

**UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND**

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ANNIE GRAHAM :

Plaintiff, :

:

v. :

:

JOSEPH K RENSIN :

7000 Security Boulevard :

Baltimore, Maryland 21244 :

:

RICHARD I. PALMER :

CIVIL ACTION NO.

7000 Security Boulevard :

Baltimore, Maryland 21244 :

CLASS ACTION COMPLAINT

:

J. BARRY DUMSER :

7000 Security Boulevard :

Baltimore, Maryland 21244 :

Jury Trial Demanded

:

and :

:

JOHN L. DAVIS :

7000 Security Boulevard :

Baltimore, Maryland 21244 :

:

Defendants. :

-----:

Plaintiff, on behalf of herself and all others similarly situated, by and through plaintiff's attorneys, alleges the following upon the investigation made by and through plaintiff's attorneys, which investigation included, without limitation, analysis of press releases, analyst and other reports, and public filings with respect to Creditrust Corporation ("Creditrust" or the

"Company").

INTRODUCTION AND OVERVIEW

1. This is a class action on behalf of all persons, other than defendants and their affiliates, who purchased Creditrust common stock during the period July 29, 1998, through March 31, 2000, inclusive (the "Class Period"), and who sustained damage as a result.
2. Founded in 1991 and taken public on or about July 29, 1998, Creditrust claims to be "a leading information-based purchaser, collector and manager of defaulted consumer receivables." Basically, Creditrust purchases bad debt receivables (mostly uncollected credit card debt that the banks have given up trying to collect) at a discount to the total debt owed and then attempts to collect more than what it paid for the debt.
3. Defendants, who were Creditrust's top officers and directors during the Class Period, claimed that Creditrust uses "proprietary pricing models and software systems as well as extensive information, databases to generate high rates of return on purchased receivables." Defendants also claimed that Creditrust uses these models, systems, and databases to estimate the amount it will collect on any given bad debt receivables. The Company reports such estimated amounts as actual revenues and earnings. Creditrust funds its purchases of bad debt receivables through a combination of bank and other credit facilities, public and private equity funding, and asset-backed securitizations.
4. During the Class Period, defendants schemed to inflate Creditrust's stock price by issuing materially false and misleading public statements that fraudulently inflated the Company's reported financial results.

5. Defendants misrepresentations and omissions served to inflate artificially the market price of the Creditrust's securities during the Class Period. During the same period,

Company insiders sold \$8.2 million of their personal Creditrust holdings at inflated prices. Those who purchased the Company's stock relying on the market price accurately to reflect its true value, including plaintiff and members of the Class, suffered damages.

6. On March 31, 2000, defendants belatedly disclosed previously misrepresented or omitted facts with the issuance of Creditrust's Form 10-K Report for the year ended December 31, 1999. In reaction, the Company's stock lost more than 24% of its value in just one day, declining to a level nearly 91% below its high of \$33.81 during the Class Period. Thereafter, on June 21, 2000, Creditrust filed a petition for protection under the U.S. bankruptcy laws.

JURISDICTION AND VENUE

7. Plaintiff brings this action pursuant to Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "Exchange Act") (15 U.S.C. §§78j(b), and 78t(a)) and Rule 10b-5 promulgated thereunder. 17 C.F.R. §240.10b-5.

8. This Court has jurisdiction over the subject matter of this action pursuant to Section 27 of the Exchange Act (15 U.S.C. §78aa), and 28 U.S.C. §1331, as amended.

9. Venue is proper in this District pursuant to Section 27 of the Exchange Act, 15 U.S.C. §78aa. Many of the acts and transactions giving rise to the violations of law complained of herein, including the preparation and dissemination to the investing public of false and

misleading information, occurred in this District. Further, Creditrust has its principal place of

business in this District at 7000 Security Boulevard, Baltimore, Maryland 21244.

