Message from the Chair

Our Committee has had an active year. This is our second newsletter summarizing developments in the law, highlighting tips and trends for practitioners and keeping members up to date on Committee activities. At our spring meeting, we had a robust discussion of how the increasing criminalization of certain activities poses risks for directors and officers and raises potential conflicts between the interests of a company and the interests of D's and O's. During our Committee meeting on August 10 from 10-11:00 a.m. in the Empire Room of the Fairmont Hotel, Jim Wing, chair of our insurance sub-committee, will lead a discussion to explain to inside counsel and outside practitioners the context in which this issue arises, how recent cases have addressed the issue and the current state of D&O insurance as it relates to this issue. We will also receive Committee reports from Bill Johnston concerning the advancement and indemnification sub-committee, from Frances Goins concerning the developments sub-committee, from Matt Boos and John Grossbauer concerning the anticipated publication date of our model indemnification agreement and from Dan Formeller concerning the implications of the new JOBS Act for director and officer liability, and a brief update on the Committee's efforts to combat human trafficking, which our own Bill Johnston co-chairs.

I look forward to seeing you in San Francisco. If you are unable to attend in person the dial-in information is as follows:

Toll-free dial-in number (U.S. and Canada):
(866) 646-6488

International dial-in number:
(707) 287-9583

Conference code:
1145265056

Lewis H. Lazarus
Morris James LLP
Chair, Directors and Officers Liability Committee
ABA Business Law Section
reversing the Court of Chancery decision of last June. Click here for a complete copy of the Supreme Court's opinion.

The Delaware Supreme Court found that the Court of Chancery erred in failing to give preclusive effect to a final California federal court judgment dismissing with prejudice a derivative action on behalf of a Delaware company on demand futility grounds. Applying principles of judicial comity and the Full Faith and Credit Clause, the Supreme Court held: "[A] state court is required to give a federal judgment the same force and effect as it would be given under the preclusion rules of the state in which the federal court is sitting [in this case, California]. Accordingly, federal common law imposes on the state of Delaware a full-faith-and-credit requirement to give the California Federal judgment the same force and effect as it would be entitled to in the California federal or state courts under California's preclusion rules."

Applying this premise, the Supreme Court found that the Court of Chancery had mistakenly "conflated collateral estoppel with demand futility." Although Delaware demand futility law governed that issue for a Delaware company wherever it was sued, the Supreme Court found that "[o]nce a court of competent jurisdiction has issued a final judgment . . . a successive case is governed by the principles of collateral estoppel, under the full faith and credit doctrine, and not by demand futility, under the internal affairs doctrine." The Supreme Court also rejected what it called an "irrebuttable presumption" imposed by the Court of Chancery that a derivative plaintiff who failed to conduct a Section 220 books and records review prior to filing suit was an inadequate representative of the company. However, in the circumstances of this case where the Supreme Court held that California law governed the preclusive effect of the judgment, it declined to review the Court of Chancery's analysis of the issue of the California plaintiff's privity status with the company.

In another approach to the issue of multi-forum litigation and Delaware's ability to exercise judicial control over its companies, Chevron Corp. and FedEx Corp. argued in the Delaware Court of Chancery, in two separate but related lawsuits, against stockholder-plaintiffs' challenges to the validity of the companies' "forum selection" bylaws. These bylaws generally provided that derivative claims, fiduciary duty claims and other claims under the Delaware General Corporation Law or subject to the internal affairs doctrine must be litigated in the Court of Chancery. (At least 9 companies that had enacted such bylaws revoked them in the face of similar litigation.) On June 25, 2013, the Delaware Court of Chancery upheld these "forum selection" bylaws. For a complete copy of the opinion, please click here.

Mt. Hawley Insurance Company v. Lopez

This California appellate court decision provides an instructive analysis of some of the public policy arguments supporting advancement of defense costs when a director or officer is facing criminal prosecution. Click here for a complete copy of the opinion. The decision arose as a result of an insurer's denial of coverage for defense costs based on a California statute, California Insurance Code 533.5(b), which states: "No policy of insurance shall provide, or be construed to provide, any duty to defend" in certain situations. The insured claimed the statute applied only to civil and criminal claims seeking recovery of a fine, penalty or restitution under certain specific California statutes addressed to unfair competition and unfair advertising, brought by one of four specific state agencies. The insured was charged by federal prosecutors with criminal violations of federal statutes. The insurer argued, and the trial court held, that Section 533.5(b) barred insurers from covering defense costs in any criminal action.

The Mt. Hawley decision reversed the trial court, and held that Section 533.5(b) was limited in scope to proceedings brought by one of the named state agencies under the specifically identified state statutes, and did not bar the advancement of defense costs in a criminal proceeding brought by a federal prosecutor. The appellate court relied on the legislative history of Section 533.5(b) and on other California statutes, which authorize insurance that "provides a defense to individual defendants in various kinds of proceedings, including criminal proceedings." For a corporation, advancement of defense costs is allowed assuming the person to be
advanced "acted in good faith and in a manner the person reasonably believed to be in the best interests of the corporation" and, in a criminal case, where the person "had no reasonable cause to believe the conduct of the person was unlawful." See, e.g., Cal. Corp. Code 317(b) & (c). The appellate court also supported the concept that "[a]llowing insurers to provide for defense costs in criminal cases against corporate agents enhances the ability of for-profit and non-profit organizations to attract directors [and officers] who otherwise might hesitate or decline to serve because of fear of lawsuits and criminal prosecutions," and held that advancement was "consistent with the principle that insureds charged with crimes begin with a presumption of innocence." For this purpose, the court differentiated between indemnification and defense, and noted that "there is no public policy in California against insurers contracting to provide a defense to insureds facing criminal charges, as opposed to indemnification for those convicted of criminal charges."

The opinion does not, however, address the issue that this Committee has been discussing: whether advancement may be required when the person seeking advancement from either the corporation or an insurer asserts the Fifth Amendment privilege (or the work product privilege) in response to inquiries by the corporation or the insurer. But the opinion does reiterate that Section 533.5 does not preclude an insurer providing a defense of a federal criminal proceeding, especially where, notably, the Mt. Hawley policy at issue defined "Claim" to include certain types of criminal proceedings, including an indictment.

**Salinas v. Texas**

The U.S. Supreme Court reached a decision in the matter of Salinas v. Texas, which arose out of the criminal prosecution of a defendant, who, when voluntarily responding to a police officer's questions about a murder, became suddenly silent when asked whether ballistics testing would match his shotgun to shell casings found at the scene of the crime. For a copy of the opinion, please click [here](http://www.corporatecomplianceinsights.com/how-to-handle-corporate-internal-investigations/). The defendant was charged, and in a closing statement at trial, the prosecutor commented on the defendant's sudden silence as an indication of guilt. The defendant claimed that this use of his silence violated the Fifth Amendment, while the government relied on his failure to "invoke" his Fifth Amendment rights. The Court found that defendant's challenge to his conviction on Fifth Amendment grounds failed because he did not expressly invoke the privilege.

While the context of Salinas does not lend itself to garden-variety director and officer liability matters, the opinion's arguable expansion of prosecutorial rights and its limitation of the Fifth Amendment privilege in situations where the subject of questioning is not in custody may have far-reaching implications for directors and officers responding to internal corporate investigations.

In the words of one commentator, "Although no one wants to formally admit it, in the typical internal investigation the company lawyers are basically highly-paid deputy prosecutors with the badge hidden under their suits." See [http://www.corporatecomplianceinsights.com/how-to-handle-corporate-internal-investigations/](http://www.corporatecomplianceinsights.com/how-to-handle-corporate-internal-investigations/). The issue has arisen in recent years in cases where the Department of Justice has charged corporate executives with obstruction of justice based on lies told during corporate internal investigations being conducted by outside law firms. The DOJ relies on the reasoning that the investigating lawyers frequently pass on the false information received from company employees in reports to federal agencies such as the U.S. Attorney's Office. See, e.g., U.S. v. Singleton, 2006 WL 1984467 (S.D. Tex. July 14, 2006).

The **Salinas** opinion notes that a witness's failure to invoke the Fifth Amendment privilege is excused in certain circumstances including: "where governmental coercion makes its forfeiture of the privilege involuntary," and "where threats to withdraw a governmental benefit such as public employment sometimes make exercise of the privilege so costly that it need not be affirmatively asserted." These exceptions mirror the situation faced by a corporate executive or employee who refuses to be interviewed. Such an individual does so only at risk of losing his job since, as a practical matter, any individual who refuses to cooperate with a company's internal
investigation will likely be terminated. *Cf., Garrity v. New Jersey,* 385 U.S. 493, 497 (1967) (no explicit assertion of the Fifth Amendment required during an investigation where such assertion would, by law, have cost police officers their jobs).

The implications for directors and officers are twofold. First, officers and directors who are formally interviewed in an internal investigation should be cautious about participating in interviews, particularly after they receive an Upjohn Warning, without the advice of counsel. Whether the corporation or an insurance company will pay such counsel may be problematic, particularly in jurisdictions where directors must waive their Fifth Amendment rights and assert innocence of breach of fiduciary duty as a condition to obtaining advancement. *Salinas* moves the problem up earlier in time, before there is a formal investigation and before any Upjohn Warning, a circumstance made even more challenging because today virtually no advancement bylaw or insurance policy on the market covers the *Salinas* facts. At a minimum directors and their counsel should consider the implications of *Salinas* in determining whether to participate in internal investigations. Second, from the perspective of an attorney conducting the investigation, *Salinas* may signal a need to consider more specific warnings to interviewees concerning their rights and risks.

