UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA ALEXANDRIA DIVISION

:

SECURITIES AND EXCHANGE

:

COMMISSION,

Civil Action File No.

1:10cv667

LEE B. FARKAS,

v.

:

Defendant.

Plaintiff,

COMPLAINT FOR INJUNCTIVE AND OTHER RELIEF

Plaintiff, Securities and Exchange Commission ("Commission"), files this Complaint and alleges as follows:

SUMMARY

- 1. From approximately March 2002 through August 2009, Defendant Lee B. Farkas ("Farkas") engaged in a pattern of fraudulent conduct for the purpose of selling at least \$1.5 billion of fictitious and impaired residential mortgage loans from Defendant Farkas' company, Taylor, Bean and Whitaker Mortgage Corp. ("TBW") to Colonial Bank, and for Colonial Bank, and its publicly traded parent company, The Colonial BancGroup, Inc. ("BancGroup"), to falsely record these fictitious and impaired mortgage loans as high quality assets.
- 2. Defendant Farkas continued this pattern of fraudulent conduct by attempting to defraud the U.S. Department of Treasury's Troubled Asset Relief Program ("TARP").

 Defendant Farkas represented directly to BancGroup and to the public in a series of press releases that TBW had secured a \$300 million equity investment in BancGroup that would allow

BancGroup and its wholly owned subsidiary, Colonial Bank, to qualify for approximately \$550 million in TARP funds (the "Capital Infusion"). The Capital Infusion, however, was a sham orchestrated by Defendant Farkas. Contrary to his representations to BancGroup and to the investing public, he had never secured financing or sufficient investors to fund the transaction.

3. Through his conduct, Defendant Farkas has engaged, and unless restrained and enjoined by this Court, will continue to engage in acts and practices that constitute and will constitute violations of the antifraud provisions of Section 17(a) of the Securities Act of 1933 ("Securities Act") and [15 U.S.C. § 77q(a)] and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]. Defendant Farkas, has further engaged, and unless restrained and enjoined by this Court, will continue to engage in acts and practices that constitute and will constitute violations, as well as aiding and abetting violations, of the reporting, books and records and internal control provisions of Sections 13(a), 13(b)(2)(A), 13(b)(2)(B) and 13(b)(5) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), 78m(b)(2)(B) and 78m(b)(5)], and Rules 12b-20, 13a-1, 13a-11, 13a-13, 13b2-1 and 13b2-2 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-1, 240.13a-13, 240.13b2-1].

JURISDICTION AND VENUE

4. The Commission brings this action pursuant to Sections 20 and 22 of the Securities Act [15 U.S.C. §§ 77t and 77v] and Sections 21(d) and 21(e) of the Exchange Act [15 U.S.C. §§ 78u(d) and 78u(e)], to enjoin Defendant Farkas from engaging in the transactions, acts, practices, and courses of business alleged in this complaint, and transactions, acts, practices, and courses of similar purport and object, for disgorgement with prejudgment interest thereon, civil penalties and for other relief.

- 5. This Court has jurisdiction over this action pursuant to Sections 20 and 22 of the Securities Act [15 U.S.C. §§ 77t and 77v] and Sections 21(d), 21(e), and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e) and 78aa].
- 6. Defendant Farkas directly and indirectly, made use of the mails, the means and instruments of transportation and communication in interstate commerce and the means and instrumentalities of interstate commerce in connection with the transactions, acts, practices, and courses of business alleged in this complaint.
- 7. Certain of the transactions, acts, practices, and courses of business constituting violations of the Securities Act and the Exchange Act occurred in the Eastern District of Virginia. The fraudulent conduct of Defendant Farkas directly caused BancGroup to transmit and to file multiple false and misleading Forms 10-K, 10-Q and 8-K to the Commission's electronic data gathering, analysis and retrieval system ("EDGAR"), the servers of which are physically located within the Eastern District of Virginia.
- 8. Defendant Farkas unless restrained and enjoined by this Court, will continue to engage in the transactions, acts, practices, and courses of business alleged in this complaint, and in transactions, acts, practices, and courses of business of similar purport and object.

DEFENDANT

9. <u>Lee B. Farkas</u> is 57 years of age and is a resident of Ocala, Florida. Until August 2009, Farkas was the chairman and majority owner of TBW.

RELATED ENTITIES

10. <u>Taylor, Bean & Whitaker Mortgage Corp.</u>, is a privately-held Florida corporation organized in 1982 and headquartered in Ocala, Florida. TBW expanded rapidly, and by 2008, was the largest non-depository mortgage lender in the United States.