10. In connection with the acts, conduct and other wrongs complained of herein, the defendants, directly or indirectly, used the means and instrumentalities of interstate commerce,

including the United States mails and interstate telephone communications, and the facilities of the national securities exchanges.

THE PARTIES AND CREDITRUST

11. Plaintiff purchased shares of Creditrust common stock during the Class Period as described in full on the Certification attached hereto.

12 Creditrust, a Delaware corporation with headquarters in Baltimore, Maryland, is

not a defendant in this action because of its bankruptcy filing. Primarily, Creditrust purchases bad credit card debt that the credit card issuer has charged off as uncollectible and then attempts to collect the debt. As of March 31, 2000, 10.5 million shares of Creditrust common stock were outstanding. During the Class Period, the Company's common stock was actively traded on the NASDAQ National Market System, a well-developed and efficient market.

13. The following are "Individual Defendants:"

a. Defendant Joseph K. Rensin ("Rensin") is, and at all times relevant hereto has been, President and Chief Executive Officer of Creditrust. Defendant Rensin signed the Company's Annual Report on Form 10-K for the fiscal years ended December 31, 1998 and December 31, 1999. During the Class Period, Defendant Rensin sold a total of 500,000 shares of his personal holdings on July 29, 1998 at \$15.50, and 450,000 shares of his personal holdings on February 24, 1999, at \$23.19 per share for total proceeds of \$18,185,500.00.

b. J. Barry Dumser, joined Creditrust in 1997 as its General Counsel and was named President and Chief Operating Officer in December, 1999.

c. Richard J. Palmer has been Chief Financial Officer of Creditrust since 1966.

d. John L. Davis joined Creditrust in 1993 and is the Vice President, Business Development and Corporate Secretary.

14. By reason of their management positions, their ability to make public statements in the name of the Company, and their stock ownership, defendants Rensin, Dumser, and Palmer were controlling persons of the Company and had the power and influence to cause the Company to engage in the unlawful conduct complained of herein. The Individual Defendant had access to the adverse non-public information about the Company's business, finances, products, markets and present and future business prospects, as particularized herein, via access to internal corporate documents, conversations or connections with corporate officers or employees, attendance at Company management and/or Board of Directors meetings and committees thereof; and/or reports and other information provided to them.

15. Defendants had a duty to disseminate promptly accurate and truthful information with respect to the Company's operations and financial condition in order to correct any previously disseminated information that was misleading to the market. As a result of their failure to do so, the value of Creditrust common stock was artificially inflated during the Class Period, causing injury to plaintiff and the Class.

16. Defendants participated in and, consciously or recklessly pursued the unlawful conduct alleged herein in order to enrich themselves at the public's expense to profit from illegal insider trading, to protect emoluments and privileges of corporate office, to maintain the value of their stock holdings in Creditrust, and/or to avoid embarrassment and loss of prestige.

17. Defendants had the opportunity to commit and participate in the fraud detailed below. Defendants, by virtue of their position with Creditrust, controlled the drafting and dissemination of information provided to the investing public such as press releases, corporate reports, filings with the Securities and Exchange Commission ("SEC"), and communications with securities analysts, including misrepresentations and omissions about Creditrust's reported revenues and earnings. This information reached the investing public and artificially inflated the price of Creditrust's common stock.

CLASS ACTION ALLEGATIONS

18. Plaintiff brings this action as a class action pursuant to Rules 23(a) and 23(b)(3) of the Federal Rules of Civil Procedure on behalf of a class (the "Class") consisting of all persons who purchased the common stock of Creditrust during the period July 29, 1998 through March

31, 2000, inclusive (the "Class Period"). Excluded from the Class are the defendants, members of the immediate family of each of the Defendants; any entity in which any defendant has a controlling interest; and the legal affiliates, representatives, heirs, controlling persons, successors, and predecessors in interest or assigns of any such excluded party.

19. Because over 10 million shares of the Company's common stock were outstanding and because the Company's common stock was actively traded during the Class Period, the members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members can only be determined by appropriate discovery, plaintiff believes that Class members number at least in the hundreds and that they are geographically dispersed.

