PUBLIC (REDACTED) VERSION OF
REPORT OF THE SPECIAL LITIGATION COMMITTEES
OF THE
BOARDS OF DIRECTORS
OF
DARDANELLE TIMBER CO., INC.
AND
SUTHERLAND LUMBER-SOUTHWEST, INC.

March 26, 2007

(Date of Redaction: April 10, 2007)

(PART 2 OF 3)
investigation, the Special Committee has noted that many of the Companies' current store locations are geographically remote, not only from each other, but from major commercial airports, such that use of a private aircraft minimizes the amount of executive time required to complete inventory and related business activities at the store locations. *See Exhibit 1* hereto. The Special Committee further notes that, rather than purchase a jet outright, the decision was made to purchase a 50% interest in the Aircraft. The Special Committee also concludes that the Aircraft has been used for fifty-two trips (most with multiple legs) for business purposes.

The Special Committee also finds that the fifty-two business flights represent in excess of 110,000 miles and that approximately 11,000 (or 10%) of those miles represent "deadhead" miles where no passengers were on the flight and the flight miles were incurred to reposition the Aircraft to or from the Tulsa location. The deadhead flights occur as a result of the Aircraft being based in Tulsa and the Companies' corporate officers being based in Kansas City. The Special Committee

---

29 The Special Committee notes that Perry routinely visits multiple store locations on a single trip and tries to spend at least several hours, if not a full day, at each store visited. By using the Aircraft the timing can remain flexible and, in most instances, the Aircraft can land on smaller airfields within a few miles of the store. When store business is complete, Perry can travel to the next location in a relatively short time. In many instances less than one or two hours' time is required to travel from one store to the next. In stark contrast to this, the Special Committee has found that in order to visit several of the stores using commercial aircraft and/or rental cars, that due to the commercial aircraft schedules and the requirements of pre-travel arrival, trips would need to be extended for several days and that in many instances the travel time between the airport and the store would be in excess of several hours in each direction.
concludes that the Companies are aware of the cost associated with basing the Aircraft in Tulsa, and that for tax and other administrative reasons it is less expensive to base the Aircraft in Tulsa than in Kansas City. Also, deadhead flights are not incurred each time the Aircraft is used by the Companies. The Special Committee has determined that of the potential one hundred four deadhead flights resulting from the fifty-six business flights, there in fact were only fifty-eight deadheads, such that in approximately 46% of the Aircraft usage by the Companies there were no deadhead charges since the Aircraft was either already in Kansas City as a result of another Timesharee’s flight that ended there or where another Timesharee began their flight out of the Kansas City location. Notably, because the Aircraft is co-owned with another Sutherland family entity and because other Timesharees are Sutherland related entities or family members, significant opportunities exist to share costs on flights. For example, when Home Center schedules a trip to Corpus Christi, Texas, it may inquire if Perry needs to visit the Austin area stores operated by Southwest, providing an opportunity to split the costs. In fact, the Companies entered into cost-sharing on 23% of all business flights.

Pursuant to the Owners’ Time Sharing Agreement, Southwest is invoiced and pays to use the Aircraft, and from 2001 through December 2006, the total invoiced cost to Southwest from such business flights was $268,883.35. In addition to the invoiced cost for actual Aircraft use, Southwest incurs expenses of ownership – as well as revenues – based on its 50% ownership interest in the Aircraft. Based on its review of the documentary record, the Special Committee concludes that in fiscal year 2006,
Southwest received revenue of $205,569 and incurred operating expenses (labor, insurance, maintenance, fuel, travel and miscellaneous) of $207,842, resulting in negative cash flow to Southwest of $2,273. The negative cash flow for earlier years was: $32,587 for 2005; $51,528 for 2004; $50,957 for 2003; and $50,319 for 2002. The Special Committee’s investigation further revealed that the depreciation expense for fiscal years 2006 through 2002 was as follows: $28,612; $216,845; $361,409; $602,456; and $376,722. The Special Committee notes that to the extent the Aircraft is later sold and it retains its market value, the depreciation amounts represent a potential tax deferral. A Market Survey of the Aircraft prepared in November 2006 indicated an appraisal value for the Aircraft of $3.1 million, evidencing that, as was true of the Lear Jet, it has retained a substantial portion of its value from its original purchase price. That said, the Special Committee also has taken into account in its analysis the time value of carrying the investment in the Aircraft and the possibility that the total principal paid for the Aircraft may not be recovered upon its sale.

3. The Use of Maysville.

At paragraph 47 of the Complaint, plaintiff alleges that Perry’s employment agreement gives him, his family, and friends (if he authorizes it), the unlimited right to use Maysville at the Companies’ expense. Plaintiff alleges Perry has in fact availed himself of this contractual perquisite. The Complaint also alleges (at paragraph 52) that Todd has the right, at the Companies’ expense, to unlimited use of Maysville, and that “Todd has used Maysville regularly, including at least annual family trips as well as for
special occasions where friends are invited.” More specifically, paragraph 63 alleges that “Todd used Maysville to host a birthday party for his daughter and approximately twelve guests in the Summer of 2003.” The Special Committee’s investigation of the documentary record and interviews of witnesses revealed that Perry and Todd have in fact used Maysville and that the Companies have paid the expenses associated with such use billed to it by Sutherland Lumber, which expenses have been added as compensation received by Perry and Todd.\textsuperscript{30}

In 2001, Todd Sutherland used the Maysville facility on February 17-18, July 12-14, and September 21-23. The total cost to the Companies for such usage in 2001 was $2,925. In 2002, Todd used Maysville on July 12-14 and October 4-5. The total cost to the Companies for Todd’s 2002 use of Maysville was $1,875. That year, Perry also used Maysville on June 27-29, and August 30 through September 1. The total expense to the Companies was $1,875. In 2003, Todd used Maysville on July 3-6, and November 28-30 for a total cost to the Companies of $3,000. Perry used Maysville on May 29-31, 2003 for a total charge of $400. In 2004, Todd again used Maysville over the Independence Day holiday, for a total expense to the Companies of $1,300. In 2005, Todd stayed at Maysville on November 11-13, for a total cost of $360. In 2006, neither Todd nor Perry stayed at Maysville.

\textsuperscript{30} In 2001, Dardanelle also paid $3,170 for Dwight Jr. and his family to use Maysville, and in 2002 it paid $900.
In summary, the Special Committee finds that the cost to the Companies of Todd’s use of Maysville between 2001 and 2006 never exceeded $3,000 in any given year, and the total annualized value of the Maysville perquisite from 2001 through 2006 to Todd was $1,560. The cost to the Companies of Perry’s use of Maysville from 2001 through 2006 never exceeded $2,000, and the total annualized value to Perry was approximately $380.

4. **Tax and Accounting Services.**

Paragraph 46 of the Complaint alleges that Perry’s employment contract provides him with “the right to receive *unlimited* personal tax and accounting services at company expense.” (Emphasis in original). Martha alleges that this perquisite presents a substantial potential cost because there is no limitation “on what constitutes tax and accounting services for Perry” and also alleges that Perry has “obtained extensive tax and accounting services at company expense for his personal horseracing venture, commonly known as Choctaw Racing Stables (‘Choctaw’).” Complaint ¶ 46. The Complaint similarly alleges that the potential cost of the tax and accounting services perquisite in Todd’s employment agreement is quite substantial because he “is free to use them for any of this [sic] other business ventures [including a bank that requires extensive accounting work] under the premise that such services are for him personally.” Complaint ¶ 50.

The Complaint further alleges that Cimarron has provided tax and accounting services for members of the Sutherland family, and that “while Martha has always been charged for and paid in full for such services, Dardanelle and Southwest
have ‘absorbed’ and paid for at least Perry to receive such services at no cost to himself.” Complaint ¶ 61. Plaintiff alleges that around 2001, Choctaw was “the subject of a substantial ongoing IRS audit” and that a Cimarron employee has worked full-time on the audit at the Companies’ expense.\(^{31}\) Plaintiff further alleges that, notwithstanding a March 17, 2004 letter from Dave Dotson indicating a change (retroactive to the time of Dwight Sr.’s death in October 2003) in the practice for billing and payment of tax and accounting services, the Companies “continued to absorb the substantial fees and costs for, among other things, the substantial ongoing IRS audit of Choctaw.” Complaint ¶ 75.

