

STATE GRAND JURY OF SOUTH CAROLINA

STATE OF SOUTH CAROLINA

vs.

KAREN MILLER,

Defendant.

Case No. **05GS47 11**

**Indictment for Conspiracy**  
**§ 16-17-410**

**FILED**  
**SEP 13 2005**  
LISA C. DUNBAR,  
CLERK, STATE GRAND JURY

At a session of the State Grand Jury of South Carolina, convened in Columbia, South Carolina, on September 13<sup>th</sup>, 2005, the State Grand Jurors present upon their oath and charge as follows:

**Background and Summary**

**A. Relevant Entities**

1. At all times relevant to this Indictment, HomeGold Financial, Inc. ("HGFI") was a publicly-traded holding company subject to the disclosure and other reporting requirements of the Securities and Exchange Commission ("SEC"), with approximately nine wholly-owned subsidiaries, of which only two, Home Gold, Inc. and Carolina Investors, Inc. were operating in recent years.
2. HGFI, together with HomeGold, Inc ("HGI"), was a specialty finance company engaged in the business of originating, selling and servicing sub-prime first and second-lien residential mortgage loan products.
3. Carolina Investors, Inc. ("CII") was formed in 1963, ostensibly to finance the sale of cemetery plots. This was accomplished through the sale of subordinated debentures and notes to the general public. CII also engaged in a variety of asset based lending, including "retail" (*i.e.* direct to the

borrower) sub-prime home mortgage lending; small construction loans; sub-prime automobile loans; and sub-prime loans for the purpose of appliances.

4. In 1987 and 1989, CII formed two subsidiaries, The Loan Pro\$, Inc. ("Loan Pro\$") and Premier Financial Services, Inc. ("Premier") respectively, to conduct its automobile and appliance financing business.
5. In May 1991, National Railway Utilization Corporation ("NRUC"), purchased CII and its subsidiaries. NRUC, formed in 1968, was a public company subject to the disclosure and reporting requirements of the SEC. In August 1991, NRUC changed its name to Emergent Group, Inc. ("Emergent"). Under Emergent, CII expanded into the "wholesale" mortgage business and small-business loan products partially guaranteed by the United States Small Business Administration.
6. In June 1995, Emergent began a restructuring, which involved, among other things, the formation of a new subsidiary, Emergent Mortgage Corporation ("EMC"), to conduct and expand the wholesale mortgage and retail mortgage operations. Emergent borrowed \$15,000,000.00 from CII in order to form EMC. The formation of EMC marked the beginning of the inter-company loans between CII and Emergent.
7. Also in June 1995, CII ceased its lending activities. In addition, many of CII's internal administrative functions, including accounting, were undertaken by Emergent. Consequently, CII ceased to be a stand-alone business and its operations were devoted to the sale of debt

instruments to South Carolina investors to raise funds that were transferred to Emergent and its various subsidiaries. In essence, CII became little more than the funding arm for Emergent.

8. Beginning in 1998, Emergent began suffering substantial operating losses. As a result, it sold all of the assets of its subsidiaries except for EMC and CII. In March 1998, EMC changed its name to HGI and in July 1998, Emergent changed its name to HGFI.
9. Likewise in 1998, HGFI began to buy back bonds it had sold in 1997 in a \$125,000,000.00 offering. During the years 1998 – 2001, HGFI was able to repurchase the bonds for between 37% - 60% of face value, reflecting concern in the bond market that HGFI's financial condition would prevent it from paying the bonds when due. CII, nevertheless, continued to sell its debt instruments to the public at 100% face value and to upstream virtually all funds to HGFI.
10. Beginning in May of 1998, several officers of HGFI and CII held meetings prior to any announcements of quarterly losses to coordinate ways in which to downplay negative information and put a positive spin on information that would be disseminated to the public and to potential or current investors. This practice continued until March of 2003.
11. In addition to holding meetings prior to any public announcements regarding quarterly losses, several officers of HGFI and CII discussed ways in which to downplay negative information and put a positive spin on information that was disseminated to the South Carolina Securities



Commission. The information was disseminated in response to inquiries by the South Carolina Securities Commission regarding the financial condition of CII.