**J.P. Morgan Securities, Inc. v. Vigilant Insurance Company**

In a recent decision reinstating a complaint on a motion to dismiss, the highest court of New York State recently held that insurers could not deny coverage for "restitution" damages where the policy was silent on that issue. In *J.P. Morgan Securities, Inc. v. Vigilant Insurance Co.*, No. 113, NYLJ 1202603747925 (Ct. of App. June 11, 2013), (a copy of the decision may be found at [http://www.newyorklawjournal.com/CaseDecisionFriendlyNY.jsp?id=1202603747925](http://www.newyorklawjournal.com/CaseDecisionFriendlyNY.jsp?id=1202603747925)), the New York Court of Appeals refused to accept the insurers' argument that the New York "public policy rationale . . . to prevent the unjust enrichment of the insured by allowing it to, in effect, retain the ill-gotten gains by transferring the loss to its carrier" applied where most of the Bear Stearns' $160 million agreed settlement payment was calculated on the basis of profits allegedly received by Bear Stearns' hedge fund customers rather than Bear Stearns itself. The Court held the payment did not implicate that policy, despite being described in the settlement agreement as "disgorgement."

In defense of an SEC enforcement action and related private litigation, Bear Stearns had argued that it acted solely as a clearing firm in the challenged transactions, that it did not knowingly violate the law, and that it did not share in the profits or benefits of the allegedly improper trading by its customers. Nevertheless, to avoid being charged on a strict liability basis with violations of federal securities laws based on late trading and market timing allegations, Bear Stearns negotiated a settlement with the Securities and Exchange Commission ("SEC") and the private plaintiffs that included a $90 million penalty and a $160 million "disgorgement" payment. Bear Stearns did not seek coverage for the penalty payment from the insurers.

The insurers cited two public policy reasons to justify denying coverage. First, they argued that "Bear Stearns enabled its customers to make millions through its trading tactics;" and second, they argued "that there is a separately applicable public policy category that prohibits insurance coverage for intentionally-caused harm." The Court applied a strict motion to dismiss standard of review, insisting that the insurers "must establish that the documentary evidence 'conclusively refutes' [Bear Stearns'] allegations."

Noting that "insurance contracts, like other agreements, will ordinarily be enforced as written," the Court found there was no evidence to support the insurers' first argument. Further, as to the second argument, the Court held that the language of the contract and the SEC cease and desist order did not support the insurer's position. There was neither a specific policy exclusion nor a recognized public policy excluding payment for loss incurred by the insured which had not been established to be the return of the insured's own ill-gotten gains, regardless of whether such payment was labeled as "disgorgement" in the SEC order.

Despite some discussion of whether or not a payment like Bear Stearns' qualified as a "loss" under the policies, the Court noted that the insurers did
not "earnestly dispute" this issue, and as a result did not reach it. Thus, it remains in play for future litigation. And, since this decision was reached on a preliminary motion to dismiss, it does not foreclose the possibility that development of a factual record could yield a different result down the line.

The JOBS Act - Implications for Director and Officer Liability

By Daniel R. Formeller, Tressler LLP

On April 5, 2012 the Jumpstart Our Business Startups Act (JOBS Act) (Public Law 112-106) became effective. There is much debate about whether companies wishing to take advantage of the provisions of this Act are taking on increased risk and whether current available forms of D&O insurance will cover potential resulting claims.

The Act includes three fundamental changes to laws and regulations affecting how emerging companies can raise capital. These changes will become effective when final SEC implementing regulations are authorized.

- Emerging Growth Companies (EGC) - companies with annual revenues of less than $1 billion in their most recent fiscal year - will have significant flexibility in determining the appetite of potential investors for their initial public offerings before they disclose their finances and other management information to the general public.
- Certain limitations concerning how and to whom private companies can market their private Rule 144A securities offerings will be either relaxed or removed completely.
- "Crowdfunding" will be authorized so that raising up to $1 million in capital over a 12-month period from numerous small investors will be not only permitted but encouraged.

Under the Act, EGCs can file a registration statement with the SEC on a completely confidential basis to determine any regulatory or financial issues up to 21 days prior to making the registration documents available to the general public for scrutiny. EGCs can also gauge institutional investor interest in their company prior to a planned IPO through published research by investment banks. Finally, there is a reduction in disclosure requirements for up to five years as long as the company remains an EGC. Most significantly, there is no requirement for an auditor attestation report on internal controls. In addition, the EGC is exempt from certain executive compensation disclosures.

The stated purpose of the Act is to make it easier and less expensive for private companies to go public and raise capital. What are the implications for director and officer liability and protection of directors and officers through D&O insurance?

- Will there be insurance coverage that will respond to claims arising from the new, limited SEC disclosure and broadened publicity allowed by the Act?
- Does the 21-day public disclosure period give EGCs sufficient time to negotiate and procure public D&O coverage to adequately protect directors and officers transitioning from a private company environment?
- Will the underwriting standards for D&O insurance change materially in response to limited access to the filed S-1? Will additional warranty statements be required or necessary?
- How will the pricing of public company D&O policies respond to the narrowed public disclosure requirements for EGCs?

The Act also significantly changes two sections of Rule 144A of the Securities Act of 1933.

- Private companies can now engage in general solicitation and general advertising in the offer and sale of their securities in the private market. Do the new SEC Rules on this issue mean that EGCs will be able to employ investor seminars, dedicated websites and/or social networks to attract the "crowd"?
- The threshold for private company registration with the SEC for the sale of securities has changed from 500 shareholders or $1 million to...
2000 shareholders or $10 million as long as there are no more than 499 non-accredited investor shareholders. The listing company must use "reasonable steps" to determine qualified investor status.

There are a number of issues related to these changes that impact D&O insurance. Private companies using these new private offering mechanisms will need to analyze the specific language of any desired policy to determine if Rule 144 activities are covered or if there are limitations that exclude such activities.

Title III of the JOBS Act amends the Securities Exchange Act of 1934 for Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure (CROWDFUNDING). These provisions will, when fully implemented, allow a private company to use a web portal that has been registered with the SEC to raise up to $1 million in any 12-month period. Although this may appear to open a new major capital market to entrepreneurs, Section 302(c) of the Act imposes express liability on issuers and their officers and directors for material misrepresentations and omissions made in connection with any crowdfunding offering.

The following inquiries about this funding mechanism as related to the standard D&O insurance policy provisions seem germane:

- Is the "Loss" definition in the policy broad enough to cover liability under Section 302(c)?
- Is the policy's exclusion language regarding public offerings (and road shows) a concern when Crowdfunding is used?

There are a few parts of the Act that are self-effectuating, but a majority of the Act's provisions will require substantial SEC rulemaking before they become effective. The first set of final regulations dealing with lifting the ban on general solicitations and advertising by private funds in the sale of securities and certain "bad boy" provisions denying the benefit of the new exclusions to persons found to have committed securities fraud were issued by the SEC on July 10, 2013, and will become effective in mid-September 2013, 60 days after publication in the Federal Register.
IN THE SUPREME COURT OF THE STATE OF DELAWARE

DAVID PYOTT, HERBERT W. §§
BOYER, LOUIS J. LAVIGNE, §§
GAVIN S. HERBERT, STEPHEN §§
J. RYAN, LEONARD D. §§
SCHAEFFER, MICHAEL R. §§
GALLAGHER, ROBERT §§
ALEXANDER INGRAM, TREVOR §§
M. JONES, DAWN E. HUDSON, §§
RUSSELL T. RAY, DEBORAH §§
DUNSIRE, and ALLERGAN, INC., §§

Defendants Below, §§
Appellants, §§

v. §§

LOUISIANA MUNICIPAL POLICE §§
EMPLOYEES’ RETIREMENT §§
SYSTEM and U.F.C.W. LOCAL §§
1776 & PARTICIPATING §§
EMPLOYERS PENSION FUND, §§

Plaintiffs Below, §§
Appellees. §§

No. 380, 2012

Court Below:

Court of Chancery of the State of Delaware

C.A. No. 5795

Submitted: February 5, 2013
Decided: April 4, 2013

Before STEELE, Chief Justice, HOLLAND, BERGER, JACOBS and RIDGELY, Justices, constituting the Court en Banc.

Upon appeal from the Court of Chancery. REVERSED.

Of Counsel: Wayne W. Smith, Esquire, Jeffrey H. Reeves, Esquire, Kristopher P. Diulio, Esquire, Gibson, Dunn & Crutcher LLP, Irvine, California and Mark A. Perry, Esquire (argued) and Geoffrey C. Weien, Esquire, Gibson, Dunn & Crutcher LLP, Washington, D.C.

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Danielle Gibbs, Esquire and Nicholas J. Rohrer, Esquire, Young Conaway Stargatt & Taylor, LLP, Wilmington, Delaware for Amicus Curiae Chamber of Commerce of the United States of America.


BERGER, Justice:
In this appeal we consider whether the Court of Chancery was required to dismiss a Delaware derivative complaint after a California federal court entered a final judgment dismissing essentially the same complaint brought by different stockholders. The trial court held that it was not required to give preclusive effect to the California judgment for two reasons. First, the Court of Chancery held, as a matter of Delaware law, that the stockholder plaintiffs in the two jurisdictions are not in privity with each other. Second, the trial court found that the California stockholders were not adequate representatives of the defendant corporation. The Court of Chancery erred in both respects. Under California law, which controls on this issue, derivative stockholders are in privity with each other because they act on behalf of the defendant corporation. As to adequacy of representation, the trial court adopted a presumption of inadequacy without any record to support the factual premise on which the presumption was based. Accordingly, the judgment of the Court of Chancery is reversed.

**Factual and Procedural Background**

Allergan, Inc. is a Delaware corporation that develops and markets specialty pharmaceuticals. One such product is BOTOX, a prescription neurotoxin that has been approved by the U.S. Food and Drug Administration (FDA) for several therapeutic and cosmetic uses. The medical community routinely prescribes BOTOX for therapeutic uses that have not been FDA approved (off-label uses). That practice
is well known, and not illegal. It is unlawful, however, for Allergan to market BOTOX for off-label uses.

In 2007, the Department of Justice began an investigation into Allergan’s allegedly improper marketing of BOTOX. On September 1, 2010, Allergan announced that it pled guilty to the criminal misdemeanor of misbranding, and that it agreed to pay a total of $600 million in civil and criminal fines. Several Allergan stockholders responded to the news by filing derivative suits. The Louisiana Municipal Police Employees’ Retirement System (LAMPERS) filed this action on September 3rd, and other stockholders filed actions in the United States District Court for the Central District of California during the next three weeks. The California actions were consolidated on October 24, 2010.

