THE PROSTESTANT EPISCOPAL CHURCH
IN THE DIOCESE OF SOUTH CAROLINA, *et al.*
v.
THE EPISCOPAL CHURCH, *et al.*

EXPERT REPORT OF PROFESSOR MARTIN C. McWILLIAMS, JR.

I, Martin C. McWilliams, Jr., have been engaged by Hellman Yates & Tisdale as an expert witness in the above-described matter. I am Professor of Law at the University of South Carolina, where I have been a member of the faculty of the School of Law since 1983. My courses have included Advanced Business Corporations, Agency & Partnership, Business Corporations (including limited liability companies), Contracts, Mergers & Acquisitions, Nonprofit Corporations, and Securities Regulation, among others. I am a member of the faculty of the South Carolina Bar Review, Inc., in which I teach Agency, Partnership, Corporations (including Nonprofit Corporations) and Limited Liability Companies. I base my opinions herein on my teaching experience and my education (LLM, Harvard University; JD, University of Mississippi, BA, University of Virginia), my professional experience and training (Law Clerk to the Hon. Robert A. Ainsworth, Jr., Judge of the United States Court of Appeals for the Fifth Circuit; corporate and securities practice with Davis Polk & Wardwell in their New York and London offices, 1977-83; corporate and securities practice with Haynsworth Sinkler Boyd, P.A., and predecessor firms, as counsel in their Columbia, South Carolina office, 1987-2013), my experience as Co-Reporter for the South Carolina Nonprofit Corporation Act of 1994 and co-author of the South Carolina Reporters' Comments thereto, and my review of the record in this matter, described in my response to the *subpoena duces tecum* I have received. My short-form *c.v.* is attached.

OPINIONS

Since the 18th Century, the Protestant Episcopal Church in the Diocese of South Carolina ("PECDSC") functioned, like all Episcopal dioceses, under the jurisdiction of a duly ordained Bishop of the Episcopal Church, as a self-declared, active member of The Episcopal Church ("TEC"). In 1973 then-serving Bishop filed articles of incorporation (the "Corporate Charter") with the South Carolina Secretary of State pursuant to the provisions of S.C. Code § 33-31-10 *et seq*. ("Nonprofit Corporations Generally"), thereby obtaining for PECDSC the benefits of a South Carolina nonprofit corporation. This action, which gave PECDSC the protection of the corporate veil, was likely a reaction to the demise of charitable immunity in South Carolina. In 1994 the South Carolina nonprofit-corporations statute was repealed; adopted in its place was the South Carolina Nonprofit Corporation Act of 1994, S.C. Code §§ 33-31-101 *et seq.* (the "Act").

The Act is a slightly modified version of the Official Text of the Revised Model Nonprofit Corporation Act (the "Model Act").

Upon the effective date of the Act, in 1994, PECDSC, as an existing nonprofit corporation organized for religious purposes, was by statute designated a "religious corporation."[1] The Model Act recognizes that religious corporations are not, as a matter of religious polity and organization, a comfortable fit with the usual corporate form. Further, it was recognized that religious nonprofits already in existence at the time of adoption of the Act would certainly have in place a regime of administration and internal organization that would, to a lesser or greater extent, be in conflict with the provisions of the new Act and would, in many cases, have religious implications that might be protected by constitutional mandates. Accordingly, the South Carolina General Assembly, as a neutral principle of law, accorded to religious corporations greater flexibility than is accorded to other nonprofit corporations. As the Introduction to the Official Text of the Model Act observes at page xxix,

> [F]or sound constitutional and policy reasons the Revised Act provides religious corporations with more flexibility in structure and operations than public benefit corporations. The constitutional limitations on state regulation of religious corporations are recognized by section 1.80. . . . By applying fewer rules to religious corporations, allowing them greater flexibility . . . the Revised Act recognizes the need to avoid unconstitutional intrusions into the activities of religious corporations and the desirability of allowing religious corporations great flexibility in their structure and procedures.

Section 1.80 of the Model Act was adopted as S.C. Code § 33-31-180. That section provides as follows:

> If religious doctrine *governing the affairs* of a religious corporation is inconsistent with the provisions of this chapter on the same subject, the religious doctrine controls to the extent required by the Constitution of the United State or the Constitution of South Carolina, or both.