The factual record developed from interviews and available documents demonstrates that, as alleged by Martha, Cimarron has in fact provided accounting and tax services to members of the Sutherland family, as well as their related trusts and affiliated businesses. The record also demonstrates that the extended Sutherland family has attempted to operate Cimarron at a small profit and that, for many years, Cimarron provided tax and accounting services based on its estimated “cost” of the services that was not tied directly to the actual time required to provide them. For example, with respect to tax preparation work, Cimarron’s estimated charges generally varied depending upon the generation the individual was in the Sutherland family tree, whether he or she was an employee of the Sutherland lumber businesses, and whether the tax

\(^{31}\) During their interview by the SLC, plaintiff and Dwight Jr. identified this individual as Connie Campfield. The Special Committee interviewed Ms. Campfield to inquire regarding the facts pertaining to this assertion.
return was considered simple or complex. Members of the Dwight Sr. generation were charged $4,000, their children were charged $3,000, and their grandchildren were charged $2,500 if they worked in the family lumber business, and either $2,000 or $1,000 if they did not work in the family lumber business (depending on whether the tax return was complex or simple). Great-grandchildren, all of whom are minors, were charged $500.

In or around 2003, in an effort to assure that one branch or member of the Sutherland family was not subsidizing the provision of services to other branches or members of the Sutherland family, John Sutherland suggested that Cimarron begin to bill for actual time charges, rather than relying on estimated charges as the basis for billing for Cimarron’s services. Perry and Dave Dotson also discussed a move toward actual time charges and, after Dwight Sr.’s death and following further discussion, Dave Dotson, by letter dated March 17, 2004, wrote to Perry, Dwight Jr., Martha and Todd to advise them that five affiliated entities — Choctaw, Latigo Cattle Co., the Norma H. Sutherland Revocable Trust, the Dwight D. Sutherland Estate & Revocable Trust, and M. Sutherland Fine Arts, Ltd. — would be billed actual time charges rather than a fixed fee. The March 17 letter also noted that:

Lawrence Financial Limited Partnership has always paid actual time and charges to Cimarron for tax and accounting work performed because the partnership also has ‘outside’ partners. Cimarron does no tax or accounting work for any
other Dwight D. Sutherland Family entities with ‘outside’ investors. (Emphasis in original.)

Finally, the March 17 letter indicated that the Companies “will continue to absorb actual
time charges for all other DDS Family individuals, trusts, partnerships, LLCs and
corporations as it does currently, billing each a fixed fee quarterly.” (Emphasis in original).

The Special Committee’s factual investigation revealed that from August 1, 2000 through July 31, 2005 Perry Sutherland had $5,000 added on an annual basis to his
W-2 for tax preparation work Cimarron performed for Perry and his dependents. For the
same period, Todd had $6,000 added on an annual basis to his W-2 for tax preparation
work Cimarron performed for Todd and his dependents. The Special Committee’s
investigation further revealed that for the period August 1, 2003 to July 31, 2004, the
actual cost allocation for Perry and his dependents, which was paid by the Companies,
exceeded the billed amount by $2,387, and the actual cost allocation for Todd and his
dependents, paid by the Companies, exceeded the billed amount by $359. For the

32 Lawrence Financial Limited Partnership owns the real estate on which The
University National Bank, of which Todd is the President, is located. Although
her Complaint makes reference to the March 17 letter, it makes no reference to
these statements in the letter, notwithstanding allegations that Todd might attempt
to have the Companies pay for Cimarron to provide services to the Bank, a
wholly-owned subsidiary of an entity with “outside” investors.

33 During the SLC’s interview of plaintiff, she repeatedly expressed her discontent
with the fact that the expense of tax preparation work for Sutherland family
members who worked for the lumber business is paid by one of the businesses,
while she was required to pay the full, actual cost. Based on its review of the
(cont’d)
period August 1, 2004 to July 31, 2005, the actual allocation for Perry and his dependents, paid by the Companies, exceeded the billed allocation by $7,506, and the actual allocation for Todd and his dependents, paid by the Companies, exceeded the billed allocation by $41. For the period August 1, 2005 to July 31, 2006, a billed and actual allocation of $12,615 was paid by the Companies and added to the W-2 for Perry, and a billed and actual allocation of $10,399 was paid by the Companies and added to the W-2 for Todd.

From August 1, 2000 until July 31, 2003, Choctaw, which was then owned by Dwight Sr. and Perry, was billed $7,500 per year by Cimarron for tax and accounting services. This number was a fixed fee based upon Cimarron’s estimate of the actual records, the Special Committee concludes that plaintiff is correct that the expense of tax return preparation for employee family members is, in large part, treated as compensation from the family companies. However, for the period August 2003 through July 2004, the actual cost allocation for Martha Sutherland and her dependents exceeded the billed allocation to her of $5,000 by $10,406, with the balance being absorbed by the Companies. The actual cost allocation for Dwight Jr. and his children exceeded the billed allocation of $5,000 by $3,649.

For the same period, the actual allocation for Dwight Jr. and his dependents, paid by the Companies, exceeded the allocation billed to him by $6,701.

The relative percentage interests of Dwight Sr. and Perry in Choctaw is derived from a fairly complex formula based upon each person’s relative interests in the racehorses owned through Choctaw. David Dotson’s March 2004 letter indicated that Dwight Sr. owned 99% of Choctaw prior to his death, a statement vigorously disputed by Dwight Jr. and Martha during the Special Committee’s interview. The Special Committee has reviewed Schedules K-1 pertaining to Choctaw and determined that in 2001, Dwight Sr. had a capital account balance of approximately $2.9 million and received distributions of approximately $800,000.
charges that were incurred in connection with services provided to Choctaw. Importantly, the Special Committee concludes that the estimates for Choctaw, as well as for other affiliated entities and for the individual and trust tax return preparation, were derived by Cimarron employees, without any input from Perry, Todd or Mark Sutherland. The Special Committee’s investigation revealed that, although Cimarron employees have for many years accounted for their time, the time sheets utilized prior to July 31, 2003 are not of the type often kept by professional service providers. They were not used as a method of deriving actual billings, but were used to allocate time as among the various lines of the Robert Sutherland family. Thus, although Cimarron “billed” Choctaw an estimated fee, it did not keep records of time actually devoted to Choctaw matters: the time was all recorded as time attributable to “DDS Family Investments.”

As noted above, certain members of the Sutherland family began to express a preference that billings be based on actual time charges rather than the historical, fixed fee approach. For the period August 1, 2003 through July 31, 2004, Choctaw was billed $7,948, based on actual time charges, rather than an estimated fixed fee. For services rendered from August 1, 2004 to July 31, 2005, Choctaw was billed $12,174, and for

(continuation)

while Perry had a capital account of negative $1,000 and received distributions of $215. Similarly, in 2002, Dwight Sr. had a capital account balance of more than $2 million and received distributions of approximately $250,000 while Perry had a capital account of negative $4,110 and received distributions of $29. Simply put, the position taken by Dwight Jr. and plaintiff is contradicted by the documentary evidence reviewed by the Special Committee.
August 1, 2005 to July 31, 2006, Choctaw was billed $8,766, all based on actual time charges.