Allergan and its directors (collectively Allergan) moved to dismiss both actions for failure to plead demand futility under Rule 23.1. The Court of Chancery postponed briefing to allow another stockholder, U.F.C.W. Local 1776 & Participating Employers Pension Fund (UFCW), to inspect books and records relating to Allergan's allegedly wrongful Botox activities. After obtaining the books and records, UFCW intervened in this action. In July 2011, appellees and the California plaintiffs filed essentially the same amended complaint in their respective courts.

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1 In the California federal action, the motion was based on Fed. R. Civ. P. 23.1. In the Delaware action, the motion was based on Ch. Ct. R. 23.1. The two rules are substantially the same.
Allergan again moved to dismiss, and the parties concluded briefing in the fall. In January 2012, shortly before the motion was to be argued in the Court of Chancery, the California Federal Court issued an order dismissing the California action with prejudice. The parties to this action then filed supplemental briefs addressing the preclusive effect of the California Judgment. The Court of Chancery held that the California Judgment did not bar the Delaware action, and denied appellants’ motion to dismiss. This interlocutory appeal followed.

Discussion

Collateral Estoppel Applies

The Court of Chancery recognized that it was required to “give a judgment [from another jurisdiction] the same force and effect that it would be given by the rendering court.” The rationale for that determination originates from the United States Constitution’s Full Faith and Credit Clause and the Full Faith and Credit Act (FFCA). The FFCA “has long been understood to encompass the doctrines of res

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2 The California Federal Court denied the stockholder plaintiffs’ motion for reconsideration, and the matter is now under consideration by the Ninth Circuit Court of Appeals. If the appellate court reverses, appellants will be able to file a motion for relief from the judgment under Ch. Ct. Rule 60(b).


4 “Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State.” U.S. Const., Art. IV § 1.

judicata, or ‘claim preclusion,’ and collateral estoppel, or ‘issue preclusion.’”

The Full Faith and Credit Clause does not explicitly apply when the “rendering court” is a federal court rather than a state court. Nonetheless, the United States Supreme Court has held that a state court is required to give a federal judgment the same force and effect as it would be given under the preclusion rules of the state in which the federal court is sitting. In this case, that state is California. Accordingly, federal common law imposes on the state of Delaware a full-faith-and-credit requirement to give the California Federal Judgment the same force and effect as it would be entitled to in the California federal or state courts under California’s preclusion rules. Delaware law, likewise, requires our courts to afford the same respect to federal court judgments that the Full Faith and Credit Clause requires them to afford to judgments from other states.

The Court of Chancery failed to apply this settled law because it conflated collateral estoppel with demand futility. It began its analysis with a mistaken premise, stating that: “[w]hether a stockholder in a Delaware corporation can sue

8 Iowa-Wisconsin Bridge Co. v. Phoenix Finance Corp., 25 A.2d 383, 391 (Del. 1942) (holding that “[t]he same sanctity and effect is granted to a judgment of a federal court rendered in a like case and in similar circumstances, as is conceded to a judgment of a state court.”).
9 Id.
derivatively after another stockholder attempted to plead demand futility raises a question of demand futility law."\textsuperscript{10} Once a court of competent jurisdiction has issued a final judgment, however, a successive case is governed by the principles of collateral estoppel, under the full faith and credit doctrine, and not by demand futility law, under the internal affairs doctrine.

The Rule 23.1 motion in the California Federal Court implicated the internal affairs doctrine. The internal affairs doctrine required the California Federal Court to apply its understanding of Delaware law on the issue of demand futility. The California Federal Court held, as a matter of Delaware law, that demand was not futile and dismissed the derivative complaint. It then entered the final California Federal Judgment on the merits of demand futility.

In the Court of Chancery, the motion to dismiss, based on collateral estoppel, was about federalism, comity, and finality. It should have been addressed exclusively on that basis. Under this Court’s precedents, the undisputed interest that Delaware has in governing the internal affairs of its corporations must yield to the stronger national interests that all state and federal courts have in respecting each other’s judgments.\textsuperscript{11} The United States Supreme Court has held that the full faith and credit


obligation is "exacting" and that there is "no roving 'public policy exception' to the full faith and credit due judgments."\textsuperscript{12}

The Court of Chancery should have applied California law or federal common law to analyze all elements of collateral estoppel. If the Court of Chancery had done so, rather than invoking the internal affairs doctrine to apply Delaware law to the issues of privity and adequacy of representation, the decision in \textit{LeBoyer v. Greenspan}\textsuperscript{13} would have compelled it to dismiss the case.

Under California law, collateral estoppel precludes a subsequent action when the following five factors are satisfied:

First, the issue sought to be precluded . . . must be identical to that decided in a former proceeding. Second, the issue must have been actually litigated in the former proceeding. Third, it must have been necessarily decided in the former proceeding. Fourth, the decision in the former proceeding must be final and on the merits. Finally, the party against whom preclusion is sought must be the same as, or in privity with, the party to the former proceeding.\textsuperscript{14}

The dismissal of the California action for failure to adequately plead demand futility meets each requirement. The issue sought to be precluded is whether, under Rule 23.1, the failure to make demand on the Allergan board is excused because such a demand would have been futile. The California court addressed that exact question.

\textsuperscript{12} \textit{See}, \textit{e.g.}, \textit{Baker v. General Motors Corp.}, 522 U.S. 222, 232-33 (1998).

\textsuperscript{13} 2007 WL 4287646 (C.D. Cal.).

\textsuperscript{14} \textit{LeBoyer v. Greenspan}, 2007 WL 4287646 at *1 (C.D. Cal.) (Quotation and citation omitted.).
The issue was actually litigated in that the appellees had "notice, opportunity and incentive to litigate the issue at the prior proceeding."\textsuperscript{15} The California court entered a final judgment with prejudice, and that decision was on the merits.\textsuperscript{16} Finally, because the real plaintiff in a derivative suit is the corporation, "differing groups of shareholders who can potentially stand in the corporation's stead are in privity for the purposes of issue preclusion."\textsuperscript{17}

The trial court acknowledged that a California court would conclude that the California decision precludes appellees from pursuing the Delaware action. Indeed, the trial court noted that numerous other jurisdictions, and at least one Delaware decision, also hold that stockholders bringing derivative suits are in privity for purposes of collateral estoppel.\textsuperscript{18} But the trial court stated that because one's status as a derivative plaintiff falls within the internal affairs doctrine, derivative status must be decided as a matter of Delaware law. The court then opined that all the other jurisdictions finding privity for purposes of collateral estoppel missed the dual nature of a Delaware derivative action. According to the Court of Chancery, there is no

\textsuperscript{15} Id. at *2.

\textsuperscript{16} Id. at *3, citing Kaplan v. Peat, Marwick, Mitchell & Co., 540 A.2d 726, 730 (Del. 1988).

\textsuperscript{17} Ibid.

privity between derivative stockholders because, until a stockholder survives a motion to dismiss based on failure to make demand, the stockholder is not acting for the corporation. Rather, the stockholder is asserting an “individual claim to obtain equitable authority to sue.”19 Thus, a final judgment denying that individual claim has no preclusive effect on other stockholders’ derivative claims.

We will not address this analysis because, as discussed, the Court of Chancery should not have applied Delaware law in deciding whether the California Federal Court Judgment must be given preclusive effect. We note, however, as did the Court of Chancery, that numerous other jurisdictions have held that there is privity between derivative stockholders. Although the Court of Chancery is divided on the privity issue as a matter of Delaware law,20 we cannot address the merits of that issue in this case.

The adequacy of the California plaintiffs’ representation remains to be considered. If they were inadequate representatives, collateral estoppel will not bar a second, identical claim.21 The trial court held that the California plaintiffs were

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21 See, e.g., Restatement (Second) Judgments, § 42(1) (“A person is not bound by a judgment for or against a party who purports to represent him if . . . (e) [t]he representative failed to prosecute or defend the action with due diligence and reasonable prudence . . . .”); Career Educ., 2007 WL 2875203, at *10 (Del. Ch.); Sonus Networks, 499 F. 3d at 64; Prezant v. De Angelis, 636 A.2d 915, 924 (Del. 1994); see also Matsushita Elec. Indus. Co., Ltd. v. Epstein, 516 U.S. 367, 395-96 (1996) (Ginsburg, J., concurring in part, dissenting in part) (finding final judgments can be attacked
inadequate representatives. It found that, "[r]ather than representing the best interests of the corporation, the California plaintiffs sought to maximize the potential returns of the specialized law firms who filed suit on their behalf." In doing so, the Court of Chancery sua sponte announced and applied an irrebuttable presumption that derivative plaintiffs who file their complaints without seeking books and records, very shortly after the announcement of a "corporate trauma," are inadequate representatives.

Unlike the issue of privity, we address the inadequate representation issue because the Court of Chancery addressed it both as a matter of Delaware law and as a matter of California Law. We reject the "fast filer" irrebuttable presumption of inadequacy. Undoubtedly there will be cases where a fast filing stockholder also is an inadequate representative. But, there is no record support for the trial court's premise that stockholders who file quickly, without bringing a § 220 books and records action, are a priori acting on behalf of their law firms instead of the corporation. This Court understands the trial court's concerns about fast filers. But remedies for the problems they create should be directed at the lawyers, not the

collaterally on due process grounds for failure to satisfy the adequate representation requirement).


23 8 Del. C. § 220 provides that stockholders have the right to inspect corporate books and records for a proper purpose.
stockholder plaintiffs or their complaints.\textsuperscript{24}

Absent the presumption, there was no basis on which to conclude that the California plaintiffs were inadequate. The two complaints are so similar that the California complaint could not be "grossly deficient" when, according to the Court of Chancery, the Delaware complaint adequately states a claim for relief.\textsuperscript{25}

\textbf{Conclusion}

Based on the foregoing, the Court of Chancery’s judgment denying appellee’s motion to dismiss is reversed. Jurisdiction is not retained.


\textsuperscript{25} \textit{In re Sonus Networks, Inc. S’holder Deriv. Lit.}, 499 F.3d at 66.(Quoting \textit{Restatement (Second) Judgments}, § 42(1)(e) Comment f.)
IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

BOILERMAKERS LOCAL 154
RETIREMENT FUND and KEY WEST
POLICE & FIRE PENSION FUND,

Plaintiffs,

v.

