

Investing With The Heart
“Doing Good by Doing Well”
A Case Study

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ABSTRACT

This case is intended to illustrate the lessons learned (business, personal and spiritual) from experiences where the best intentions of a generous, caring Christian business person are found to conflict with Christian principles of stewardship.

In this three part case study, written collaboratively by a CBFA faculty member and the business executive principally affected by the case (John Bacey is the name used in the case), the executive was entrusted with control over a significant amount of funds set aside by his employer to secure an employment contract between John and the employer. At John’s request, the employment agreement called for John to direct the income earned by the invested funds to a charity of his choice. After making investment decisions with what he believed to be a charitable motive, John finds that he has become the victim of a Ponzi scheme where his employer’s funds are lost and John’s job and his career are threatened. The case presents the related emotional and spiritual impact of John’s actions followed by a description of the deep spiritual lessons learned from the experience.

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PART I
“Help for Single Parent Families”

John Bacey recently accepted the position of Northeast Regional Vice-president of Sales (RVP) for a major Canadian lumber company doing substantial business in the United States. John has worked in wood products sales for many years. He is pleased to have reached the point in his career where he has been given responsibility for a major market of a large company. Because John had to leave a very secure position at a company where he had been employed for many years and was somewhat uncertain about the security of the position with the new company, he insisted on entering into an employment contract with the new company. Included in John’s employment contract was a provision that the company would deposit \$100,000 in a bank to “secure the employment of Mr. Bacey”. Wording of the employment contract with regard to this security arrangement is as follows:

“Canadian Lumber Corporation (CLC) will deposit on US\$100,000 in an account the RVP determines for a period of 36 months. On or before the termination of the 36 month period, the RVP will return the principal to CLC except for the following reasons:

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1. The contract is substantially breached by CLC.
2. CLC becomes insolvent or bankrupt.
3. CLC terminates operations that impair the performance of the business.
4. CLC operates in such a manner as to impede the service of the RVP.
5. CIC terminates the employment agreement for any reason prior to its fulfillment.

If any of the above events occur, the US\$100,000 shall become the property of the RVP without recourse by CLC.”

John’s lawyer reviewed the employment contract and found it to be in good order, worded such that John’s interests were carefully protected.

Several days after signing the employment contract John, in consultation with the assistant treasurer of CLC, decided to have the \$100,000 placed in a certificate of deposit at a major bank that John had done business with in the past. Within a week John received the check for \$100,000 made payable to the bank along with a letter addressed to the bank and signed by CLC’s assistant treasurer. The letter read, in part, as follows:

“Enclosed please find the completed Corporation Resolution and Certificate of Taxpayer Identification Number for your handling in regard to opening the Certificate of Deposit account that we discussed for Mr. John Bacey, our Regional Vice-president.

This letter also serves as the confirmation to your bank that Mr. John Bacey is the only authorized signer on this Certificate of Deposit account in the name of our company.

Furthermore, interest earned on this account should be paid by check to Canadian Lumber Corporation and sent to my attention at the above address.

Thank you for your attention to this matter. If you have further questions, please feel free to contact me.”

Jim Clayton has known John Bacey for several years. They attend the same church. On Sundays after church they often compare notes on their work week. Jim knows that John and his wife feel a personal burden to help the increasing number of single mothers who attend the church. Because Jim is the church treasurer, John told Jim about an idea he and his wife have been considering for the last few weeks. John described his new job to Jim and explained the details of the employment contract, including the \$100,000 certificate of deposit. John explained that he has an informal agreement with his employer that the interest earned on the certificate of deposit account will be paid to John or anyone John designates. John and his wife have decided that they would like to have this money contributed to the church for the support of needy single mothers in the congregation. Jim was, of course, pleased to hear of John’s generous intent, but explained to Jim that IRS rules prohibit the church from providing his employer with a charitable

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contribution receipt if Jim designates the ultimate recipient of the funds by name. However, if John wants to direct that the funds be designated to the church ‘membership assistance fund’, a receipt could be issued.