As to plaintiff’s assertion that Connie Campfield, a Cimarron employee, was engaged full-time to work on Choctaw in connection with an IRS audit of Choctaw, the Special Committee has determined that the assertion is not supported by the documentary record or its interview of Ms. Campfield. At all relevant times, including during the period of the IRS audit of Choctaw, Ms. Campfield has been responsible for approximately seven DDS Family investments, but has had simultaneous responsibility for even more entities owned by other branches of the Sutherland family. She indicated that there have been times she has devoted a full business day to Choctaw, but at no time was she working exclusively on Choctaw. Moreover, the Special Committee’s investigation revealed that Choctaw engaged and paid outside professionals for services in connection with the IRS audit, including accounting and legal professionals who were paid more than $60,000.\textsuperscript{36}

Although not specifically identified in the Complaint, the Special Committee also reviewed Cimarron’s charges for services provided to other DDS Family

\textsuperscript{36} The Special Committee determined that in 2001 a total of $2,700 for such services was, due to a clerical error, paid by Dardanelle. The first invoice, in June 2001, was for $1,400 and primarily for services rendered to Dardanelle, but included a $550 charge for Choctaw that was not separately invoiced. A December 2001 invoice for $2,150 was improperly coded by an employee of Cimarron for payment by Dardanelle, rather than Choctaw. There was no evidence that Perry, Todd or Mark caused, or were even aware of, the improper coding of the invoices.
interests. The Special Committee’s investigation revealed that the actual allocation exceeded Cimarron’s billed allocation for Perry H. Sutherland Family Interests, L.P. by $2,024 over the course of August 1, 2003 to July 31, 2006, and that the actual allocation exceeded Cimarron’s billed allocation for Perry’s children’s trusts by a total of $845 over the same three-year period. With respect to Finney-Kearney County Gas Venture, L.P., the actual allocations for accounting services exceeded Cimarron’s billed allocation by a total of $5,531 over the three years August 1, 2003 to July 31, 2006. With respect to Deep Water Farms, L.P., the owner of farmland leased to Latigo Cattle Co., the actual allocations exceeded Cimarron’s billed allocations by $1,494 for the period August 1, 2003 to July 31, 2006. As to the Dwight D. Sutherland Family Investment Co., L.P., approximately 48% of the limited partnership interests are held by the Norma H. Sutherland QTIP Marital Trust and the Norma H. Sutherland Revocable Trust, and the

37 Plaintiff’s children’s trusts actual allocations exceeded the billed allocations by $41, $144 and $95 for the periods August 1, 2003 to July 31, 2004, August 1, 2004 to July 31, 2005, and August 1, 2005 to July 31, 2006, respectively. As in the case of all the circumstances in which actual allocations exceeded Cimarron’s billed estimates, the difference was effectively paid by the Companies.

38 Southwest is the General Partner of Finney-Kearney and holds a 25% interest. The Norma H. Sutherland Revocable Trust owns 50%, and each of the revocable trusts of each of Perry and Todd owns 12.5%. Accordingly, the Special Committee concludes that plaintiff’s economic interest in Dardanelle is not fully-aligned with her indirect interest in Finney-Kearney.

39 Southwest is the General Partner and owns 49% of Deep Water. The remaining interests are owned equally by Dwight Jr. and revocable trusts for Perry and Todd. To the extent the Companies subsidize Cimarron’s services to Deep Water, each of her brothers theoretically benefits at the expense of plaintiff.
remaining interests are owned (directly or indirectly) in equal portions by Dwight Jr., Martha and Perry, such that any benefit conferred upon it by the Companies would be to the primary detriment of Todd. For the three-year period August 1, 2003 through July 31, 2006, the actual allocation exceeded the billed allocation by a total of $19,376. Finally, with respect to Indian Creek Land & Investment Co., L.P., approximately one-third of the limited partnership interests are held by Martha or her children, with Dwight Jr. holding limited partnership interests that are smaller than his interest in Dardanelle.\footnote{To the extent costs of Cimarron attributable to Indian Creek are absorbed by the Companies, plaintiff indirectly benefits, primarily to the indirect detriment of Dwight Jr.} Actual allocations exceeded Cimarron’s billed allocations by $11,896 over the same three years.

B. The Section 220 Claims.

On July 13, 2004, Martha S. Sutherland, as Trustee of the Martha S. Sutherland Revocable Trust dated August 18, 1976, sent a letter to Dardanelle seeking to inspect certain books and records of Dardanelle pursuant to 8 Del. C. § 220 (the “Demand”). The Demand sought access to books and records of the Companies as follows:

1. All documents relating to the ownership or leasing of any aircraft by Dardanelle or [Southwest] for the last 7 years.

2. All documents relating to the costs to Dardanelle or [Southwest] of owning or leasing any aircraft, during
the last 7 years, including without limitation all documents relating to the costs and expenses for operation (including fuel, flight crews, and other costs), maintenance, storage and insurance as well as any mortgage, lease or other payments.

3. All documents relating to the use of any aircraft owned or leased by Dardanelle or [Southwest], for the past 7 years, including without limitation, documents reflecting business versus personal use, flight logs and plans, maintenance records and passenger lists.

4. All documents relating to the assessment or calculation of the amount of taxable income that was to be, or was, attributed or allocated to Dwight Sutherland, Sr., Perry Sutherland or Todd Sutherland, for the personal use of any aircraft owned or leased by Dardanelle or [Southwest], including but not limited to all documents relating to the costs to Dardanelle or [Southwest] for each personal flight taken by Dwight Sutherland, Perry Sutherland, or Todd Sutherland, for the past 7 years.

5. All documents relating to any payments or reimbursements to Dwight Sutherland, Sr., Perry Sutherland or Todd Sutherland, for their payments of any taxes on any amounts attributed or allocated to any of them as taxable income for the personal use by any of them of any aircraft owned or leased by Dardanelle or [Southwest] for the past 7 years.

6. All documents relating to expense accounts or expense reimbursement records for Dardanelle or [Southwest], for each of Dwight Sutherland, Sr., Perry Sutherland or Todd Sutherland, for the last 7 years.

7. All documents relating to expenditures of Dardanelle or [Southwest] pertaining to Choctaw Racing Stables, whether such expenditures were made directly by Dardanelle or [Southwest] or indirectly by Dardanelle or [Southwest] through Cimarron Lumber & Supply Company ("Cimarron"), for the last 7 years.
8. All documents relating to any services provided by Cimarron to Choctaw Racing Stables, Dardanelle or [Southwest], and any payments, compensation or other remuneration paid to Cimarron in connection with any such services, for the past 7 years.

9. All documents relating to any loans by Dardanelle to Perry Sutherland, Todd Sutherland, [Southwest] or any other company or entity in which Perry Sutherland or Todd Sutherland have any ownership interest, or any loan by any other party to Perry Sutherland, Todd Sutherland, [Southwest] or any company or entity in which Perry Sutherland or Todd Sutherland has an ownership interest and which loan is guaranteed (in whole or in part) by Dardanelle or secured (in whole or in part) by any asset owned by Dardanelle.

10. All documents related to the operation, funding, reimbursement, usage, eligibility for usage, at company expense or otherwise, of Maysville Training Center by Dardanelle, by any subsidiary or affiliate of Dardanelle, or by any employee, officer, director or shareholder of Dardanelle or any subsidiary or affiliate of Dardanelle, for the last 7 years.

11. Copies of all audited and unaudited financial statements (including any and all related notes and/or summaries of significant accounting policies for such financial statement) for Dardanelle, [Southwest] and Cimarron, for the last 7 years.

12. All documents relating to the salaries, bonuses or other remuneration paid, given, distributed or otherwise transferred in any way by Dardanelle, [Southwest] or Cimarron to Perry Sutherland or Todd Sutherland, for the last 7 years.

13. Copies of all federal and state tax returns for Dardanelle, [Southwest] or Cimarron for the last 7 years.
14. Documents reflecting all dividends and distributions paid, or contemplated, by Dardanelle or [Southwest], during the last 7 years.

15. All documents relating to any loan(s) to Perry Sutherland or Todd Sutherland, whether such loan(s) were made directly by one or more of Dardanelle, [Southwest], Cimarron, or any affiliate of Dardanelle, [Southwest] or Cimarron, whether such documents relate to the making of, payments on, or guarantee(s) or forgiveness of any such loan(s), for the last 7 years.

16. All documents relating to the sale(s) of any real or personal property of Dardanelle, [Southwest], Cimarron, any affiliate of any of the foregoing or any other company or partnership or other entity in which any of Dardanelle, [Southwest] or Cimarron have any equity or other ownership interest, and Perry Sutherland or Todd Sutherland, for the last 7 years.

17. All documents relating to any other transactions between Dardanelle, [Southwest], Cimarron, any affiliate of any of the foregoing or any other company or partnership or other entity in which any of Dardanelle, [Southwest] or Cimarron have any equity or other ownership interest, and Perry Sutherland or Todd Sutherland, for the last 7 years.

18. All documents relating to the salaries, bonuses, distributions, or other remuneration paid, given, distributed or otherwise transferred from any company or partnership in which Dardanelle, [Southwest] or Cimarron have any equity or ownership interest, to Perry Sutherland or Todd Sutherland, for the last 7 years.