20. Plaintiff's claims are typical of the claims of the members of the Class because

plaintiff and all of the Class members sustained damages arising out of the defendant's wrongful conduct complained of herein.

21. Plaintiff will fairly and adequately protect the interests of the Class members and has retained counsel who are experienced and competent in class and securities litigation. Plaintiff has no interest which is contrary to or in conflict with those of the members of the Class plaintiff seeks to represent.

22. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable.

Furthermore, as the damages suffered by individual members of the Class may be relatively small, the expense and burden of individual litigation make it impossible for the members of the Class individually to redress the wrongs done to them. There will be no difficulty in the management of this action as a class action.

23. Questions of law and fact common to the members of the Class predominate over any questions which may affect only individual members, in that defendants have acted on grounds generally applicable to the entire Class. Among the questions of law and fact common to the Class are:

a. Whether the federal securities laws were violated by defendants

acts as alleged herein;

b. Whether the Company's publicly disseminated releases and statements during the Class Period omitted and/or misrepresented material facts and whether defendants breached any duty to convey material facts or to correct material facts previously disseminated;

c. Whether defendants participated in and pursued the common course of conduct complained of;

d. Whether defendants acted willfully or recklessly in omitting and/or misrepresenting material facts;

e. Whether the market prices of Creditrust common stock during the Class Period were artificially inflated due to defendants' material nondisclosures and/or misrepresentations;

f. Whether the members of the Class have sustained damages and, if so, what is the appropriate measure of damages.

STATUTORY SAFE HARBOR

24. The statutory safe harbor provided for forward looking statements under certain circumstances does not apply to any of the false statements pleaded in this Complaint. None of the statements pleaded herein was adequately identified as a "forward-looking statement" when made nor did meaningful cautionary statements identifying relevant and important factors that could cause actual results to differ materially from those in the forward-looking statements.

Alternatively, to the extent that the statutory safe harbor does apply to any forward-looking statements pleaded herein, the defendants are liable for those false forward-looking statements because, at the time each of those forward-looking statements was made, the speaker knew of the falsity of the forward-looking statements and/or the statements were authorized and/or approved by an executive officer of Creditrust who knew or was reckless in not knowing that those statements were false when made.

BACKGROUND AND FACTUAL ALLEGATIONS

25. Founded in 1991, Creditrust issued shares to the public in an Initial public offering ("TPO") on or about July 29, 1998. Creditrust claims to be "a leading information-based purchaser, collector and inanager of defaulted consumer receivables. Basically, Creditrust purchases bad debt (mostly uncollected credit card debt that the banks have given up trying to collect) at a discount to the total debt owed arid then attempts to collect more than what it paid for the debt.

26. Creditrust funds its purchases of bad debt receivables through a combination of bank and other credit facilities, public and private equity funding, and asset-backed securitizations.

27. Creditrust uses accretion accounting to report its revenue and earnings. This method allows the Company to record suspect revenue and earnings based on the assnmed fair value of the receivables at each reporting date. In essence, the Company decides how much it can collect on a given receivable over five years and bases its reported revenu.es and accretion of receivables on this assumption. Creditrust claims that it uses "proprietary pricing models and. software systems as well as extensive information databases" to generate its estimated rate of retuxii on its purchased receivables.

28 On July 28, 1998, defendants filed the Companys Form S-1 registration statement for its initial public offering ("IPO") of 2,500,000 shares of common stock, including 500,000 shares being sold by defendant Rensin, at \$15.50 per share. Prior to the IPO, defendant Rensin owned 100% of the outstanding common stock.

29. On August 13, 1998, defendants issued a press release, announcing Second Quarter and Six Months 1998 Financial Results; Revenues Strong, Surpassing Comparable Six

Months by 203% ". In that press release, defendants reported that Creditrusts revenues for the

second quarter 1998, ended June 30 1998, were \$8.4 million, compared to \$2.0 million for the same period in the prior year and net earnings were \$3.0 million, compared to \$420,000 for the same period in the prior year.