CHEVRON CORPORATION, SAMUEL H.
ARMACOST, LINNET F. DEILY, ROBERT
E. DENHAM, ROBERT J. EATON, CHUCK
HAGEL, ENRIQUE HERNANDEZ, JR.,
FRANKLYN G. JENIFER, GEORGE L.
KIRKLAND, SAM NUNN, DONALD B.
RICE, KEVIN W. SHARER, CHARLES R.
SHOEMATE, JOHN G. STUMPF, RONALD
D. SUGAR, CARL WARE, and JOHN S.
WATSON,

Defendants.

ICLUB INVESTMENT PARTNERSHIP,

Plaintiff,

v.

FEDEX CORPORATION, JAMES L.
BARKSDALE, JOHN A. EDWARDSON,
J.R. HYDE, III, SHIRLEY A. JACKSON,
STEVEN R. LORANGER, GARY W.
LOVEMAN, SUSAN C. SCHWAB,
FREDERICK W. SMITH, JOSHUA I. SMITH,
DAVID P. STEINER, and PAUL S. WALSH,

Defendants.

OPINION
Date Submitted: April 12, 2013
Date Decided: June 25, 2013


STRINE, Chancellor.
I. Introduction

The board of Chevron, the oil and gas major, has adopted a bylaw providing that litigation relating to Chevron’s internal affairs should be conducted in Delaware, the state where Chevron is incorporated and whose substantive law Chevron’s stockholders know governs the corporation’s internal affairs. The board of the logistics company FedEx, which is also incorporated in Delaware and whose internal affairs are also therefore governed by Delaware law, has adopted a similar bylaw providing that the forum for litigation related to FedEx’s internal affairs should be the Delaware Court of Chancery. The boards of both companies have been empowered in their certificates of incorporation to adopt bylaws under 8 Del. C. § 109(a).¹

The plaintiffs, stockholders in Chevron and FedEx, have sued the boards for adopting these “forum selection bylaws.” The plaintiffs’ complaints are nearly identical and were filed only a few days apart by clients of the same law firm. In Count I, the plaintiffs claim that the bylaws are statutorily invalid because they are beyond the board’s authority under the Delaware General Corporation Law (“DGCL”). In Count IV, the plaintiffs allege that the bylaws are contractually invalid, and therefore cannot be enforced like other contractual forum selection clauses under the test adopted by the Supreme Court of the United States in The Bremen v. Zapata Offshore Co.,² because they were unilaterally adopted by the Chevron and FedEx boards using their power to make bylaws. The plaintiffs have attempted to prove their point by presenting to this court a

¹ 8 Del. C. § 109(a) (“[A]ny corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws upon the directors . . . .”).
number of hypothetical situations in which, they claim, the bylaws might operate inconsistently with law or unreasonably. The plaintiffs have also claimed that the boards of Chevron and FedEx breached their fiduciary duties in adopting the bylaws.

In this opinion, the court resolves the defendants’ motion for judgment on the pleadings on the counts relating to the statutory and contractual validity of the bylaws. Because the two bylaws are similar, present common legal issues, and are the target of near-identical complaints, the court decided to address them together. This is efficient, and is also in the interests of the parties, because a decision on the legal validity of the bylaws under the DGCL will moot the plaintiffs’ other challenges if the bylaws are found to be invalid. And, it also aids the administration of justice, because a foreign court that respects the internal affairs doctrine, as it must, when faced with a motion to enforce the bylaws will consider, as a first order issue, whether the bylaws are valid under the “chartering jurisdiction’s domestic law.” Furthermore, the plaintiffs’ facial statutory invalidity claim and their related contention that, as a matter of law, the bylaws are not

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3 See CTS Corp. v. Dynamics Corp., 481 U.S. 69, 90 (1987) (“[A] corporation—except in the rarest situations—is organized under, and governed by, the law of a single jurisdiction, traditionally the corporate law of the State of its incorporation.”); Edgar v. MITE Corp., 457 U.S. 624, 645 (1982) (“The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation’s internal affairs—matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders—because otherwise a corporation could be faced with conflicting demands.”) (citation omitted)); see also Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90, 92 (1991) (holding that in a derivative suit “the scope of the demand requirement embodies the incorporating State’s allocation of governing powers within the corporation”); Burks v. Lasker, 441 U.S. 471, 478 (1979) (“[T]he first place one must look to determine the powers of corporate directors is in the relevant State’s corporation law.”) (citations omitted)).

contractually enforceable, have cast a cloud over the defendants’ bylaws and those of other corporations. A decision as to the basic legal questions presented by the plaintiffs’ complaints will provide efficiency benefits to not only the defendants and their stockholders, but to other corporations and their investors.

For these reasons, the court consolidated the Chevron and FedEx cases to address the purely facial legal challenges to the statutory and contractual validity of the bylaws raised by Counts I and IV of the plaintiffs’ complaints. The defendants filed a motion for judgment on the pleadings, seeking a dismissal of Counts I and IV, and this is the motion before the court today.

After considering the parties’ contending arguments on Count I of the complaints, the court finds that the bylaws are valid under our statutory law. 8 Del. C. § 109(b) provides that the bylaws of a corporation “may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.” The forum selection bylaws, which govern disputes related to the “internal affairs” of the corporations, easily meet these requirements. 5 The bylaws regulate the forum in which stockholders may bring suit, either directly or on behalf of the corporation in a derivative suit, to obtain redress for breaches of fiduciary duty by the board of directors and officers. The bylaws also regulate the forum in which stockholders may bring claims arising under the DGCL or

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other internal affairs claims. In other words, the bylaws only regulate suits brought by stockholders as stockholders in cases governed by the internal affairs doctrine. Thus, the bylaws, by establishing these procedural rules for the operation of the corporation, plainly relate to the “business of the corporation[s],” the “conduct of [their] affairs,” and regulate the “rights or powers of [their] stockholders.” Because Delaware law, like federal law, respects and enforces forum selection clauses, the forum selection bylaws are also not inconsistent with the law.⁶ For these reasons, the forum selection bylaws are not facially invalid as a matter of statutory law.

As to Count IV of the complaints, the court finds that the bylaws are valid and enforceable contractual forum selection clauses. As our Supreme Court has made clear, the bylaws of a Delaware corporation constitute part of a binding broader contract among the directors, officers, and stockholders formed within the statutory framework of the DGCL.⁷ This contract is, by design, flexible and subject to change in the manner that the DGCL spells out and that investors know about when they purchase stock in a Delaware corporation. The DGCL allows the corporation, through the certificate of incorporation, to grant the directors the power to adopt and amend the bylaws unilaterally.⁸

The certificates of incorporation of Chevron and FedEx authorize their boards to amend the bylaws. Thus, when investors bought stock in Chevron and FedEx, they knew

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⁶ See 8 Del. C. § 109(b) (“The bylaws may contain any provision, not inconsistent with law . . . .”); Ingres Corp. v. CA, Inc., 8 A.3d 1143 (Del. 2010) (holding that forum selection clauses are presumptively valid and enforceable under Delaware law).
⁷ For two cases making this clear, eighty years apart, see Airgas, Inc. v. Air Products & Chemicals, Inc., 8 A.3d 1182, 1188 (Del. 2010), and Lawson v. Household Finance Corp., 152 A. 723, 726 (Del. 1930).
⁸ 8 Del. C. § 109(a).
(i) that consistent with 8 Del. C. § 109(a), the certificates of incorporation gave the boards the power to adopt and amend bylaws unilaterally; (ii) that 8 Del. C. § 109(b) allows bylaws to regulate the business of the corporation, the conduct of its affairs, and the rights or powers of its stockholders; and (iii) that board-adopted bylaws are binding on the stockholders. In other words, an essential part of the contract stockholders assent to when they buy stock in Chevron and FedEx is one that presupposes the board’s authority to adopt binding bylaws consistent with 8 Del. C. § 109. For that reason, our Supreme Court has long noted that bylaws, together with the certificate of incorporation and the broader DGCL, form part of a flexible contract between corporations and stockholders, in the sense that the certificate of incorporation may authorize the board to amend the bylaws’ terms and that stockholders who invest in such corporations assent to be bound by board-adopted bylaws when they buy stock in those corporations.\(^9\)

The plaintiffs’ argument to the contrary—that stockholders’ rights may not be regulated by board-adopted bylaws—misunderstands the relationship between the corporation and stockholders established by the DGCL, and attempts to revive the outdated “vested rights” doctrine. As cases like Kidsco Inc. v. Dinsmore show, that doctrine is inconsistent with the fundamental structure of Delaware’s corporate law.\(^10\) Thus, a forum selection clause adopted by a board with the authority to adopt bylaws is valid and enforceable under Delaware law to the same extent as other contractual forum selection clauses. Therefore, this court will enforce the forum selection bylaws in the

\(^9\) See, e.g., Centaur P’rs, IV v. Nat’l Intergp., Inc., 582 A.2d 923, 928 (Del. 1990).
\(^10\) 674 A.2d 483 (Del. Ch. 1995).
same way it enforces any other forum selection clause, in accordance with the principles set down by the United States Supreme Court in *Bremen*\textsuperscript{11} and adopted explicitly by our Supreme Court in *Ingres Corp. v. CA, Inc.*\textsuperscript{12}

In an attempt to defeat the defendants’ motion, the plaintiffs have conjured up an array of purely hypothetical situations in which they say that the bylaws of Chevron and FedEx might operate unreasonably. As the court explains, it would be imprudent and inappropriate to address these hypotheticals in the absence of a genuine controversy with concrete facts. Delaware courts “typically decline to decide issues that may not have to be decided or that create hypothetical harm.”\textsuperscript{13} Under the settled authority of cases such as *Frantz Manufacturing Co. v. EAC Industries*\textsuperscript{14} and *Stroud v. Grace*,\textsuperscript{15} there is a presumption that bylaws are valid. By challenging the facial statutory and contractual validity of the forum selection bylaws, the plaintiffs took on the stringent task of showing that the bylaws cannot operate validly in any conceivable circumstance.\textsuperscript{16} The plaintiffs cannot evade this burden by conjuring up imagined future situations where the bylaws might operate unreasonably, especially when they acknowledge that in most internal affairs cases the bylaws will not operate in an unreasonable manner.\textsuperscript{17}