19. All agendas, minutes or resolutions from any shareholder or director meetings for Dardanelle or [Southwest], as well as any notices or unanimous consents relating to any such meetings, for the last 7 years.
The Companies retained Spradley & Riesmeyer, P.C., a law firm located in Kansas City, Missouri, to represent them in responding to the Demand. The Companies, by letter dated July 21, 2004, asserted that plaintiff did not have a proper purpose to seek inspection and denied her access to the requested books and records. The Companies paid Spradley & Riesmeyer $8,880.41 for the services it provided in responding to the Demand.

On August 31, 2004, plaintiff filed a complaint in the Delaware Court of Chancery pursuant to 8 Del. C. § 220 (the “220 Complaint”), captioned Sutherland v. Dardanelle Timber Co., Inc., C.A. No. 671-N, seeking an order from the Court compelling the production of the books and records listed in the Demand (the “Section 220 Action”). The 220 Complaint alleged that plaintiff had credible bases to believe that there was corporate mismanagement, excessive compensation, waste, breaches of fiduciary duty and other wrongdoing that took place at the Companies. The Companies hired the law firm of Skadden, Arps, Slate, Meagher & Flom LLP (“Skadden”) to represent them in defending the Section 220 Action. Chancellor Chandler referred the matter to Master Sam Glasscock, III for consideration.

1. **Proceedings before Master Glasscock.**

On September 27, 2004, the Companies filed a motion to dismiss the 220 Complaint (the “Motion to Dismiss”) on the grounds that plaintiff’s stated purpose was not her actual purpose and that she did not plead factual evidence sufficient to prove a credible basis to suspect that wrongdoing had occurred at Dardanelle and Southwest. On
October 29, 2004, plaintiff filed an answering brief arguing that she had alleged sufficient factual evidence to prove a credible basis to suspect wrongdoing, and on November 8, 2004, the Companies filed their reply brief. In their reply brief, the Companies argued that plaintiff’s list of “concerns” did not provide the necessary factual support to prove a credible basis to find probable wrongdoing on the part of the Companies’ management. The reply brief also attempted to refute plaintiff’s contention that the IRS Stipulation from January 1999\textsuperscript{41} provided evidence of wrongdoing.

Oral argument was held on the Motion to Dismiss on December 17, 2004 before Master Glasscock. Master Glasscock issued a draft report on December 22, 2004, denying the Motion to Dismiss. The Master concluded that the 220 Complaint, when read together with the Demand, “states allegations of wrong-doing which, if demonstrated at trial, may indicate a probability of fiduciary wrong-doing.” The Master’s draft report acknowledged that the allegations in the 220 Complaint were conclusory, but denied the Motion to Dismiss based upon plaintiff’s assertion at oral argument that “the plaintiff and other witnesses would testify at a hearing as to the factual basis for all of the claims of fiduciary wrong-doing alleged in the [Demand].” Noting

\textsuperscript{41} As described above, § III.A, \textit{supra}, the January 1999 IRS Stipulation covers the use of a corporate jet from 1988 through 1993, specifically detailing the use of that corporate jet for Southwest’s airplane charter business, for other Southwest-related business, and for Southwest executives’ personal use. The IRS stipulation indicated that the corporate jet was used approximately 3\% of the time for Southwest-related business, with the bulk of its use being for Southwest’s airplane charter business.
that the Companies were not publicly-traded, and therefore not subject to stringent disclosure obligations, and that the Section 220 Action was a summary proceeding, the Master concluded that granting the Motion to Dismiss “would serve neither public policy nor judicial or litigants’ economy.”

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 85.40 hours on the Motion to Dismiss and related oral argument, with 24.30 hours of that time billed by partners at hourly rates ranging from $619 to $760, and 63.10 hours billed by an associate at an hourly rate of $235. The Companies were billed a total of $30,196 for this phase of the litigation.

On January 4, 2005, the Companies filed their exceptions to the draft report of Master Glasscock on the Motion to Dismiss. The Companies’ exceptions to the draft report asserted that Master Glasscock erroneously relied on plaintiff’s counsel’s assertions made at oral argument that plaintiff would present factual evidence of the alleged wrongdoing and that the 220 Complaint did not meet the standard necessary to prove a credible basis to suspect wrongdoing. Dardanelle also disputed Master Glasscock’s findings regarding its response to the Demand, as well as who has voting control of Dardanelle, how much Dardanelle stock plaintiff owns individually, and regarding when and how plaintiff acquired her stake in Dardanelle. The Companies decided, however, to agree to proceed with discovery and trial, rather than pressing the exceptions to the draft report. Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 12.0 hours drafting the exceptions to
Master Glasscock’s draft report, with 5.80 hours of that time billed by a partner at an hourly rate of $625 and 6.20 hours billed by an associate at an hourly rate of $235. The Companies were billed a total of $5,254 for this phase of the litigation.

On January 25, 2005, Dardanelle filed its answer to the 220 Complaint. Dardanelle denied that plaintiff had a proper purpose for seeking inspection, but did not assert any affirmative defenses. Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 3.0 hours drafting the answer to the 220 Complaint, with 2.20 hours of that time billed by a partner at an hourly rate of $625 and 0.80 hours billed by an associate at an hourly rate of $235. The Companies were billed a total of $1,663 for this phase of the litigation.

On February 8, 2005, plaintiff served her first set of interrogatories and first request for production of documents. The written discovery requests included eighteen interrogatories (with additional subparts) and twenty-six document requests. The discovery requests were directed to the Companies’ “improper purpose” contention and to other positions plaintiff believed the Companies might take at trial for refusing to comply with the Demand. Plaintiff’s written discovery also sought to obtain information about specific incidents of other pre- and post-litigation conduct by the Companies that might lead to the discovery of admissible evidence regarding plaintiff’s stated purpose for seeking inspection. On March 15, 2006, plaintiff noticed the depositions of Perry, Todd, and David Dotson, as well as a deposition of an employee of Dardanelle under Rule
30(b)(6). Plaintiff filed an amended notice of deposition for Perry, Todd, and David Dotson on April 22, 2005.

Defendant also served its first request for production of documents on plaintiff on February 8, 2005. The twenty-three item document request covered such areas as plaintiff’s allegations regarding the improper use of the corporate aircraft owned by Southwest, the improper use of the Maysville Training Center, the improper use of Cimarron’s services, and compensation paid to Dardanelle executives. In addition, Dardanelle noticed the deposition of plaintiff on March 24, 2005 and the deposition of Dwight Jr. on May 2, 2005.

On March 9, 2005, plaintiff’s counsel sent a letter to the Companies’ counsel raising concerns over alleged deficiencies in the Companies’ responses to plaintiff’s discovery requests. After the parties failed to reach an agreement, plaintiff filed a motion to compel (the “Motion to Compel”) seeking “complete and verified answers” to her interrogatories, a complete set of documents responsive to certain of her document requests, clear responses to certain of her document requests, and an order requiring Perry, Todd, and David Dotson to appear for depositions. The Companies filed their opposition to the Motion to Compel on March 30, 2005, generally arguing that plaintiff’s requests exceeded the limited scope of discovery permitted from a defendant in a Section 220 action.

After plaintiff filed her reply brief, a teleconference was held on April 6, 2005 with Master Glasscock regarding the Motion to Compel. Although many issues
were resolved during the teleconference, the parties still disputed whether the Companies needed to produce documents concerning two amendments made to Dardanelle and Southwest’s certificates of incorporation after the Demand was sent to Dardanelle. On April 25, 2005, Master Glasscock issued a final report on the Motion to Compel that denied plaintiff access to documents concerning the amendments to the certificates of incorporation because those documents did not “directly involve the [ ] wrongdoing” alleged in the Demand.

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 52.55 hours opposing the Motion to Compel, including 16.55 hours billed by a partner at an hourly rate of $665 and 36.0 hours billed by an associate at an hourly rate of $330. The Companies were billed a total of $22,885.75 for this phase of the litigation.

Five depositions were ultimately taken in the Section 220 Action – three by plaintiff and two by the Companies. Robert S. Saunders deposed plaintiff on March 28, 2005 in New York, New York. Bonita L. Stone, on behalf of plaintiff, deposed Perry on April 26, 2005 in Kansas City, Missouri and both Todd and David Dotson on April 27, 2005 in Kansas City, Missouri. Robert S. Saunders defended the depositions of Perry, Todd, and David Dotson, and deposed Dwight Jr. on May 4, 2005 in Chicago, Illinois.