- 11. On August 24, 2009, TBW filed a voluntary Chapter 11 bankruptcy petition, operating as a debtor-in-possession.
- 12. The Colonial BancGroup, Inc., is a Delaware corporation organized in 1974 as a bank holding company and is currently head-quartered in Montgomery, Alabama. Colonial Bank is a wholly-owned subsidiary of BancGroup and was its primary operating division. As of August 14, 2009, Colonial Bank had approximately 350 bank branches, located in Alabama, Florida, Georgia, Texas and Nevada, customer deposits of approximately \$18 billion, and total assets of approximately \$23 billion making it one of the fifty largest banks in the United States. On August 14, 2009, the Alabama State Banking Department seized Colonial Bank and appointed the Federal Deposit Insurance Corp. (the "FDIC") as receiver.
- 13. Subsequent to the closure, an unrelated financial holding company assumed substantially all of Colonial Bank's deposits and purchased approximately \$22 billion of Colonial Bank's assets in a transaction facilitated by the FDIC.
- 14. Following Colonial Bank's seizure and sale, BancGroup filed a voluntary Chapter 11 bankruptcy petition, operating as a debtor-in-possession.
- 15. BancGroup's common stock currently is registered with the Commission pursuant to Section 12(g) of the Exchange Act. During the relevant period, BancGroup's securities were registered pursuant to Section 12(b) of the Exchange Act and were listed on the New York Stock Exchange ("NYSE") under the symbol "CNB" until the NYSE suspended trading on August 17, 2009. BancGroup's stock currently is quoted on a quotation medium utilized by Pink OTC Markets, Inc. under the symbol CBCGQ.PK.

FACTS

Colonial Bank's Relationship with TBW

- 16. Colonial Bank's operating divisions consisted of its regional banking groups and the Mortgage Warehouse Lending Division (the "MWLD"). The MWLD provided short-term funding to residential mortgage originators, who typically lacked sufficient assets of their own to fund the mortgage loans they originated. The MWLD has historically been a major income source for BancGroup, and between 2005 and 2009, accounted for no less than 21% of BancGroup's reported net income.
- 17. The MWLD's largest customer was TBW, a privately-held mortgage company based in Ocala, Florida and controlled by its majority owner and chairman, Farkas. In 2008, TBW was the nation's largest non-depository mortgage lender, originating more than \$30 billion in loans. TBW's primary business operations included the origination, acquisition, sale and servicing of residential mortgages. The bulk of the residential mortgage loans that TBW originated flowed from its contracted network of small, local mortgage brokers and banks.
- 18. TBW's most valuable asset, and one of its primary sources of revenue, consisted of its right to service the mortgages that it originated and typically sold to the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac") (collectively, the "Agencies"). TBW typically valued these mortgage servicing rights in excess of \$500 million on its financial statements.
- 19. As a loan servicer, TBW was required to collect and segregate principal, interest, and designated escrow amounts (such as insurance and property taxes) from the payments by the underlying mortgage borrower and to properly disburse such amounts to the ultimate investor in the mortgage loans, once the loans were sold. TBW's servicing rights entitled it to retain a portion of these amounts as fee for the services provided. In order to act as a loan servicer for

the Agencies and to retain the servicing fees, however, TBW was still contractually obligated to make all required payments to the ultimate investors until an event of default.

- 20. TBW generally did not have sufficient capital to internally fund the mortgage loans it originated. TBW thus relied on various financing arrangements, primarily with Colonial Bank's MWLD, to fund such mortgage loans.
- 21. Pursuant to one of these financing arrangements, referred to as the "COLB" Agreement, Colonial Bank purchased a 99% interest in certain residential mortgage loans originated by TBW. When TBW sold these loans to Colonial Bank, it represented that they were of a certain quality and that there was a commitment from a third-party investor to ultimately purchase the loan. When that investor purchased the loan, the proceeds would be used to repay Colonial Bank for the funding advance. TBW represented that it typically re-sold loans financed under the COLB Agreement to a third-party within 90 days after the loan was originated.
- 22. Another financing arrangement was referred to as the Assignment of Trade or "AOT" Agreement. Pursuant to this arrangement, Colonial Bank purchased a 99% participation interest in a bundled group of mortgage loans, referred to as a "trade," that had been pre-certified as mortgage-backed securities that TBW would issue, market and re-sell to a third-party. These participation interests under the AOT Agreement constituted securities under the Securities Act and the Exchange Act.
- 23. TBW certified each trade as either an "Agency" trade (<u>i.e.</u>, to be purchased by Fannie Mae or Freddie Mac) or a "private label" trade (<u>i.e.</u>, to be purchased by a non-government-related institution). To sell a trade to Colonial Bank under the AOT Agreement, TBW had to provide evidence of a binding commitment from a third-party investor to purchase

the trade from Colonial Bank within a specified period of time, usually between 30 days (if certified as an Agency trade) or 60 days (if certified as a private label trade).