\textsuperscript{12} 8 A.3d 1143 (Del. 2010).
\textsuperscript{14} 501 A.2d 401, 407 (Del. 1985).
\textsuperscript{16} E.g., *Frantz*, 501 A.2d at 407.
\textsuperscript{17} Tr. of Oral Arg. 64:13-65:6.
Nor does the adherence to the accepted standard of review in addressing facial invalidity claims work any unfairness. Under Bremen and its progeny, like our Supreme Court’s recent Carlyle decision, as-applied challenges to the reasonableness of a forum selection clause should be made by a real plaintiff whose real case is affected by the operation of the forum selection clause. If a plaintiff faces a motion to dismiss because it filed outside the forum identified in the forum selection clause, the plaintiff can argue under Bremen that enforcing the clause in the circumstances of that case would be unreasonable. In addition, if a plaintiff-stockholder believes that a board is breaching its fiduciary duties by applying a forum selection clause to obtain dismissal of an actual case filed outside the forum designated by the bylaws, it may sue at that time. But the plaintiffs here, who have no separate claims pending that are affected by the bylaws, may not avoid their obligation to show that the bylaws are invalid in all circumstances by imagining circumstances in which the bylaws might not operate in a situationally reasonable manner. Such circumstantial challenges are required to be made based on real-world circumstances by real parties, and are not a proper basis for the survival of the plaintiffs’ claims that the bylaws are facially invalid under the DGCL.

Therefore, the defendants’ motion for judgment on the pleadings on Counts I and IV is granted.

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II. Background And Procedural Posture

A. The Chevron And FedEx Forum Selection Bylaws

Critical to the resolution of this motion is an understanding of who has the power to adopt, amend, and repeal the bylaws, and what subjects the bylaws may address under the DGCL. 8 Del. C. § 109(a) identifies who has the power to adopt, amend, and repeal the bylaws:

[T]he power to adopt, amend or repeal bylaws shall be in the stockholders entitled to vote . . . . Notwithstanding the foregoing, any corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws upon the directors . . . . The fact that such power has been so conferred upon the directors . . . shall not divest the stockholders . . . of the power, nor limit their power to adopt, amend or repeal bylaws.

8 Del. C. § 109(b) states the subject matter the bylaws may address:

The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.

Both Chevron’s and FedEx’s certificates of incorporation conferred on the boards the power to adopt bylaws under 8 Del. C. § 109(a). Thus, all investors who bought stock in the corporations whose forum selection bylaws are at stake knew that (i) the DGCL allows for bylaws to address the subjects identified in 8 Del. C. § 109(b), (ii) the DGCL permits the certificate of incorporation to contain a provision allowing directors to adopt bylaws unilaterally, and (iii) the certificates of incorporation of Chevron and FedEx contained a provision conferring this power on the boards.

Acting consistent with the power conferred to the board in Chevron’s certificate of incorporation, the board amended the bylaws and adopted a forum selection bylaw.
Generally speaking, a forum selection bylaw is a provision in a corporation’s bylaws that designates a forum as the exclusive venue for certain stockholder suits against the corporation, either as an actual or nominal defendant, and its directors and employees. On September 29, 2010, the board of Chevron, a Delaware corporation headquartered in California, adopted a forum selection bylaw that provided:

Unless the Corporation consents in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware shall be the sole and exclusive forum for (i) any derivative action or proceeding brought on behalf of the Corporation, (ii) any action asserting a claim of breach of a fiduciary duty owed by any director, officer or other employee of the Corporation to the Corporation or the Corporation’s stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, or (iv) any action asserting a claim governed by the internal affairs doctrine. Any person or entity purchasing or otherwise acquiring any interest in shares of capital stock of the Corporation shall be deemed to have notice of and consented to the provisions of this [bylaw].

Several months later, on March 14, 2011, the board of FedEx, a Delaware corporation headquartered in Tennessee, adopted a forum selection bylaw identical to Chevron’s. Like Chevron, FedEx’s board had been authorized by the certificate of incorporation to adopt bylaws without a stockholder vote, and the FedEx board adopted the bylaw unilaterally.

Chevron’s board amended its bylaw on March 28, 2012 to provide that suits could be filed in any state or federal court in Delaware with jurisdiction over the subject matter and the parties. The amended bylaw also provides that the bylaw would not apply unless

19 Chevron Compl. ¶ 21.
20 FedEx Compl. ¶ 20.
the court in Delaware had personal jurisdiction over all the parties that were “indispensable” to the action.\textsuperscript{21} The amended bylaw, with the changes in italics, states:

Unless the Corporation consents in writing to the selection of an alternative forum, the sole and exclusive forum for (i) any derivative action or proceeding brought on behalf of the Corporation, (ii) any action asserting a claim of breach of a fiduciary duty owed by any director, officer or other employee of the Corporation to the Corporation or the Corporation’s stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, or (iv) any action asserting a claim governed by the internal affairs doctrine shall be a state or federal court located within the state of Delaware, in all cases subject to the court’s having personal jurisdiction over the indispensable parties named as defendants. Any person or entity purchasing or otherwise acquiring any interest in shares of capital stock of the Corporation shall be deemed to have notice of and consented to the provisions of this bylaw.\textsuperscript{22}

In their briefing, the boards of Chevron and FedEx state that the forum selection bylaws are intended to cover four types of suit, all relating to internal corporate governance:

- \textit{Derivative suits}. The issue of whether a derivative plaintiff is qualified to sue on behalf of the corporation and whether that derivative plaintiff has or is excused from making demand on the board is a matter of corporate governance, because it goes to the very nature of who may speak for the corporation.

- \textit{Fiduciary duty suits}. The law of fiduciary duties regulates the relationships between directors, officers, the corporation, and its stockholders.

- \textit{D.G.C.L. suits}. The Delaware General Corporation Law provides the underpinning framework for all Delaware corporations. That statute goes to the core of how such corporations are governed.

\textsuperscript{21} Pls.’ Revised Supplement to Compl. ¶¶ 1-2 [hereinafter “Chevron Supp.”] (quoting Chevron Corp., Current Report (Form 8-K) (Mar. 28, 2012)).

\textsuperscript{22} \textit{Id.}
Internal affairs suits. As the U.S. Supreme Court has explained, “internal affairs,” in the context of corporate law, are those “matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders.”

That is, the description of the forum selection bylaws by the Chevron and FedEx boards is consistent with what the plain language of the bylaws suggests: that these bylaws are not intended to regulate what suits may be brought against the corporations, only where internal governance suits may be brought.

B. The Defendant Boards Have Identified Multiforum Litigation Over Single Corporate Transactions Or Decisions As The Reason Why They Adopted The Bylaws

The Chevron and FedEx boards say that they have adopted forum selection bylaws in response to corporations being subject to litigation over a single transaction or a board decision in more than one forum simultaneously, so-called “multiforum litigation.” The defendants’ opening brief argues that the boards adopted the forum selection bylaws to address what they perceive to be the inefficient costs of defending against the same claim in multiple courts at one time.

The brief describes how, for jurisdictional purposes, a corporation is a citizen both of the state where it is incorporated and of the state where it has its principal place of business. Because a corporation need not be, and frequently is not, headquartered in the state where it is incorporated, a corporation may be subject to personal jurisdiction as a defendant in a suit involving corporate governance matters in

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24 See also Grundfest & Savelle, Forum Selection Provisions, at 370-73.
25 Defs.’ Opening Br. at 6-9.
26 Id. at 9-22.
27 Id.; see also 28 U.S.C. § 1332(c)(1) (defining corporate citizenship for the purposes of federal diversity jurisdiction).
two states.\textsuperscript{28} Therefore, any act that the corporation or its directors undertake is potentially subject to litigation in at least two states.\textsuperscript{29} Furthermore, both state and federal courts may have jurisdiction over the claims against the corporation. The result is that any act that the corporation or its directors undertake may be challenged in various forums within those states simultaneously.\textsuperscript{30} The boards of Chevron and FedEx argue that multiforum litigation, when it is brought by dispersed stockholders in different forums, directly or derivatively, to challenge a single corporate action, imposes high costs on the corporations and hurts investors by causing needless costs that are ultimately born by stockholders, and that these costs are not justified by rational benefits for stockholders from multiforum filings.\textsuperscript{31}

Thus, the boards of Chevron and FedEx claim to have tried to minimize or eliminate the risk of what they view as wasteful duplicative litigation by adopting the forum selection bylaws.\textsuperscript{32} Chevron and FedEx are not the only boards to have recently unilaterally adopted these clauses: in the last three years, over 250 publicly traded corporations have adopted such provisions.\textsuperscript{33}

\textsuperscript{28}Defs.’ Opening Br. 6-9.
\textsuperscript{29}Id.
\textsuperscript{30}Id.
\textsuperscript{32}Defs.’ Opening Br. 9 (“The detriments of multi-jurisdictional duplicative litigation are significant.”).
\textsuperscript{33}Id. at 21 (citing Grundfest & Savelle, \textit{Forum Selection Provisions}, at 326).
As the court next explains, neither the wisdom of the Chevron and FedEx boards in adopting the forum selection bylaws to address the prevalence of multiforum litigation, or in proceeding by way of a bylaw, rather than proposing an amendment to the certificate of incorporation, are proper matters for this court to address. Those questions are not relevant on this motion.34

C. The Plaintiffs Challenge The Forum Selection Bylaws

Within the course of three weeks in February 2012, a dozen complaints were filed in this court against Delaware corporations, including Chevron and FedEx, whose boards had adopted forum selection bylaws without stockholder votes.35 As a threshold issue, these complaints, which were all substantively identical and filed by clients of the same accomplished law firm, alleged that the boards of the defendant corporations had no authority to adopt the bylaws, and sought a declaration that the bylaws were invalid and a

34 Cf. CA, Inc. v. AFSCME Emps. Pension Plan, 953 A.2d 227, 240 (Del. 2008) (“[W]e express no view on whether the [b]ylaw as currently drafted, would create a better governance scheme from a policy standpoint.”).