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 145.10 hours engaging in discovery, including drafting and answering discovery requests, reviewing and producing documents
responsive to discovery requests, and taking and defending five depositions. Of the 145.10 hours devoted to discovery, 96.35 hours of that time were billed by partners at hourly rates ranging from $665 to $810 and 48.75 hours were billed by associates at hourly rates ranging from $250 to $330. The Companies were billed a total of $79,945.25 for this phase of the litigation.

On May 18, 2005, Dardanelle filed its eighteen page pre-trial brief. In that pre-trial brief, Dardanelle asserted that it was clear from the deposition testimony of plaintiff and Dwight Jr. that plaintiff’s actual purpose for seeking to inspect the requested books and records “was to harass Dardanelle with litigation distraction and expense in the hope that Norma [Sutherland (Dwight Sr.’s wife)], Perry, and Todd [would] reverse Dwight Sr.’s testamentary decisions.” Dardanelle also reiterated its position that plaintiff lacked any credible evidence of probable wrongdoing, even after the Companies voluntarily disclosed “three years of financial statements and accompanying notes for both Dardanelle and Southwest.” Plaintiff also filed her pre-trial brief on May 18, 2005, generally outlining the bases for her suspicions of wrongdoing.

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 138.40 hours in connection with the pre-trial brief and related activities, including 42.50 hours billed by a partner at an hourly rate of $665 and 95.90 hours billed by an associate at an hourly rate of $330. The Companies were billed a total of $59,909.50 for this phase of the litigation.
On May 23, 2005, plaintiff filed a motion *in limine* seeking to bar the defendant from introducing evidence at trial “(i) regarding any purported ‘improper purpose’ of Ms. Sutherland in bringing this Section 220 action, or the Companies’ contention that Ms. Sutherland’s stated purpose for demanding books and records is not her actual purpose, and (ii) regarding the subject matters of documents Dardanelle failed to timely produce.” Plaintiff claimed that the Companies’ “pattern of discovery violations and abuses have prevented Ms. Sutherland from conducting permissible discovery into Dardanelle’s theory of defense in preparation for trial,” as well as preventing the proper questioning of Perry, Todd, and David Dotson during their depositions. Specifically, plaintiff argued that the defendant obstructed depositions through improper instructions not to answer questions based upon “scope” and withheld non-privileged, responsive documents.

In a letter dated May 25, 2005, defendant argued that Master Glasscock had held that the depositions of Perry, Todd, and David Dotson would be limited in scope and that Dardanelle’s counsel properly instructed them not to answer certain questions. Dardanelle also argued that the documents plaintiff alleged were improperly withheld were equally available to plaintiff, such that there was no duty to produce them. Time records reviewed by the Special Committee indicate that the Companies’ counsel worked 15.0 hours drafting the letter opposing plaintiff’s motion *in limine*, including 5.10 hours billed by a partner at an hourly rate of $665 and 9.90 hours billed by associates at hourly
rates ranging from $330 to $465. The Companies were billed a total of $6,780 for this phase of the litigation.

A one-day trial was held on May 26, 2005 before Master Glasscock to consider the merits of plaintiff’s allegations in the Section 220 Action and plaintiff’s motion in limine. At trial, three witnesses testified: plaintiff, Dwight Jr., and Perry. Eighty-seven exhibits, as well as the transcripts of the five depositions taken in connection with this matter, were introduced into evidence. Master Glasscock reserved judgment on both the merits and plaintiff’s motion in limine.

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 191.95 hours preparing for and attending the trial before Master Glasscock. Of the 191.95 hours worked by the Companies’ counsel on this phase of the litigation, 81.95 hours were billed by partners at hourly rates ranging from $665 to $810, and 109.10 hours were billed by associates at hourly rates ranging from $330 to $465. The Companies were billed a total of $98,922 for this phase of the litigation.

Approximately six weeks after the trial concluded, plaintiff filed her opening post-trial brief on July 8, 2005. In her brief, plaintiff alleged, among other things, that she had a credible belief of wrongdoing and that her belief was supported by (a) her removal as a director and officer of Southwest; (b) Perry and Todd’s self-interested votes to approve their employment agreements; (c) Perry and Todd’s personal
use of the corporate aircraft at company expense; (d) Perry and Todd’s improper use of corporate funds and resources; and (e) Dardanelle’s response to the Demand.

Dardanelle filed its fifty-page answering post-trial brief on July 29, 2005. That brief reiterated the contentions that plaintiff did not prove that her actual purpose was to investigate wrongdoing and that plaintiff did not prove a credible basis to find probable wrongdoing. Defendant argued that plaintiff did not provide credible evidence that (a) the corporate aircraft had been misused; (b) the Companies’ executives had abused the use of Dardanelle expense accounts; (c) the Companies’ executives had lived a “lavish lifestyle” at the expense of Dardanelle; (d) the Companies’ executives and Choctaw had misused the tax and accounting services provided by Cimarron; (e) the Companies’ financial statements were false or that there was an “apparent continued decline in company business and assets”; (f) the approval of and the terms of Perry’s and Todd’s employment agreements with Dardanelle and Southwest were inappropriate; and (g) the removal of plaintiff from Southwest’s board of directors was improper. On August 17, 2005, plaintiff filed her post-trial reply brief, responding to defendant’s arguments and setting forth the bases for her belief of wrongdoing.

Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 313.75 hours in connection with preparing the post-trial brief and related activities. Of those 313.75 hours, partners billed 61.15 hours at hourly rates ranging from $665 to $810, and associates billed 252.60 hours at hourly
rates ranging from $330 to $465. The Companies were billed a total of $156,606.50 for this phase of the litigation.

On August 22, 2005, Dardanelle sent a letter to Master Glasscock requesting post-trial oral argument, which occurred on August 31, 2005. At the conclusion of the argument, Master Glasscock orally issued his draft report (the “Draft Report”). Master Glasscock found that plaintiff’s stated purpose of investigating probable wrongdoing was her primary purpose and that there was a credible basis to believe that probable wrongdoing had and was occurring at Dardanelle and Southwest in connection with compensation and perquisites that Perry and Todd had been and were providing themselves. Master Glasscock therefore concluded that plaintiff was entitled to inspection but did not specify which books and records should be made available or what time period the inspection should cover, leaving it to counsel to craft a form of order. Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 55.30 hours preparing for and participating in the post-trial oral argument. Of those 55.30 hours, 34.70 hours were billed by a partner at an hourly rate of $665 and 20.60 hours were billed by associates at hourly rates ranging from $330 to $465. The Companies were billed a total of $32,384.50 for this phase of the litigation.

The parties could not agree on a form of order and, with Master Glasscock’s approval, suspended briefing on exceptions to the Draft Report to seek clarification regarding his findings. On September 23, 2005, both parties provided letters to Master Glasscock explaining their respective positions and submitting their proposed
forms of order. Master Glasscock thereafter issued a letter ruling dated November 18, 2005 in an effort to clarify the Draft Report. See Sutherland v. Dardanelle Timber Co., Inc., 2005 WL 3272125 (Del. Ch.) (the “Final Report”). Master Glasscock stated that “this letter together with my bench decision constitute my final report in this matter.” Id. at *3. He further stated that “[a]ll exceptions to my report are preserved for presentation to the Chancellor.” Id. at *1. In the Final Report, Master Glasscock reiterated that the evidence provided a credible basis to believe probable wrongdoing had been and was occurring at Dardanelle and Southwest in connection with Perry and Todd’s compensation and perquisites. Therefore, Master Glasscock concluded that plaintiff had demonstrated a proper purpose to allow access to documents “relating to the enjoyment of salary and benefits by Perry and Todd for the period commencing one full fiscal year before the death of Mr. Sutherland Sr.” Id. at *3. The Master specifically defined the inspection to track “the language of the plaintiff’s initial demand letter, narrowed to the documents that [the Master] found sufficient to fulfill the purpose demonstrated at trial.”42 Id. Time records reviewed by the Special Committee indicate that the

---

42 These documents were described as follows: “all documents which relate to the salary and benefits and perquisites received by Perry or Todd, at the expense of Dardanelle or Southwest, whether pursuant to a written contract of employment, an oral contract of employment, or otherwise, and to have the financial statements of the corporations to put this compensation in context. This includes all documents relating to the use by Perry or Todd or their immediate families, for personal purposes, of any aircraft owned or leased by Southwest or Dardanelle including documents relating to the tax ramifications of such use to the corporations involved; documents relating to the expense accounts and to expense (cont’d)
Companies' counsel worked a total of 20.9 hours negotiating with opposing counsel and
drafting the letter to Master Glasscock regarding the form of order. Of those 20.9 hours,
a partner spent 4.3 hours at an hourly rate of $740, and associates spent 16.6 hours at
hourly rates ranging from $395 to $530 on the issue. The Companies were billed a total
of $11,710 for this phase of the litigation.

