

Memorandum

VIA EMAIL

To: NC Baptist Convention Counsel
From: Ed Chaney, Andy Andrews, Marshall Schmitt
Date: September 19, 2023
Subject: Summary – Financial Investigation at BCH

Our client, Baptist Children's Homes of North Carolina ("BCH"), asked us to prepare and provide to you the following summary of our investigation. Please contact us if you have any questions.

Background. BCH engaged us during the last week of May 2023 to review certain expenditures made by its President, Dr. Michael C. Blackwell, after it identified apparently personal expenses of Dr. Blackwell paid by BCH. Shortly before our engagement, the Personnel Policy Committee of the BCH Board of Trustees had been alerted to these expenditures, and after further review thereof, brought them to the attention of the Executive Committee. On May 10, BCH's Personnel Policy Committee met with Dr. Blackwell where an initial decision was made to retain an expert to review certain expenditures by Dr. Blackwell. On May 25, Dr. Blackwell's attorney sent a letter to the BCH Executive Committee. On May 26, BCH's Executive Committee met with Dr. Blackwell. After discussion, the Executive Committee decided to pursue a financial investigation and to offer Dr. Blackwell the option of taking a leave of absence with pay during the financial investigation pursuant to the same terms of BCH policy applicable to employees who are suspended with pay and if he refused, he would be suspended with pay. In this report, certain names are redacted in order to maintain confidentiality consistent with applicable law and BCH policy.

The initial scope of review included assessing Dr. Blackwell's personal expenses charged to his American Express ("AMEX") card and paid for by BCH during the past three years as well as a review of a certain BCH account maintained by Dr. Blackwell known as Account 2695 (also referred to as the Sabbatical Fund or President's Education Fund). During the investigation, we also learned that, in 2022 BCH had purchased a new car as a gift for Mrs. Blackwell, which we added to our investigation given the timing and personal nature of such an expense.

To assist in the financial review, we engaged a forensic accountant, Davis Forensic Group, LLC, who provided a report of the expenditures to the BCH Board of Trustees ("Board"). In addition, we interviewed certain BCH personnel and donors and reviewed relevant email correspondence, minutes, and other related documents.

Throughout this process, the Board has acted diligently, prudently, and consistent with the advice and guidance of counsel, while also holding Christian compassion for a widely admired leader.

- 1) Account 2695.** Account 2695 is a separate account on the BCH books and records with the special purpose of providing Dr. Blackwell funds for his personal use. The account was funded almost exclusively through contributions from individual donors except for one \$5,000 transfer to the account of BCH operating funds. Expenditures primarily were personal in nature to Dr. Blackwell and

Dr. Blackwell exercised complete control over the account. Account 2695 was created in 2004 by the BCH executive committee with a \$50,000 allocation of proceeds derived from the sale of certain real estate. Further detail is provided below.

We examined four issues related to Account 2695: (1) the presence of conflicts of interest and potential violations of fiduciary duties; (2) whether the Board authorized Dr. Blackwell to replenish and continue to use Account 2695 beyond the \$50,000 allocated specifically in 2004; (3) whether donors to Account 2695 were aware (a) that their charitable funds were being allocated to this account (by any of its names), and (b) of the full nature of the account – its purposes and uses; and (4) the personal nature of the expenses paid from Account 2695.

- a. **Conflict of Interest, Fiduciary Duties.** Officers have fiduciary duties similar to those of trustees – the duty of care, the duty of loyalty, and the duty of obedience.¹ We found no evidence that anyone other than Dr. Blackwell and his family members benefitted directly from Account 2695. Given that this fund was maintained solely for the personal benefit of Dr. Blackwell, its continued existence and management has been a prolonged conflict of interest for Dr. Blackwell that was not managed consistently with either BCH's conflict of interest policy or Dr. Blackwell's fiduciary duty of loyalty. Further, the continued replenishment of Account 2695 using donated funds that would have otherwise been spent on business operations in service of BCH's mission conflicts with Dr. Blackwell's fiduciary duty of care and fiduciary duty of obedience.
- b. **Lack of Authorization to Replenish Account 2695.** We found no evidence that the Board or Executive Committee authorized or approved the existence or replenishing of Account 2695 beyond the motion approved by the Executive Committee in 2004 for \$50,000. That motion does not contemplate or authorize funds other than the \$50,000 allocated at that meeting. Nor does it grant Dr. Blackwell any authority except to spend that \$50,000. In relevant part, the May 11, 2004 minutes state:

