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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF TEXAS
TYLER DIVISION

IN RE:	§	
	§	
LON MORRIS COLLEGE, a	§	**CASE NO. 12-60557**
Not-for-Profit Corporation,	§	**Chapter 11**
Debtor	§	
	§	

	§	
Lon Morris College,	§	
Plaintiff,	§	
v.	§	
	§	
Dr. Miles McCall, Bill Wagner,	§	
Frank Ashcroft, Bob Staten,	§	
Gene Brumbelow, Windol Cook,	§	
Helen Dubcak, June Deadrick,	§	
Jim Crawford, and Mark Brown,	§	**Adversary No. 13-_____**
	§	
Defendants	§	

LON MORRIS COLLEGE'S ORIGINAL COMPLAINT

Plaintiff Lon Morris College hereby files its Original Complaint Against Defendants Dr. Miles McCall, Bill Wagner, Frank Ashcroft, Bob Staton, Gene Brumbelow, Windol Cook, Helen Dubcak, June Deadrick, Jim Crawford, and Mark Brown, respectfully stating as follows:

INTRODUCTORY STATEMENT

1. Lon Morris College ("Lon Morris" or "the College") was the oldest existing two-year college in Texas. Lon Morris survived two World Wars and the Great Depression. But, Lon Morris could not survive Dr. Miles McCall ("McCall"). Indeed, the fiduciary failings, incompetence, mismanagement, gross negligence, and cover-up of McCall and certain members of Lon Morris's Board of Trustees (the "Board") would ultimately destroy Lon Morris and cause millions of dollars in damages to the institution that they were entrusted with protecting.

2. From 2005 until 2012, Defendant Dr. Miles McCall ("McCall") served as the president of Lon Morris College ("Lon Morris" or "the College"). As its president, McCall owed fiduciary duties to Lon Morris, including the duty to always act in Lon Morris's best interest. Moreover, as Lon Morris President, McCall was required under the law to act with complete candor on Lon Morris's behalf. McCall failed in his duties and, ultimately, in concert with others, caused Lon Morris to incur significant damages in, *inter alia*, the following ways:

> (1) By encouraging Lon Morris's Board of Trustees (the "Board") to authorize a secured loan transaction with Amegy Bank in 2006, which included a side agreement swapping the floating rate of interest provided for in such loan with an obligation to pay Amegy a fixed rate of interest. The side agreement was evidenced by an ISDA[1] Master Agreement dated April 10, 2006, Form ISDA®1992, and related Schedule and Confirmation (collectively, the "Side Agreement"). Neither McCall nor any other Board member had any idea how the Side Agreement operated or what its legal effect was on the loan transaction. The Side Agreement caused Lon Morris to owe Amegy Bank in extra interest payments over what the loan would have otherwise cost;

[1] An ISDA Master Agreement is a reference to standard form of commercial documentation approved by the International Swaps and Derivatives Association, Inc. Such documentation is complex and while standardized should not be utilized by someone without extensive experience in (a) the negotiating and documenting of transactions with such documentation and (b) the relevant market terms for the modification of such documentation."

(2) By improperly using certain endowment funds (the "Long Endowment") for operational expenses, when the use of those funds was specifically restricted by the underlying gift and Lon Morris's own endowment policy (the "Endowment Policy"), and then failing to disclose his improper actions to the Board;

(3) By failing to disclose to the Board that he had improperly used endowment funds and then making or knowingly allowing those under his control to make retroactive adjustments to Lon Morris's books and records to indicate that the Long Endowment remained intact as a loan when there was no loan and, in fact, the funds had already been spent for improper and unauthorized purposes;

(4) By executing an unauthorized wraparound real estate lien note with Tilley, LLC ("Tilley") in excess of $6 million to replace an existing lease with Tilley (the "Tilley Lease"), when doing so significantly increased Lon Morris's secured debt and its overall liability exposure in the event of a default;

(5) By refinancing existing debt facilities with Texas National Bank without authority and imprudently pledging Lon Morris's valuable mineral interests as collateral for a loan that would almost certainly be in default—and did result in default—soon thereafter;

(6) By failing to collect approximately $1 million in tuition from students who were allowed to take classes, earn credit for those classes, and/or graduate; and

(7) By destroying Lon Morris's value as a going concern by implementing a grossly negligent business plan, which plan included, without limitation, expanding Lon Morris's student population in a manner that would cause Lon Morris to incur substantial debt and new expenses beyond Lon Morris's ability to pay same and adding programs like football, hospitality, and agriculture when the addition of such programs would require massive expenditures well beyond any increase in revenues that reasonably might flow from such programs.

3. McCall's improper actions and breaches of his fiduciary duties caused Lon Morris in excess of $20 million in damages. For example, and without limitation, McCall's improper

use of the Long Endowment caused Lon Morris damages in excess of $1.017 million. McCall's failure to protect Lon Morris in connection with the Side Agreement damaged Lon Morris by approximately $1 million. McCall's unauthorized refinance with Texas National Bank caused Lon Morris damages of, at least, $400,000. McCall's failure to collect tuition cost Lon Morris close to $1 million. McCall's gross mismanagement, unauthorized actions, and nondisclosures devalued Lon Morris by millions of additional dollars, including $8-$10 million in accreditation value alone. McCall's grossly negligent conduct, unauthorized actions, and nondisclosures also exposed Lon Morris to another $17 million in claims filed in the bankruptcy case by Sam Houston State (the alternate beneficiary of the Long Endowment) and the Texas Attorney General for violating the public trust.