In summary, Master Glasscock generally limited the inspection of
documents to a period commencing one full fiscal year before the death of Dwight Sr.,
_i.e._, from October 25, 2002, rather than the seven-year period, _i.e._, from July 13, 1997, as
requested by plaintiff; and did not require the production of: (a) documents relating to
any business transactions between Perry or Todd and Cimarron or any other Dardanelle
or Southwest affiliates; (b) documents relating to any remuneration paid by Cimarron or
any other Dardanelle or Southwest affiliates to Perry or Todd; and (c) copies of audited
and unaudited financial statements of Cimarron. Specifically, Master Glasscock denied

(continued)

(reimbursement records for Dardanelle or Southwest concerning Perry or Todd;
documents relating to expenditures of money or services by Southwest or
Dardanelle pertaining to Choctaw Racing Stables; documents relating to any loans
from Dardanelle or Southwest to Perry, Todd, their immediate family members or
tentities in which they have an ownership interest; documents relating to
expenditures by Dardanelle or Southwest for the use of the Maysville Training
Center on behalf of Perry, Todd or their immediate families; copies of financial
statements for Dardanelle and Southwest for the period in question; documents
relating to all remuneration in cash or kind paid by Dardanelle or Southwest to
Perry or Todd; documents relating to the sale of assets by Dardanelle or Southwest
to Perry or Todd, as well as documents relating to any transactions between those
companies and Perry or Todd.) _Id._ at *2.
the requests for: (a) all documents relating to the ownership or leasing of any aircraft by Dardanelle or Southwest; (b) all documents relating to the costs to Dardanelle or Southwest of owning or leasing any aircraft limiting plaintiff’s requests for documents relating to the use of any aircraft owned or leased by Dardanelle or Southwest by Perry, Todd, or their families; (c) all documents relating to any services provided by Cimarron to Choctaw, Dardanelle, or Southwest; (d) copies of all federal or state tax returns for Dardanelle, Southwest, or Cimarron; (e) all documents reflecting all dividends or distributions paid, or contemplated, by Dardanelle or Southwest; and (f) all agendas, minutes, or resolutions from any shareholder or director meetings for Dardanelle or Southwest.

2. Proceedings before Vice Chancellor Lamb.

Dardanelle filed its notice of exceptions to the Final Report on December 1, 2005, asking for a de novo evidentiary hearing at which new evidence could be presented and witnesses could be called to testify. On December 22, 2005, the matter was reassigned to Vice Chancellor Stephen P. Lamb for consideration of exceptions to the Final Report. Plaintiff filed her opening brief in support of her exceptions to the Final Report and in opposition to defendant’s exceptions to the Final Report on January 9, 2006. In her brief, plaintiff raised two exceptions to the Final Report: (a) that Master Glasscock improperly limited her inspection to books and records for one full fiscal year prior to the death of Dwight Sr. and should have allowed much broader inspection because Perry and Todd’s alleged wrongdoing dated back even beyond the seven-year
period for which books and records were sought in the Demand, and (b) that Master Glasscock improperly limited the subject matter of the Demand to the extent he narrowed the categories of documents set forth in the Demand.

Defendant filed its sixty-page opening brief in support of its exceptions to the Final Report and in opposition to plaintiff’s exceptions on January 30, 2006. Defendant argued in its opening brief that (a) the 220 Complaint was conclusory and should be dismissed; (b) Master Glasscock erred in finding that plaintiff’s stated purpose was her actual purpose; (c) Master Glasscock erred in finding that plaintiff was entitled to inspection of documents relating to Perry and Todd’s employment agreements; (d) Master Glasscock properly rejected plaintiff’s contentions that there was misuse of the corporate aircraft and of the Companies’ funds and resources; and (e) Master Glasscock erred with respect to the subject matter and temporal scope of the granted inspection relief. Time records reviewed by the Special Committee indicate that the Companies’ counsel worked a total of 167.2 hours in connection with the drafting of the Companies’ exceptions to the Final Report and in opposition to plaintiff’s exceptions, including 36.8 hours billed by partners at hourly rates ranging from $740 to $835 and 130.4 hours billed by an associate at an hourly rate of $530. The Companies were billed a total of $96,534 for this phase of the litigation.

Plaintiff filed her reply brief in support of her exceptions and in opposition to defendant’s exceptions on February 21, 2006. Plaintiff argued in her brief that (a) the Companies could not at this stage of the proceedings argue that the 220 Complaint was
insufficient; (b) the Companies misinterpreted the standard of review of a master’s findings; (c) the Companies could not overcome the objective evidence supporting plaintiff’s credible belief of probable wrongdoing; and (d) the inspection sought in the Demand should be granted in its entirety.

Oral argument was held on March 20, 2006 before Vice Chancellor Lamb. On May 16, 2006, Vice Chancellor Lamb, within two months of the argument but almost twenty-one months after the 220 Complaint was filed, issued an opinion and order substantially affirming the Final Report. The Court conducted its de novo review based on the record alone and held that an evidentiary hearing to examine the credibility of plaintiff’s testimony was not necessary. The Court further held that plaintiff had proven a credible basis to believe that wrongdoing was afoot at the Companies because of the secret meeting held to remove plaintiff from Southwest’s board of directors and because of the terms of Perry’s and Todd’s employment agreements that allow them access to the corporate aircraft, access to effectively free financial services, and access to the Maysville Training Center. The Court also held that plaintiff’s stated purpose was her actual and primary purpose. The Court upheld Master Glasscock’s limitation of the production of documents to a period of one full fiscal year before Dwight Sr.’s death. Finally, the Court slightly expanded the scope of documents that Dardanelle was to provide to plaintiff to include all documents concerning Dardanelle and Southwest’s ownership and lease of aircraft and all agendas, minutes, resolutions, and unanimous consents for shareholder or director meetings of Dardanelle or Southwest.
Time records reviewed by the Special Committee indicate that Dardanelle’s counsel worked 19.0 hours preparing for and attending the oral argument before Vice Chancellor Lamb. Of those 19.0 hours, a partner billed 16.7 hours at an hourly rate of $740 and an associate billed 2.3 hours at an hourly rate of $530. The Companies were billed a total of $13,577 for this phase of the litigation.

During June 2006, the Companies’ counsel reviewed and gathered documents responsive to Martha’s requests for books and records. Also during this time, the parties came to an agreement on a confidentiality stipulation regarding the production of documents by the Companies to Martha. Time records reviewed by the Special Committee indicate that Dardanelle’s counsel worked 53.3 hours reviewing documents and negotiating a confidentiality stipulation. Of those 53.3 hours, partners billed 30.4 hours at hourly rates ranging from $665 to $810 and associates billed 22.9 hours at hourly rates ranging from $330 to $465. The Companies were billed a total of $30,484 for this phase of the litigation.

The total amount billed by Skadden for all of the book and records activity was $734,845, which included $691,029 for professional services rendered and $43,816 in disbursements. Skadden’s total bill of $734,845 is after write-offs totaling

---

43 The $734,845 total bill includes 28.65 hours spent by partners at hourly rates ranging from $619 to $760 and 13.50 hours spent by associates at hourly rates ranging from $375 to $387 reviewing the pleadings and background materials relating to the Section 220 Action, as well as researching various legal issues relating to the Section 220 Action. The $734,845 total bill also includes 15.95 (cont’d)
$146,706.50 given by Skadden at its discretion and at the Companies’ request. Skadden billed the Companies at its standard hourly rates throughout the Section 220 Action.