- 24. When Colonial Bank purchased a trade from TBW pursuant to the AOT Agreement, Colonial Bank's accounting systems no longer tracked or identified the individual mortgage loans that comprised that trade.
- 25. Loans that Colonial Bank purchased under the COLB Agreement were recorded in Colonial Bank's internal accounting records in the "COLB Account" and ultimately included as assets on BancGroup's balance sheet, in an account entitled "Loans Held for Sale."
- 26. Trades purchased under the AOT Agreement were recorded in Colonial Bank's internal accounting records in the "AOT Account" and ultimately reflected as assets on BancGroup's balance sheet as "Securities Purchased under Agreements to Resell." TBW was the only MWLD customer that utilized an AOT arrangement and, as a result, all of the assets listed in the AOT Account originated from TBW.
- 27. By 2007, the total amount of financing that Colonial Bank had outstanding to TBW, primarily under the COLB and AOT arrangements, was approximately \$3.5 billion, almost 82% of the \$4.3 billion in total MLWD assets that Colonial reported in its 2007 Form 10-K.

The Fraud to Alleviate TBW's Cash Flow Problems

- 28. Beginning in the first-quarter of 2002, TBW began to experience liquidity problems, primarily because the cash generated from its mortgage servicing rights was insufficient to cover its growing business.
- 29. Around this time, TBW began to overdraw its then limited warehouse line of credit with Colonial Bank by approximately \$15 million each day. Defendant Farkas, who

controlled TBW, pressured an officer of Colonial Bank (the "Colonial Bank Officer") to assist in concealing TBW's overdraws.

- 30. Defendant Farkas, with the assistance of the Colonial Bank Officer, thereafter began a pattern of "kiting" in TBW's accounts at Colonial Bank, whereby certain debits to TBW's warehouse line of credit were not entered until after credits due to the warehouse line of credit for the following day were entered. This kiting activity increased in scope such that by December 2003, TBW was overdrawing its accounts with Colonial Bank by approximately \$150 million on a nearly daily basis.
- 31. Recognizing the continued difficulty in concealing this initial fraudulent conduct,
 Defendant Farkas, with the assistance of the Colonial Bank Officer, devised a plan whereby
 TBW would create and submit fictitious loan information to Colonial under the COLB
 Agreement.
- 32. On or around December 11, 2003, Defendant Farkas directed TBW to submit approximately \$150 million in non-existent loans for funds advancement from the COLB Account. Defendant Farkas referred to these fictitious COLB loans as "Plan B."
- 33. Additional drains on TBW's cash arose when Agencies or individual third-party investors occasionally determined that certain mortgage loans they had purchased from TBW did not qualify under their respective purchase agreements with TBW. When this occurred, TBW was required to refund the investor, but was still obligated to repay Colonial Bank for advancing the funds to make these now unmarketable, aged and/or impaired loans. These loans, along with significantly aged loans (which were also likely impaired in value), foreclosed loans and real estate owned by virtue of foreclosure sales (which were also significantly impaired), along with paid-in-full loans (which had no value whatsoever since there was no future payment stream)

were referred to by Defendant Farkas as the "Crap," and were sold by TBW to Colonial Bank pursuant to the COLB arrangement.

- 34. As a direct result of Defendant Farkas' misconduct, fictitious Plan B loans and significantly impaired Crap loans purchased by Colonial Bank were typically represented as high-quality assets on BancGroup's financial statements and carried at par value.
- 35. In 2004, as the Plan B and Crap loans in Colonial Bank's COLB Account began to increase in number and to age further, Defendant Farkas, with the assistance of the Colonial Bank Officer, devised a plan to conceal these loans. Defendant Farkas, with the assistance of the Colonial Bank Officer, created fictitious trades that consisted of Plan B or Crap loans and rolled these loans from the COLB Account to trades on the AOT Account. Once on the AOT Account, Colonial Bank's accounting systems could not identify the individual loans, or the age of those loans, within that trade.
- 36. Because the fictitious trades containing Plan B or Crap loans could not readily be sold to third-party investors, Defendant Farkas, with the assistance of the Colonial Bank Officer, utilized several manipulative and deceptive devices to conceal these trades as they aged on the AOT Account. For example, from approximately 2004 onward, Defendant Farkas directed that information be provided to Colonial Bank that, with the assistance of the Colonial Bank Officer, would alter Colonial Bank's accounting records and "reset" the commitment dates on certain trades and modify the identifying trade numbers, making it appear that Colonial Bank had only recently purchased those trades and their third-party commitments had not expired. On other occasions, Defendant Farkas directed that information be provided to Colonial Bank that, with the assistance of the Colonial Bank Officer, would "refresh" trades, by re-entering trades on the

AOT Account that had recently been sold to a third-party and then back-filling these re-entered trades with Plan B or Crap loans.

