IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

MARTHA S. SUTHERLAND, as Trustee of the Martha S. Sutherland Revocable trust dated August 18, 1976,	)	
Plaintiff,	)	
v.	)	C.A. No. 2399-VCL
PERRY H. SUTHERLAND, TODD L. SUTHERLAND, and MARK B. SUTHERLAND,	)	
Defendants,	)	
and	)	
DARDANELLE TIMBER CO., INC., and SUTHERLAND LUMBER SOUTHWEST, INC.,	)	
Nominal Defendants.	)	

MEMORANDUM OPINION AND ORDER

Submitted: February 3, 2009
Decided: March 23, 2009

J. Travis Laster, Esquire, Matthew F. Davis, Esquire, ABRAMS & LASTER, LLP, Wilmington, Delaware; Bonita L. Stone, Esquire, Stewart T. Kusper, Esquire, KATTEN MUCHIN ROSENMAN LLP, Chicago, Illinois, *Attorneys for the Plaintiff.*

Robert S. Saunders, Esquire, Linda Beebe, Esquire SKADDEN ARPS SLATE MEAGHER & FLOM, LLP, Wilmington, Delaware, *Attorneys for the Individual Defendants.*

A. Gilchrist Sparks, III, Esquire, S. Mark Hurd, Esquire, Jay N. Moffitt, Esquire, MORRIS NICHOLS ARSHT & TUNNELL, LLP, Wilmington, Delaware, *Attorneys for the Nominal Defendants*.

LAMB, Vice Chancellor.

This case concerns a derivative and double derivative complaint filed by a 25% stockholder of a closely held corporation with the support of her brother, who is also a 25% stockholder of the corporation. The complaint alleges that the plaintiff's other two siblings, through their power as controlling stockholders, directors, and officers of the corporations, have caused the corporations to enter into a variety of self-dealing and/or wasteful transactions.

The individual defendants have moved to dismiss the complaint for failure to state a claim upon which relief can be granted. In support of this motion, the defendants have offered a variety of grounds, including an allegedly exculpatory provision of each corporation's charter and the statute of limitations. The court finds that the statute of limitations restricts the claims that the plaintiff may pursue, but disagrees with the defendants as to the applicable date. The court will deny the motion to dismiss, except with respect to actions taken prior to the time-bar date.

I.

A. The Parties

Nominal defendant Dardanelle Timber Company, Inc. is a closely held, family-owned Delaware corporation.

Nominal defendant Sutherland Lumber–Southwest, Inc. ("Southwest") is a Delaware corporation and a wholly owned subsidiary of Dardanelle.

The plaintiff, Martha S. Sutherland,[1] is a stockholder of Dardanelle Timber Company, Inc. She is both trustee and beneficiary of a trust by which she is the beneficial owner of 17% of Dardanelle's common stock. Her children are the beneficiaries of other trusts (through gifts made by her) that own approximately 8% of the common stock of Dardanelle.

Defendant Perry H. Sutherland is the brother of Martha. He is one of three directors of both Dardanelle and Southwest, as well as the president and chief executive officer of both companies. Perry and his children beneficially own (and Perry has the power to vote) 25% of the common stock of Dardanelle. Perry also controls a trust which owns all of the voting preferred stock of Dardanelle.

Defendant Todd L. Sutherland is the twin brother of Perry. He is one of three directors of both Dardanelle and Southwest, as well as an officer of both companies. Todd and his children are the beneficial owners of (and Todd has the power to vote) 25% of the common stock of Dardanelle.

Defendant Mark B. Sutherland is the cousin of the Sutherland siblings, and the third of the directors of both Dardanelle and Southwest. He holds no equity interest in either corporation.

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[1] Because all of the relevant individuals involved in this suit are members of the Sutherland family and bear the same last name, the court will follow the convention of the parties and refer to the various individuals throughout this opinion by their first names.