The Official Comment to § 33-31-180 explains the function of the section:

> The Model Act . . . allows religious corporations to be formed and gives them the same rights and privileges as other corporations. The Model Act avoids interfering with the free exercise of religion by negating or allowing religious corporations to negate provisions of the Model Act that might result in excessive entanglement in religious activities by the state. By limiting state intrusion the Model Act uses the least restrictive means to provide an *orderly structure in which religious corporations can be formed and operate.* Section 1.8 is based on the recognition that some provisions of the Model Act may conflict with the United States Constitution or state constitutions. . . . [Section 1.80

[1] *See* S.C. Code § 33-31-1706(a)(2).

providcs] that to the extent religious doctrine applicable to a religious corporation sets forth provisions inconsistent with provision of the Model Act, the religious doctrine law shall control to the extent required by the United States Constitution or applicable state constitutions.

The text emphasized in the two paragraphs quoted above makes clear that § 33-31-180 applies to the operating rules for religious corporations – religious law, custom, internal organization, administration – that are protected under United States and South Carolina case law interpreting constitutional limitations on civil regulation of religious organizations. Subsection 180 functions by nullifying provisions of the Act that conflict with protected operational rules found within the polity of religious corporations. The religious corporation's operational rules thus imported by subsection 180 become, in effect, the controlling civil rules – the relevant neutral principles of corporate law.

The source of operational rules for South Carolina religious-nonprofit corporations are the corporation's bylaws and articles of incorporation. Every nonprofit must have both.[2] According to S.C. Code § 33-31-140(4), bylaws are "the code or codes of rules, other than the articles, adopted pursuant to this chapter for the regulation of management of the affairs of the corporation irrespective of the name or names by which the rules are designated." A corporation's articles may also include provisions "managing and regulating the affairs of the corporation [and] defining, limiting, and regulating the powers of the corporation [and] its board of directors."[3] In case of conflict, the articles govern.

The federal and South Carolina caselaw interpreting constitutional protection of religion holds that the articles and bylaws of religious corporations are protected from civil interference. Subsection 180 performs this constitutional function by substituting the operational provisions of the articles and bylaws of religious corporations for inconsistent provisions of the Act. As above, the operational rules of religious corporations thereby become the relevant corporate law.

Long usage and practice can also be a source of a corporation's governance provisions.

Once the governance provisions of a religious corporation are identified they are, effectively, a set of agreements, the contract expressing the rights and duties among a corporation and the persons who govern it. As such, they are subject to interpretation using familiar neutral principles of contract law.

A South Carolina nonprofit must also have a board of directors.[4] If the articles so provide, this may be a single person. Directors may be elected if there are members entitled to vote for directors; whether there are to be such members must be established in the articles. If

[2] Articles of incorporation are required to begin a corporation's life. Bylaws are required by S.C. Code § 33-31-206.
[3] S.C.Code § 33-31-202(c)(3).
[4] S.C. Code § 33-31-801.

there are no such members, the board members may be delegated or appointed as provided in the articles or bylaws.[5]

PECDSC's 1973 Charter contains no reference to members entitled to vote for directors. Accordingly, PECDSC has no such members. Therefor the board must be designated or appointed as provide in the articles or bylaws. The Charter requires that "all Managers, Trustees, Directors or other officers" be named. Two officers are named – a Secretary and Treasurer. The only other named person is the Bishop. Because a nonprofit is required by statute to have at least one director, the Bishop is by default that "Director," designated in the articles.

Where a corporation has no members to elect directors, and the articles and bylaws are silent on a method to appoint or designate subsequent directors, subsequent directors must be "elected" by the board. It is my opinion that the custom initiated in 1973, and honored ever since, was that the articles designate the Bishop in office from time to time as the sole director.

In 1973 and for the next 37 years PECDSC did not have a document called "bylaws." The Act mandates bylaws, by whatever name they may be called. The 1973 articles provide that the Corporation is to "continue the operation of an Episcopal Diocese under the Constitution and Canons of The Protestant Episcopal Church in the United States of America." In this way the Charter incorporates by reference the Constitution and Canons of TEC. It is my opinion that, as such, the Constitution and Canons – a set of corporate governance rules – constitute the bylaws of PECDSC. For the next 37 years no other set of corporate governance rules was substituted for the TEC Constitution and Canons, by long practice firmly establishing them as the governance rules of the PECDSC – the bylaws required by the Act.

In 1994, when the administrative provisions of the Act came into the picture, TEC's well-established law, custom, administration, and internal organization were protected from conflicts with the new statute by § 33-31-180.

In 2009-10, under the leadership of the Rt. Rev. Mark Lawrence, the PECDSC entered into a process of disassociation from TEC. As a part of that process, Bishop Lawrence and those cooperating with him purported to amend PECDSC'S Corporate Charter to remove the legal connection with TEC from the Charter's purpose statement, and to provide that the PECDSC would abide thereafter by its own Constitution and Canons. The purported amendment was adopted at the 2010 Diocesan convention and filed with the Secretary of State on October 22, 2012. Bishop Lawrence signed the filing as "president" of the PECDSC.