4. During the relevant times of McCall's tenure, Defendants Bill Wagner ("Wagner"), Frank Ashcroft ("Ashcroft"), Bob Staton ("Staton") Gene Brumbelow ("Brumbelow"), Windol Cook ("Cook"), Helen Dubcak ("Dubcak"), June Deadrick ("Deadrick"), Jim Crawford ("Crawford"), and Mark Brown ("Brown") (collectively, the "Board Defendants") served as Board members and served on the Executive, Finance Committee and/or Endowment Committees of the College. The Board Defendants were required to act in Lon Morris's best interest and supervise McCall's actions, including by authorizing financial and endowment transactions made outside of day-to-day operations. The Board Defendants breached their duties to Lon Morris during McCall's tenure in, at least, the following ways:

(1) Authorizing McCall's execution of the sophisticated Side Agreement when the participating Board Defendants did not know what the agreement was, did not understand the agreement, did not know the negative implications the agreement could have on Lon Morris, did not seek guidance from a competent professional, and knew that they could not reasonably rely upon McCall's advice with regard to the agreement when they knew (or should have

known) that McCall was not competent to advise on complex or sophisticated financial transactions;

(2) By allowing McCall and his staff to invest the Long Endowment in a manner contrary to the Endowment Policy and by wholly failing to follow-up regarding the use and investment of the Long Endowment when the Board Defendants—particularly those on the Endowment Committee—were charged with assuring that the Long Endowment was invested and used in accordance with the Endowment Policy and the other restrictions placed on its use;

(3) By failing to disclose to the Board that McCall had improperly used the Long Endowment after learning of McCall's actions, and then ignoring McCall's retroactive adjustments to Lon Morris's books and records to show that the Long Endowment remained intact as a loan when there was no loan and, in fact, the funds had already been spent for improper and unauthorized purposes;

(4) By failing to assure that Lon Morris collected approximately $1 million in tuition from students who were allowed to take classes, earn credit for those classes, and/or graduate; and

(5) By destroying Lon Morris's value as a going concern by authorizing the implementation of a grossly negligent business plan, which plan included, without limitation, expanding Lon Morris's student population in a manner that would cause Lon Morris to incur substantial debt and new expenses beyond Lon Morris's ability to pay same and adding programs like football, hospitality, and agriculture, when the addition of such programs would require massive expenditures well beyond any increase in revenues that reasonably might flow from such programs.

5. Like McCall's actions, the Board Defendants' breaches of their duties caused Lon Morris in excess of $20 million in damages. For example, and without limitation, the Board Defendants' breaches of their duties in connection with the sophisticated derivatives agreement caused Lon Morris to incur close to $1 million in damages. The Board Defendants' breaches of their duties in connection with the Long Endowment caused Lon Morris in excess of $1.017

million in additional damages. Moreover, the Board Defendants' grossly negligent actions further devalued Lon Morris by millions of dollars, including a loss of approximately $8-$10 million in connection with its accreditation value alone. The Board Defendants' grossly negligent actions also exposed Lon Morris to another $17 million in claims filed in the bankruptcy case by Sam Houston State (the alternate beneficiary of the Long Endowment) and by the Texas Attorney General for violating the public trust and other wrongs.

6. McCall and the Board Defendants should now be held responsible for their grossly negligent, improper, and financially devastating actions.

PARTIES

7. Plaintiff Lon Morris is a Texas non-profit corporation.

8. Defendant Miles McCall is the former president of Lon Morris. McCall is a resident of Jacksonville, Texas and may be served with process at 1025 County Road 3131 Lakeview Drive, Jacksonville, Texas, or wherever he may be found.

9. Defendant Bill Wagner is a former member of the Board and chair of the Executive Committee. Wagner is a resident of Houston, Texas and may be served with process at 4420 FM 1960 W Suite 101, Houston, Texas 77068, or wherever he may be found.

10. Defendant Frank Ashcroft is a former member of the Board and Endowment Committee. Ashcroft is a resident of Nacogdoches, Texas and may be serviced with process at 4117 Mystic Lane, Nacogdoches, Texas 75965, or wherever he may be found.

11. Defendant Bob Staton is a former member of the Board and Endowment Committee. Staton is a resident of Lindale, Texas and may be served with process at 15419 McMillan Dr., Lindale, Texas 75771, or wherever he may be found.

12. Defendant Gene Brumbelow is a former member of the Board, including the Board's Executive and Finance Committees. Brumbelow is a resident of Cherokee County, Texas and may be served with process at 995 CR 3131, Jacksonville, Texas 75766, or wherever he may be found.

13. Defendant Windol Cook is a former member of the Board and the Board's Executive and Finance Committee. Cook is a resident of Jacksonville, Texas and may be served with process at P.O. Box 937, Jacksonville, Texas 75766, or wherever he may be found.

14. Defendant Helen Dubcak is a former member of the Board and the Board's Executive and Finance Committees. Dubcak is a resident of Crockett, Texas and may be served with process at 4301 FM 132, Crockett, Texas 75835, or wherever she may be found.

15. Defendant June Deadrick is a former member of the Finance Committee. Deadrick is a resident of Houston, Texas and may be served with process at 11603 Mullins Dr., Houston, Texas 77035, or wherever she may be found.

16. Defendant Jim Crawford is a former member of the Board and the Endowment Committee. Crawford is a resident of Huntsville, Texas and may be served with process at 1054 Elkins Lake, Huntsville, Texas 77340, or wherever he may be found.

17. Defendant Mark Brown is a former member of the Board and the Executive and Finance Committees. Brown is a resident of Austin, Texas and may be served with process at 11762 Jollyville Road, Austin, Texas 78759, or wherever he may be found.

JURISDICTION

18. This Court has jurisdiction to consider this matter under 28 U.S.C. §§ 157(a) and (b) as a matter arising in, arising under and/or related to this bankruptcy case under Chapter 11 of the United States Bankruptcy Code. This is a non-core matter, but is "related to" the bankruptcy.

19. Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409. The predicate for the relief sought herein is Sections 105, 541 and 1107 of Title 11 of Title 11 of the United States Bankruptcy Code.

FACTUAL BACKGROUND

A. General Background

20. Prior to its demise, Lon Morris was the oldest existing two-year college in Texas. Lon Morris provided quality collegiate level education to students for more than 157 years (1854-2012) and was managed by the Board and the various Board Committees, including the Executive Committee, the Endowment Committee, and the Finance Committee. The Board worked closely with Lon Morris's president with regard to Lon Morris's operations and, indeed, was charged with providing oversight and authorization to Lon Morris's president for all transactions outside of normal day-to-day operations (*e.g.*, financial transactions, endowment transactions, etc.).