- 37. TBW's cash flow problems intensified in or around 2007, when a private label purchaser reneged on its obligation to purchase an approximately \$600 million trade held in the AOT Account (the "Failed Trade"). TBW was unable to immediately repackage and resell the Failed Trade and therefore was unable to repay its contractual obligations to Colonial Bank for advancing the funds necessary to make the underlying loans in the first place. TBW ultimately sub-divided the Failed Trade into smaller trades and individual loans and was able to timely sell a portion of the Failed Trade. Defendant Farkas, with the assistance of the Colonial Bank Officer, thereafter recycled the remaining portion of the Failed Trade, approximating \$300 million of now aged loans, into smaller Crap trades on the AOT Account.
- 38. By the end of 2007, and continuing through 2009, Colonial Bank's AOT account had approximately \$500 million in completely unsecured Plan B loans and an additional approximately \$1 billion in Crap loans.
- 39. A subset of the Plan B and Crap loans inured directly to the benefit of Defendant Farkas as either personal mortgage loans for his benefit, commercial mortgage loans for his benefit, or mortgage loans made to friends of Farkas.

The Fraud Causes BancGroup to Misstate Its Assets

40. As of BancGroup's last Form 10-Q filed with the Commission, via the EDGAR system, for the period ended March 31, 2009, Colonial reported \$26 billion of total assets, including MWLD assets of \$4.9 billion. The MLWD assets consisted primarily of \$2.7 billion in Loans Held for Sale (COLB) and \$1.6 billion in Securities Purchased under Agreements to Resell (AOT). At the time of filing this Form 10-Q, the entirety of the AOT Account (\$1.6 billion) was comprised of trades consisting primarily of fictitious Plan B and Crap loans.

- 41. At the time of Colonial Bank's seizure in August of 2009, most if not all of the trades in the AOT Account, representing assets of \$1.6 billion on BancGroup's financial statements, failed to contain the underlying collateral to either support the values entered into Colonial Bank's accounting systems by the MWLD or be capable of being sold to either the Agencies or any third-party.
- 42. BancGroup's disclosures on mortgage warehouse assets in its filings with the Commission contained numerous material misrepresentations as a direct result of the fraudulent conduct of Defendant Farkas. Defendant Farkas knew that his conduct would cause BancGroup's false and misleading statements within its financial statements and reports filed with the Commission via the EDGAR system.
- 43. Specifically, BancGroup's 2007 to 2009 annual, quarterly and current reports filed with the Commission, as a result of Defendant Farkas' fraudulent conduct, wrongly represented at various points that:
 - (1) The MWLD assets are "secured by high quality mortgage loans";
 - (2) Securities Purchased Under Agreements to Resell (AOT) "represent mortgage backed securities which have been securitized by [TBW] and are under agreements to be sold to third-party investors";
 - (3) The MWLD's customers "are experiencing no difficulty in selling their production in a timely fashion"; and
 - (4) The MWLD is "has not had any credit or other loss ... since the initiation of the unit in 1998."
- 44. BancGroup also frequently referenced the significance of the MWLD in various press releases and referenced the "excellent credit quality" of the real estate assets within the

- MWLD. Defendant Farkas' fraudulent conduct directly resulted in BancGroup's misrepresentations regarding the credit quality of the MWLD.
- 45. During a fourth quarter 2008 earnings call with analysts, senior BancGroup officers emphasized the company's commitment to the mortgage warehouse business, noting that it had "strong profitability even during . . . a very difficult mortgage market." Also, a January 27, 2009 press release announcing the company's 2008 financial results stated that "Colonial's support of warehouse lending is essential to the [housing] industry.... The division is highly profitable with minimal credit losses." Defendant Farkas' fraudulent conduct directly resulted in BancGroup's misrepresentations regarding the MWLD's profitability.
- 46. Defendant Farkas' fraudulent conduct also caused BancGroup to materially understate its allowance for loan losses ("Loss Allowance"), and therefore, overstate its reported net income. Defendant Farkas' fraudulent conduct further caused BancGroup to record the advances to TBW as assets that would be quickly sold to third-parties, rather than either unsecured loans to a company with severe liquidity problems (Plan B loans) or secured loans for which the underlying collateral might be impaired (Crap loans). BancGroup did not record any increases to the Loss Allowance in connection with these assets. Reclassifying the MWLD assets in an appropriate fashion would have impacted BancGroup's Loss Allowance and earnings in a material fashion.
- 47. Defendant Farkas also routinely signed and returned confirmations to BancGroup's outside auditors, in which he confirmed the amounts TBW had outstanding under the various financing arrangements with Colonial Bank, including the COLB and AOT arrangements. In those confirmations, Defendant Farkas represented that the information was

"complete and accurate," without disclosing that substantial sums in the AOT and COLB balances represented Plan B and Crap loans.