*Ward Mullis made a motion, seconded by Lee Davis, that \$50,000 be set aside from the sale of the beach property for a sabbatical fund (President's Sabbatical Fund) to be used by Dr. Blackwell at any time for any purpose, personal or professional. This fund can be carried over or used immediately at Dr. Blackwell's discretion. If there is a way that the money can accrue to Dr. Blackwell tax free, that would be the choice of the Executive Committee. The motion was unanimously approved.*²

As reported by the forensic accountant BCH engaged for an in-depth review of this account, subsequent Board minutes do not contain any evidence that (a) anyone ever authorized that the

¹ See, e.g., NCGS § 55A-8-42; *Davis v. Davis Funeral Serv.*, 2022 NCBC 38, 7, 2022 NCBC LEXIS 79, *4, 2022 WL 2841211; *Seraph Garrison, LLC ex rel. Garrison Enterprises, Inc. v. Garrison*, 247 N.C. App. 115, 787 S.E.2d 398 (Ct. App. 2016).

² Minutes of the BCH Executive Committee, closed session, May 11, 2004. Executive Committee members in attendance: Abe Elmore (Chair), Lee Davis, Gene Herrell, Ward Mullis, Tannis Nelson. Also in attendance: Staff, Dr. Michael Blackwell, Jennie Counts.

fund be replenished, or (b) the Board was ever provided any financial reporting on Account 2695.³ In fact, based on BCH's minutes, neither the Board as a whole nor any committee has even been made aware of the fund. Instead, the evidence we found shows that the President's office set varying internal targets for Account 2695 and controlled all aspects of it without any apparent oversight or accountability from the Board.

Our understanding of Account 2695 was supplemented by our discussion with long-time donor and former Board member, [Donor Redacted] who has maintained a long relationship with BCH. [Donor Redacted] noted that he learned about Account 2695 only a few weeks ago during this investigation and that its existence and use concern him.

Between 2009 and the date of this memorandum, Dr. Blackwell directed \$312,500 into Account 2695 without Board authorization.⁴ As noted above, all these funds came exclusively from donors except for \$5,000 that was transferred to the account from BCH operating funds. Since 2009, 75% of the contributions to Account 2695 occurred during the three-year period from 2020 to 2022. Only \$78,000 of the total amount contributed to the fund since 2009 was given before 2020.

Not all the funds deposited in Account 2695 have been spent. Account 2695 has a current balance of \$183,096. After receipt of our reports, BCH's Board closed Account 2695 and returned all remaining funds to general charitable operations.

- c. **Donor Awareness.** Many of the donor contributions to Account 2695, including those of certain individual trustees (or organizations with which they are affiliated), were specifically designated by such donors to support that account. We found no evidence that these donors knew either (a) that the Board neither approved nor was even aware of any ongoing expenses paid from the fund, or (b) that Dr. Blackwell was using the fund for expenditures unrelated to BCH's charitable purposes.

Perhaps more important is that one of BCH's most significant individual donors lacked awareness that Account 2695 existed and that significant portions of two of their recent donations to BCH were deposited into that account.

[Donor Redacted] donations account for 62% of the funds that Dr. Blackwell directed the accounting staff to transfer to Account 2695, but the documentation for his gifts conspicuously lack any designation for Account 2695. In an interview, [Donor Redacted] informed us that he was not aware of any account known as Account 2695, Sabbatical Fund, or the President's

³ Draft Report from Bert Davis, CPA to BCH, August 2023, Executive Summary.

This account was authorized and budgeted for with \$50,000 by the BCH executive committee in 2004. Subsequent Board and committee minutes contain no record that the Board authorized the continuation or replenishment of the fund beyond the initial \$50,000. Based on a review of documents, neither the budgeting for nor the continued use of these funds has been included in the annual budgets approved by the Board, nor are they reported separately on financial reports provided to the Board. Nevertheless, the 2695 Account continued to exist and to be replenished from time to time from inception through 2023.