B. The Facts

The following facts are drawn from the well-pleaded allegations in the amended complaint, along with any exhibits attached thereto.[2] Because the facts in this case have been discussed in detail by this court on more than one occasion, only those facts relevant to the disposition of the present motion will be detailed below.[3]

Dardanelle is a family owned and operated Delaware corporation, which, in part through its wholly owned subsidiary Southwest, is in the business of operating retail lumber yards and stores. Both companies were founded by Dwight D. Sutherland, Sr. ("Dwight Sr."), who served as president until his death in October 2003.

Approximately three decades ago, Dwight Sr. gave 25% of Dardanelle's common stock to each of his children: Martha, Dwight Jr., Perry, and Todd. At the time, Dwight Sr. and his wife Norma jointly owned all of Dardanelle's preferred stock, which carries voting rights. After Dwight Sr.'s death, the shares of preferred stock were transferred to a trust for Norma's benefit.

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[2] When referring to allegations in the complaint, the term "complaint" will be used synonymously with the amended complaint.

[3] The facts of the case are extensively set forth in three prior opinions of this court. *See Sutherland v. Sutherland*, 2008 WL 1932374 (Del. Ch.); *Sutherland v. Sutherland*, 2007 WL 1954444 (Del. Ch.); *Sutherland v. Dardanelle Timber Co.*, 2006 WL 1451531 (Del. Ch.).

Despite the even split of the common equity between the siblings, Perry and Todd have voting control over Dardenelle and Southwest because Perry is the trustee for Norma's trust, and Todd has allied himself with Perry. Perry and Todd constitute a majority of Southwest's three-member board, a majority of Dardanelle's board, and serve as the principal officers of both companies. Mark serves as the third director of both Dardanelle and Southwest. Martha was a director of Southwest until February 20, 2004. On that date, Dardanelle, the sole stockholder of Southwest, called an annual meeting for Southwest at which the number of Southwest directors was reduced to three and each of Perry, Todd, and Mark was elected to the board.[4]

Relying upon the documentation she received as a result of a hard-fought action brought pursuant to 8 *Del. C.* § 220, Martha filed this suit on September 6, 2006. Following this court's denial of a motion to dismiss by the special litigation committees of the two nominal corporate defendants, Martha amended her complaint on September 15, 2008. The complaint is in three counts: the first is for breach of fiduciary duty and asserts claims derivatively on behalf of Dardanelle; the second count is for waste; the third count is for breach of fiduciary duty and

[4] The next day, Perry, Todd, and Mark approved employment agreements for Perry and Todd.

asserts double derivative claims on behalf of Southwest. Although not a named plaintiff, Dwight Jr., a lawyer, supports Martha in bringing this action.

Centrally, the complaint alleges that the individual defendants have used the companies' "corporate funds and assets for personal benefit."[5] Specifically, Martha asserts that Perry and Todd have caused the companies to pay for (1) personal flights they have taken on the corporate airplane; (2) personal tax and accounting services provided to them by Cimarron Lumber & Home Supply Company, Ltd., a Dardanelle affiliate; (3) use for personal vacations of a facility commonly known as the Maysville Training Center; and (4) "things [such] 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."[6]

The complaint also challenges the decision to purchase a new corporate aircraft as well as the decision to maintain continuing ownership in it, alleging that the aircraft serves no legitimate business purpose. The complaint further alleges that Perry and Todd's decision to approve their own employment agreements at a February 21, 2004 board meeting constitutes waste and a breach of fiduciary duty. Martha asserts that the agreements pay Perry excessively for "part-time" work and

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[5] Am. Compl. ¶ 150.
[6] *Id.* ¶ 106.

contain excessive perquisites, such as payment for personal use of the aircraft and for personal tax and accounting services. Finally, the complaint bases its breach of fiduciary duty and waste claims on allegations that the individual defendants improperly caused Dardanelle to spend over $750,000 to defend against Martha's Section 220 action, and improperly amended Dardanelle's bylaws pursuant to 8 *Del. C.* § 102(b)(7) to include a limitation of liability provision.

The individual defendants, in response to the amended complaint, filed a motion to dismiss for failure to state a claim upon which relief can be granted.[7] The defendants primarily offer three grounds for their motion: (1) a certain allegedly exculpatory provision of the charters of both corporations protects self-dealing transactions from attack; (2) claims based on actions taken prior to September 6, 2003 are time-barred; and (3) the plaintiff has failed to sufficiently plead the unfairness of one of the categories of challenged transactions.