A separate derivative complaint against the board of directors of Chevron, relating to the board’s enactment of the forum selection bylaw, was filed in the United States District Court for the Northern District of California on March 30, 2012. That action was stayed in favor of this Delaware litigation. Bushansky v. Armacost, 2012 WL 3276937 (N.D. Cal. Aug. 9, 2012).
breach of fiduciary duty. The complaints also brought a salmagundi of other claims, alleging hypothetical ways in which the forum selection bylaws could potentially be enforced in an unreasonable and unfair manner, and accusing the directors of breaching their fiduciary duties by adopting them.

Ten of the twelve defendant corporations repealed their bylaws, and the complaints against them were dismissed. Chevron and FedEx did not repeal their bylaws and answered the plaintiffs’ complaints. The defendants then asked the court to hear a consolidated action on the facial validity of the forum selection bylaws, not only because the plaintiffs’ lawsuits were chilling the adoption of such bylaws under the DGCL, but, most importantly, because the “fundamental question[s]” of statutory validity and contractual enforceability were “ripe for adjudication now[.]”36 The plaintiffs wrote in response that they objected to the defendants’ “attempt to truncate discovery and abruptly seek an advisory opinion on the theoretical permissibility of the director-adopted exclusive forum bylaws.”37

Shortly after the receipt of those letters, the court held an office conference on how the case should proceed. The defendant corporations argued that the statutory validity and contractual enforceability of their forum selection bylaws—as challenged by Counts I and IV—were important legal questions that could be addressed by dealing with these counts on motion practice now. The defendants believed that an adjudication of those purely legal issues would benefit the stockholders of Delaware corporations,

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36 Letter to the Ct. from Counsel for Defs. (Oct. 9, 2012).
37 Letter to the Ct. from Counsel for Pls. (Oct. 11, 2012).
because the statutory validity and contractual enforceability of the companies’ bylaws in actual, real-world situations involving their effect on substantive internal affairs litigation had been clouded by the present case. On the other hand, the plaintiffs’ other counts, which involve their fiduciary duty claims and arguments about the ways in which the forum selection clauses could be inequitably adopted or applied in particular situations, could be determined after the core questions of facial statutory validity and contractual enforceability had been resolved. The defendants pointed out that, if they lose, the legal issues are settled against them, and if the bylaws are invalid, then the plaintiffs’ other as-applied claims are moot. But, if the bylaws are statutorily and contractually valid and enforceable as a facial matter, then there would be a more concrete legal context for consideration of whether the plaintiffs’ fiduciary duty and as-applied claims are meritorious or even, on account of the purely hypothetical nature of the latter arguments, justiciable.

The plaintiffs resisted this approach, arguing that their facial challenges in Counts I and IV should not be resolved until discovery was completed on all their other claims. But, because Chevron and FedEx had made persuasive arguments that addressing the facial challenges to the bylaws would avoid unnecessary costs or delay, especially given the doubt the plaintiffs themselves created about a corporation’s statutory power to adopt forum selection bylaws at all, the court consolidated their cases to resolve those

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38 Compare Galaviz v. Berg, 763 F. Supp. 2d 1170, 1174-75 (N.D. Cal. 2011) (ruling that a board-adopted forum selection clause was unenforceable), with In re Revlon, Inc. S’holders Litig., 990 A.2d 940, 960 & n.8 (Del. Ch. 2010) (suggesting that corporations could adopt “charter provisions selecting an exclusive forum for intra-entity disputes,” but properly noting
common and narrow questions of law: (i) whether the forum selection bylaws are facially invalid under the DGCL (Count I); and (ii) whether the board-adopted forum selection bylaws are facially invalid as a matter of contract law (Count IV). For those reasons, a scheduling order was entered that specifically contemplated motion practice on the statutory and contractual validity issues common to both cases in Counts I and IV.39

But the plaintiffs have taken the position that the court cannot consolidate the cases to address purely legal issues, because, as they say, it is improper for this court to make “a determination of the validity of the [b]ylaw[s] in the abstract.”40 The court’s power to consolidate cases to address purely legal issues is codified in Delaware Court of Chancery Rule 42(a), which provides that:

When actions involving a common question of law or fact are pending before the Court, it may order a joint hearing or trial of any or all the matters in issue in the actions; it may order all the actions consolidated; and it may make such orders concerning proceedings therein as may tend to avoid unnecessary costs or delay.

Under that rule, the court may consolidate any cases involving a “common question of law” to decide “any or all the matters.” And, here, the order to consolidate these actions to address the ripe legal issues—the facial statutory and contractual validity and enforceability of the forum selection bylaws adopted by Chevron’s and FedEx’s board of directors under the DGCL—rests on that clear authority.41

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39 See Order Regarding Limited Coordination & Scheduling (Nov. 19, 2012).
40 Pls.’ Br. in Opp’n 30 (citation omitted).
41 The plaintiffs have also ignored the appropriate procedural mechanism, Court of Chancery Rule 59(f), to reargue the court’s October ruling in which it consolidated the cases to address the
Even more surprising still was that the plaintiffs also argued in their brief that the pleadings had not been closed yet, and for that reason alone, the court must stay its hand, and not rule on the purely legal issues presented by their own Counts I and IV. The basis for the plaintiffs’ claim was that they had filed a supplemental pleading (which this court had authorized it to do) in response to Chevron’s amended bylaw.

But the schedule that the court entered on this consolidated action specifically contemplated that the court would address the counts contesting the facial statutory validity and contractual enforceability of the forum selection bylaws in a consolidated action, and as part and parcel of that decision, permitted the plaintiffs to file supplemental pleadings in the Chevron case that Chevron did not have to answer until this consolidated action was resolved, because the supplement would only raise certain additional counts not related to facial statutory or contractual invalidity. That order was consistent with the court’s finding that it would be efficient to resolve the legal questions first, given that it could moot other claims in both cases and even the new ones raised by the supplemental pleadings in the Chevron case. By order, a briefing schedule was put in place for the resolution of this motion, which addresses only Counts I and IV of the facial validity claims. Having failed to avail themselves of the appropriate procedural mechanism, the plaintiffs have waived this procedural argument. See McDaniel v. DaimlerChrysler Corp., 860 A.2d 321, 323 (Del. 2004). For that reason alone, the plaintiffs’ argument that the court cannot address the consolidated legal issues must fail.

See Order Regarding Limited Coordination & Scheduling (Nov. 19, 2012) (“Plaintiffs shall file their revised Supplement to the Complaint . . . . The Chevron Defendants will agree that the Revised Supplement shall become part of the Complaint[.]”).

Id. (providing a schedule for a motion for judgment on the pleadings and permitting the plaintiffs to file supplemental pleadings); see also Tr. of Office Conf. (Oct. 31, 2012) (granting the defendants’ request to consolidate the cases to address the facial validity of the forum selection bylaws before proceeding with the other claims).
plaintiffs’ complaints, for which the pleadings are closed.⁴⁵ These counts allege that the bylaws are statutorily invalid because they are beyond the board’s authority under the DGCL, and that board-adopted forum selection bylaws are contractually invalid and therefore not enforceable.⁴⁶ The plaintiffs’ claims that the boards breached their fiduciary duties in adopting the bylaws have been stayed.⁴⁷ The plaintiffs understood this, and their argument in their brief, that this motion addressing their counts relating to purely legal, facial challenges to the forum selection bylaws cannot be considered until their fact-intensive counts are addressed, contradicts the clear order of this court and has no support in the law. If this novel contention were adopted, plaintiffs could cast corporate action in doubt and impair the functioning of a corporation, while not allowing a corporation to clear up the doubt by means of traditional motion practice often used to resolve purely legal questions in a timely manner. Rather, the corporation would not be able to get a ruling on the purely legal challenge of facial validity until the court addressed all the more fact-laden counts in the complaint. Our law does not require that approach. Rather, “[f]acial challenges to the legality of provisions in corporate instruments are regularly resolved by this Court.”⁴⁸

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⁴⁵ Order Regarding Limited Coordination & Scheduling (Nov. 19, 2012).
⁴⁶ Chevron Compl. ¶¶ 48-56, FedEx Compl. ¶¶ 49-57 (Count I); Chevron Compl. ¶¶ 73-81, FedEx Compl. ¶¶ 72-80 (Count IV).
⁴⁷ See Tr. of Office Conf. 24-26, 44-45 (Oct. 31, 2012).
III. The Standard Of Review

The standard of review on this motion is important in framing this consolidated motion. The two sides approach this issue differently. The plaintiffs, for their part, simply recite the basic procedural standard, by noting that this court may only grant judgment on the pleadings if there are no material facts in dispute, and one party is entitled to judgment as a matter of law.\footnote{Pls.’ Br. in Opp’n 29.} Thus, the plaintiffs say, “[t]he Court can grant Defendants’ [motion] only if unambiguous and unmistakably clear language of the Bylaws renders Defendants’ constructions the only reasonable interpretation.”\footnote{Id. (citing JANA Master Fund, Ltd. v. CNET Networks, Inc., 954 A.2d 335, 338 (Del. Ch. 2008); United Rentals, Inc. v. RAM Hldgs., Inc., 937 A.2d 810, 830 (Del. Ch. 2007)).} The plaintiffs then devote much of their complaints and briefing to arguing that the bylaws are ambiguous, because, they say, the forum selection bylaws could be applied in different ways in different factual situations.\footnote{E.g., Pls.’ Br. in Opp’n 5-24, 32-36; Chevron Compl. ¶¶ 59-67, FedEx Compl. ¶¶ 58-66 (Count II) (the bylaws conflict with Delaware statutes); Chevron Compl. ¶¶ 68-72, FedEx Compl. ¶¶ 67-71 (Count III) (the bylaws improperly grant jurisdiction over all stockholders); Chevron Compl. ¶¶ 82-87, FedEx Compl. ¶¶ 81-86 (Count V) (the bylaws require claims to be brought where the court does not have jurisdiction over all defendants); Chevron Compl. ¶¶ 88-99, FedEx Compl. ¶¶ 87-98 (Count VI) (the bylaws impinge on jurisdiction of federal courts); Chevron Supp. ¶¶ 51-52 (Count IX) (the amended Chevron bylaw impinges on federal jurisdiction).}