21. During July 2005, the Board selected McCall to serve as Lon Morris's president. Despite the Board's obligation to assure that they hired someone competent to serve as Lon Morris's president, the Board failed to thoroughly vet McCall prior to hiring him. While McCall held a doctorate in Curriculum & Instruction, Training, and Development from Texas A&M University, he did not have any experience whatsoever managing a college or any other business for that matter. The Board would have learned of McCall's lack of relevant experience had they fulfilled their duty to thoroughly vet McCall prior to hiring him. Moreover, the Board would have learned that McCall was functionally illiterate in accounting and finance matters, having never taken any accounting courses, having taken no substantive finance courses and having no business or managerial or operational expertise of any significance. McCall could not even read a financial statement without significant help. McCall was simply not qualified for the job of

operating a multimillion-dollar educational institution. The Board failed completely to undertake an appropriate hiring process, to seek the help of experienced third parties, or to recognize that McCall was totally unqualified prior to hiring him.

22. The Board's failure to properly vet McCall prior to hiring him and McCall's failure to disclose his financial incompetence to the Board would cause significant and detrimental problems within Lon Morris. Indeed, the Board's failures and McCall's concealment would ultimately cost Lon Morris millions of dollars and its ultimate collapse.

B. The Side Agreement

23. It did not take long for the Board's negligence in hiring McCall and McCall's lack of candor with regard to his financial incompetence to set Lon Morris up for failure. On or about April 10, 2006, McCall executed a series of loan and finance-related documents with Amegy Bank on Lon Morris's behalf. These documents included a loan agreement, a deed of trust, and the Side Agreement. The Side Agreement was the type of agreement that was well beyond McCall's limited financial knowledge and, by McCall's own admission, was beyond any of the Board's expertise or understanding.

24. Despite the fact that McCall had a duty to disclose his financial incompetence and to demand that the Board seek guidance from a qualified professional, McCall remained silent and failed to otherwise take any action to protect Lon Morris. Instead, McCall championed the Side Agreement at a time when he had no idea what the Side Agreement was, how it functioned, what it meant, or how the Side Agreement could damage Lon Morris.

25. McCall now acknowledges that Amegy Bank presented the Side Agreement as a tool to make Lon Morris "get the feeling of a fixed [interest] rate[,]" even though the Side Agreement did not actually provide for a fixed interest rate. McCall did not know, however, if Amegy Bank's presentation was true. Moreover, McCall failed to disclose his lack of

understanding or knowledge to the Board. Instead, McCall blindly charged full steam ahead with the transaction.

26. The Board did nothing to protect Lon Morris from the Side Agreement. The Board did not seek a competent professional to advise on implications of entering into the Side Agreement. Instead, the Board blindly approved the Side Agreement without having any idea whether the transaction would be in Lon Morris's best interest or not. The Board should have been fully aware of McCall's financial incompetence, particularly with regard to complex financial matters. Yet, the Board apparently deferred to McCall's wisdom—or lack thereof—in authorizing McCall to execute the Side Agreement. The Board simply had no basis to reasonably believe that the Side Agreement was or might be in the best interest of Lon Morris. Like McCall, the Board simply had no idea.

27. The Board and McCall's negligent approval and execution of the Side Agreement ultimately proved costly for Lon Morris. Lon Morris would later face in excess of $1.5 million in costs and would have to borrow almost $1 million dollars from the Scurlock Foundation to stop the costs from continuing to increase.

C. McCall Proposes A Program Of Expansion In The Face Of Economic Crisis.

28. Under McCall's leadership, Lon Morris struggled financially. Nevertheless, by mid- to late- 2008, McCall determined that the answer to Lon Morris's struggles was an aggressive program of expansion when conventional wisdom would call for austerity. McCall encouraged the Board to vote on an expansion plan that would include the addition of new programs, including an agriculture program, a hospitality program, and a football program with recruiting. McCall's answer to the Lon Morris then existing financial problems was to irresponsibly borrow, spend, and expand Lon Morris into prosperity.

29. McCall's decision to borrow, spend, and expand Lon Morris into prosperity was not well reasoned or advisable. A secured lender had already "captured" $400,000 of Lon Morris's assets. Lon Morris's expenses at that time generally exceeded its cash revenues for several years. Furthermore, Lon Morris did not have the infrastructure (*e.g.*, housing, athletic, academic and other facilities) to immediately accommodate significant expansion and growth. Accordingly, Lon Morris had to incur significant new debt to improve its infrastructure with no reasonable basis for believing that its revenues would be sufficient to cover its ever-increasing expenses. Finally, and perhaps more alarming, McCall ignored or wholly failed to investigate the fact that athletic programs, like football, are generally a financial burden on all but a select number of educational institutions—generally established Division I institutions and did not disclose this to the Board.[2] In other words, McCall's idea to add a football program, at a minimum, was almost guaranteed to cause significant new financial problems, not solve them. McCall simply did not seek the counsel of a competent third-party consultant who could have advised him regarding the economic impact of an aggressive expansion program. Instead, McCall sold his "spend and expand program" to the Board, who also chose not to properly investigate or evaluate the propriety and viability of McCall's program.

30. The Board was on notice that McCall's program of expansion was fraught with peril. Indeed, the debate over expansion in the face of a looming financial crisis for the College created a great divide in the Board that led to mass resignations in October 2008. Board members that astutely recognized the almost certain disaster of unreasonable expansion resigned,

[2] USA Today published an article on May 15, 2008 titled "Few athletics programs in black; most need aid[.]" The article noted that, without being subsidized by the institution, only 19 of the 119 Division I schools, made money from their athletic programs as a whole during fiscal year 2006 and only 67 of 119 of the Division I programs made money on football or men's basketball during the same fiscal year. Logically, these are likely Division I programs that enjoy lucrative television contracts—a benefit that lower division schools, particularly community colleges, do not enjoy. Indeed, the article noted that Division I-AA athletic programs received about 76% of their revenues from other institutional sources—meaning the athletic programs were heavily subsidized.

while remaining Board members, like Ashcroft, Brumbelow, Cook, Brown, Wagner, Dubcak, and Staton, irresponsibly and unreasonably bought in to the idea of expansion, without requiring an economic analysis or feasibility study from a third party professional that evaluated such expansion.