The membership assistance fund, as the name indicates, was set up to allow members to give to meet the financial needs of other members. Gifts are made to the fund without designating specific recipients. Disbursements are made from the fund based on the expressed needs of individual members as well as the suggestions made to the pastor about needs of which members become aware. The pastor and the chair of the deacon board make the final decisions about disbursements. John agreed with Jim that designating gifts to the membership assistance fund was the best way to meet the needs of the single mothers in the congregation. John realized that, as a member of the church, he could always suggest to the pastor that he consider specific needs among the membership.

For about a year checks would periodically arrive in the mail from John’s employer. Jim deposited these checks in the church checking account, recording the contribution as an increase to the membership assistance fund and sending a receipt to Canadian Lumber Corporation. As a courtesy to John, Jim notified him each time a check was received.

Al Westerbrook, another church member, serves as the volunteer church auditor. While examining the church financial records, Al wondered about the appropriateness of Jim’s arrangement with John. One of Al’s concerns in auditing the church financial records has always been to consider if the church is doing anything that would jeopardize its status (with the IRS) as a not-for-profit charitable organization, eligible to give tax deduction receipts to donors.

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Part II
“A Better Yield”

Interest rates fell dramatically in the year after Canadian Lumber Company transferred the \$100,000 to the certificate of deposit in accordance with its employment agreement with John Bacey. John was disappointed that the amounts of the checks the church received from his employer had become smaller. John wondered whether he might earn enough in some other investment to make some much needed improvements to his home while continuing to provide substantial funds to the church. John decided to investigate alternative higher yield investment possibilities for the \$100,000 employment security deposit. John asked several of his friends for their investment advice and suggestions, including Jim Clayton. Reluctant to give advice on specific investments, Jim advised John to consult a professional investment advisor.

Several weeks later, after church one Sunday, John told Jim about an outstanding investment opportunity. John had recently been introduced to a wealthy investor named Gedne Howe, a descendent of Elias Howe, inventor of the sewing machine. According to Jim, for the last twenty years Gedne Howe has been responsible for managing the Howe family investment portfolio. Over the years Howe developed an uncanny ability to “outperform the market”. In addition to managing the Howe family portfolio, Gedne had begun to make investments for some of his friends and a few other people. After an introduction by a friend and a lengthy conversation about the stock market and Howe’s consistent success in “growing” portfolios, Gedne Howe told John he would be willing to manage his \$100,000. Because the amount John had to invest was so small, Howe suggested he give John a promissory note for the \$100,000 and invest John’s money along with his family funds to insure maximum diversification and growth in the investment. John thought the opportunity to make his \$100,000 a part of a much larger portfolio looked like an excellent opportunity.

Jim, somewhat skeptical, asked why John’s new friend, Gedne Howe, was being so generous in offering to help John meet his investment goals. John explained that Howe said he had been frustrated for some years about what he considered poor performance by “expert” investment advisors. Howe knows how the stock market works and is tired of seeing hard working people who save their money get the mediocre returns produced by the large investment firms. To demonstrate his experience, Howe showed John some past performance records which indicated he had consistently earned rates of return of 40% or more. John said he was initially surprised that Howe’s earnings record was so good, since most investment advisors were able to demonstrate little more than a 12-15% historical rate of return (and that was on rather risky investments, such as initial public offerings of new corporations in emerging industries like biotechnology or investments in companies whose stock is traded on certain overseas stock markets.) Howe said that anyone willing to do the work necessary to understand the market could easily match his record.

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Because Howe worked full time to manage his family trust funds, he had the time and the motivation to study the market. He also had the financial resources to move quickly to make significant investments when the right opportunity presented itself. Howe said his success was also due to much reading about individual companies, their management team, and their plans for the future. All that was left was to learn to “time the market” so that maximum returns were earned on the fluctuation in the price of the stock of companies he became convinced were going to be successful in the long term. Howe said that most investment managers were simply unwilling to do the work necessary to be successful. He believes that in order to make their job easier the investment management industry has sold the public on the idea that 15% is a high rate of return.