⁴ Draft Report from Bert Davis, CPA to BCH, August 2023, Executive Summary.

Education Fund. In addition to asking him about the various names of the account, we described the account and its purpose – a discretionary account that the 2004 Executive Committee set up for Dr. Blackwell. We noted examples of expenses paid from Account 2695. [Donor Redacted] confirmed that he was not aware of the account based on any of its various names, its functions, or its uses.

[Donor Redacted] made two substantial donations to BCH - [Redacted Amount] at year-end 2020 and [Redacted Amount] in Fall 2022. In each instance, Dr. Blackwell instructed the accounting staff to allocate a portion of [Donor Redacted] donations to Account 2695. Documentation regarding these gifts was provided to the Board.

- The first donation consisted of two contemporaneous components, one from [Donor Redacted] personally and the other from a donor-advised fund. A portion of the gift was specifically designated to support a particular project, and the rest was designated by [Donor Redacted] “as you determine is the best use in the general operations of BCHNC.” At the time it was made, Dr. Blackwell instructed accounting staff to “keep available” \$295,000 of the amount and he (Dr. Blackwell) “will let you know where that should be applied.”⁵ Two months later, in hand-written notes dated February 25, 2021, Dr. Blackwell instructed accounting staff to allocate \$95,000 of the remaining \$295,000 funds to “fund 2695 which allows MCB discretion as discussed w/the donor.” In our interview, [Donor Redacted] did not recall ever discussing with Dr. Blackwell any individual account over which Dr. Blackwell had discretion, including Account 2695 or a functional equivalent.
- The second donation came by way of his donor-advised fund and was designated for “Where it’s needed most.” Dr. Blackwell exchanged emails with [Donor Redacted] on [Redacted Date] that referenced a telephone call they had about the donation. The check arrived in the mail on [Redacted Date], and Dr. Blackwell instructed a staff accountant to come to his office so he could “give [the accountant] the distribution of these funds.” In accounting records dated that same day, which appear to be based on Dr. Blackwell’s instructions, \$100,000 of the donation was allocated to Account 2695. In our interview, [Donor Redacted] did not recall discussing the donation or how it would be allocated.

As noted above, Account 2695 has a current balance of \$183,096. Using a first-in, first-out approach, the total amounts of the most recent four gifts to the account, as well as \$70,500 of the \$95,000 contribution made by [Donor Redacted].

In addition, Dr. Blackwell has contended that, after the \$50,000 funding in 2004, subsequent donations to Account 2695 were “unsolicited” meaning that, without his guidance, donors gratuitously directed considerable funds for Dr. Blackwell’s benefit because of his importance to the organization.⁶ That explanation lacks credibility given that several large donors specifically directed their donations to Account 2695, yet the donor of 62% of funds to Account 2695 does

⁵ See email from Dr. Blackwell to a staff accountant, dated December 29, 2020.

⁶ Email response from Lee Davis to Andy Andrews and Ed Chaney, dated August 16, 2023.

not recall ever having heard of that account or a functional equivalent. In conclusion, regardless of whether Dr. Blackwell solicited donations specifically to Account 2695, the key issue is that a major donor was apparently unaware that significant portions of his donations ended up in Account 2695 and were used for non-charitable personal expenses, in contravention of applicable tax laws.

- d. **Personal Nature of Expenses.** Dr. Blackwell's personal expenses charged to BCH include those from Account 2695 as well as other expenses charged to Dr. Blackwell's AMEX that were paid by BCH from accounts other than Account 2695 and that were not reimbursed by Dr. Blackwell (discussed in more detail below).