31. The minutes from Lon Morris's November 2008 Board meeting highlight the conflict that led to the resignations and the remaining Board members' decision to agree to an irresponsible program of expansion. In relevant part, the minutes provide as follows:

> "A select group of board leaders began to demand that additional expenses be cut, expansion of potential new programs be curtailed or halted, and pressure was applied to the administration to change the model from growth to decreasing the programs without disclosure and discussion with the full board. Ultimately, the select group of board members began to advocate that the college move to liquidation and closure. Other board members and members of the executive committee were adamant that instead, the college pursue alternative banking options, pursue additional revenue generating growth options, and challenged the thought process of closing. This discourse led to several board members resigning and the remaining members of the executive committee continued moving forward to discover options for survivability as an institution."

32. With dissenting Board members out of the way, McCall sold his spend and expand program by acting as if he actually understood the complex financial implications of such a program—which he did not. For example, the following excerpt from the November 2008 Board minutes reflect McCall passing himself off as a financial and regulatory expert:

> Michael Schneider asks the status of the Cooper gift? Dr. McCall responds: the gift was a non-endowed naming gift. In the past we (LMC) have borrowed from gifts of this kind and that such actions are legal, followed GAAP guidelines and was approved by the external auditor prior to any action.
>
> Dr. McCall: Cooper gift can't be used if he doesn't sign the letter. Chairperson Wagner said the situation was shared with Mr. Cooper. If he signs the letter it will still require board approval to utilize the funds. The school is good, administration is good but

> enrollment has to increase. At present there are no funds to draw on. School is dependent on donations and student tuition only.
>
> Dr. McCall explains how the Cooper gift was received and booked.
>
> * * *
>
> Dr. McCall says student revenues need to be equal to operational expenses. We have depended on development and investment income in the past. Development work should be for development of the school and revenue has to increase from students.
>
> Financial challenges: Too much debt and has to be collateralized (debt ratio), stock portfolio devalued due to current economic situation in the USA. LMC needs $750K to operate on until Spring 2009. Bank captured $400K in cash assets to bring debt/collateral ratio within compliance.
>
> * * *
>
> Dr. McCall discusses net asset increase and the debt service.
>
> * * *
>
> Miles McCall discusses Banking options Page 4 [of board book]
>
> * * *
>
> . . . . Dr. McCall explains that these are the options presented by the bank. There are other options listed in the board book. Otherwise there are really no other developed options. Discusses the cash flow per year…

33. The remaining Board members, including the Board Defendants, unreasonably adopted McCall's expansion program with direct knowledge of facts that would have placed any reasonable person on notice that expansion as McCall proposed at the time would exacerbate, not improve, Lon Morris's fragile financial condition. Indeed, the November 2008 Board minutes confirm that the Board knew Lon Morris's student revenues lagged behind operational expenses, too much debt had to be collateralized, and its stock portfolio was being devalued by then current economic conditions. At that same time, the Board was even exploring the possibility of tapping into a restricted endowment (*i.e.*, the Cooper Endowment) so that it could secure cash to use for

on-going operational expenses. Despite this knowledge, the same Board minutes reflect that the Board, particularly Brown, Dubcak, and Brumbelow, were fully in agreement with McCall's expansion proposal in the face of the College's economic crisis.

34. McCall's program of irresponsible and unjustifiable expansion would eventually cost Lon Morris millions of dollars. Had McCall been honest about his financial incompetence at the time, the Board likely would have recognized (or certainly should have) that irresponsible expansion would be disastrous. Instead, the Board unreasonably agreed with McCall when the Board was fully aware of facts that would have made any reasonable person (or board member) proceed on a path of restraint rather than an aggressive path of irresponsible expansion. The Board's irresponsible decisions eventually cost Lon Morris millions of dollars.

D. The Long Endowment

35. In hindsight, McCall's decision to utilize the Cooper Endowment during 2008 to help cover operational expenses was foretelling. Indeed, McCall's willingness and desire to access endowment resources would later damage Lon Morris by at least $1.017 million when McCall improperly, and without authority, raided the Long Endowment.

36. On April 27, 1984, James D. Long ("Long"), a Lon Morris alumnus and committed benefactor, executed his Last Will and Testament (the "Long Will"). The Long Will expressly intended to bequeath a gift to Lon Morris out of the residue of his property. Lon Morris's use of the gift, however, was expressly restricted as evidenced by the following excerpt from the Long Will:

> . . . I give, devise and bequeath all the rest and residue of my property to Lon Morris College, Jacksonville, Texas . . . in perpetuity, for the following uses and purposes:
>
> (a) To be invested and re-invested as the College shall see fit;

(b) for the first fifty years, one-half of the income shall be applied to the corpus and the other half of the income shall be used exclusively (1) to purchase books and journals for the College's main library and (2) to modernize library services and improve student access to library resources by the purchase of computer search and photography equipment and other similar equipment which may become common to libraries in the future;

(c) after fifty years have elapsed, the entire income from this trust shall be used in support of the Lon Morris Library as directed in (b) above. Funds not expended during any calendar year shall be added to the corpus. If the cost of some major piece of equipment requires expending more than one year's revenue generated by this trust during a single year, however, a portion of the annual income may be allowed to accumulate for such purchase over a period not to exceed five years;

(d) no charge shall be required of anyone using any item purchased with these funds;

(e) purchases to be made with these funds shall be determined by a committee of five (5) faculty members and librarians (one of which shall be the head librarian) rather than administration. The other four committeemen shall be selected by the head librarian and shall serve for staggered three (3) year terms (two committeemen first appointed shall serve two years and the other shall serve three years, thereafter each to serve three years).

37. Following Long's death, during early December 2009, Long's estate donated $1,017,382.00 to Lon Morris (the "Long Endowment"). The College placed these funds in a restricted account on December 9, 2009. On that same day, Heloise Long, the executrix of Long's estate, and Dr. McCall also signed a memorandum of understanding (the "Memorandum") that detailed the purpose of the Long Endowment. The language contained in the Memorandum regarding the purpose of the Long Endowment is identical to the language contained in the Long Will. As such, the Long Endowment is a permanently restricted fund and the Memorandum limits Lon Morris' use of the funds.