12. HGFI's losses continued in 1999, and HGFI formulated a plan to merge with another company. The apparent intent was to merge with a company that possessed substantial experience in the mortgage origination industry. Two merger attempts failed after the due diligence efforts revealed negative financial information regarding the merger targets.
13. On May 9, 2000, HomeSense Financial Corporation and affiliated companies ("HomeSense"), a privately owned entity located in Lexington, South Carolina was merged into HGI, HGFI's mortgage business. HomeSense was believed to have the industry experience since HomeSense specialized in originating and selling mortgage loans in the sub-prime mortgage industry. HGFI, however, continued to report losses in 2000, 2001 and 2002.
14. During May 2000, several officers of HGFI and HomeSense discussed ways in which to downplay negative information and put a positive spin on information that was disseminated to the South Carolina Securities Commission, the Securities and Exchange Commission, stockholders and investors of both HGFI and CII regarding the structure and terms of the merger between HomeSense and HGI.
15. As HGFI's substantial operating losses continued, the indebtedness of HGFI to CII also substantially increased. From 1995 through the end of

2002, HGFI's indebtedness to CII increased from approximately \$204,000.00 to \$242,200,000.00 dollars.

16. Notwithstanding HGFI's substantial operating losses, its negative net worth, the financial market's assessment of its ability to repay, and the dramatic growth in the indebtedness owed to CII, HGFI's continued to received "clean" opinions and was not required to write-down the inter-company debt in 1998, 1999, or 2000. Finally, at meeting held on March 14, 2002 by HGFI's auditors, Elliott Davis, communicated that it would issue a going concern qualification to the 2001 consolidated financial statements that would appear both in HGFI's SEC filings and in the 2002 CII Prospectus to be registered with the State of South Carolina.
17. In addition, Elliott Davis communicated that it would report an impairment of CII's notes receivables from HGFI, subsequently determined to be in the amount of \$6,400,000.00. The impairment figure was based upon the conclusion that if the recorded and off-book assets of HGFI were liquidated in an orderly manner, HFGI would fall approximately \$6,400,000.00 short of repaying CII.
18. In April 2002, CII issued a prospectus that contained the going concern qualification by Elliott Davis, meaning that Elliott Davis had substantial doubt as to whether CII would be able to stay in business as a going concern. In addition, Elliott Davis required CII to deduct an impairment allowance from the value of the loans it had made to HGFI because it was

probable that CII would be unable to collect the entire amount owed by HGFI.

19. During Summer and Fall of 2002, HGFI attempted to actively market for sale the retail mortgage operations of HGI. While these efforts proceeded, with no viable offers, HGFI consulted bankruptcy counsel to prepare a disaster plan, which included some form of conservatorship for CII.
20. Notwithstanding the conclusions of Elliott Davis, the unsuccessful efforts to sell the retail mortgage operations of HGI and the consultation of bankruptcy counsel by HGFI, CII continued to sell its securities to the public and upstream the funds. HGFI continued to spend lavishly and sustain substantial losses. CII sold over \$74,000,000.00 of debt securities between April 1 and December 31, 2002 and over \$16,000,000.00 from January 1 through March 21, 2003. During this period, HGFI also extended approximately \$10,000,000.00 of funding to a startup payday lending company, FlexCheck Holdings, LLC ("FlexCheck"), as apart of a \$15,000,000.00 funding commitment.
21. On December 31, <sup>2002 KF</sup> ~~2003~~, HGFI consummated the sale of the majority of the assets of its retail mortgage business to EMMCO for \$150,000 cash and a capped earn out. In connection with the purchase of assets by EMMCO, HGFI loaned \$5,000,000.00 to R-DOC, an office location at 113 Reed Avenue in Lexington, South Carolina and certain vacant land at their combined net book value of approximately \$3,445,000.00, as well as certain furniture, fixtures, equipment and other assets. <sup>HGFI KF</sup> ~~HGFI~~ received a



promissory not in the amount of \$8,445,000.00 upon <sup>which KF</sup> with no payments have been made.

22. As a result of the EMMCO sales transaction, the ability of HGFI to repay CII and other creditors became dependant solely upon the success of three startup companies: EMMCO, R-DOC and FlexCheck.
23. On March 21, 2003, CII closed its doors to the public, and thousands of investors were unable to obtain monies they had invested in CII.
24. Subsequent to the EMMCO transaction, HGI's operations were generally limited to mortgage servicing. With insubstantial revenues from operations, no payments forthcoming from EMMCO, and unable to sell sufficient debt instruments to cover losses and redemptions, HGFI ran out of funds by March 2003 and filed voluntary Chapter 11 Bankruptcy petitions on March 31, 2003. Business operations were terminated shortly thereafter.

#### B. Karen Miller

25. At all times and relevant to this Indictment, Karen Miller, the defendant, was a employee of HGFI and held the following positions:
  - a. In 1996, Miller was hired as the Chief Technology Officer ("CTO") for Emergent.
  - b. In 1998, Miller was promoted to Executive Vice President ("EVP") of Emergent.