The factual findings are detailed in the draft report (the "Forensic Report") by Davis Forensic Group. The key finding from the Forensic Report is that during the three-year examination period, BCH funds paid for \$95,970.78 of Dr. Blackwell's credit card charges that were not reimbursed by Dr. Blackwell or deducted from his paycheck. Applying a reasonable standard, \$88,803.14 of the expenses paid by BCH were personal in nature. The Forensic Report describes the personal nature of these expenses, which include snacks, drinks, nutritional supplements, clothes, health care costs, subscriptions, and stays at Structure House—a self-improvement center where program participants stay in "luxury apartments."⁷

The overwhelming IRS guidance is clear that expenses for medical care, self-improvement/physical conditioning, food and drink, subscriptions, and clothing are "personal" and not "business." If the IRS were to review these nearly \$89,000 of transactions, there is a high probability they would be classified as personal. Indeed, the IRS and the US Tax Court have determined in other reported cases that expenses were "personal" and not "business" where the taxpayer's case was much stronger, *e.g.*, a pilot's contact lenses,⁸ a lawyer's hearing aids,⁹ an FBI

⁷ See description of accommodations at <https://www.structurehouse.com/>

⁸ "Expenses which are so inherently personal in nature and which represent items that are used for both personal and business purposes are not deductible as business expenses." *Masat v. Commissioner*, 784 F.2d 573 (5th Cir. 1986), *aff'd* 48 T.C.M. 317 (1984).

⁹ "Even if it is used in petitioner's business, in fact even if it is necessary for his successful law practice, the device is so personal as to preclude it from being a business expense." *Bakewell v. Commissioner*, 23 T.C. 803 (1955).

agent's gym membership,¹⁰ a news anchor's clothes and grooming,¹¹ and medical care related to professional activity.¹²

[Accountant] understood that personal expenses from Account 2695 were taxable as income based on advice from BCH's auditor in 2009, and he reminded Dr. Blackwell of this on several occasions. On the other hand, [Staff Member] and [a different employee] reported that they were not aware of either the nature or existence of Account 2695 until 2023.

Accounting staff were also aware that Dr. Blackwell had elected to be treated as a minister for federal tax purposes.¹³ The ministerial exception permits individuals to be treated as self-employed for some tax purposes, and accordingly, accounting staff we interviewed indicated that they assumed Dr. Blackwell was self-reporting income resulting from Account 2695 expenses. At that time, the law firm retained by BCH for general purposes also provided tax advice and form preparation for its personal clients, including Dr. Blackwell, which strengthened [Accountant's] assumption.

- 2) **AMEX Expenses Charged to Operational Funds.** Of the nearly \$89,000 of personal expenses described above, Dr. Blackwell charged nearly \$45,000 in personal expenses to operating funds (and not Account 2695).¹⁴ Unlike the \$50,000 the Executive Committee authorized for Account 2695 in

¹⁰ An FBI agent who was required to maintain good physical condition could not deduct health club membership dues. *Kessler v. Commissioner*, 49 T.C.M. 1565 (1985). Health spa expenses incurred by a law enforcement officer required to be in excellent physical condition were personal expenses not deductible as business expenses notwithstanding that they may have been necessitated by his employment. Rev. Rul. 78-128.

¹¹ A newscaster's costs for grooming were nondeductible personal expenses. *Hynes v. Commissioner*, 74 T.C. 1266, (1980). The cost of acquiring and maintaining clothing worn for work is not a business expense unless a certain uniform is required as a condition of employment and the clothing is not adaptable to general use. For example: cost of uniforms of police officers, firefighters, and letter carriers, among others, are business expenses because the uniform is required for work and is not suitable for ordinary wear. Rev. Rul. 70-474.

Television news anchor's costs for business suits, sports jerseys and other clothing worn on-air was not a business expense. "The general rule is that where business clothes are suitable for general wear, a deduction for them is not allowable...even when it has been shown that the particular clothes would not have been purchased but for the employment." *Hamper v. Commissioner*, TC Summary Opinion 2011-17.

