Lee Bentley Farkas, former chairman of Florida based Taylor, Bean & Whitaker has been indicted on bank fraud and other charges. Taylor Bean was one of the nation's largest privately held mortgage lending companies and has been under bankruptcy protection for the past year. Farkas and co-conspirators misappropriated more than $400 million from Colonial Bank (their banking institution) and $1.5 billion from a Taylor Bean owned firm to cover operating losses. Farkas has also been charged of trying to defraud the government out of $553 million in Troubled Asset Relief Program funds.

You may view the article at: http://www.washingtonpost.com/wp-dyn/content/article/2010/06/16/AR2010061603438.html

In the following analysis I would like to examine various aspects of fraud examination. I would like to analyze the application of the fraud triangle to the article. The various aspects of fraud recruitment will be discussed. Fraud detection will be touched upon and finally fraud prevention will be examined in this case.

The fraud triangle presents us with three aspects of a fraud to begin an examination with: perceived pressure, opportunity, and rationalization. In this article the perceived pressure is work related pressure and financial pressure. The pressure is to cover up operating losses. The financial pressure is greed and living beyond ones means. Farkas obviously wants more than is salary can provide him with so he turned to embezzlement to fulfill his greed. The opportunities in this instance are ignorance, apathy, and incapacity, lack of controls that prevent and/or detect fraudulent behavior, and lack of access to information. With regard to ignorance, apathy, and incapacity, Colonial bank was unaware of the losses that were being fraudulently covered up at Taylor Bean by Farkas when Farkas began to assist colonial with receiving TARP funds as a result of their poor financial position. The lack of controls that prevent and/or detect fraudulent behavior in this case is that management went undetected and was able to successfully steal $20 million in funds from the bank for personnel use without being detected. Further, control procedures over documents and records possibly lacked a proper system of authorizations that lead to Farkus being able to destroy evidence of his embezzlement of $20 million and falsify documents in order to make Colonial look healthier than it was. The lack of access to information allowed hundreds of millions of dollars to be shuffled amongst firms avoiding internal controls of each firm in order to improve the reported financial position of Colonial. Rationalizations that Farkas rationalized that the money that was available from TARP was something that he was entitled to in order to help colonial get since its purpose was to bail out ailing banks. Farkas may have rationalized that he deserved the money he embezzled because he was overworked in his position and deserved more from the company or he may have thought since he was a big cheese that he deserved personal amenities like a private jet and three personnel properties. He also may have rationalized that he would be able to fix the fraud he was perpetrating within Taylor Bean and Colonial once Colonial obtained the TARP funds and began to recuperate their losses.

With regard to fraud recruitment, power may have been a way that Farkas influenced his conspirators to participate in his scam. He may have used the power to reward them with his embezzled millions to entice them into cooperating with his scheme. Coercive power may have been used by Farkas in a manner such as you do it or you are fired and his conspirators eventually got in over their heads. Farkas may have used his legitimate power as chairman to influence the employees to do what they were told regardless of their responsibilities in the organization as a result of his absolute authority. Referent power could have been a possible influence as the conspirators may have related to him that they deserved more from the organization or that they were overworked too much.

Concerning fraud detection, fraud was detected in this instance by chance when a special inspector general for the Treasury Department detected the fraud. However, the failure of fraud detection within Taylor Bean may have been the result of transaction records and documents not being examined thoroughly within Taylor Bean by the internal audit department and the independent auditor since documents were being falsified.

Factors in fraud prevention that may have helped prevent fraud within Taylor Bean are having a positive work environment including having a well defined code of conduct, which may have deterred Farkus' conspirators, an open-door policy coupled with an employee assistance program may have brought the co-conspirators to confess their involvement during the early stages of the fraud if there was someone to talk too, and a low fraud atmosphere which may have also helped deter Farkus' conspirators from participating in the fraud. In this instance internal controls that could have helped prevent the fraud were circumvented by collusive fraud between Farkas and coconspirators at Colonial. Coconspirators at Colonial helped Taylor Bean run up tens of millions of dollars in overdrafts. These overdrafts were then hidden by Colonial buying more than $400 million in fake mortgage assets from Taylor Bean, including loans that Taylor Bean had already sold. This method of collusion made it very difficult to detect the fraud, however if there was an independent verification of the ownership of the securities perhaps the purchase of previously owned securities could have been avoided and the fraud could have been discovered at this point. A policy of discouraging collusion at Colonial between employees and others could have also been effective in this fraud. This type of policy could have also been implemented at Taylor Bean in such a manner that customers were alerted to an antifraud policy and perhaps this would have discouraged the coconspirators at Colonial from becoming involved with Farkas. An expectation of punishment is being created by the authorities in manner that communicates that abuse of Tarp funds and fraud will not be tolerated. It would be wise for Taylor Bean and Colonial to use Farkus and his coconspirators as an example to create the expectation of punishment within their organizations for when they emerge from bankruptcy. A proactive fraud auditing program may have also helped prevent this fraud if one was not in place. It may have helped identify the exposure to fraud that Colonial had as a result of them not checking the ownership of securities and could have led to an investigation.

We can see from the fraud triangle that there are various aspects that led to the development of this fraud. Fraud recruitment also played an important role in this fraud is it involved coconspirators. Fraud detection in this case was not effective and the lack of it resulted in the bankruptcy of Taylor Bean and Colonial. Fraud prevention in this instance could also improve to mitigate fraud more effectively at Taylor Bean and Colonial in the future.