nation's largest auditing firms in the savings and loan collapse — in particular whether the firms should be held more accountable for giving insolvent institutions clean accounting bills of health.

An important case is that of Arthur Young & Company, now called Ernst & Young, whose top officials are scheduled to appear before the House Banking Committee on Tuesday.

In 1986 and 1987, the firm gave Lincoln and its parent company, the American Continental Corporation, unqualified auditing opinions. According to House investigators, the firm did not include in any of its opinions or findings warnings about problems with Lincoln, at a time when Federal regulators in San Francisco were asserting that Lincoln was essentially insolvent.

Indirectly Aided 'Junk Bond' Sale

Helped by the Arthur Young auditors' report that American Continental's records accurately reflected its financial condition, the company was able to sell to more than 23,000 investors more than $200 million of high-risk, high-yield bonds, or "junk bonds," which are now worthless. American Continental filed for bankruptcy on April 13, 1988. A day later, regulators took control of Lincoln and soon predicted that losses at the $6 billion savings institution could exceed $2 billion, perhaps the biggest failure in the industry crisis.

Moreover, Arthur Young's partner in charge of the Lincoln account, Jack D. Atchison, left the firm in early 1988 after heading up the Lincoln and American Continental audits for two years to become a top official at the parent company, at a salary of $930,000, far above his previous salary level at the accounting firm.

Citing continuing criminal investigations in the Lincoln collapse and invoking his Fifth Amendment rights against self-incrimination, Mr. Atchison last week refused to answer questions from the Banking Committee.

Auditors' Expected Defense

On Tuesday, three of Arthur Young's top officials are expected to defend the auditing opinions as well as Mr. Atchison's actions before the committee, contending that troubles at Lincoln did not begin until after the firm resigned as Lincoln's auditors in the fall of 1988.

To be sure, Arthur Young is not the only big accounting firm to encounter such problems. The Office of Thrift Supervision, formerly the Federal Home Loan Bank Board, has sued

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two other big firms — Touche Ross for its auditing of the Beverly Hills Savings and Loan Association of Mission Viejo, Calif., and Deloitte, Haskins & Sells for its role in auditing the Sunrise Savings and Loan Association of Boynton Beach, Fla.

Earlier this year, the General Accounting Office reviewed the failure of 11 savings institutions and concluded that in six of them, accountants "did not properly audit and/or report the savings and loans' financial or internal control problems in accordance with professional standards."

Some Actions Defended

But some Government officials, while noting that accountants failed to detect problems in some savings institutions, defended some of their actions — particularly attempts by the accounting profession in the early 1980's to keep Congress and regulators from permitting the savings industry to use lax accounting methods.

"I will say that in general the accounting profession pushed for generally accepted accounting principles, over the more lax regulatory accounting priniciples," said Charles A. Bowsher, Comptroller General and head of the General Accounting Office.

Moreover, Bert Ely, a financial consultant based in Alexandria, Va., suggested that in the case of Lincoln for Arthur Young, it might have been more a matter of one partner engaging in questionable practices, rather than systemic problems at the firm.

Questions on 'Bottom Fishing'

The savings industry crisis has revived questions repeatedly raised in the past about the profession's independence in auditing big corporate clients: whether the accounts need more controls, whether some firms are willing to sanction questionable financial statements in exchange for high fees, a practice called "bottom fishing."

For Arthur Young, Lincoln was only the latest in a series of giant — and now failed — banking institutions it audited. The list includes two large insolvencies in Dallas — the collapse of Vernon Savings and Loan Association, which will cost taxpayers $1.1 billion, and the collapse of Western Federal Savings and Loan Association, which could also cost as much as $1 billion.

A spokesman for Arthur Young said officials would not be available for comment.

The Banking Committee last week released a letter from Mr. Atchison to Senator Donald W. Riegle Jr., Democrat of Michigan, in which Mr. Atchison referred to a meeting he had with Mr. Riegle to discuss accusations that bank board examiners were harrassing Lincoln officials.

In that letter, dated March 13, 1987, Mr. Atchison not only wrote that Lincoln was solvent and had received an unqualified opinion for 1986, but also complained about hostile and pejorative actions by bank board examiners.

Mr. Atchison also spoke directly with Federal regulators, attempting to intervene for Lincoln, Banking Committee staff members said.

House investigators and others have questioned the intervention by an outside auditor, warning that such actions can quickly compromise the independence of the auditor.

"Straight-line accountants and auditors are not supposed to be advocates for their clients," Mr. Ely, the financial consultant, said. "You hire lawyers for that."

Arthur Young has been named in at least one class action suit filed by investors in California, seeking damages of $250 million. It also faces possible legal action from investors in American Continental.