¹² Hospital and medical care expenses of an attorney who was incapacitated by a severe attack of arthritis were personal expenses and not business loss expenses. *Bourne v. Commissioner*, 23 B.T.A. 1288 (1931), *aff'd*, 62 F.2d 648 (4th Cir. 1933), *cert. denied*, 290 U.S. 650 (1933). An actor could not deduct his expense for new dentures that eliminated a hiss caused by his existing dentures. "Although [the expense] may have occurred in connection with his professional activity, the expenditure was nevertheless so purely personal in character as to deny it classification as a business expense." *Sparks v. Commissioner*, 8 B.T.A.M. 180 (1939); *aff'd sub nom. Sparkman v. Commissioner*, 112 F.2d 774 (9th Cir. 1940). A corporation's costs for a registered nurse to accompany the company's president and principal shareholder on business trips following removal of a brain tumor were not ordinary and necessary business expenses. *Cummins Diesel Sales of Or., Inc. v. United States*, 321 F.2d 503 (9th Cir. 1963), *aff'g* 207 F. Supp. 746 (D. Ore. 1962). Expenses incurred by a professional singer for treatment of his throat by a medical specialist are personal medical expenses not deductible as ordinary and necessary business expenses. Rev. Rul. 71-45, 1971-1 C.B. 51

¹³ We express no opinion as to whether it is appropriate for Dr. Blackwell to avail himself of the ministerial exception.

¹⁴ Draft Report from Bert Davis, CPA to BCH, August 2023, Page 7.

2004, no general operating funds were ever intended, explicitly or implicitly, to cover Dr. Blackwell's personal expenses.

In addition, \$17,550 of the total expenses charged to the AMEX and paid by BCH were for Mrs. Blackwell to stay at the Structure House with Dr. Blackwell. Of these charges, \$9,800 were paid through BCH operating funds (and not from Account 2695).¹⁵

We also found discrepancies when we compared how Dr. Blackwell characterized expenses when he submitted his AMEX statements for payment against the actual nature of the expense. For example, many of the Amazon charges (which do not indicate the product purchased) are simply noted as "supplies" or "general admin" or "subscription." Similarly, Dr. Blackwell's categorization of personal expenses frequently was not consistent for the same product or service purchased at different points in time. As discussed further below, Dr. Blackwell also did not provide receipts consistent with the process applicable to all BCH employees.

- 3) **Car Purchases for the Blackwells.** BCH purchased a new 2022 Nissan Altima for Mrs. Blackwell in May of 2022, valued at \$30,283.49. The Board did not authorize this gift, nor was it provided the opportunity to do so as required by BCH's conflict of interest policy.

In response to an inquiry from the Personnel Policy Committee, Dr. Blackwell stated in a May 9, 2023 email, that "all I [Dr. Blackwell] know is that [Donor Redacted]...called [him] and said that they wanted to give my wife a car..." and that "I [Dr. Blackwell] had nothing to do with the transaction."

In an email to BCH counsel, Dr. Blackwell's counsel stated: "[Donor Redacted] offered to purchase a car for Mrs. Blackwell. He discussed that with Dr. Blackwell and Dr. Blackwell discussed it with his wife, who conveyed her 'wish list,' which Dr. Blackwell passed along to [Donor Redacted]. Dr. Blackwell did not know that the gift was only for ½ the car. [Staff Member] handled that and apparently made the decision to add the additional charges to Dr. Blackwell's income as per the [Staff Member's] email. This was done by [Staff Member] without instruction or direction by Dr. Blackwell."

We interviewed [Donor Redacted], certain BCH staff, and reviewed the transaction documents as well as BCH emails on the subject. According to [Donor Redacted], Dr. Blackwell initiated the transaction himself, not the other way around. Dr. Blackwell approached [Donor Redacted] about BCH purchasing for his wife a car from [Donor Redacted] to reward her sacrifice over the years. [Donor Redacted] also agreed to contribute to BCH some of the funds to cover the costs of the vehicle.

Sometime afterwards, according to [Accountant], [Donor Redacted] called to inform him that Mrs. Blackwell wanted to purchase an Altima and that he would be contributing half of the funds. [Accountant] presumed that [Donor Redacted], who was a BCH Board member, would discuss this transaction with the Trustees and seek necessary approvals. [Donor Redacted] presumed that [Accountant] would make the Board aware.

On May 9, 2022, Dr. Blackwell sent an email to [Donor Redacted] picking out the make and model of the car, as well as exterior and interior colors. The May 9 email was obviously a follow up from earlier

¹⁵ Draft Report from Bert Davis, CPA to BCH, August 2023, Exhibit 6, Page 20.

conversations on the same topic – e.g., “Dear [Donor Redacted]: My wife has done due diligence and here is her best thinking...I could not have built this Organization to what it is today without her support, encouragement, and sacrifice.”