Jim Clayton was not convinced, but he had not met Gedne Howe. Also, Jim realized John was, at most, only looking for the reaction of a friend, not professional advice. As church treasurer, however, Jim asked John how future contributions, if any, to the membership assistance fund would be received. John assured Jim that it was his intention to continue making contributions to the membership assistance fund. In fact, he hoped future gifts would be much larger.

As to how the gifts would be received, John said Gedne Howe would pay him directly and he (John) would make the contributions to the church. By commingling John’s and his family’s funds, Gedne Howe made himself liable to pay taxes on the income from the funds. Howe did not think that hard working people like John Bacey should have to pay taxes on the income earned from their investments. John told Jim he had been surprised by this statement and apparent generosity by Howe. John was concerned enough about this tax issue that he contacted a friend who had worked for the Internal Revenue Service to check on the legality of such an arrangement. John’s friend assured him that there would be no problem with the IRS as long as Howe paid the appropriate taxes.

Jim Clayton did not like the sound of Howe’s explanation of the tax consequences of this arrangement. Having had some experience solving tax problems at work, Jim told John that he would want more information about the tax implications of this deal with Gedne Howe. Logic seemed to indicate that any money received from Howe that was not a return of his investment of \$100,000 would be taxable income.

Several weeks passed before Jim and John had another opportunity for a lengthy conversation after church. Finally, one Sunday John sought out Jim and gave him a personal check for \$5,000 to be added to the membership assistance fund. Jim was startled. This was more than the amount of interest the church had received in all of the previous year from the bank where the Canadian Lumber Company had deposited the \$100,000. John said this was one half of the quarterly return recently paid by Gedne Howe, as promised. John used the other half to make some improvements to his home. A few months later John gave Jim another check for \$5,000. Gedne Howe had again performed as promised. Jim Clayton was amazed that Howe was able to produce such exceptional investment returns.

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Part III
“Disaster Strikes”

Several months had passed since Jim Clayton had last received a major check from John Bacey. On occasion Jim had wondered why no more checks had come from John, but Jim knew John had other charitable interests and, anyway, Jim thought it was inappropriate to ask church members about their giving practices.

When Jim opened to the business section of the Boston Globe he was shocked to read that Gedne Howe was a fake! Gedne Howe, whose real name is Joseph Zirkell, was involved in what has been called a Ponzi scheme, named after a Boston swindler from the 1880's. This fraudulent scheme involves attracting unsuspecting investors with a promise of a high rate of return on their investment. The scheme is kept alive by paying early investors from the money received from succeeding investors. Of course, as the scheme continues there are an increasing number of investors to pay. The fraud is exposed when the scheme gets so big that the swindler can no longer satisfy investors. Jim hoped that John had recovered his investment before the scheme unraveled.

The next Sunday John gave Jim the bad news. John had received from Zirkell a total of \$29,000 over the twelve months of the “investment”, all of which had been spent or given away. John owed his employer \$100,000 and the employment contract was due to expire in less than 90 days. John had a meeting scheduled with the president of his company to discuss other business matters. He realized he would have to tell his boss about the loss of the \$100,000. John felt terrible. He was embarrassed, humiliated and angry. John was also fearful he would lose his job and would have to sell his house to repay the \$100,000.

In his written statement to the FBI John made the following comments:

“It is impossible at this stage to grasp the full implications of Mr. Zirkell’s theft. The monies entrusted to him solely because of his claims of family wealth, tradition of prudent financial management and myriad of fallacious claims which led me to believe in his abilities, will virtually wipe out 15 years of hard work. He has made a mockery of lives based on a complete charade. He is evil and once he returns to society he will begin again to fleece unsuspecting pigeons. There is little else to say, but he will assuredly do this type of crime again. Listen to him. He feels he has done nothing wrong.”

Jim and John spoke for some time about the implications of what had happened. John was obviously very concerned about the personal financial disaster that had been created as well as the potential damage to his reputation in the business community. Buying and selling in the lumber industry had long been conducted on the basis of trust in the seller to deliver the quantity and the quality promised. However, John also confessed to Jim that he was more concerned to understand the spiritual meaning of what had happened. John said he truly felt that if he could understand the spiritual implications of the mess he was facing, the personal and business problems could be resolved.