The decision of Vice Chancellor Lamb was not appealed to the Delaware Supreme Court.

C. Claims Pertaining To Terms Of The Employment Contracts And Other Miscellaneous Claims.

Plaintiff’s Complaint challenges the terms of the employment agreements on the grounds that Perry’s agreements permit “part-time work,” give him unlimited access to certain perquisites at the Companies’ expense, and:

give him the unlimited right to compete with Dardanelle and Southwest and also provide that, upon termination “for any reason,” Perry will receive continued payments under the purported agreements for two years. Thus, Perry is free to disregard his fiduciary duties to Dardanelle and Southwest and their shareholders by competing with Dardanelle and Southwest and working for any other business venture of any nature, no matter how the family companies are harmed. And, even if Perry is terminated for committing criminal or fraudulent acts, no matter what the harm caused to Dardanelle and Southwest and their shareholders, Perry will still be entitled to receive his compensation from Dardanelle and Southwest for two full years after termination.

(cont’d)

hours spent by partners at hourly rates ranging from $625 to $835 and 1.8 hours spent by an associates at an hourly rate of $395 attending to various miscellaneous tasks, including drafting letters to opposing counsel and the Court, reviewing public filings of the Companies, and conducting teleconferences with officers at the Companies to discuss strategy and other topics.
Complaint ¶ 48. Plaintiff makes similar claims as to the terms of Todd’s employment agreement with Dardanelle, except she does not challenge a “part-time” provision (since Todd’s agreement contains no such reference), but alleges that the compensation he receives “is effectively a gift because Todd has and performs no real duties for Dardanelle.” Id. ¶ 49.

The Complaint also alleges that a variety of extravagant personal expenses have been charged to the Companies, challenges a charitable contribution made by the Companies, and challenges certain changes made to the Companies’ certificates of incorporation. Specifically, the Complaint alleges, upon information and belief, that Perry and Todd:

have also indulged in a myriad of other personal extravagances at company expense, including such things as rental cars, expensive hotels, limousines, club memberships, chartered private railroad cars for extended personal trips, private parties, and personal living expenses, among many others. The cumulative expenses for these extravagances are considerable and there is no business reason why Dardanelle or Southwest should have or did bear them.

Complaint ¶ 64. During the interview of plaintiff and Dwight Jr., the Special Committee asked for identification of specific transactions or extravagances which they thought the Special Committee should investigate. Plaintiff and Dwight Jr. identified stays at the Lowell Hotel in New York City, use of Carey Limousine, membership in the River Club in Kansas City, the use of Southwest credit cards to pay for rental vans in connection with a memorial service for Dwight Sr. that occurred in Oklahoma, vacations involving private railroad cars, Perry’s construction of an expensive personal residence, and certain
litigation, all of which they indicated was personal but paid for by the Companies.\textsuperscript{44} Plaintiff and Dwight Jr. also questioned loans from the Companies to Todd and Perry, and loans by their mother’s trust to the Companies. At paragraph 66 of the Complaint, plaintiff also complains that:

Perry and Todd even found it appropriate to have the companies make a $360,000 charitable contribution in the fiscal year ended July 31, 2003, where net operating losses from operations were again approximately over $1 million, rather than minimizing the companies’ losses or distributing such amounts to shareholders rather than Perry and Todd’s chosen charity.\textsuperscript{45}

Finally, the Complaint alleges that in early September 2004, the Individual Defendants amended Dardanelle’s certificate of incorporation to eliminate cumulative voting and, shortly thereafter, amended the certificate of incorporation of each of the Companies to add a provision authorized by Section 102(b)(7) of the Delaware General Corporation Law. Complaint ¶¶ 81, 83. Plaintiff alleges that these amendments “serve

\textsuperscript{44} They also urged the Special Committee to review the Companies’ general ledgers, made allegations that checks were routinely written from an account to pay personal expenses, expressed suspicion that the financials indicated a larger travel and entertainment expense than that contained in the credit card records plaintiff received in the Section 220 Action (with a suggestion that Perry had the Companies reimburse him for mileage on rented vehicles) and expressed concerns about what items were included in a miscellaneous expense category on the financials.

\textsuperscript{45} During the interview, plaintiff suggested this amount was given to The University of Kansas.
only the personal interests of the Individual Defendants and provide no benefit whatsoever to Dardanelle or its shareholders.” Complaint ¶ 84.

Based on its review of the documentary record and interviews of persons with knowledge of the relevant facts, the Special Committee concludes that the Complaint accurately describes the terms of the employment agreements Perry and Todd have with the Companies. Outside counsel was retained to prepare employment agreements for Perry and Todd, but acted primarily in the role as a scrivener for terms that were provided to him, rather than as an advocate for either party. The first draft provided by outside counsel included deferred compensation provisions to the surviving spouse equal to one-half of the compensation paid at the time of death. These provisions were removed from the draft agreements because Perry and Todd did not understand such a provision to be part of the informal and unwritten agreements by which they had been working for the Companies. The Special Committee’s investigation

---

46 The Complaint alleges that the employment agreements with Perry and Todd were the “first and only” employment agreements in the history of the Companies. Complaint ¶ 41. In fact, Dwight Sr. and Dardanelle entered into a June 2002 Employment and Deferred Compensation Agreement providing that upon his death, Norma would receive $50,000 per annum until her death. It is the Special Committee’s understanding that none of her children challenge this payment to Norma.

47 The Special Committee’s investigation revealed that prior to the adoption of the employment agreements, Perry and Dwight Sr.’s use of the Aircraft for personal purposes resulted in additional compensation at the SIFL rate, which amount was “grossed-up” for employment and federal income taxes. The gross-up was discontinued when the employment agreements were entered into and, as of (cont’d)
further revealed that the “part time” provisions were inserted into Perry’s agreements in part because there are separate contracts with Southwest and Dardanelle making it impossible to work “full time” for both and in part because Perry also devotes some time to other enterprises, including as executor of his mother’s trust and as the owner of Choctaw.

Each of plaintiff’s allegations relating to the terms of the employment contracts and miscellaneous claims will be addressed in greater detail at Sections IV.D. and IV.E. of this Report.

IV. LEGAL ANALYSIS AND CONCLUSIONS.

The Special Committee, in the course of its work, has consulted with its counsel concerning the legal principles applicable to plaintiff’s claims and has sought to apply those principles to the facts it has ascertained in the course of its investigation. The legal principles considered and certain of the determinations made by the Special Committee are discussed in this section of the Report.

A. General Legal Principles Applicable To Plaintiff’s Claims.

Counts I and III of plaintiff’s Complaint assert claims for breach of fiduciary duties against the directors of Dardanelle, a Delaware corporation, and Southwest, its wholly-owned subsidiary and also a Delaware corporation. Those claims (cont’d)

October 2004, there is no additional compensation or gross up for personal use of the Aircraft.
are governed by Delaware law. See Sternberg v. O’Neil, 550 A.2d 1105, 1123-24 (Del. 1988); Armstrong v. Pomerance, 423 A.2d 174, 177 (Del. 1980). Delaware law requires directors, who stand in a fiduciary relationship to the corporation and its stockholders, to act with due care, in good faith, and in a manner that protects the best interests of the corporation. See Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993). Because they are ill-equipped to second guess decisions made by a board of directors, Delaware courts accord to board decisions by disinterested directors acting in good faith and with due care the protections of the business judgment rule. E.g., Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (absent “abuse of discretion,” board’s judgment “will be respected by the courts”). In circumstances where the business judgment rule does not apply, fiduciaries must demonstrate the entire fairness of transactions between directors and the corporation. See Weinberger v. UOP, Inc., 457 A.2d 701, 710-11 (Del. 1983).