On May 18, 2022, Mrs. Blackwell purchased the car according to the sales documents.

The dealership sales manager then called [Accountant] to inform him what car Dr. Blackwell had picked out and that an invoice would be sent over to BCH. [Accountant] presumed the Board had handled any necessary approvals and signed the invoice. [Accountant] then provided the invoice to another employee and discussed the invoice with [Staff Member]. This was the first [Staff Member] had heard about the transaction. [Accountant] then called the BCH’s external auditor to inquire how this transaction should be booked. The auditor informed [Accountant] that the amount of the invoice would need to be included in Dr. Blackwell’s compensation and that it would be taxable to him.

On May 26, 2022, [Staff Member] then sent Dr. Blackwell an email explaining how the transaction would be handled from a tax perspective. [Accountant] calculated the amount of tax that Dr. Blackwell would owe on the car and authorized a gross up payment to Dr. Blackwell of that amount.

[Donor Redacted] donated \$15,300 on May 24, 2022, which was received by BCH on May 31, 2022.

In our review of prior year minutes, we did not find where BCH’s Board approved or was even made aware that BCH purchased Dr. Blackwell’s wife a new 2022 Nissan Altima. This lack of disclosure was confirmed during our interview with [Donor Redacted], where he confirmed that the Board and the Executive Committee were not involved in approving the 2022 car transaction for Mrs. Blackwell. Based on our interviews with [Accountant] and [Donor Redacted], it appears they were the only BCH personnel aware of the purchase before it was made, other than Dr. Blackwell.

[Accountant] confirmed that general operating funds were transferred to [Donor Redacted] to purchase the car for Mrs. Blackwell. There is no apparent connection to that expenditure accomplishing BCH’s charitable purpose.

In addition to the 2022 Altima, we learned that BCH transferred at least four used “fleet” cars to Mrs. Blackwell during Dr. Blackwell’s tenure at BCH. Dr. Blackwell disclosed this past practice in his May 9, 2023 email to the Personnel Policy Committee. We learned from interviews that these cars were normally 4-8 years old at the time of transfer to the Blackwells. In review of past minutes, we found that only one of these transfers was authorized by the Board – the transfer of a 2008 Buick Park Avenue in 2016. The others were not. We understand from BCH staff that the Chair at the time of the 2016 transfer, [Redacted], raised a concern about the transfer. As a result, it was approved by the Board’s Executive Committee. Based on the minutes, the 2016 Board transfer demonstrates that Dr. Blackwell and [Donor Redacted] understood that Board approval should have been taken.

- 4) **Accounting Process.** In emails and in conversations, Dr. Blackwell and his counsel have attributed responsibility of Dr. Blackwell’s improper expenses and lack of documentation to BCH’s Treasurer. To confirm that, we (1) reviewed BCH policies and procedures and other relevant internal documents, (2) interviewed three key staff members, [Donor Redacted], and (3) gleaned information from relevant email correspondence. Our investigation revealed that Dr. Blackwell created a process outside of BCH policy that enabled him to keep the actual expenses paid by the AMEX card hidden.

This process has been practiced consistently for decades, dating back well before the hiring of the current Treasurer.

The process would begin with Dr. Blackwell marking up his AMEX statements – designating which expenses he considered “personal” and which he considered “business.” He would also indicate the nature or attribution of the various expenditures (*e.g.*, “payroll deduction,” “supplies,” “conference,” “2695”). Some he would mark individually, and some he would group together by category.

His assistant would then aggregate the expenses by their nature or attribution. The amount of expenses noted as “personal” would then be sent to payroll processing for the purpose of deduction from Dr. Blackwell’s paycheck.

Whatever expenses were not designated “personal” would be considered “business,” and BCH would pay the entirety of the AMEX credit card. All business expenses would be allocated for accounting purposes as Dr. Blackwell indicated on the AMEX statements. Dr. Blackwell and his assistants insisted that his office would be responsible for keeping all related receipts.

When the process was originally created, Dr. Blackwell’s office diligently kept receipts, aided in no small part by his assistant and BCH’s controller at the time. As BCH has experienced natural turnover, however, the diligence in preserving receipts declined, although, as described below, record retention was converted to electronic systems.