<u>Fraudulent Use of the Ocala Funding Commercial Paper Facility to</u> **Pay-Down TBW's Debt to Colonial Bank and Obtain Additional Capital**

- 48. Defendant Farkas initially hoped that, by increasing the amount of mortgage originations, TBW could generate sufficient revenues from its mortgage serving rights to resolve its cash shortfalls and repay the funds Colonial Bank had advanced for the Plan B and Crap loans. However, when the revenues proved inadequate, Defendant Farkas employed additional manipulative and deceptive devices to pay down debts to Colonial Bank. Under one such pattern of conduct, Defendant Farkas utilized Ocala Funding, LLC ("Ocala Funding"), a subsidiary wholly-owned by TBW that raised capital from investors to purchase mortgages from TBW, in a fraudulent manner.
- 49. In an effort to conceal the fact that Crap and Plan B loans on BancGroup's books were not being sold, Defendant Farkas directed the diversion of funds from Ocala Funding, thereby defrauding the two institutions that had invested in that firm. Between 2007 and 2009, Ocala Funding obtained cash by issuing \$1.75 billion in commercial paper to two institutional investors (the "Ocala Investors"). The commercial paper was secured by the mortgages that Ocala Funding acquired from TBW, plus the proceeds from the sale of any mortgages to third-party investors.
- 50. As initially contemplated, Ocala Funding purchased mortgages originated by TBW that Colonial Bank had acquired under the COLB arrangement. Ocala Funding was repaid when a third-party purchaser, usually Freddie Mac, ultimately acquired those mortgages. The proceeds from the sale of these mortgages were to be deposited in an Ocala Funding account (the "Ocala Investors Account"). The collateral agent for the Ocala Investors Account was required

every 30 days to confirm that the commercial paper remained fully secured (<u>i.e.</u>, the value of the mortgages held by Ocala Funding plus the proceeds in the Ocala Investors Account were no less than the value of the commercial paper outstanding). Once the collateral agent determined that the commercial paper was fully secured, the commercial paper would be renewed for another 30 days.

- 51. Defendant Farkas exploited TBW's control over Ocala Funding to divert substantial sums from Ocala Funding to cover TBW's existing cash needs. Specifically, Defendant Farkas frequently directed that the Ocala Funding collateral agent be instructed to disburse funds from the Ocala Investors Account to TBW's operating accounts to pay-down unrelated obligations to Colonial Bank or other creditors.
- 52. Defendant Farkas affected this fraudulent activity primarily by directing that the collateral agent be sent falsified collateral lists that misrepresented the loans held by Ocala Funding. Many of these loans had already been sold to Freddie Mac. Notably, Colonial Bank's records indicated that it continued to own many of these loans. Thus, as a result of Defendant Farkas' fraudulent conduct, Colonial Bank, the collateral agent, the Ocala Investors, and Freddie Mac have competing claims to approximately \$1 billion of mortgage loans originated by TBW.

Fraud to Obtain TARP Funds

- 53. In addition to directly causing BancGroup to misrepresent its assets, Defendant Farkas employed a further series of manipulative and deceptive devices that resulted in BancGroup misrepresenting publicly, as well as to the U.S. Department of Treasury's TARP, that it had obtained commitments for the \$300 million Capital Infusion, which was a prerequisite for Colonial Bank to receive TARP funds.
- 54. Colonial Bank applied for TARP funds in advance of the U.S. Department of Treasury's November 14, 2008 initial deadline. On December 2, 2008, two hours before trading

closed, BancGroup issued a press release, thereafter filed in a Form 8-K, in which it announced that it had obtained preliminary approval to receive \$550 million of TARP funds. BancGroup's stock price jumped 54% in the remaining two hours of trading, representing the largest one-day price increase since 1983.

- 55. On January 27, 2009, BancGroup issued a press release, and thereafter filed a Form 8-K with the Commission attaching the press release, announcing that Colonial Bank's receipt of TARP funds was conditioned upon increasing equity by \$300 million.
- 56. The success of the Capital Infusion was critically important to both BancGroup and TBW, as ongoing capital issues had become the largest issue at Colonial Bank. For TBW, Colonial Bank remained its primary source of operating capital, and Defendant Farkas went so far as to tell BancGroup that if the TARP funds were not obtained, TBW would go bankrupt.
- 57. In early February 2009, Defendant Farkas approached Colonial Bank with an offer to organize an investment group to raise the entire \$300 million Capital Infusion.
- 58. Though not disclosed publicly at the time, the initial break-down for the investor group was to be as follows: (a) TBW would contribute \$150 million; (b) two private equity or investment firms solicited by TBW would each contribute \$50 million; and (c) a "friends and family" investor group consisting of Colonial Bank's MWLD customers and several of TBW's correspondent mortgage network lenders (the "Friends and Family") would contribute a combined \$50 million. The Friends and Family investor group was jointly solicited by Defendant Farkas and the Colonial Bank Officer.
- 59. TBW's ability to participate in the Capital Infusion was a sham led by Defendant Farkas. Defendant Farkas repeatedly misrepresented to BancGroup and to the Friends and

Family investors that a foreign held investment bank (the "Investment Bank") had committed to finance TBW's equity investment in Colonial Bank, when it had not.