But, the plaintiffs ignore the nature of this motion, and the counts of their own complaints to which the defendants’ motion is directed. This motion concerns Count I, in which the plaintiffs alleged that “the bylaw[s are] invalid because [they are] beyond the authority granted in 8 Del. C. § 109(b),” and Count IV, in which the plaintiffs claim that
“the bylaw[s are] not [] valid and enforceable forum selection provision[s].” 52 Thus, this motion is only concerned with the facial statutory and contractual validity of the bylaws, and the motion is expressly not concerned with how the bylaws might be applied in any future, real-world situation. The plaintiffs’ proposed standard, by contrast, is based on a case in which this court resolved an actual, live controversy over whether a bylaw could be applied to the real human events underlying that case. 53

The defendants correctly point out this error in the plaintiffs’ approach. As our Supreme Court held in the Frantz Manufacturing case, “[t]he bylaws of a corporation are presumed to be valid, and the courts will construe the bylaws in a manner consistent with the law rather than strike down the bylaws.” 54 Thus, the plaintiffs’ burden on this motion challenging the facial statutory and contractual validity of the bylaws is a difficult one: they must show that the bylaws cannot operate lawfully or equitably under any circumstances. 55 So, the plaintiffs must show that the bylaws do not address proper

52 Chevron Compl. ¶¶ 48-56, FedEx Compl. ¶¶ 49-57 (Count I); Chevron Compl. ¶¶ 73-81, FedEx Compl. ¶¶ 72-80 (Count IV) (capitalization omitted).
53 See JANA, 954 A.2d at 344.
54 Frantz, 501 A.2d at 407 (citation omitted); see also Hollinger Int’l, Inc. v. Black, 844 A.2d 1022, 1080-83 (Del. Ch. 2004) (distinguishing between the board’s legal authority to adopt a bylaw and the board’s equitable use of that authority), aff’d, 872 A.2d 559 (Del. 2005); R. Franklin Balotti & Jesse A. Finkelstein, The Delaware Law of Corporations & Business Organizations § 1.10 [hereinafter Balotti & Finkelstein, Corporations] (explaining that courts attempt to interpret “by-laws in harmony” with the corporation’s certificate of incorporation and positive law, and thus hold a bylaw to be invalid when a “conflict is unavoidable”).
55 Frantz, 501 A.2d at 407; Edward P. Welch et al., Folk on the Delaware General Corporation Law § 109.4 (2009) [hereinafter Welch et al., Folk on the DGCL] (“Bylaws are presumed to be valid. Courts will interpret a bylaw in a manner consistent with the law rather than striking it down. The rules of construction used to interpret statutes, contracts, and other written instruments apply to bylaws.” (citations omitted)). Of course, often, claims about the facial invalidity of a provision come to the courts when a party challenges the legislature’s power to enact a statute. Those principles are equally applicable here. See, e.g., Hibbert v. Hollywood
subject matters of bylaws as defined by the DGCL in 8 Del. C. § 109(b), and can never operate consistently with law. The plaintiffs voluntarily assumed this burden by making a facial validity challenge, and cannot satisfy it by pointing to some future hypothetical application of the bylaws that might be impermissible.

The answer to the possibility that a statutorily and contractually valid bylaw may operate inequitably in a particular scenario is for the party facing a concrete situation to challenge the case-specific application of the bylaw, as in the landmark case of Schnell v. Chris-Craft Industries. The settled approach of our law regarding bylaws is that courts should endeavor to enforce them to the extent that it is possible to do so without violating

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Park, Inc., 457 A.2d 339, 342-43 (Del. 1983) (noting that “the rules which are used to interpret statutes, contracts, and other written instruments are applicable when construing corporate charters and bylaws” (emphasis added)); Downs v. Jacobs, 272 A.2d 706, 707 (Del. 1970) (“Courts presume every legislative act constitutional and indulge every intendment in favor of validity.”); State v. Hobson, 83 A.2d 846, 851 (Del. 1951) (“Even if the Delaware statute, read literally, were susceptible of the construction which defendant urges, it would be our duty to reject that construction, since we are required, as between two possible constructions, to adopt the one which will uphold its validity.”); see also, e.g., R.M. v. V.H., 2006 WL 1389864, at *8 (Del. Fam. Ct. Jan. 19, 2006) (“A party may challenge a statute as unconstitutional on its face or as applied to a particular set of facts. A facial challenge is the most difficult to bring successfully because the challenger must establish that there is no set of circumstances under which the statute would be valid.”); accord United States v. Salerno, 481 U.S. 739, 745 (1987) (describing a facial challenge as the “most difficult” challenge to succeed on because the statute must not operate lawfully in any circumstances).


57 Welch et al., Folk on the DGCL § 109.3.1 (“The party asserting that bylaws were not properly adopted bears the burden to prove it.”).

58 E.g., Stroud, 606 A.2d at 79 (“The validity of corporate action under [a bylaw] must await its actual use.”).

59 Schnell v. Chris-Craft Indus., Inc., 285 A.2d 437 (Del. 1971); see also Moran v. Household Int’l, Inc., 500 A.2d 1346, 1357 (Del. 1985) (concluding that although the board had the power to adopt a poison pill, the “ultimate response” of the board to a takeover must be judged by the “[d]irectors’ actions at that time”); accord Stroud, 606 A.2d at 96 (“It is not an overstatement to suggest that every valid by-law is always susceptible to potential misuse. Without a showing of abuse . . . we must . . . uphold the validity of [a bylaw].”).
anyone’s legal or equitable rights.\textsuperscript{60} This is also consistent with the doctrine laid down by the U.S. Supreme Court decision in \textit{Bremen} and its progeny, which requires courts to give as much effect as is possible to forum selection clauses and only deny enforcement of them to the limited extent necessary to avoid some fundamentally inequitable result or a result contrary to positive law.\textsuperscript{61} Thus, a plaintiff can challenge the real-world enforcement of a forum selection bylaw. But that review happens when there is a genuine, extant controversy in which the forum selection bylaw is being applied. Under our Supreme Court’s precedent in \textit{Stroud} and \textit{Frantz}, which this court must follow, the appropriate question now is simply whether the bylaws are valid under the DGCL, and whether they form facially valid contracts between the stockholders, the directors and officers, and the corporation.\textsuperscript{62}

\textsuperscript{60} Welch et al., \textit{Folk on the DGCL} § 109.4; Balotti & Finkelstein, \textit{Corporations} § 1.10.


\textsuperscript{62} The \textit{Frantz} and \textit{Stroud} approach is the traditional one. Although it differs from the approach taken by the Supreme Court in the 2008 \textit{CA} case, the Supreme Court in that case cited \textit{Frantz} and \textit{Stroud} approvingly and as good law, stating that the novel posture of the case dictated the different standard of review. \textit{CA, Inc. v. AFSCME Emps. Pension Plan}, 953 A.2d 227, 238 (Del. 2008) (“Were this issue being presented in the course of litigation involving the application of the Bylaw to a specific set of facts, we would start with the presumption that the Bylaw is valid and, if possible, construe it in a manner consistent with the law. The factual context in which the Bylaw was challenged would inform our analysis, and we would ‘exercise caution [before] invalidating corporate acts based upon hypothetical injuries . . . .’ (citing \textit{Frantz}, 501 A.2d at 407, and quoting \textit{Stroud}, 606 A.2d at 79)). The reason for this different approach may be intuited. In \textit{CA}, the Supreme Court was operating under a novel constitutional amendment that gave it the authority to answer questions posed to it by the Securities and Exchange Commission on a limited paper record, without the full benefit of context that comes from traditional adversarial litigation. \textit{See} 76 Del. Laws ch. 37, § 1 (2007) (amending Del. Const. art. IV, § 11(8)). The Supreme Court may have feared that by giving a federal regulatory body a flat indication that a bylaw was “valid” or not based on a record consisting of a long letter, it would create the false impression that bylaws of the kind at issue were immune from challenge in all circumstances. Thus, rather than risk such an overbroad implication, the court took a different approach, finding that in that unusual context the variance from the settled standard was the more modest approach. In the more traditional context here of a facial challenge to the validity of a
The court turns to these questions now.

IV. Legal Analysis

A. The Board-Adopted Forum Selection Bylaws Are Statutorily Valid

Given this procedural context, the court structures its analysis to mirror the two facial claims of invalidity as they have been presented in the complaints. First, the court looks at Count I’s challenge that the “bylaw[s are] invalid because [they are] beyond the authority granted in 8 Del. C. § 109(b).” As to that claim, the court must determine whether the adoption of the forum selection bylaws was beyond the board’s authority in the sense that they do not address a proper subject matter under 8 Del. C. § 109(b), which provides that:

The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.

Thus, the court must decide if the bylaws are facially invalid under the DGCL because they do not relate to the business of the corporations, the conduct of their affairs, or the rights of the stockholders.

After first making that determination, the court then addresses Count IV’s challenge that “the bylaw[s are] not a valid and enforceable forum selection provision.”

bylaw, the more modest, restrained, and prudent approach is the traditional one under Frantz and Stroud. That approach involves judicial reticence to chill corporate freedom by condemning as invalid a bylaw that is consistent with the board’s statutory and contractual authority, simply because it might be possible to imagine situations when the bylaw might operate unreasonably. By long-standing, settled law, such as-applied challenges are to be raised later, when real-world circumstances give rise to a genuine, concrete dispute requiring judicial resolution.