In 2011, BCH undertook an internal reorganization. As this point, an external candidate was hired to serve as Treasurer and remains in that position today. Dr. Blackwell’s system of processing AMEX statements remained in place.

The new Treasurer oversaw a transition from BCH’s paper-based accounting system to an electronic one. This system enabled invoices and receipts to be uploaded for review and approval by various parties. This system also allowed certain users to create an electronic stamp for various purposes (*e.g.*, “received on” or “approved by”). This stamp could only be applied by the applicable user. The Treasurer worked with Dr. Blackwell’s assistant to fashion a stamp that she could apply to AMEX statements. That stamp read “Confidential: See President’s Office for Documents.” According to our interviews, this stamp was created because Dr. Blackwell’s reimbursement process was a “fixed” part of the BCH accounting system that created gaps for auditing purposes. The “stamp” was a way of filling those gaps, that is, to inform BCH’s external auditors that receipts were in fact being kept and the location of such receipts.

In 2016, BCH changed to a new electronic accounting system that remains in use today. This system allows users to take and upload photos of invoices and receipts and no longer requires an electronic stamp on such documents. Thus, the practice of applying an electronic stamp ceased system-wide, including with respect to Dr. Blackwell’s AMEX statements.

On multiple occasions from his hiring date through 2023, [Accountant] was assured by Dr. Blackwell’s staff that, with respect to the AMEX expenses, receipts were being kept. [Accountant] also stated that he reminded Dr. Blackwell to keep all receipts associated with his AMEX payments. Dr. Blackwell did not utilize the new system for the AMEX statements, instead keeping his own system in place. According to [Accountant], Dr. Blackwell expressed frustration with those reminders regarding the

receipts and tax issue (his need to pay taxes on personal expenses), at one point “bowing up” in [Accountant]’s presence after one such reminder.

Even if BCH employees were aware of the relevant details of the impropriety of Dr. Blackwell’s expenses and lack of documentation, the reporting relationships and management approach inhibited action by Dr. Blackwell’s subordinates regarding these issues.

For example, in mid-May, before Mr. Goldston’s resignation, when [certain employees] attempted to engage directly with Trustees regarding Account 2695 and the AMEX expenses, Mr. Goldston sent them an email that included, among other things, the following:

The By-Laws are clear that Staff should not be reporting to individual trustees, but rather, to Dr. Blackwell. Reporting to Trustees is a violation of the By-Laws and a violation of the adopted chain of command. It is, in a nutshell, insubordination. Individual trustees (or for that matter committees) have no authority over Dr. Blackwell and no authority to give him directions.

Mr. Goldston and Dr. Blackwell communicated about this specific direction to [those employees]. In fact, Mr. Goldston appeared to have been more uncertain about the content of the email, asking “Are y’all pretty sure this will not push someone to go to full board or public. Would that look good to public, like trying to squash it?” Nevertheless, he subsequently sent the message to [those employees].

Further, BCH’s whistleblower policy directs all complaints to top management. It does not provide a mechanism to report complaints against Dr. Blackwell to anyone that oversees him. In addition, BCH’s Bylaws give Dr. Blackwell, as President, the unusual authority power to hire and terminate all employees, in addition to supervising all departments and functions of BCH.¹⁶

Fiduciary Duty of Loyalty. As CEO and Assistant Treasurer, Dr. Blackwell owes fiduciary duties to BCH.¹⁷ One of the fiduciary duties required of both directors and officers is *loyalty*. Loyalty means that the fiduciary must act solely in the beneficiary’s best interests, even to the detriment of what may be the fiduciary’s own interests.¹⁸ One key component of that duty of loyalty is to avoid self-dealing or conflict-of-interest transactions. The duty of loyalty generally requires that for a fiduciary to engage in a self-interested transaction with an organization to which he owes fiduciary duties, the transaction must be all of the following: (a) fully disclosed, (b) approved by the board *without* the vote of the interested person, and (c) fair and reasonable to the corporation.

