



Court of Chancery Upholds Customary Release in Spin-Off Transactions

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The Delaware Court of Chancery last week validated a release of liability that extinguished certain claims a recently spun-off company may have had against its former parent and its directors. [In re AbbVie Inc. Stockholder Derivative Litig., C.A. No. 9983-VCG \(Del. Ch. July 21, 2015\)](#). The decision confirms that the mutual releases customary in spin-off arrangements are presumptively appropriate and enforceable.

Abbott Laboratories spun off AbbVie, its research-based pharmaceutical subsidiary, in January 2013. Before the spin, Abbott was a defendant in a False Claims Act action alleging unlawful off-label marketing of an AbbVie product. As part of the spin-off, AbbVie broadly released all claims it might have against Abbott or any Abbott affiliate relating to assets transferred to AbbVie, including liability for the False Claims Act claim.

Stockholders of the newly independent AbbVie alleged that Abbott's directors had engaged in improper self-dealing by approving the release, because the release barred AbbVie from seeking recovery from Abbott and its directors for liability arising from the False Claims Act claim. Suing derivatively on AbbVie's behalf, the plaintiffs sought an order rescinding the release and allowing AbbVie to sue Abbott's directors for alleged misconduct in permitting the off-label marketing.

But the plaintiffs did not own AbbVie stock at the time of the alleged wrong—only Abbott did, because AbbVie was Abbott's wholly owned subsidiary at the time the release was executed. As the Court of Chancery recognized, this fact doomed the plaintiffs' lawsuit under Delaware's "continuous ownership" rule, which limits standing to bring derivative claims to stockholders who owned shares at the time of alleged wrong and at all times thereafter. Vice Chancellor Glasscock refused to exempt the plaintiffs from the continuous ownership requirement, holding that exceptions to the rule will be recognized only in "egregious" circumstances. This strict test is appropriate, the Court held, because "derivative litigation is burdensome to companies, by way of the direct costs of the litigation, including advancement and indemnification obligations, as well as indirect costs, such as distraction to management and the board and possible detriment to employee morale." The Court found nothing in the customary release of claims provided in the AbbVie spin-off to justify an exception from the general rule and that, to the contrary, such mutual

releases benefit both the parent and the spun-off subsidiary by ensuring “their full legal separation, free of entanglement.”

We expect further development in the law governing spin-offs as spin-off activity accelerates in the marketplace. The *AbbVie* ruling recognizes the “value [of] a clean break between the new entity and the old” in the context of such transactions and confirms that directors and their advisors can rely on the consistent application of settled law in spin-off related litigation.