II.

When considering a motion to dismiss a complaint for failure to state a claim, the court assumes as true all well-pleaded allegations of fact in the complaint.[8] Although the court accepts as true "all facts of the pleadings and reasonable inferences to be drawn therefrom, . . . neither inferences nor

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[7] Ct. Ch. R. 12(b)(6).
[8] *See Grobow v. Perot*, 539 A.2d 180, 187 & n.6 (Del. 1988); Ct. Ch. R. 12(b)(6).

conclusions of fact unsupported by allegations of specific facts . . . are accepted as true."[9] The court may also take judicial notice of the contents of the certificate of incorporation of a Delaware company where, as here, there is no dispute among the parties as to its actual contents (as opposed to the legal effect of those contents).[10]

III.

The defendants contend that a provision found in both the Dardanelle and the Southwest certificates of incorporation acts to sterilize director interest when approving self-dealing transactions. In other words, according to the defendants, by virtue of this provision, directors are by definition disinterested for the purpose of business judgment rule analysis, even with regard to transactions in which they would otherwise be thought to have an interest. Because, the defendants argue, the plaintiff has put forth no basis, other than director interest, for rebutting the business judgment rule, the plaintiff's breach of fiduciary duty claims must be dismissed. The defendants' argument hinges on two questions. First, does the provision mean what the defendants claim it means? Second, is such a provision enforceable?

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[9] *Id.*
[10] *See In re Wheelabrator Techs. Inc. S'holders Litig.*, 1992 WL 212595, at *11-12 (Del. Ch.); D.R.E. 201.

The provision the defendants rely upon is identical in both certificates of incorporation. It reads in pertinent part:

> Any director individually . . . may be a party to or may be pecuniarily or otherwise interested in any contract or transaction of the corporation, provided that the fact that he . . . is so interested shall be disclosed or shall have been known to the board of directors, or a majority thereof; and any director of the corporation, who is . . . so interested, may be counted in determining the existence of a quorum at any meeting of the board of directors of the corporation which shall authorize such contract or transaction, and may vote thereat to authorize any such contract or transaction, with like force and effect, as if he were not . . . so interested.[11]

Provisions such as the one at issue were quite common in Delaware corporate charters prior to the 1967 revision to the Delaware General Corporation Law (the "DGCL"), in order to ameliorate the otherwise harsh effect of the common law that self-interested transactions would always be void as a result of the disability of interested directors to participate in a quorum. The Delaware

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[11] Dardanelle Cert. of Incorp. Art. X (Defs.' Op. Br. Ex. A); Southwest Cert. of Incorp. Art. XI (Defs.' Op. Br. Ex. B). The complete provision reads:

> No contract or other transaction between the corporation and any other corporation, and no act of the corporation shall in any way be affected or invalidated by the fact that any of the directors of the corporation are pecuniarily or otherwise interested in or are directors or officers of such other corporation. Any director individually, or any firm of which such director may be a member, may be a party to or may be pecuniarily or otherwise interested in any contract or transaction of the corporation, provided that the fact that he or such firm is so interested shall be disclosed or shall have been known to the board of directors, or a majority thereof; and any director of the corporation, who is also a director or officer of such other corporation, or is so interested, may be counted in determining the existence of a quorum at any meeting of the board of directors of the corporation which shall authorize such contract or transaction, and may vote thereat to authorize any such contract or transaction, with like force and effect, as if he were not such director or officer of such corporation or not so interested.

Supreme Court, in a representative decision considering the meaning and effect of a nearly identical provision, stated at the time:

> We see no reason to hold that stockholders may not agree that interested directors may be counted toward a quorum. Such a provision does no more than to permit the directors to act as a board, leaving untouched questions of alleged unfairness or inequity that it is the duty of the courts in a proper case to resolve.[12]

The court sees no reason to disagree with those courts which interpreted the identical provision at a time when such a provision was common.[13] The court thus holds in accordance with *Sterling* that the provision at issue simply deals with issues of quorum, and does nothing to sanitize disloyal transactions.