38. In addition to the Memorandum's restrictions, the Endowment Policy placed further restrictions on the Long Endowment. For example, the Endowment Policy requires the preservation of the fair value of the original gift as of the gift date of any donor-restricted endowment funds, absent explicit donor stipulations to the contrary—none of which are contained in the Long Will or Memorandum. As a result, Lon Morris classifies as permanently restricted net assets "the original value of the gifts donated to the permanent endowment and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation was added to the fund."

39. The Endowment Policy also states that endowment assets should be invested "in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 index while assuming a moderate level of investment risk." Lon Morris expected "its endowment funds, over time, to provide an average rate of return of approximately six to eight percent annually." To achieve this level of performance, Lon Morris relied on a "total return strategy" that targeted a diverse asset allocation within prudent risk restraints.

40. After receiving the Long Endowment, McCall and the Board, including Board Defendants that were members of the Executive Committee (i.e., Wagner, Brumbelow, Cook, Deadrick, and Dubcak) and the Endowment Committee (i.e., Ashcroft and Crawford), knowingly ignored the Long Will, the Memorandum, and/or the Endowment Policy. During the December 11, 2009 Board Meeting attended by Brown, Brumbelow, Cook, Crawford, Wagner, and Ashcroft, the Endowment Committee chair, stated that the Endowment Committee was responsible for working with Lon Morris's "partners" to determine where to place the Long Endowment funds—presumably in some type of investment. In the interim, Ashcroft represented that the Long Endowment would be placed in four 90-day certificates of deposit

("CDs") with Austin Bank, Southside Bank, Texas National Bank, and Prosperity Bank (collectively, "the CD Banks").

41. During a February 5, 2010 Board Meeting, attended by McCall, Brumbelow, Cook, Crawford, Deadrick, Dubcak, and Wagner, the Board specifically discussed the investment of the Long Endowment funds. During the meeting, McCall represented that the Long Endowment had been placed in four certificates of deposit with the CD Banks pending a decision by the Endowment Committee as to how to invest the funds. McCall's representation that the funds had been placed in four CDs was patently false, since McCall knew that Lon Morris had purchased only three CDs and that $250,000 remained in a cash account.

42. Incredibly, there is no record that Ashcroft, the other Endowment Committee members, including Crawford and Staton, or the members of the Executive Committee, including Wagner, Brumbelow, Cook, Deadrick, and Duback, ever followed up on their responsibilities relating to the Long Endowment. There is no indication in subsequent Board minutes that any Endowment Committee member or other Board member attempted to confirm that McCall's representations were correct with regard to his purchase of the four CDs. There is no evidence that any Endowment Committee member or other Board member took issue with the fact that the Long Endowment had been placed in low-yielding CDs, instead of being directly invested in a manner consistent with the Endowment Policy. There is also no record that the Endowment Committee or any Board member followed up on whether any proper investment vehicle had been identified for the Long Endowment despite board minutes that clearly indicate that they had represented that they would work with Lon Morris's "partners" to assure the funds were properly invested. Instead, the Endowment Committee and other Board members remained silent, which allowed McCall and his staff to hold the Long Endowment funds in a manner that

provided them with easy access—particularly the $250,000 not used to purchase a CD—for use on improper expenditures. The Endowment Committee and other Board members were either "asleep at the switch" or intentionally looked the other way so that McCall could raid the Long Endowment.

43. The Endowment Committee and other Board members' silence unquestionably caused Lon Morris immediate and long-term damages. In this connection, following McCall's purchase of the three CDs, McCall oversaw the immediate and improper expenditure of all or substantially all of the remaining $250,000 for purposes other than investment. In fact, any use of the $250,000 other than for investment pursuant to the Endowment Policy would have been unauthorized since the Long Will and the Memorandum made clear that Lon Morris was only allowed to use one-half of any investment profits for the benefit of the Library.

44. Had the Endowment Committee and other Board members objected to McCall's purchase of CDs and simply followed up on their obligations to assure that the Long Endowment was properly invested, they could have protected the Long Endowment from McCall's misuse.

45. With the Endowment Committee turning a blind eye, McCall began to further raid the Long Endowment. During May 2010, McCall and his staff cashed the three CDs previously purchased with Long Endowment funds and deposited the cash back into an aptly named "Restricted Account" at Austin Bank. McCall then presided over the transfer of more than $700,000 of those funds to another account aptly named "General Fund." Once the cash was in the "General Fund," McCall and his staff had unfettered access to funds. Most, if not all, of the funds were then spent for improper and unauthorized purposes. The result of these actions is that Sam Houston State (the alternate beneficiary to the Long Endowment) is now making a claim against Lon Morris for the loss of the funds.

E. The Executive, Finance, and Endowment Committees Fail to Disclose McCall's Misuse of the Long Endowment

46. Lon Morris's financial statements did not reflect the improper expenditure of Long Endowment funds. To the contrary, Lon Morris's financial statements show that the funds were still intact. For example, an endowment report contained within the May 8, 2010 Board meeting materials represented that the Long Endowment balance was $1,020,682—an increase over the original gift amount. Reports in the August 13, 2010 and August 2011 Board materials similarly represented that the Long Endowment balance had grown to $1,023,234 and $1,027,117, respectively. The reports were misleading and failed to disclose the fact that McCall and his staff had already spent the majority, if not all, of the Long Endowment by August 2010.

47. So why would the endowment reports reflect a balance greater than the original gift? McCall and his staff, including Bob Prigmore ("Prigmore"), the Controller, had decided to retroactively alter Lon Morris's books to reflect a "loan" transaction between the Long Endowment and Lon Morris using the already spent Long Endowment Funds. In other words, McCall and his staff altered the books to represent that Lon Morris had simply borrowed the Long Endowment funds rather than spend the funds for improper purposes. A loan from the Long Endowment to Lon Morris (the "Endowment Loan"), however, never existed and, in any event, would have been contrary to the terms of the Long Will, the Memorandum, and the Endowment Policy.

