

Client Alert

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Delaware Supreme Court Holds that Collateral Estoppel Applies to Dismissal on Demand-Futility Grounds

The past several years have seen a significant rise in the filing of derivative lawsuits in multiple jurisdictions against the same defendants for the same alleged wrongdoing. These duplicative actions can result in a substantial increase in costs of defense and risk. A decision released yesterday by the Delaware Supreme Court, *Pyott v. Louisiana Municipal Police Employees Retirement System*, offers the hope of some relief from this trend through application of the doctrine of collateral estoppel—at least for defendants who are successful at the early demand-futility stage of the litigation.

In *Pyott*, shareholders of Allergan, Inc., filed substantially identical shareholder derivative complaints in the Delaware Chancery Court and in the U.S. District Court for the Central District of California. The complaints alleged that the Allergan board breached its duty of loyalty by allowing the company to engage in unlawful off-label marketing, thereby subjecting the company to a misdemeanor conviction and \$600 million in fines. The California federal court dismissed the case with prejudice on the ground that the complaint failed to plead facts sufficient to excuse a pre-suit demand on the board of directors. Allergan and its directors then sought dismissal of the Delaware case on collateral-estoppel grounds, as well as for failing to plead demand futility. The Delaware vice chancellor denied the motion, holding that collateral estoppel did not apply because the Delaware and California plaintiffs were not in privity with each other, and because the California plaintiffs were inadequate, as shown by their lawyers rushing to file their lawsuit before inspecting the company's books and records under Delaware's inspection statutes. The Chancery Court then found that plaintiffs had adequately pleaded demand futility, permitting the case to go forward even though the California federal court had rejected it.

The Delaware Supreme Court reversed. It explained that the doctrine of full faith and credit required the Chancery Court to give the California judgment the same force and effect that it would be given under California law. It found that California courts would have held that the Delaware and California plaintiffs were in privity, because both sought to represent the same company in asserting the same claims. And it concluded that the vice chancellor had no factual basis for concluding that the California federal court plaintiffs were inadequate representatives simply because they filed their complaint before inspecting the corporation's books and records. For these reasons, the Delaware Supreme Court found that the Chancery Court should have dismissed on collateral-estoppel grounds.

To view the Court's decision, click [here](#).

Morrison & Foerster filed an amicus brief on behalf of the United States Chamber of Commerce in the Delaware Supreme Court in support of Allergan.

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