30. On or about September 11, 1998, defendants filed Creditrusts Form 10-Q for the second quarter ended June 30, 1998, incorporating the same false and misleading revenues and net earnings figures discussed above.

31. On October 29, 1998, defendants issued a press release, announcing "Third Quarter And Nine Months 1998 Financial Results; Third Quarter Revenues Up 69%." In that press release, defendants reported that Creditrusts revenues for the third quarter 1998, ended September 30 1998, were \$4.3 million, compared to \$2.6 million for the same

period in the prior year. The Company reported a net loss of \$680,000, compared to net earnings of \$37,000 for the same period in the prior year, due in part to an extraordinary loss of \$567,000 from the early retirement of \$5 million in subordinated debt. Defendant Rensin stated:

Our first quarter as a publicly traded company has proven a success by every measure. Our exclusive Portfolio Analysis Tool (PAT) software, coupled with a streamlined cost structure and conservative pricing model, provide Creditrust with a highly predictable cash flow.

* * *

It is important to note that analysts predicted that the lack of a securitization during the quarter would result in a much more significant loss. The actual results are a testament to the efficiency of our business model.

32. On or about November 16, 1998, defendants filed Creditrusts Form 10-Q for the third quarter ended September 30, 1998, incorporating the same false and misleading revenues and net earnings figures discussed above.

33. On February 17, 1999, defendants issued a press release, announcing "Record Fourth Quarter and Year-End 1998 Financial Results." Creditrust reported revenues of \$18.2 million for the fourth quarter 1998, compared to \$3.4 million for the same period in the prior year, and \$34.3 million for fiscal year 1998, compared to \$9.8 million for the prior fiscal year. 34. On or about March 31, 1999, defendants filed the Companys Form 10-K for fiscal year 1998, incorporating the same false and misleading revenues and net earnings figures discussed above.

35. On April 21, 1999, defendants issued a press release, announcing a "300% earnings Increase Over First Quarter 1998." Creditrust reported revenues of \$12.0 million for the first quarter 1999, compared to \$3.4 million for the same period in the prior year and net income of \$2.4 million, compared to \$415,000 for the same period in the prior year.

36. On or about May 17, 1999, defendants filed Creditrusts Form 10-Q for the first quarter ended March 31, 1999, incorporating the same false and misleading revenues and net earnings figures discussed above.

37. On July 21, 1999, defendants issued a press release, announcing "64% Per Share Earnings Increase Over Last Quarter." For the second quarter ended June 30, 1999, defendants caused Creditrust to report revenues and earnings of \$18.4 million and \$4.9

million, respectively compared to \$12 million and \$2.4 million, respectively for the previous quarter.

38. On or about August 15, 1999, defendants filed Creditrusts Form IO-Q for the second quarter ended June 30, 1999, incorporating the same false and misleading revenues and net earnings figures discussed above.

39. On September 1, 1999 defendants announced; "Creditrust Completes \$40 Million Securitization Industry's First Non-Gain on Sale Deal." In that press release, Creditrusts Chief Financial Officer, defendant Palmer stated:

In keeping with our business model, our conservative accounting standards, and our desire to provide our investors with a steady and predictable earnings stream, this securitization will not be recorded utilizing gain on sale accounting methods.

40. On October 20, 1999, defendants issued a press release announcing a "26% Per Share Earnings Increase Over Last Quarter, Income from Operations Up 40%." For the third quarter, ended September 30, 1999, Creditrust reported revenues and earnings of \$24.2 million and \$63 million compared to \$18.4 million and \$4.9 million, respectively, for the previous quarter.

41. On or about November 15, 1999, defendants filed Creditrusts Form 10-Q for the third quarter ended September 30, 1999, incorporating the same false and misleading revenues and net earnings figures discussed above.