48. While McCall did not disclose his unauthorized actions to the Board, McCall contends that the Executive Committee, which included Wagner, Brumbelow, Cook, Ashcroft, Deadrick, and Dubcak, were aware of and had discussed the Endowment Loan. Yet, based on the Board minutes, neither McCall nor the Executive Committee disclosed the alleged Endowment Loan to the Board, secured Board approval for the Endowment Loan, or otherwise

assured that the alleged Endowment Loan complied with the Long Will, the Memorandum, and the Endowment Policy. Indeed, the Executive Committee apparently remained silent while McCall created and/or knowingly allowed his staff (e.g., Prigmore) to retroactively adjust Lon Morris's books and records to reflect the non-existent Endowment Loan.

49. Lon Morris's long-time auditor, Lynn Acker ("Acker"), was aware of McCall's actions and the purported Endowment Loan. Moreover, Acker stated in his deposition that he understood that the Executive Committee was aware of McCall's improper use of the Long Endowment and the Endowment Loan idea. Acker's July 31, 2010 audit report, however, does not reflect that existence of the Endowment Loan. To the contrary, Acker's July 31, 2010 audit report represents that the Long Endowment was still intact since the report does not reflect that any permanently restricted funds (which include the Long Endowment) were withdrawn during the audit period. Yet, the Executive Committee members, including Wagner, Brumbelow, Cook, Ashcroft, Deadrick, and Dubcak, never advised the Board that Acker's audit did not reflect the true status of the Long Endowment.

50. The fact is there was never an actual Endowment Loan. Lon Morris's lack of any loan documents and the handwritten notes on financials evidence that the "loan" was not a legitimate loan. Rather, Lon Morris's documents reflect the intentional efforts of McCall and his staff to retroactively attempt to create a loan with a fictitious interest rate and investment payables. For example, a journal entry printout dated January 13, 2011 shows handwritten notations that make adjusting journal entries for July 31, 2010, August 1, 2010 and December 9, 2010 in an attempt to retroactively create a "loan" on Lon Morris's books. They note that the first adjustment is an "entry to correct J.D. Long Endowment as of 7-31-2010." The author then computes interest expense for the four months and nine days from August 1, 2010 to

December 9, 2010. To do so, the author of these entries arbitrarily assigned a 3.8% interest rate to the distributions taken by Lon Morris. In other words, the author backdated the loan calculation in order to create the illusion that the Long Endowment was actually intact and earning interest via the non-existent Endowment Loan.

51. Had the Executive Committee members satisfied with the fiduciary duties owed to Lon Morris, they would not have allowed McCall and his staff to conceal their misuse of the Long Endowment by retroactively creating a non-existent Endowment Loan. Moreover, they would not have allowed Acker to subsequently submit an audit report that misleadingly created the impression that the Long Endowment was still intact and had not been spent. Instead, the Executive Committee would have immediately reported McCall's actions to the Board and McCall would have been fired. Unfortunately, the Executive Committee did not act in a reasonably prudent manner or in the best interest of Lon Morris. Lon Morris suffered damages of, at least, $1.017 million as a direct result.

F. The Landmark Building

52. As part of McCall's "spend and expand program," McCall also wanted to develop a hospitality program at the college. In this connection, on March 25, 2010, Archive Management, Inc. and McCall, on behalf of Lon Morris, entered into an agreement whereby Lon Morris executed a deed of trust to take title to property known as the Landmark Building, subject to a third-party restaurant lease on the premises. Lon Morris intended to use the Landmark Building to house/develop a new hospitality program.

53. Lon Morris's acquisition of the Landmark Building was another poor decision spearheaded by McCall. The conveyance of the Landmark building was subject to a 30-year mortgage in the original principal amount of $908,335. The College, however, did not have the excess funds from operations to pay the mortgage nor could the College cover the mortgage with

the limited number of hospitality students enrolled in any given semester. The Landmark building was not located on Lon Morris's campus; rather it was in the downtown Jacksonville area, which would create transportation issues. Moreover, the Landmark building was also old and registered as an historic property, which contributed to significant additional expense for repairs and upkeep.

54. Like McCall's other financial transactions on behalf of Lon Morris, McCall's decision to enter into the Landmark transaction set Lon Morris up for certain default and further financial distress. Indeed, the Landmark transaction did not benefit Lon Morris and, ultimately, failed.

G. The Unauthorized Wraparound Note with Tilley LLC

55. During December 2011, McCall, acting on behalf of Lon Morris, entered into a transaction with Tilley LLC for the purchase of certain real property owned by Tilley (the "Tilley Property"). Prior to that time, Lon Morris leased the Tilley Property pursuant to a lease (the "Tilley Lease"), but had struggled to timely meet its lease obligations. In this connection, Lon Morris had incurred late payment penalties under the lease of approximately $12,446.97 by December 2011.

56. On December 29, 2011, McCall executed a certain letter agreement (the "Letter Agreement") and wraparound real estate lien note (the "Wraparound Note) with Tilley LLC, substituting it for the Tilley Lease. The Letter Agreement extinguished the Lease penalties owed by Lon Morris for a modest amount so that Lon Morris and Tilley LLC could close on the conveyance of the Tilley Property. The Wraparound Note evidenced Lon Morris's agreement to pay Tilley LLC the total sum of $6,210,032.20 to purchase the Tilley Property. In exchange, Tilley LLC executed a certain warranty deed with vendor's lien (the "Tilley Deed") conveying the Tilley Property to Lon Morris.

57. The Tilley transaction described above was not well advised and was financially disastrous for Lon Morris. Lon Morris was now burdened with in excess of $6 million in new debt payments, secured by property of questionable value. While Lon Morris was previously bound by the Tilley Lease and would be liable for any default thereunder, Lon Morris's liability exposure was significantly lower under the Lease because of the limitations on liability for breach of a commercial lease imposed by Texas law. Yet, McCall, a person who was admittedly incompetent in financial affairs, nevertheless executed the Letter Agreement and Wraparound Note without conferring with or otherwise securing authority from the Board.[3]

H. The $2.7 Million Unauthorized "Refinance" with Texas National Bank

58. Between December 2009 and April 2011, Lon Morris entered into a series of loan transactions with Texas National Bank. The loan transactions included the following: (1) a loan of $1.8 million on December 22, 2009 secured by certain property owned by Lon Morris; (2) a loan of $500,000 on November 4, 2010 secured by certain property owned by Lon Morris; and (3) a loan of $600,000 (the "$600,000 Note") on April 29, 2011 (Texas National Bank actually acquired this not from Texas National Bancorporation). The $600,000 Note was secured by liens on certain mineral interests owned by Lon Morris in eight Texas counties, one Louisiana Parish, and one county in Arkansas.