- 60. For example, on March 20, 2009, while Defendant Farkas and the Colonial Bank Officer were actively soliciting the Friends and Family investors, Defendant Farkas sent an email to the Colonial Bank Officer that misrepresented the Investment Bank's involvement, stating: "Our financing with [the Investment Bank] is in the approval process. I expect final approval next week. I am very confident that this process will proceed smoothly. The loan docs are being finalized this weekend."
- 61. On March 27, 2009, in the midst of a BancGroup board meeting focused on the Capital Infusion, a senior BancGroup officer e-mailed Defendant Farkas, asking: "Did [the Investment Bank] approve [y]our loan today?" Defendant Farkas immediately e-mailed back that the "financing is in place for the \$150mm." The senior BancGroup officer concurrently announced Defendant Farkas' representation to those in attendance at BancGroup's board meeting.
- 62. In truth, although Defendant Farkas approached the Investment Bank with the possibility of participating in an equity investment capacity, or financing TBW's investment, the Investment Bank never committed to or told anyone that it would invest in or finance TBW's participation in the Capital Infusion.
- 63. Defendant Farkas further misrepresented to BancGroup that TBW had secured all the necessary commitments from third-parties to invest \$300 million in Colonial Bank. TBW delivered to BancGroup, on March 31, 2009, a stock purchase agreement to consummate the Capital Infusion (the "Stock Purchase Agreement"). Farkas signed the agreement on behalf of

TBW and its investor group, knowing that the representations therein regarding investor commitments were false.

- 64. Within the Stock Purchase Agreement, TBW misrepresented that it had obtained commitments from two private equity sources (the "\$50 Million Investors") that it identified by name within Schedule 1 to the Stock Purchase Agreement, to each invest \$50 million in the Capital Infusion. TBW specifically warranted to BancGroup the identity of each investor and the amount each investor had agreed to invest. In truth, neither of the \$50 Million Investors were private equity investors and neither ever agreed to participate in the Capital Infusion.
- escrow account an amount equal to ten percent of such [investor's commitment]." The escrow account was maintained at Platinum Community Bank, a thrift that was wholly-owned by TBW. Before issuing any public announcement regarding the Capital Infusion, BancGroup's senior management reviewed the escrow account to ensure that the investors had complied with this obligation. In an effort to convince BancGroup and Colonial Bank's regulators that TBW had obtained sufficient commitments, Defendant Farkas instructed the commencement of what was referred to internally as "Project Squirrel" designed to divert money from the Ocala Investors Account to the Capital Infusion escrow account. Further pursuant to Project Squirrel, TBW provided BancGroup with a summary of escrow deposits, which falsely represented that the \$50 Million Investors had each deposited \$5 million into the escrow account. Neither of the \$50 Million Investors, however, ever agreed to participate in the Capital Infusion or made such escrow deposits.
- 66. Based on the fraudulent conduct of Defendant Farkas, BancGroup executed the Stock Purchase Agreement late in the day of March 31, 2009 and issued a press release that same

day announcing its entry into a "definitive agreement" with the TBW-led investor group.

Defendant Farkas reviewed and approved BancGroup's press release before it was disseminated.

- 67. Defendant Farkas and TBW also issued their own press release on March 31 regarding the Capital Infusion. The caption of TBW's release stated "[TBW] leads investor group in signing definitive agreement for a \$300 million investment in Colonial BancGroup" [sic]. TBW's release quoted Defendant Farkas as saying "We view this as a unique opportunity and TBW is delighted to be able to participate in this important transaction with Colonial."
- 68. The market responded aggressively to the news, with shares of BancGroup trading 20% higher the next trading day. BancGroup filed a Form 8-K with the Commission on April 1, 2009, via the EDGAR system, which contained the press release and the Stock Purchase Agreement signed by Defendant Farkas.
- 69. The Stock Purchase Agreement contained a financing contingency, which made the investors' obligation to participate in the Capital Infusion dependent on their ability to obtain financing.
- 70. By May 2009, Defendant Farkas had advised BancGroup that TBW would not rely on the Investment Bank to finance its share of the Capital Infusion and that TBW would fund its share of the Capital Infusion by liquidating several derivative securities that involved hedges of TBW's mortgage servicing rights. This statement was false, and Defendant Farkas knew that it was false, in that TBW did not have the ability to fund its share of the Capital Infusion internally.
- 71. Based on Defendant Farkas' representations, BancGroup and TBW amended the Stock Purchase Agreement to delete the financing contingency and BancGroup filed a Form 8-K

- on May 4, 2009 announcing this amendment to the Stock Purchase Agreement. Defendant Farkas reviewed and approved the Form 8-K before it was filed.
- 72. In response to the news that the financing contingency had been removed from the Stock Purchase Agreement, BancGroup's share price rose approximately 10%, while trading volume jumped almost 68% over the average trading volume during the prior five trading days.
- 73. On July 31, 2009, after trading closed, BancGroup and TBW mutually announced the termination of the Stock Purchase Agreement, essentially signaling the end of Colonial Bank's pursuit of TARP funds. BancGroup's stock declined 20% that day to \$0.49, and has not been above \$0.77 since that date.