42. On February 28, 2000, defendants announced: "Record Year Profits; Earnings Up 79%; Collections over 400% of Last Year." Defendants caused Creditrust to report revenues of \$26.4 million and \$8.1 million for the fourth quarter 1999 and fiscal year 1999, respectively. Earnings for the fourth quarter 1999 and fiscal year 1999 were reported as \$4.7 (prior to special charges) and 18.3 million, respectively.

43. On March 31, 2000, defendants filed Creditrust's Form 10-K for fiscal year 1999 revealing for the first time that the Company had been materially overestimating the amount it could collect on its bad debt receivables for 1999, resulting in an overstatement of pre-tax income by at least \$4.9 million. In addition, defendants revealed in a press release that the Company could not obtain a \$55 million financing package to purchase additional bad debt receivables. That day Creditrust stock fell more than 24% closing at \$3 per share. Thereafter, on June 22, 2000, Creditrust sought protection from creditors by filing a petition under the U.S. bankruptcy laws.

WHY DEFENDANTS' STATEMENTS WERE FALSE AND MISLEADING

44. In order to create the illusion of a fast growing Company, defendants knew it was essential that the Company report strong revenues and gross profits. 4 Thus, defendants caused the Company to overstate materially its reported revenues and earnings reported in, inter alia Creditrust's (i) IPO Form S-1, as amended; (ii) 1998 Form 10K; and (iii) Form 10Qs for the quarters ended June 30, 1998, through September 30, 1999, by overstating revenues and earnings in each of those time periods. Thus, the financial statements filed during the Class Period were false when made, materially overstated Creditrust's revenues and earnings, and were presented in violation of Generally Accepted Accounting Principles ("GAAP").

45. Under the guise of "proprietary software," defendants simply inflated the estimated amounts that could be collected on the bad debt receivables purchased by the Company thereby inflating revenue and pte-tax earnings by at least, \$4.9 million, for fiscal year 1999alone.

46. Creditrusts reported financial results during the Class Period were false and misleading, as such financial information was not prepared in accordance with GAAP, nor did the financial information "present fairly" the Companys operations cue to the Companys improper accounting and inflated estimates of revenues from collections on the bad debt receivables purchased by the Company. Defendants improper accounting caused the Companys revenues and earnings to be materially overstated in violation of GAAP and SEC rules.

47. GAAP are those principles recognized by the accounting profession as the conventions, rules and procedures necessary to define accepted accounting practice at a particular time. Regulation S-X (17 C.F.R. §210.4-01(A) (1) states that financial statements flied, with the SRC which are not prepared in compliance with GAAP are presumed to be misleading and inaccurate. Regulation S-X requires that interim financial statements must also comply with GAAP, with the exception that interim financial statements need not include disclosure which would be duplicative of disclosures accompanying annual financial statements. 17 CF.R §219.10-01(a).

48. A basic and fundamental concept of GAAP is that revenue must be realizab1e or collectible prior to recognition.

49. In addition to the accounting violations noted above, Creditrust presented its financial statements in a manner which also violated at least the following provisious of GAAP:

a. The principle that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions (Concepts Statement No.1, ¶34);

b. The principle that financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and the effects of transactions, events and circumstances that change resources and claims to those resources (Concepts Statement No. 4, ¶40);

c. The principle that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it. To the extent that management offers securities of the enterprise to the public, it voluntarily accepts wider responsibilities for accountability to prospective investors and to the public in general (Concepts Statement No.1, ¶50);

d. The principle that financial reporting should provide information about an enterprise's financial performance during a period. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance (Concepts Statement No.1, ¶42);

e. The principle that financial reporting should be reliable in that it represents what it purports to represent. That information should be reliable as well as relevant is a notion that is central to accounting (Concepts Statement No. 2, ¶¶58-59);

f. The principle of completeness, which means that nothing is left out of the information that may be necessary to ensure that it validly represents underlying events and conditions (Concepts Statement No. 2, ¶79);

g. The principle that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered. The best way to avoid injury to investors is to try to ensure that what is reported represents what it purports to represent (Concepts Statement No. 2, ¶¶95, 97).

