'I Feel Like an Idiot'

Land Project Gone Wrong Shows How Even Well-Off Lured By Go-Go Climate

By ANN CARRNS
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SPRUCE PINE, N.C. -- On a crisp fall afternoon in 2002, a crowd gathered under a big tent near the Penland School of Crafts, an artists' colony tucked in the Blue Ridge Mountains. While a harpist played, real-estate developer Tony Porter talked up a plan he promised could bring big financial payoffs to the isolated community and anyone who invested in it.

At the party and in subsequent sessions, Mr. Porter and others at his company, Peerless Real Estate Services Inc., described his vision for a 2,000-lot residential and retail development called the Village of Penland. According to people who heard the pitches and received promotional documents, Mr. Porter said the village would provide places for artists to live and sell their work to baby boomers and retirees, who were flocking to the area in droves and rapidly driving up land values. But the developer said he needed investors to launch the project in time to catch the real-estate wave. To help them get in on the action, Mr. Porter promised to arrange loans of as much as $2 million, according to offering documents and other materials circulated by Mr. Porter's company and reviewed by The Wall Street Journal.

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Penland development site with a road sign showing a proposed building; so far no houses have been built.

Even more enticing, Mr. Porter and documents promoting the project said investors would receive large cash payments -- as much as 10% of the proceeds -- when the loans closed. The investors also were promised they wouldn't have to make down payments with their own money and Mr. Porter or one of his companies would make their monthly mortgage payments for at least a year, according to the documents in a civil suit filed in June by the North Carolina Attorney General against Mr. Porter and more than a dozen associates and related companies.

The suits alleges they used inflated appraisals and phony down payments and performed other misdeeds to cheat investors and mislead the banks.

Over the next several years, investigators say, nearly 200 investors -- mostly well-heeled professionals including real-estate lawyers, doctors and Air Force officers -- borrowed more than $100 million from a handful of banks, including Winston-Salem, N.C.-based BB&T Corp., the 12th-largest U.S. bank. Nearly all of the money was turned over to Mr. Porter.

Nearly five years after the tent party, no houses have been built. Weeds are invading the lawn at the empty sales office. Payments stopped on many loans in April or May, according to borrowers and court records.

It isn't clear what happened to the money Mr. Porter collected. Some was allegedly spent on other real-estate projects and luxury trips by investors and employees of Mr. Porter's company to the Greek islands and Swiss Alps. "These developers squandered more than $100 million in financing, leaving consumers stuck with property that isn't worth what they owe on it," said Attorney General Roy Cooper.

"I feel like an idiot now," says Henry Gerrits, an engineer in Cary, N.C., who worked with Mr. Porter to borrow $375,000 and then invested it in Penland, purchasing four vacant lots.

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No one has been charged with a crime in the matter, but state and federal agents are examining the Penland project in North Carolina.

Mr. Porter's lawyer, Douglas Kingsbery, says the developer is at an unspecified location in North Carolina and unavailable to comment. He says Mr. Porter disputes allegations in the suit and "very much wants to do everything he can to make sure that all of the individuals who invested in the project receive all of their money back." The lawyer said he couldn't comment further due to the "active criminal investigation."

Most of the attention surrounding sub-prime and high-risk lending in recent months has focused on lower-income or high-risk borrowers who didn't realize they were taking loans that would be difficult to repay. But the Village of Penland project shows how the go-go climate of a real-estate boom, combined with an environment of easy borrowing, also infected well-off borrowers with healthy credit records -- many of whom now say they should have realized the deals were too good to be true.

No one has been charged with a crime, but state and federal agents are combing through the Penland project. The suit by North Carolina attorney general alleges that Mr. Porter and several associates engaged in a "continuing pattern of unfair and deceptive business practices," including using "insider sales" to artificially inflate the apparent value of the land they were selling and submitting multiple applications for loans secured by the same piece of property. The suit demands that the defendants refund the $100 million in loan proceeds borrowed by investors and repay the loans. Federal Bureau of Investigation agents have raided Mr. Porter's office. The FBI won't confirm or deny an investigation.

Jimmy Tallent, chief executive of United Community Banks Inc., Blairsville, Ga., with $24 million in loans tied to the project, says he now believes Mr. Porter's project was built on defrauding his and other banks, that many borrowers misrepresented their financial situation on loan documents and that the cash payments from the developer at the closings were improper. "When you add all of that together, that is wrong, that is fraud, that is criminal," Mr. Tallent says.

Mr. Porter, who is fond of slapping backs and sporting Hawaiian shirts, was welcomed by many in this picturesque corner of the Appalachians when he bought more than 1,200 forested acres in 2002. His credibility was bolstered by a $16 million loan obtained in 2005 from a predecessor of Alesco Financial Inc., a lender based in Philadelphia, that was used at least partly to get the North Carolina project underway. Alesco declined to comment.

Mr. Gerrits became intrigued when a real-estate broker in Charlotte, N.C., emailed him in December 2005 saying Village of Penland promised "guaranteed" returns of up to $2.5 million. Soon, he and about 35 prospective investors attended a meeting with Mr. Porter. Mr. Gerrits and other investors say Mr. Porter told brokers and investors he could arrange loans from local lenders and major banks, such as BB&T, United Community Banks Inc. and First Charter Corp. In one scenario, participants could buy as many as 10 lots for $125,000 apiece -- or a total of $1.25 million per investor -- and receive as much as $250,000 cash back at closing, according to court filings.

Mr. Gerrits says Mr. Porter's company, Peerless Real Estate Services Inc., helped him arrange two loans totaling $375,000. He bought four lots at Penland.

Mr. Gerrits says he was duped by Mr. Porter. He declined to say whether he received a cash payment at his loan closings.

Sherron Shields, of San Leandro, Calif., heard about the Village of Penland through a friend in July 2006. The 38-year old loan officer in Oakland, Calif., agreed to buy eight lots. She let his company help arrange for her to borrow a total of more than $900,000 from four banks, ranging from $175,000 to $272,000. At the closing, Ms. Shields also received $160,000, which she says she believed was payment for the one-year lease on the lots.

One of the first signs of trouble came in an email to some investors last year. Mr. Porter said the lots they had purchased weren't rising in value as quickly as predicted. Then Ms. Shields and other investors got a letter from Mr. Porter stating that he couldn't afford the mortgages, citing the "significant downturn" in the U.S. real-estate market.

Ms. Shields tried to sell her lots. But appraisers laughed when she revealed what she had paid for them. Investigators now say many lots sold for as much as $125,000 are actually worth no more than $20,000.

The four banks now are demanding that Ms. Shields make the loan payments, totaling about $9,000 a month. "This whole thing has really traumatized me," she says. "I had great credit, I pay my debts. This isn't how I do business."

Rachel Dollar, a Santa Rosa, Calif., attorney and expert on lending fraud, says borrowers didn't break the law unless they knowingly misrepresented their financial situation on a loan application -- such as by concealing other loans they were simultaneously obtaining or falsely calling the proceeds of a second loan a cash down payment. "If all they were doing was not exercising due diligence, they can't be held criminally liable," says Ms. Dollar, who has no connection to the Penland situation.

Attorneys for the borrowers say they are trying to reach deals with the banks to avoid having their clients' assets seized.

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