Authorization of 2695. We did not find any evidence that funding of Account 2695 was authorized beyond the first \$50,000 allocated by the Executive Committee in 2004, but even if it were, the Forensic Report shows that the entire amount spent from the account was personal in nature and not for legitimate

¹⁶ Bylaws, Art V. Section 7.

¹⁷ See, e.g., *Davis v. Davis Funeral Serv.*, 2022 NCBC 38, 7, 2022 NCBC LEXIS 79, *4, 2022 WL 2841211; *Seraph Garrison, LLC ex rel. Garrison Enterprises, Inc. v. Garrison*, 247 N.C. App. 115, 787 S.E.2d 398 (Ct. App. 2016).

¹⁸ See Thomas L. Hazen & Lisa L. Hazen, *Duties of Nonprofit Corporate Directors - Emphasizing Oversight Responsibilities*, 90 N.C. L. Rev. 1845 (2012).

business or charitable purposes. Given that this fund was maintained solely for the personal benefit of Dr. Blackwell, its continued existence and management has been a prolonged conflict of interest for Dr. Blackwell that was not managed consistently with either BCH's conflict of interest policy or Dr. Blackwell's fiduciary duty of loyalty.

In addition, Dr. Blackwell directed [Donor Redacted] gifts away from their purpose of supporting BCH's general operations to benefit himself, and he was not fully transparent with donors who knowingly contributed to Account 2695. Doing so puts at risk donor and public trust, one of the most fundamentally important intangibles for any charity. In addition, using donated funds for noncharitable purposes contradicts tax and state laws governing charities.

Personal Expenses Charged to Operating Accounts. Even if one disregards all Account 2695 activity on the basis that the 2004 Executive Committee action authorized that it be replenished and continued to be used for Dr. Blackwell's personal expenses, there is no apparent basis to justify covering approximately \$45,000 in personal expenses spent *outside* of Account 2695 – funds that would otherwise be used to support the operations of BCH. Simply put, these funds must be returned to BCH. Pursuant to BCH policy, any other employee who behaved similarly would be terminated for cause.

Unauthorized Compensation Increase. Contrary to his duty of loyalty, the purchase of the 2022 Altima for Mrs. Blackwell constituted an unauthorized one-time compensation increase of \$37,018.49 (the price of the car plus the tax gross-up payment). There is no material distinction between an unauthorized "in-kind" transfer (BCH buying a car for Mrs. Blackwell) or Dr. Blackwell receiving an unauthorized cash bonus.

Opportunities for Improvement to Governance. While the BCH Board acted appropriately and quickly with respect to the AMEX expenses and Account 2695, BCH would still benefit greatly from improved governance, oversight, and policies. Two reforms with immediate significant impact would be to (i) change the "hub-and-spoke" model where all authority and decision-making flows through the CEO, with corresponding revisions to the Bylaws, and (ii) appoint a Chief Compliance Officer who reports directly to the Board. The scope and complexity of its operation justify the creation of such a position. In addition, we recommend BCH consider additional changes such as lengthening the Board chair term, reviewing budgeting and financial reporting processes and systems to facilitate more complete financial oversight, significantly revising existing policies, charging the personnel committee with annual CEO review and compensation recommendation to the Board pursuant to a compensation policy, and rotating external auditors.

Conclusion: We found no evidence that the Board knew about the purposes or uses of Account 2695 or its continued replenishment after 2004. As indicated above, Dr. Blackwell's AMEX reimbursement charges were paid by BCH, many of which he directly attributed to Account 2695 and for which there was little visibility from the accounting side. Once the Board was made aware of this situation, the Board has acted diligently, prudently, and consistent with the advice and guidance of counsel. The Board made its findings available to Dr. Blackwell and his counsel. After the Board received reports from counsel and the Forensic Accountant, the Board heard from Dr. Blackwell. Dr. Blackwell has agreed to repay personal expenses that were paid for with BCH funds. Such repayment will recover all identified funds used inappropriately for personal expenses. While these personal expenses and benefits raise serious concerns, as a proportion of BCH's total annual budget, the amount of personal expenses paid with BCH funds is much less than 1% of the annual operating budget. BCH's board, having received the reports from the review, has already



begun implementing governance, personnel, and policy changes to rectify this situation and strengthen oversight going forward.