59. On or about February 1, 2012, McCall entered into a series of unauthorized renewal notes and deeds of trust in favor of Texas National Bank (the "February Renewals") designed largely to renew and extend the prior loan transactions with Texas National Bank. Under the February Renewals, Lon Morris borrowed in excess of $2.75 million from Texas National Bank, granted Texas National Bank liens on property, and cross-collateralized new

[3] Lon Morris's 2011 Board Minutes are tellingly void of any discussions relating to the Tilley transactions.

assets in favor of Texas National Bank. Specifically, the loan documents for the February Renewals purport to encumber valuable mineral interests, which had previously only secured the $600,000 Note, with the $1.8 Million note. Moreover, the February Renewals purported to convert the interest rate and payment terms from a manageable 20-year term to a one-year balloon note where the entire $2.7 million note would be fully due and payable.

60. McCall's decision to enter into the February Renewals was a bad business decision. Rather than look at other forms of revenue generation, such as selling assets, including possibly the mineral interests, rather than encumbering them to secure more indebtedness, McCall created a debt that Lon Morris could never repay. By changing the terms of the debt to a one-year balloon note, McCall put Lon Morris in a position of certain default, a default that unreasonably and unnecessarily jeopardized Lon Morris's equity in its valuable mineral interests and exacerbated Lon Morris's financially precarious position. Indeed, Lon Morris was ultimately forced to liquidate its mineral interests for $1.3 million. At the time, Lon Morris only had approximately $300,000 in equity in the mineral interests based upon the amount that Lon Morris had to expend to settle the debt with Texas National Bank because of the February Renewals. Absent the February Renewals, Lon Morris would have had, at a minimum, $700,000 in equity in those same mineral interests since those interests originally secured only the $600,000 Note. Accordingly, the February Renewals damaged Lon Morris by, at least, $400,000.

61. In addition to the fact that the February Renewals were a bad business decision and caused Lon Morris significant damages, the February Renewals were not authorized by the Board. While the original transactions (e.g., the $600,000 Note) appear to have been authorized by the Board, Board minutes immediately before and after the February Renewals do not show

any authorization for McCall to enter into these transactions. Furthermore, the loan documents produced by Texas National Bank—and attached to the Proof of Claim filed with this Court under penalty of perjury—do not show any Board authorization for McCall to execute the February Renewals. Accordingly, the damages caused by the February Renewals are directly attributable to McCall's breaches of fiduciary duty.

I. Unpaid Tuition of $1,000,000

62. Despite knowing that collection of tuition was the College's future, and specifically identified by McCall in the Board minutes as necessary to cover current operating expenses, McCall authorized over $1 million of student tuition to remain unpaid and owed. McCall did not undertake any reasonable efforts to collect the unpaid tuition, nor did he restrict the services provided to students delinquent on their accounts. Rather, McCall provided education, degrees, and transcripts to students who failed to pay their tuition, at a significant cost to the College. Had McCall taken reasonable action, he could have collected all or substantially all of the unpaid tuition and/or mitigated the additional costs associated with providing free education to non-paying students.

63. Despite the negative implications of McCall's failure to collect over $1 million in tuition, the Board, including the Board Defendants did nothing. Had the Board accepted its responsibility to act in the best interest of Lon Morris, Lon Morris could have collected all or substantially all of the unpaid tuition or, at the very least, limited Lon Morris's expenses associated with allowing students who had not paid tuition to attend classes, graduate, and otherwise receive the same benefits as paying students.

J. The Bottom Line

64. Lon Morris was worth more as a going concern than as a liquidated asset. McCall and the Board Defendants destroyed Lon Morris's going concern value by not seeking a

purchaser or educational partner when the time was right, when there were funds to operate, and when Lon Morris had not missed payrolls. By the time competent and experienced professionals were hired, Lon Morris missed three payrolls, a year's worth of catering expenses, the utilities were about to be cut off, and Lon Morris's value had been greatly reduced to a depressed liquidation value. The result was that McCall's and the Board Defendants' grossly negligent actions caused Lon Morris's going concern value to be reduced by millions of dollars.[4] Indeed, McCall's and the Board Defendant's grossly negligent actions damaged Lon Morris's accreditation value by, at least, $10 million dollars.

65. McCall and the Board Defendant's grossly negligent actions also exposed Lon Morris to millions of dollars more in damages. In this connection, the Texas Attorney General has filed suit against Lon Morris, seeking damages of, at least, $17 million for violation of the public trust. Additionally, Sam Houston State has filed a claim against Lon Morris for the amount of the loss of the Long Endowment (in excess of $1 million).

66. Throughout his tenure, McCall failed to act in the best interest of Lon Morris. He entered into unauthorized transactions, effectively granted free tuition, mismanaged finances, failed to disclose his unauthorized transactions on behalf of Lon Morris, and otherwise abused his obligation to act in the best interest of Lon Morris. Board minutes reflect that McCall was so aggressive in abusing alumni resources that he lost the goodwill of loyal Lon Morris donors who felt the school was being mismanaged. Moreover, McCall made promises to donors that went unfulfilled or were baseless. Donors were simply no longer willing to financially assist the College which further diminished Lon Morris's going concern value and its ability to continue as an operating entity.

[4] Lon Morris's audit reports show that, during McCall's tenure, Lon Morris's total liabilities increased by more than $14 million while its total assets increased by less than $5 million.

67. The Board Defendants were complicit in McCall's actions. Indeed, the Board Defendants endorsed many of McCall's recommendations and actions when they were aware of, or should have been aware of, information that established that McCall's recommendations and actions were not in Lon Morris's best interest and, in fact, would cause Lon Morris substantial harm. Furthermore, certain Board Defendants remained silent when they knew that McCall and his staff misused the Long Endowment and misled the Board regarding their misuse when McCall and his staff retroactively created a non-existent loan to make it appear that the Long Endowment was intact. The Board Defendants' grossly negligent actions further diminished Lon Morris's going concern value and its ability to continue as an operating entity.