<u>COUNT I — FRAUD</u> Violations of Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)]

- 74. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 75. From at least March 2002 through at least August 2009, Defendant Farkas, in the offer and sale of the securities described herein, by the use of means and instruments of transportation and communication in interstate commerce and by use of the mails, directly and indirectly, employed devices, schemes and artifices to defraud purchasers of such securities, all as more particularly described above.
- 76. Defendant Farkas acted knowingly, intentionally, and/or with severe recklessness in engaging in the aforementioned devices, schemes and artifices to defraud.
- 77. While engaging in the course of conduct described above, Defendant Farkas acted with scienter, that is, with an intent to deceive, manipulate or defraud or with a severe reckless disregard for the truth.

78. By reason of the foregoing, Defendant Farkas, directly and indirectly, has violated and, unless enjoined, will continue to violate Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)].

COUNT II — FRAUD Violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)]

- 79. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 80. From at least March 2002 through at least August 2009, Defendant Farkas, in the offer and sale of the securities described herein, by use of means and instruments of transportation and communication in interstate commerce and by use of the mails, directly and indirectly:
- a. obtained money and property by means of untrue statements of material fact and omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and
- b. engaged in transactions, practices and courses of business which would and did operate as a fraud and deceit upon the purchasers of such securities, all as more particularly described above.
- 81. By reason of the foregoing, Defendant Farkas, directly and indirectly, has violated and, unless enjoined, will continue to violate Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)].

COUNT III — FRAUD

Violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]

- 82. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 83. From at least March 2002 through at least August 2009, Defendant Farkas, in connection with the purchase and sale of securities described herein, by the use of the means and instrumentalities of interstate commerce and by use of the mails, directly and indirectly:
 - a. employed devices, schemes, and artifices to defraud;
- b. made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and
- c. engaged in acts, practices, and courses of business which would and did operate as a fraud and deceit upon the purchasers of such securities, all as more particularly described above.
- 84. Defendant Farkas knowingly, intentionally, and/or recklessly engaged in the aforementioned devices, schemes and artifices to defraud, made untrue statements of material facts and omitted to state material facts, and engaged in fraudulent acts, practices and courses of business. In engaging in such conduct, Defendant Farkas acted with scienter, that is, with an intent to deceive, manipulate or defraud or with a severe reckless disregard for the truth.
- 85. By reason of the foregoing, Defendant Farkas, directly and indirectly, has violated and, unless enjoined, will continue to violate Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

COUNT IV — AIDING AND ABETTING FRAUD

Aiding and Abetting of Violations by BancGroup of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]

- 86. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 87. BancGroup violated Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]. The underlying violations by BancGroup occurred when it made repeated material misrepresentations of fact in its Forms 10-K, 10-Q, 8-K and related press releases concerning the nature, value, and liquidity of the assets of Colonial Bank's MWLD.
- 88. Through the conduct described above, Defendant Farkas knowingly provided substantial assistance and aided and abetted and, unless enjoined, will continue to aid and abet violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

<u>COUNT V — AIDING AND ABETTING</u> INTERNAL ACCOUNTING CONTROLS

Aiding and Abetting of Violations by the Colonial Bank Officer of Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)]

- 89. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 90. Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] prohibits any person from knowingly circumventing or knowingly failing to implement a system of internal accounting controls or knowingly falsifying any accounting book, record, or account required by Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

- 91. Through the conduct described above, the Colonial Bank Officer violated Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)].
- 92. Through the conduct described above, Defendant Farkas knowingly provided substantial assistance and aided and abetted and, unless enjoined, will continue to aid and abet violations of Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)].

<u>COUNT VI — INTERNAL ACCOUNTING CONTROLS</u> Violations of Exchange Act Rules 13b2-1 [17 C.F.R. § 240.13b2-1]

- 93. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 94. Rule 13b2-1 of the Exchange Act [17 C.F.R. §§ 240.13b2-1] prohibits any person from directly or indirectly falsifying or causing the falsification of any such accounting books, records or accounts.
- 95. Through the conduct described above Defendant Farkas violated, directly and indirectly, and, unless restrained and enjoined, will continue to violate Exchange Act Rule 13b2-1 [17 C.F.R. §§ 240.13b2-1].

<u>COUNT VII — AIDING AND ABETTING</u> INTERNAL ACCOUNTING CONTROLS

Aiding and Abetting of Violations by BancGroup of Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)]

- 96. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 97. Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(B)] requires issuers such as BancGroup to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that, among other things, transactions are recorded as

necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and to maintain accountability for assets.