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[12] *Sterling v. Mayflower Hotel Corp.*, 93 A.2d 107, 118 (Del. 1952); *see also Gottlieb v. McKee*, 107 A.2d 240, 242-43 (Del. Ch. 1954); *Martin Found., Inc. v. N. Am. Rayon Corp.*, 68 A.2d 313, 314-16 (Del. Ch. 1949) (Seitz, V.C.); *Pappas v. Moss*, 393 F.2d 865, 867 (3d Cir. 1968) (Seitz, J.).

[13] Notably, before the law related to Section 144 of the DGCL finally settled, *see, e.g., Benihana of Tokyo, Inc. v. Benihana, Inc.*, 906 A.2d 114, 120 (Del. 2006) (providing that interested director transactions approved pursuant to the 144(a)(1) safe harbor are reviewed under the business judgment rule), it was frequently suggested that Section 144, in the same vein as the provision at issue, did no more than to remove a director's disability to participate in a quorum to vote on an interested transaction, but did nothing to sanitize such a transaction if it was inherently unfair. *See, e.g.*, *Flieger v. Lawrence*, 361 A.2d 218, 222 (Del. 1976) ("[Section 144] merely removes an 'interested director' cloud when its terms are met and provides against invalidation of an agreement 'solely' because such a director or officer is involved. Nothing in the statute sanctions unfairness . . . or removes the transaction from judicial scrutiny."); *HMG/Courtland Props., Inc. v. Gray,* 749 A.2d 94, 114 n.24 (Del. Ch. 1999) ("Satisfaction of §§ 144(a)(1) or (a)(2) simply protects against invalidation of the transaction 'solely' because it is an interested one."); *Cooke v. Oolie*, 1997 WL 367034, at *8 (Del. Ch.) ("It is now clear that even if a board's action falls within the safe harbor of section 144, the board is not entitled to receive the protection of the business judgment rule.").

However, if, *arguendo*, the meaning of the provision is as the defendants suggest, interested directors would be treated as disinterested for the purposes of approving corporate transactions. Because approval by a majority of disinterested directors affords a transaction the presumptions of the business judgment rule,[14] all interested transactions would be immunized from entire fairness analysis under this scheme. Thus, the only basis that would remain to attack a self-dealing transaction would be waste.

The question that remains then is whether such a far-reaching provision would be enforceable under Delaware law. It would not. If the meaning of the above provision were as the defendants suggest, it would effectively eviscerate the duty of loyalty for corporate directors as it is generally understood under Delaware law. While such a provision is permissible under the Delaware Limited Liability Company Act and the Delaware Revised Uniform Limited Partnership Act, where freedom of contract is the guiding and overriding principle, it is expressly forbidden by the DGCL. Section 102(b)(7) of the DGCL provides that a corporate charter may contain a provision eliminating or limiting personal liability of a director for money damages in a suit for breach of fiduciary duty, so long as such

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[14] *See, e.g.*, *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

provision does not affect director liability for "any breach of the director's duty of loyalty to the corporation or its stockholders . . . ."

The effect of the provision at issue would be to do exactly what is forbidden. It would render any breach of the duty of loyalty relating to a self-dealing transaction beyond the reach of a court to remedy by way of damages. The exculpatory charter provision, if construed in the manner suggested by the defendants, would therefore be void as "contrary to the laws of this State"[15] and against public policy. As such, it could not form the basis for a dismissal of claims of self-dealing.

Thus, the charter provision, under either interpretation, provides no protection for the defendants beyond that afforded by Sections 144 of the DGCL. Because none of the safe-harbor provisions of Section 144(a)(1) or (a)(2) apply, the challenged interested transactions are not insulated on grounds of unfairness.[16]

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[15] *See* 8 *Del. C.* § 102(b)(1).