Count III of plaintiff’s Complaint asserts claims for harm to Southwest, a wholly-owned subsidiary of Dardanelle. Such “double derivative” claims, under Delaware law, may be brought when the boards of directors of both the parent and subsidiary are not in a position to exercise business judgment with respect to the alleged wrongdoing. See, e.g., Rales v. Blasband, 634 A.2d 927, 934 (Del. 1993); Sternberg v. O’Neil, 550 A.2d at 1124. At the time the Complaint was filed, the boards of directors of each of Dardanelle and Southwest was comprised of the same three individuals: Perry, Todd and Mark Sutherland.
In the “Wherefore” clause of the Complaint, plaintiff requests a
determination that the Individual Defendants have breached their fiduciary duties and
committed corporate waste, an award of “appropriate damages,” an award of costs,
disbursements, and attorneys’ and experts’ fees, as well as equitable or other relief that
the Court deems just and proper. In the body of the Complaint, plaintiff also requests that
a receiver be appointed to “end the pervasive and continuing wrongful conduct by the
Individual Defendants that continues to drain the assets of Dardanelle and Southwest”
and to “ensure that the damages awarded in this action will be a meaningful remedy, by
preventing the Individual Defendants from simply depleting those funds through similar
wrongdoing in the future.” Complaint ¶ 13. A plaintiff who seeks the appointment of a
receiver for a solvent corporation “must show fraud, gross mismanagement or extreme
circumstances causing imminent danger of great loss which cannot be otherwise
Vale v. Atlantic Coast & Inland Corp., 99 A.2d 396, 400 (Del. Ch. 1953)). Courts will
exercise the power to appoint a receiver for a solvent corporation with “great restraint.”
Vale, 99 A.2d at 400.

In Tansey v. Oil Producing Royalties, 133 A.2d 141 (Del. Ch. 1957), the
Court appointed a receiver for a solvent corporation where there was proof that there had
been a substantial failure of management, that the basic purpose of the corporation had
“largely disappeared,” and that the managing officer contemplated the total abandonment
of the corporate enterprise. This is one of the rare examples where the “appointment of a
receiver was necessary to prevent imminent loss to the corporation.” Hall v. John S. Isaacs & Sons Farms. Inc., 163 A.2d 288, 293 (Del. 1960) (citing Tansey as a rare instance where the Court appointed a receiver for a solvent corporation). Based on its investigation, and as detailed in this Report, the Special Committee has not found any evidence of gross mismanagement or fraud, nor has it found that there is an “imminent” danger to the Companies if a receiver is not appointed. Dardanelle and Southwest are not at risk of the Individual Defendants “drain[ing]” their assets or of any award granted by this Court being depleted by the Individual Defendants. Accordingly, the Special Committee has concluded that the appointment of a receiver is not warranted.

1. The Duty of Loyalty and Standards for Director Interest and Independence.

Directors of Delaware corporations have a fiduciary duty of care and a duty of loyalty. The duty of loyalty “mandates that the best interest of the corporation and its shareholders take precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally.” Cede & Co., 634 A.2d at 361. The duty of loyalty also “requires that a ‘controlling’ shareholder not act, or cause its representatives to act, in such a manner as to deal unfairly with the minority shareholders.” Oliver v. Boston University, 2006 WL 1064169, at *18 (Del. Ch.).

48 As confirmed in the interview with plaintiff, the claims in the Complaint are not premised upon allegations that the Individual Defendants acted with gross negligence. Rather, plaintiff claims that they have not acted in good faith and have violated their fiduciary duty of loyalty.
Whether a director is interested or not independent with respect to a challenged transaction is essentially a question of fact and requires a plaintiff to introduce evidence of disloyalty. *Cede & Co.*, 634 A.2d at 363. To obviate application of the business judgment rule on the basis of alleged self-interest, “there must be evidence of a substantial self-interest [on the part of a majority of the board] suggesting disloyalty such as evidence of entrenchment motives, vote selling, or fraud.” *Goodwin v. L.I.V.E Entertainment, Inc.*, 1999 WL 64265, at *25 (Del. Ch.), aff’d, 741 A.2d 16 (Del. 1999). Disinterested directors are those who “neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of self dealing, as opposed to a benefit which devolves upon the corporation or all stockholders in general.” *Williams v. Geier*, 671 A.2d 1368, 1377 n.19 (Del. 1996).

“Independent” means that a director’s decision is based on the “corporate merits of the subject before the board rather than extraneous considerations or influences.” *In re J.P. Morgan Chase & Co.*, 2005 WL 1076069, at *8 (Del. Ch.). The mere receipt of directors’ fees or some immaterial “self-interest, standing alone and without evidence of disloyalty,” does not rebut the presumption of independence. See *Cede & Co.*, 634 A.2d at 363; *Grobow v. Perot*, 539 A.2d 180, 188 (Del. 1988).

The Special Committee, for purposes of its Report, has assumed that Mark is not independent from Perry or Todd with respect to those claims as to which Perry or Todd have a material financial interest. The Special Committee recognizes that there is Delaware case law suggesting that Mark’s status as the cousin of Perry and Todd is not
sufficient to support an inference that he is not independent. See Seibert v. Harper & Row Pub., Inc., 1984 WL 21874, at *3 (Del. Ch.) ("The fifth director's alleged 'interest' stems from the fact he is the cousin of the director who tends a subsidiary of Harper & Row. This fact, without more, is insufficient to demonstrate domination and control by the interested director."). The Complaint also alleges that Mark was chosen as a director because Perry and Todd knew he "would abdicate his duties and accede to their wishes" (Complaint ¶ 18), and further alleges that Mark has deferred to Perry with respect to decisions not directly involving the Companies, such as the response by Sutherland Lumber of Kansas City, LLC to a demand to inspect books and records made by plaintiff.49 Although such allegations may not be sufficient to establish a lack of independence, and in light of the fact that no decisions challenged by plaintiff were taken by a two to one vote such that assessment of Mark's independence becomes critical, the Special Committee has determined to assume Mark is not independent of Perry and Todd for purposes of its various analyses.

49 Plaintiff suggested the Special Committee review records pertaining to, among other things, the cost to Sutherland Lumber Co. of Kansas City, LLC of producing documents requested of it. Because the allegations relating to that LLC are made only for purposes of establishing that Mark is not independent and not as a claim for relief, and in light of the Special Committee's decision to assume for purposes of its analysis that Mark is not independent, the Special Committee exercised its judgment not to incur the additional costs associated with such tangential issues.
2. The Entire Fairness Standard and Executive Compensation.

In circumstances where the protections of the business judgment rule do not apply, directors will be required to prove that the challenged transaction is entirely fair to the corporation and its stockholders, both in the procedures followed in considering and negotiating the transaction and in the ultimate terms and price of the transaction. *See Weinberger v. UOP*, 457 A.2d at 710-11. Under Delaware law, “[a] controlling or dominating shareholder standing on both sides of a transaction . . . bears the burden of proving its entire fairness.” *Kahn v. Lynch Communication Sys., Inc.*, 638 A.2d 1110, 1115 (Del. 1994). For purposes of this Report, the Special Committee assumes that Perry and Todd should be treated collectively as a controlling stockholder.

The entire fairness standard requires the defendants to demonstrate that any challenged transaction between them and the Companies was the product of both fair dealing and fair process. The test of entire fairness, which assesses the transaction as of the time it was approved, “involves balancing the process and price aspects of the disputed transaction.” *Ryan v. Tad’s Enters., Inc.*, 709 A.2d 682, 690 & n.10 (Del. Ch. 1996). Although a transaction subject to entire fairness review is subject to “rigorous judicial scrutiny,” *Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1279 (Del. 1989), directors may satisfy the standard. *E.g., Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1177 (Del. 1995).
a. **Fair dealing.**

The fair dealing component of entire fairness “embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained.” *Weinberger*, 457 A.2d at 711. In matters of executive compensation, there is a lack of meaningful process in determining salaries if the director who is receiving the compensation, for his role as an officer, “initiates the compensation transaction[,] and determine[s] the amount of compensation to be paid” without any other directors participating in the decision or negotiating the amount of compensation on behalf of the corporation. *Carlson v. Hallinan*, 2006 WL 771722, at *13 (Del. Ch.). The directors have to be able to show that they made an “informed, deliberate judgment” concerning the executive compensation, rather than an “arbitrary” decision. *Id.* They also need to be able to show that all material facts were disclosed to each one of them so that “an informed decision [could] be made as to whether or not a transaction should be approved.” *Id.* Simply presenting the compensation proposal at a meeting of the board of directors and having it approved by a majority of interested directors does not satisfy the fair process standard. *Id.*

b. **Fair price.**

In the area of executive compensation, Delaware courts have looked to several factors in determining if the amount of compensation an executive receives is fair. Evidence of what other executives “similarly situated” at comparable companies receive