- 98. Through the conduct described above, BancGroup violated Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)].
- 99. Through the conduct described above, Defendant Farkas knowingly provided substantial assistance and aided and abetted and, unless enjoined, will continue to aid and abet violations of Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)].

COUNT VIII — AIDING AND ABETTING BOOKS AND RECORDS VIOLATIONS

Aiding and Abetting of Violations by BancGroup of Sections 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)]

- 100. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 101. Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] requires issuers such as BancGroup to make and keep accounting books, records, and accounts, which, in reasonable detail, accurately and fairly reflected the transactions and dispositions of their assets.
- 102. Through the conduct described above, BancGroup violated Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].
- 103. Through the conduct described above, Defendant Farkas knowingly provided substantial assistance and aided and abetted and, unless enjoined, will continue to aid and abet violations of Section 13(b)(2)(A) of the Exchange Act.

COUNT IX — AIDING AND ABETTING REPORTING VIOLATIONS

Aiding and Abetting of Violations by BancGroup of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(b)(5)] and Rules 12b-20, 13a-1, 13a-11 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13]

- 104. Paragraphs 1 through 73 are hereby realleged and are incorporated herein by reference.
- 105. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 12b-20, 13a-1, 13a-11, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13] thereunder require issuers of securities registered with the Commission pursuant to Section 12 of the Exchange Act to file with the Commission factually accurate annual, current and quarterly reports.
- 106. Through the conduct described above, BancGroup violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1, 13a-11 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13].
- 107. Through the conduct described above, Defendant Farkas knowingly provided substantial assistance and aided and abetted and, unless enjoined, will continue to aid and abet violations of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1, 13a-11 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13].

PRAYER FOR RELIEF

WHEREFORE, Plaintiff Commission respectfully prays that the Court:

I.

Make findings of Fact and Conclusions of Law pursuant to Rule 52 of the Federal Rules of Civil Procedure, finding that the Defendant Farkas named herein committed the violations alleged herein.

II.

Issue a permanent injunctions enjoining Defendant Farkas and his agents, servants, employees, and attorneys, and those persons in active concert or participation with them who receive actual notice of the order of injunction, by personal service or otherwise, and each of them:

- (a) from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)];
- (b) from violating Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 [17 C.F.R. § 240.10b-5] thereunder;
- (c) from aiding and abetting violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 [17 C.F.R. § 240.10b-5] thereunder;
- (d) from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1];
- (e) from aiding and abetting violations of Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)];
- (f) from aiding and abetting violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)]; and

(g) from aiding and abetting violations of Section 13(a) of the Exchange Act [15 U.S.C. §§ 78m(a)] and Rules 12b-20, 13a-1, 13a-11 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13].

III.

An order requiring disgorgement by Defendant Farkas of all ill-gotten gains or unjust enrichment with prejudgment interest, to effect the remedial purposes of the federal securities laws.

IV.

An order, pursuant to Section 20(e) of the Securities Act [15 U.S.C. § 77t(e)] and Section 21(d)(2) of the Exchange Act [15 U.S.C.§ 78u(d)(2)] prohibiting Defendant Farkas from acting as an officer or director of any issuer that has a class of securities registered with the Commission pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] or that is required to file reports with the Commission pursuant to Section 15(d) of the Exchange Act [15 U.S.C.§ 78o(d)].

V.

An order, pursuant to Section 21(d)(5) of the Exchange Act [15 U.S.C.§ 78u(d)(5)] prohibiting Defendant Farkas from: (a) serving in a senior management or control position at any mortgage-related company or other financial institution; and (b) from holding any position involving financial reporting or disclosure at a public company.

VI.

An order pursuant to Section 20(d) of the Securities Act [15 U.S.C. 77t(d)] and Section 21(d)(3) of the Exchange Act [15 U.S.C. 78u(d)(3)] imposing civil penalties against Defendant Farkas.

VII.

Such other and further relief as this Court may deem just, equitable, and appropriate in connection with the enforcement of the federal securities laws and for the protection of investors.

Dated this 16th day of June, 2010.

Respectfully submitted,

Erica Y. Williams, Trial Counsel (VA Bar No. 43303)*

Securities and Exchange Commission

100 F Street, N.E.

Washington, D.C. 20549

Tel: (202) 551-4450 Fax: (202) 772-9246

William P. Hicks, Associate Regional Director**

M. Graham Loomis, Regional Trial Counsel**
Aaron W. Lipson, Assistant Regional Director**

Yolanda M. Ross, Senior Staff Attorney**

Securities and Exchange Commission

3475 Lenox Road, N.E. Ste. 500

Atlanta, Georgia 30326-1232

Tel: (404) 842-7600 Fax: (404) 842-7666

COUNSEL FOR PLAINTIFF

^{*} Local Counsel

^{**} Pro Hac Vice Admission Pending