WHAT DEFENDANTS GAINED FROM THEIR DECISION

50. Defendants' tortious conduct resulted in substantial benefit incurring to the defendants. As a result of issuing false financial statements, defendants artificially inflated the price of Creditrusts stock.

51. For his part, defendant Rensin, while in the possession of material, undisclosed adverse information, was able to sell over 13 million dollars worth of Creditrusts stock to members of the class.

FIRST CLAIM FOR RELIEF

For Violation Of §10(b) Of The 1934 Act

And Rule 10b-5 Against All Defendant

52. Plaintiffs incorporate ¶¶1-51 by reference.

53. During the Class Period, defendants disseminated or approved the false statements specified above, which they knew or recklessly disregarded were misleading in that they contained misrepresentations and failed to disclose material facts necessary in order to make the statements made, in light of the circumstances under which they were made; not misleading; or

54. Defendants violated §10(b) of the 1934 Act and Rule 10b-5 in that they:

a. employed devices, schemes, and artifices to defraud;

b. Made untrue statements of material facts or omitted to state material facts to make statements made, in light of the circumstances under which they were

necessary in order made, not misleading; or

c. Engaged in acts, practices, and a course of business that operated as a

fraud or deceit upon Plaintiffs and others similarly situated in connection with their purchases of Creditrusts common stock and publicly traded options during the Class Period.

55. Plaintiffs and the Class have suffered damages in that, in reliance on the integrity of the market, they paid artificially inflated prices for Creditrust stock and options. Plaintiffs and the Class would not have purchased Creditrust stock or options at the prices they paid, or at all, if they had been aware that the market prices had been artificially and falsely inflated by defendants misleading statements.

56. As a direct and proximate result of these defendants wrongful conduct, Plaintiffs and the other members of the Class suffered damages in connection with their purchases of Creditrust common stock and its publicly traded options during the Class Period.

SECOND CLAIM FOR RELIEF

For Violation Of §20(a) Of The 1934 Act

Against All Individual Defendants

57. Plaintiffs incorporate ¶911-56 by reference.

58. Each of the defendants acted as a controlling person of Creditrust within the

meaning of §20(a) of the 1934 Act. By reason of their positions and their ownership of Creditrust stock, defendants each had the power and authority to cause Creditrust to engage in the wrongful conduct complained of herein.

PRAYER FOR RELIEF

WHEREFORE, plaintiff, on plaintiff's own behalf and on behalf of the Class, prays for judgment as follows:

- (a) Declaring this action to be a class action pursuant to Rules 23(a) and 23(b)(3) of the Federal Rules of Civil Procedure on behalf of the Class defined herein;
- (b) Awarding plaintiff and the members of the Class rescissory or compensatory damages in an amount which may be proven at trial, together with interest thereon.
- (c) Awarding plaintiff and the members of the Class, pre-judgment and post-judgment interest, as well as their reasonable attorneys and experts witness fees and other costs; and
- (d) Awarding such other and further relief as this Court may deem just and proper including any extraordinary equitable and/or injunctive relief as permitted by law or equity to attach, impound or otherwise restrict the defendants assets to assure plaintiff has an effective remedy.

DEMAND FOR JURY TRIAL

Plaintiff hereby demands a trial by jury

Dated:

PLAINTIFF DEMANDS A TRIAL BY JURY

Dated: August 2, 2000 **LAW OFFICES OF CHARLES J. PIVEN, P.A.**

By: _____

Charles J. Piven - Federal Bar No. 00967

The World Trade Center, Suite 2525

401 East Pratt Street

Baltimore, Maryland 21202

(410) 332-0030

WOLF HALDENSTEIN ADLER

FREEMAN & HERZ LLP

Fred Taylor Isquith

270 Madison Avenue

New York, New York 10016

(212) 545-4600