[16] The defendants argue that claims relating to personal expenses and loans from Perry, Todd, and entities affiliated with them must be dismissed because the plaintiff has failed to allege facts suggesting unfairness. As the plaintiff points out, however, the corporations produced no documents in the 220 action substantiating the terms of the loans, that the loans were actually made, or that personal expenses charged to the companies were actually reimbursed by the individual defendants. Given the cloud of self-dealing that hangs over these transactions, and the potential for the defendants to use the transactions as a means to receive non-pro rata distributions from the corporation, the motion to dismiss stage of these proceedings is an inappropriate time to consider the merits of these claims given the entire fairness standard which must be applied. The same is true for the claims of corporate waste. Although this court has, in the fairly recent past, questioned the wisdom of allowing stockholders to bring claims for waste with respect to transactions which were approved by a majority of disinterested stockholders, *see Harbor Fin. Partners v. Huizenga*, 751 A.2d 879, 901-02 (Del. Ch. 1999), that is not the

IV.

The defendants contend that the plaintiff is in any event time-barred with respect to many of the allegedly disloyal or wasteful actions complained of. Specifically, the defendants argue that all claims arising out of transactions occurring prior to September 6, 2003 are barred by the three-year statute of limitations on fiduciary duty claims.

Strictly speaking, statutes of limitation do not bind courts of equity with respect to purely equitable claims.[17] Nevertheless, in determining whether a plaintiff's claims should be barred by laches, great weight is placed on analogous statutes of limitation.[18] For actions at law to "recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant," a three-year statute of limitations applies.[19] It is well-settled law that this same three-

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situation presently before this court. The plaintiff has made at least a colorable argument that certain amounts expended by the corporation cannot be explained as an exercise in reasoned business judgment. Ultimately however, the determination of that question will be highly fact intensive. It is for that reason the court finds the prevailing precedent persuasive that claims of waste are seldom subject to disposition without trial. *See, e.g.*, *Michelson v. Duncan,* 407 A.2d 211, 223 (Del. 1979).

[17] DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 11.05[c], at 11-60 (2008) (citing *Adams v. Jankouskas*, 452 A.2d 148, 157 (Del. 1982)).

[18] *Id.*

[19] 10 *Del. C.* § 8106.

year statute of limitations applies to stockholder derivative suits which seek recovery of damages.[20]

"Under Delaware law, a plaintiff's cause of action accrues at the moment of the wrongful act, not when the harmful effects are felt, even if the plaintiff was unaware of the wrongful act."[21] The applicable three-year statute of limitations was tolled, however, during the pendency of the plaintiff's Section 220 action.[22] The final opinion in the 220 action was entered on May 16, 2006, and the plaintiff filed her complaint on September 6, 2006, less than 120 days later. Given the time between the entry of the opinion and the actual production of the demanded books and records, and affording the plaintiff time to evaluate any potential claims in light of what was produced, the short window between the closing of the 220 action and the filing of the original complaint in this action is reasonable, and the statute is likewise tolled during that period. The plaintiff's claims are therefore time-barred as to any transactions occurring more than three years prior to the date the 220 action was instituted, *i.e.,* prior to August 31, 2001.

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[20] *See, e.g.*, *Halpern v. Barran*, 313 A.2d 139, 141 (Del. Ch. 1973) (citing *Bokat v. Getty Oil Co.*, 262 A.2d 246 (Del. 1970)).

[21] 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 13.10, at 13-20 (3d ed. 2009) (citing *In re Coca-Cola Enters., Inc. S'holders Litig.*, 2007 WL 3122370, at *5 (Del. Ch.)).

[22] *See Technicorp Int'l II, Inc. v. Johnston*, 2000 WL 713750, at *9 (Del. Ch.) (citing *Cahall v. Burbage*, 119 A. 574, 576-77 (Del. Ch. 1922) ("It is settled Delaware law that the institution of other litigation to ascertain the facts involved in the later suit will toll the statute [of limitations] while that litigation proceeds.").

V.

For the reasons set forth herein, the defendants' motion to dismiss is GRANTED IN PART, and all claims arising out of actions occurring prior to August 31, 2001 are DISMISSED WITH PREJUDICE. In all other respects the defendants' motion is DENIED. IT IS SO ORDERED.