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Part IV

“Final Outcome, Lessons Learned & Remaining Questions”

1. Joseph Zirkell pleaded guilty in federal court to conspiracy to defraud, mail fraud, wire fraud, interstate transport of a person in furtherance of fraud, false statements and the fraudulent use of a social security number. He was sentenced to 57 months in federal prison (the maximum sentence under federal law), and three years of supervised release, during which time any funds which become available to Mr. Zirkell were to be used to make restitution to the sixty-three known victims of his criminal activity.

2. John Bacey met with the president of his company, Bill Jackson, and explained the entire story to him. Needless to say, Bill was not at all pleased. In a letter to John confirming their conversation and arrangements for repayment, Bill expressed shock that John had transferred the \$100,000 without seeking permission from management. However, valuing John as a hard working, honest employee and believing John to be an innocent victim of Zirkell's fraud, Bill offered the following terms for repayment:

...The company will forgive \$40,000 of the loss.

...The company will continue John's salary at its current level.

...50% of any commissions earned by John above his current salary will be withheld to repay the remaining \$60,000. This withholding of commissions will continue until the \$60,000 is repaid in full.

3. In consultation with his accountant and CLC's corporate controller, John has concluded that this entire series of transactions are nontaxable events. The argument to be made should the IRS question this conclusion is that John Bacey was acting as an employee in taking the actions he did. He clearly made some poor decisions as an employee responsible for these funds, but he and his employer have reached an agreement that results in a shared economic loss.

4. SPIRITUAL LESSONS:

DAY OF FRAUD DISCLOSURE: The Boston Globe reveals the Ponzi scheme and in prayer the Lord provides the first glimpse into John's problem. The scripture was not easy to digest nor was it the answer John was hoping for....Psalm 69:4, “You must now restore what you did not steal”.

Throughout the months that followed, John built a personal lesson file as follows:

*He who is quick to get rich shall fall into many traps and a fool and his money are soon parted.

*Love of money and high rates of return are the root of all evil.

*Thieves, liars and murderers really exist and large sums of money attract them.

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*John moved the money secretly and God proved to him that nothing is hidden from His sight. God ensured John had no escape but to humble himself and confess his deeds to the owners of the company.

*God loved John and exposed the Ponzi scheme before John made the mistake of filing his income tax return under Zirkell's false claim to have paid the taxes on John's behalf. Thereby, God kept John from having a lifetime of IRS problems.

*God honored John's love toward Him and His people. He allowed him to suffer for his lack of integrity and discretion, and in the process, taught him a hard lesson. However, God kept John from coming to any financial, legal or physical harm.

CIRCA THE 90TH DAY: As John prepares to depart for Canada to inform the owners of the loss of their money, the Lord sent His encouraging message. Jeremiah 29:11 "For I know the plans I have for you", declares the Lord, "plans to prosper you and not to harm you, plans to give you a hope and a future."

SUMMARY AND CURRENT STATUS:

John suffered emotionally and spiritually for months grappling with every aspect of the problem and was particularly anxious about God's forsaking him because of his lack of integrity. The first scripture noted above, from Psalm 64, was the Lord's message of rebuke to John on the day he read about the real Gedne Howe in the newspaper. The second scripture given, from Jeremiah 29, was the Lord's message of comfort to John on the day he left for Canada to tell the owners of the company what had happened.

Within one year after the incident, John was promoted to Executive Vice President of the company. He finished the last fiscal year with record revenues enabling him to repay half of the \$60,000 debt to the company and still increase his personal income. The company's owners want John to become a stockholder of the firm and assume all sales responsibilities.

The IRS and the FBI have found no evidence that John participated in promoting Zirkell's scheme and no inaccuracies in his tax filings.

Approximately five years later the Boston Globe reported that within months of being released from prison, Joseph Zirkell was back in court for a hearing about the revocation of his probation on charges that he was once again providing fraudulent investment advice to unsuspecting victims.