It is my opinion that the purported amendment of PECDSC's Corporate Charter was invalid and of no legal effect. This is for two reasons. The first reason is that the substance of the purported amendment was in direct conflict with the Charter's own limitations on amendment. Through its 1973 Charter and long subsequent practice, PECDSC accepted the consequences of

[5] S.C. Code § 33-31-804.

association with the TEC. The Charter provided that "The purpose of the said proposed Corporation is to continue the operation of an Episcopal Diocese under the Constitution and Canons of The Protestant Episcopal Church in the United States of America." This Charter provision (which, of course, overrides any inconsistent bylaw provision) effectively incorporates by reference TEC's Constitution and Canons as in effect from time to time, including its procedures for amendment. The Charter could not thereafter be amended in a way inconsistent with the Constitution and Canons. In my opinion, this incorporation by reference had an effect similar to that of requiring the approval of a third person to amend PECDSC's Charter. Under subsection 180, this administrative provision trumps the inconsistent charter-amendment provisions of the Act found in S.C. Code § 33-31-1001 and -1002.[6] In effect, the incorporated administrative rules, taking precedence over the inconsistent provisions of the Act via subsection 180, *become the relevant neutral principles of corporate law.* Accordingly, the purported amendment of PECDSC's Charter, which is grossly inconsistent with TEC's Constitution and Canons, is invalid.

The second reason that the purported amendment of PECDSC's Charter is invalid relates to provisions of the Act which are *not* in conflict with religious dogma and therefore *do* apply to the operations and actions of PECDSC. It is my opinion that proper procedures under the Act for amendment of the PECDSC Charter were not followed. The actions purported to be taken leading to amendments of the Corporate Charter were purported to be taken by corporate officers not authorized thereunto and in violation of their fiduciary duties to the PECDSC, and lacking proper statutory procedures, and accordingly were invalid. Included in these inappropriate and ineffective actions were these:

- Bishop Lawrence and the priests who cooperated with him took sacred ordination vows that, in effect, constituted their acceptance of fiduciary duties to carry out their promises to the corporation and the TEC. Actions taken by corporate officers in violation of their fiduciary duties of loyalty are invalid.
- Bishop Lawrence's engagement as Bishop was a contract, which he breached. A total breach of contract justifies the other party to the contract in invalidating it.
- Bishop Lawrence and those who cooperated with him, breaching their vows, committed material misrepresentations (both express and of omission) and fraud, and should be estopped from arguing that their powers within the Diocese were not extinguished.
- Bishop Lawrence and those cooperating with him have acted oppressively against the best interests of PECDSC, its parishes, and TEC, have wasted corporate assets, and have failed to carry out the corporate purpose stated in the Charter. In so doing they have violated their corporate duties under the Act, and are subject to removal from their offices by judicial action, and to have their purported actions as corporate officers set aside.

[6] Subsection -1003 would also be nullified by operation of subsection 180, but it is irrelevant as it provides for amendment by members, and PECDSC's Charter has not and does not provide for members.

- The actions purported to be taken by Bishop Lawrence and those cooperating with him in the course of attempting withdrawal from TEC were *ultra vires* and unenforceable.
- Bishop Lawrence and those cooperating with him have, in dealing with the personal, real, and intellectual property of PECDSC and its parishes, committed conversion, and their purported actions in so doing should be set aside.
- The record as developed in this case up to the present does not make clear how Bishop Lawrence at one point was authorized to characterize himself as "president" of PECDSC or how others subsequently adopted that title, or how or by what authority the Standing Committee was called "the directors," or indeed by what authority virtually any of the corporate actions taken on Bishop Lawrence's watch were justified.
- PECDSC, under the direction of Bishop Lawrence and those cooperating with him, has exceeded and abused the authority conferred upon it by law and has conducted it affairs in a persistently fraudulent and illegal manner; the corporate assets have been and are being misapplied and wasted; and the corporation is no longer able to carry out its purposes as stated in its Charter; all of the foregoing within the meaning of S.C. Code § 33-31-1430.

CONCLUSION

I hold the foregoing opinions within a reasonable degree of professional certainty. I reserve the right to alter or amend this report as the facts in this matter continue to be developed.

/s/ *Martin C. McWilliams, Jr.*

Martin C. McWilliams, Jr.
Professor of Law