CAUSES OF ACTION

K. First Cause of Action – Breach of Fiduciary Duty (McCall)

68. Lon Morris incorporates the preceding paragraphs as if fully set forth herein.

69. McCall owed Lon Morris fiduciary duties as Lon Morris's president. During his tenure as president, McCall breached his fiduciary duties owed to Lon Morris in numerous ways, including without limitation, the following:

(1) By encouraging Lon Morris's Board of Trustees (the "Board") to authorize a secured loan transaction with Amegy Bank in 2006 which included a side agreement swapping the floating rate of interest provided for in such loan with an obligation to pay Amegy a fixed rate of interest. The side agreement was evidenced by an ISDA Master Agreement dated April 10, 2006 and related Schedule and Confirmation. Neither McCall nor any other Board member had any idea how the Side Agreement operated or what its legal effect was on the loan transaction. The Side Agreement caused Lon Morris to owe approximately $1 million in extra interest payments over what the loan would have otherwise cost;

(2) By allowing McCall and his staff to invest the Long Endowment in a manner contrary to the Endowment Policy and by wholly failing to follow-up regarding the use and

investment of the Long Endowment when the Board Defendants—particularly those on the Endowment Committee—were charged with assuring that the Long Endowment was invested and used in accordance with the Endowment Policy and the other restrictions placed on its use;

(3) By failing to disclose to the full Board that he had improperly used endowment funds and then making or knowingly allowing those under his control to make retroactive adjustments to Lon Morris's books and records to misleadingly indicate that the Long Endowment remained intact as a loan when there was no loan and, in fact, the funds had already been spent for improper and unauthorized purposes;

(4) By executing an unauthorized wraparound real estate lien note with Tilley LLC in excess of $6 million to replace an existing lease with Tilley LLC, when doing so significantly increased Lon Morris's secured debt and its overall liability exposure in the event of a default;

(5) By refinancing existing debt facilities with Texas National Bank without authority and imprudently pledging Lon Morris' valuable mineral interests as collateral for a loan that did default soon thereafter;

(6) By failing to collect approximately $1 million in tuition from students who were allowed to take classes, earn credit for those classes, and/or graduate; and

(7) By destroying Lon Morris's value as a going concern by implementing a grossly negligent program without a business plan, which program included, without limitation, expanding Lon Morris's student population in a manner that would cause Lon Morris to incur substantial debt and new expenses beyond Lon Morris's existing infrastructure and ability to pay same and adding programs like football, basketball, and agriculture when the addition of such programs would require massive expenditures well beyond any increase in revenues that reasonably might flow from such programs; and

(8) By exposing Lon Morris to claims by the Attorney General for $17 million for violations of the public trust.

70. With regard to the above-referenced breaches, McCall did not act in good faith, with ordinary care, or in a manner that McCall could have reasonably believed were in Lon Morris's best interest. McCall's actions constitute gross negligence and a breach of the fiduciary duties owed to Lon Morris. As a result of McCall's gross negligence and breaches of fiduciary duty, Lon Morris has been damaged in an amount in excess of $20 million.

L. Second Cause of Action - Breach of Fiduciary Duty (the Board Defendants)

71. Lon Morris incorporates the preceding paragraphs as if fully set forth herein.

72. The Board Defendants owed Lon Morris fiduciary duties arising out of their positions on the Board. The Board Defendants breached their fiduciary duties owed to Lon Morris in, without limitation, the following ways:

(1) Authorizing McCall's execution of the sophisticated ISDA Agreement when the participating Board Defendants did not know what the agreement was, did not understand the agreement, did not know the negative implications the agreement could have on Lon Morris, did not seek guidance from a competent professional, and knew that they could not reasonably rely upon McCall's advice with regard to the agreement when they knew (or should have known) that McCall was not competent to advise on complex or sophisticated financial transactions;

(2) By allowing McCall and his staff to invest the Long Endowment in a manner contrary to the Endowment Policy and by wholly failing to follow-up regarding the use and investment of the Long Endowment when the Board Defendants—particularly those on the Endowment Committee—were charged with assuring that the Long Endowment was invested and used in accordance with the Endowment Policy and the other restrictions placed on its use;

(3) By failing to disclose to the Board that McCall had improperly used the Long Endowment after learning of McCall's actions, and then ignoring McCall's retroactive adjustments to Lon Morris's books to show that the Long Endowment remained intact as a loan when there was no

loan and, in fact, the funds had already been spent for improper and unauthorized purposes;

(4) By failing to assure that Lon Morris collected approximately $1 million in tuition from students that were allowed to take classes, earn credit for those classes, and/or graduate;

(5) By generally destroying Lon Morris's value as a going concern by authorizing the implementation of a grossly negligent business plan that included, without limitation, expanding Lon Morris's student population in a manner that would cause Lon Morris to incur substantial debt and new expenses beyond Lon Morris's ability to pay same and adding programs like agriculture, hospitality, and football when the addition of such programs would require massive expenditures well beyond any increase in revenues that reasonably might flow from such programs; and

(6) By exposing Lon Morris to claims by the Attorney General for $17 million for violations of the public trust.

73. With regard to the above-referenced breaches, the Board Defendants did not act in good faith, with ordinary care, or in a manner that the Board Defendants reasonably believed were in Lon Morris's best interest. The Board Defendants' actions constitute gross negligence and a breach of the fiduciary duties owed to Lon Morris. The Board Defendants' gross negligence and breaches of fiduciary duty in this regard caused Lon Morris damages in excess of $20 million.

PRAYER

WHEREFORE, Lon Morris respectfully requests the following:

(1) Damages for McCall's breaches of fiduciary duty in an amount to be determined at trial;

(2) Damages for the Board Defendants' breaches of fiduciary duty in an amount to be determined at trial;

(3) Statutory pre- and post-judgment interest; and

(4) Such other relief to which Lon Morris may show itself justly entitled.

Respectfully submitted,

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