- c. In April 2001, Miller was promoted to Chief Administrative Officer (“CAO”) for HGFI, with additional job responsibilities primarily involving the HGFI head quarters move from Greenville to Lexington. Miller retained her title as EVP as well.
- d. In April 2002, Miller was assigned additional duties as CAO involving training and recruiting new employees.
- e. In August 2002, Miller was named the interim Chief Financial Officer for HGFI.
- f. In September 2002, Miller was named the Chief Financial Officer (“CFO”) for HGFI.
- g. In November 2002, Miller was placed on the Board of Directors for HGFI.

**Common Law Conspiracy  
(S.C. Code Ann. § 16-17-410)**

- 26. During the time period in or about January of 1998 to in or around March 31, 2003, the Defendant, Karen Miller, at some point participated in an agreement between two or more persons for the purpose of accomplishing a criminal or unlawful object, or a lawful object by criminal or unlawful means, to wit: Karen Miller unlawfully conspired to violate § 35-1-1210 of the Code of Laws of South Carolina, as amended, in violation of Section 16-17-410 of the Code of Laws of South Carolina, as amended.
- 27. In furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, implemented accounting methods regarding the



capitalization of assets in contradiction with the Generally Accepted Accounting Principles (“GAAP”), which impacted the appearance of the financial statements of HGFI and its subsidiaries in a positive misleading light.

28. In furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, made changes in the manner in which the back income, brokerage fee receivables and salary capitalizations were handled in an effort to impact the appearance of the financial statements of HGI in a more positive light while HGFI was attempting to sell the subsidiary to IMPAC. This was done between quarterly reports so the changes could be reversed before the reports were finalized for the SEC. This was in contradiction with GAAP procedures.
29. In furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, continued the practice of making adjustments to CII’s financials in order to bring the books into compliance with the inter-company indemnification agreement. In effect, this inflated the financial statements of CII, making it look as if CII had an income of \$300,000.00 from residual receivables each month.
30. In furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, omitted material facts from the October 14, 2002 SEC 8K reporting form, to wit: that Kevin Martin, Chief Financial Officer for HGFI from June 2001 to August 2002, resigned noting the following

reason: that HGFI is no longer a company that is turning its financial position around.

31. On or about November 19, 2002, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, file a Form 10 Q report with the SEC that stated that the building located at 3901 Pelham Road in Greenville, South Carolina was worth approximately \$10,000,000.00 and that HGFI and CII intended to hold and use the building as collateral for one of the Company's warehouse lines, when in fact, the Company had entered into a contract of sale regarding the Pelham Road building with a purchase price of \$4,000,000.00 on November 12, 2002.
32. In November 2002, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, attended a CII Board of Directors meeting at which the sale of HGI's retail mortgage division to EMMCO was explained. At that meeting, the Defendant Karen Miller failed to provide CII's Board of Directors with any information regarding the recent Elliott Davis letter to HGFI management in which they report several findings, including that HGFI's cost structure continued to exceed its revenue and that HGFI continued to have extreme reliance on borrowing working capital from CII's debenture offerings.
33. In December 2002, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, engaged in a phone conversation with Larry Owen, Chief Executive Officer of CII, regarding HGFI

retaining a conservator for a disaster plan. When Larry Owen questioned the Defendant Karen Miller, she responded by stating it was part of a “contingency plan” in case CII experienced another “run”.

34. On or about January through February 2003, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, discussed the possibility of transferring many of HGI assets to the books of CII in an effort to reduce the debt owed to CII by HGFI, thus making the companies look better on paper. These would be in effect paper transactions. The assets would not actually move to CII.
35. In February 2003, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, met with the South Carolina Securities Division at the Attorney General’s office and assured them that HGFI was no longer taking funds from CII’s sale of investments.
36. On February 26, 2003, in furtherance of the conspiracy, the Defendant Karen Miller, along with other co-conspirators, attended a CII Board of Directors Meeting in which she informed them that she was working on HGFI’s three to five-year strategic plan to become profitable and pay back the debt owed to CII. However, the Defendant Karen Miller omitted material facts regarding the risks in connection with the plan, as well as the “contingency plan” of the conservatorship procedures HGFI had in place.



Against the peace and dignity of the State and contrary to the statute in each case  
made and provided.

A TRUE Bill

K.D. Felt  
FOREMAN

Henry McMaster  
HENRY McMASTER (sop)  
ATTORNEY GENERAL

**ATTEST**  
A TRUE COPY  
[Signature]  
CLERK, STATE GRAND JURY.