63 Chevron Compl. ¶¶ 50-58, FedEx Compl. ¶¶ 49-57.
64 Chevron Compl. ¶¶ 73-81, FedEx Compl. ¶¶ 72-80.
That is, even if forum selection bylaws regulate proper subject matter under 8 Del. C. § 109(b), the plaintiffs allege that forum selection bylaws are contractually invalid because they have been unilaterally adopted by the board.65

1. The Forum Selection Bylaws Regulate A Proper Subject Matter Under 8 Del. C. § 109(b)

Having challenged whether the bylaws are authorized by 8 Del. C. § 109(b), the plaintiffs have to confront the broad subjects that § 109(b) permits bylaws to address. The DGCL provides that bylaws may address any subject, “not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.”66 The most important consideration for a court in interpreting a statute is the words the General Assembly used in writing it.67 As a matter of easy linguistics, the forum selection bylaws address the “rights” of the stockholders, because they regulate where stockholders can exercise their right to bring certain internal affairs claims against the corporation and its directors and officers.68 They also plainly relate to the conduct of the corporation by channeling internal affairs cases into the courts of the state of incorporation, providing for the opportunity to have internal affairs cases

65 Chevron Compl. ¶ 74; FedEx Compl. ¶ 73.
66 8 Del. C. § 109(b).
67 E.g., New Cingular Wireless PCS v. Sussex Cty. Bd. of Adjustment, 65 A.3d 607, 611 (Del. 2013) (“It is axiomatic that a statute . . . is to be interpreted according to its plain and ordinary meaning.” (citation omitted)); Scattered Corp. v. Chi. Stock Exch., Inc., 671 A.2d 874, 877 (Del. Ch. 1994) (“A determination of the General Assembly’s intent must, where possible, be based on the language of the statute itself. In divining the legislative intent, statutory language, where possible, should be accorded its plain meaning.” (citations omitted)).
resolved authoritatively by our Supreme Court if any party wishes to take an appeal.\textsuperscript{69} That is, because the forum selection bylaws address internal affairs claims, the subject matter of the actions the bylaws govern relates quintessentially to “the corporation’s business, the conduct of its affairs, and the rights of its stockholders [\textit{qua} stockholders].”

Perhaps recognizing the weakness of any argument that the forum selection bylaws fall outside the plain language of 8 Del. C. § 109(b), the plaintiffs try to argue that judicial gloss put on the language of the statute renders the bylaws facially invalid.\textsuperscript{70} The plaintiffs contend that the bylaws do not regulate permissible subject matters under 8 Del. C. § 109(b), because they attempt to regulate an “external” matter, as opposed to, an “internal” matter of corporate governance.\textsuperscript{71} The plaintiffs attempt to support this argument with a claim that traditionally there have only been three appropriate subject matters of bylaws: stockholder meetings, the board of directors and its committees, and officerships.\textsuperscript{72}

But even if one assumes that judicial statements could limit the plain statutory words in the way the plaintiffs claim (which is dubious), the judicial decisions do not aid the plaintiffs. The plaintiffs take a cramped view of the proper subject matter of bylaws.\textsuperscript{73} The bylaws of Delaware corporations have a “procedural, process-oriented

\textsuperscript{69} See Grundfest & Savelle, \textit{Forum Selection Provisions}, at 374.
\textsuperscript{70} E.g., \textit{CA, Inc.}, 953 A.2d at 235 & n.15; \textit{Hollinger Int’l, Inc. v. Black}, 844 A.2d 1022, 1078-79 & n.128 (Del. Ch. 2004), aff’d, 872 A.2d 559 (Del. 2005); \textit{Gow v. Consol. Coppermines Corp.}, 165 A. 136, 140 (Del. Ch. 1933).
\textsuperscript{71} PIs.’ Br. in Opp’n 39-40.
\textsuperscript{72} Id. at 44.
\textsuperscript{73} See, \textit{e.g.}, \textit{Hollinger}, 844 A.2d at 1078 (“The DGCL is intentionally designed to provide directors and stockholders with flexible authority [to adopt bylaws], permitting great discretion for private ordering and adaptation. That capacious grant of power is policed in large part by the
nature.” It is doubtless true that our courts have said that bylaws typically do not contain substantive mandates, but direct how the corporation, the board, and its stockholders may take certain actions. Del. C. § 109(b) has long been understood to allow the corporation to set “self-imposed rules and regulations [that are] deemed expedient for its convenient functioning.” The forum selection bylaws here fit this description. They are process-oriented, because they regulate where stockholders may file suit, not whether the stockholder may file suit or the kind of remedy that the stockholder may obtain on behalf of herself or the corporation. The bylaws also clearly address cases of the kind that address “the business of the corporation, the conduct of its affairs, and . . . the rights or powers of its stockholders, directors, officers or employees,” because they govern where internal affairs cases governed by state corporate law may be heard. These are the kind of claims most central to the relationship between those who manage the corporation and the corporation’s stockholders.

By contrast, the bylaws would be regulating external matters if the board adopted a bylaw that purported to bind a plaintiff, even a stockholder plaintiff, who sought to bring a tort claim against the company based on a personal injury she suffered that occurred on the company’s premises or a contract claim based on a commercial contract with the corporation. The reason why those kinds of bylaws would be beyond the

common law of equity, in the form of fiduciary duty principles.”); Balotti & Finkelstein, Corporations § 1.10 (“By-laws that reasonably regulate broader [stockholder] rights may be valid, especially if courts follow the general rule of construction and attempt to harmonize the by-law regulation and the broader right.” (citation omitted)).

Id.  
8 Del. C. § 109(b).
statutory language of 8 Del. C. §109(b) is obvious: the bylaws would not deal with the rights and powers of the plaintiff-stockholder as a stockholder. As noted earlier, the defendants themselves read the forum selection bylaws in a natural way to cover only internal affairs claims brought by stockholders qua stockholders.

Nor is it novel for bylaws to regulate how stockholders may exercise their rights as stockholders. For example, an advance notice bylaw “requires stockholders wishing to make nominations or proposals at a corporation’s annual meeting to give notice of their intention in advance of so doing.” Like such bylaws, which help organize what could otherwise be a chaotic stockholder meeting, the forum selection bylaws are designed to bring order to what the boards of Chevron and FedEx say they perceive to be a chaotic filing of duplicative and inefficient derivative and corporate suits against the directors and the corporations. The similar purpose of the advance notice bylaws and the forum selection bylaws reinforce that forum selection bylaws have a proper relationship to the business of the corporation and the conduct of its affairs under 8 Del. C. § 109(b).

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78 See also Grundfest & Savelle, Forum Selection Provisions, at 369-70 (“[A]s much as contract rights can legitimately be regulated through forum selection provisions, it follows that stockholders’ rights to pursue intra-corporate claims can also be regulated by [forum selection] provisions. To be sure, this conclusion would arguably not follow (or not hold as strongly) if the forum selection provision sought to regulate the right to pursue causes of action that were not intra-corporate in nature because then the provision would not be seeking to regulate the stockholder’s rights as a stockholder and would be extended beyond the contract that defines and governs the stockholders’ rights.” (emphasis added)).

79 JANA Master Fund, Ltd. v. CNET Networks, Inc., 954 A.2d 335, 344 (Del. Ch. 2008) (citation omitted), aff’d, 947 A.2d 1120 (Del. 2008) (Table).

80 The plaintiffs seek to bolster their argument that the forum selection bylaws go beyond the board’s statutory authority under 8 Del. C. § 109(b) by claiming that the bylaws regulate not only the “rights and powers of [the] stockholders,” as is permitted under the statutory text, but also the rights and powers of former stockholders. Chevron Compl. ¶ 51; FedEx Compl. ¶ 50. The plaintiffs cite the example of stockholders who are cashed out in a short-form merger, and,
The plaintiffs’ argument, then, reduces to the claim that the bylaws do not speak to a “traditional” subject matter, and should be ruled invalid for that reason alone. For starters, the factual premise of this argument is not convincing. The bylaws cannot fairly be argued to regulate a novel subject matter: the plaintiffs ignore that, in the analogous contexts of LLC agreements and stockholder agreements, the Supreme Court and this court have held that forum selection clauses are valid.81 But in any case, the Supreme Court long ago rejected the position that board action should be invalidated or enjoined simply because it involves a novel use of statutory authority. In Moran v. Household International in 1985, the plaintiff argued that a corporation could not use its powers to issue rights to purchase shares of preferred stock in the form of a shareholder rights plan—a.k.a. poison pill—the sole purpose of which was to allow the board to defend against tender offers addressed solely to stockholders.82 The Supreme Court rejected the appellants’ argument that 8 Del. C. § 157 had never been used to authorize the issuance of rights for the purpose of defeating a hostile takeover.83 Rather, echoing its recent iconic decision in Unocal, the court reiterated that “our corporate law is not static. It

having been cashed out, sue the board for a breach of fiduciary duty. As with many of the plaintiffs’ challenges to the bylaws, this is properly seen as an as-applied challenge, which should be addressed when the issue is actually ripe. But in any case, the plaintiffs do not cite any rule of statutory construction that justifies reading 8 Del. C. § 109(b) in the contorted fashion they propose. The only reason that so-called “former stockholders” can sue under 8 Del. C. § 253 is because they were stockholders at the time of the merger. In other words, it is not the case that a bylaw in effect at the time that a stockholder’s internal affairs claim arose cannot bind that stockholder simply because the transaction she is challenging resulted in her no longer being a stockholder. That bylaw continues to bind her because her right to sue continues to be based on her status as a stockholder.

83 Id. at 1351.
must grow and develop in response to, indeed in anticipation of, evolving concepts and needs. Merely because the General Corporation Law is silent as to a specific matter does not mean that it is prohibited.”

Just as the board of Household was permitted to adopt the pill to address a future tender offer that might threaten the corporation’s best interests, so too do the boards of Chevron and FedEx have the statutory authority to adopt a bylaw to protect against what they claim is a threat to their corporations and stockholders, the potential for duplicative law suits in multiple jurisdictions over single events. As Moran makes clear, that a board’s action might involve a new use of plain statutory authority does not make it invalid under our law, and the boards of Delaware corporations have the flexibility to respond to changing dynamics in ways that are authorized by our statutory law. Nor, in addressing this facial challenge, is it possible to conceive that choosing the most obviously reasonable forum—the state of incorporation, Delaware—so that internal affairs cases will be decided in the courts whose Supreme Court has the authoritative final say as to what the governing law means, somehow takes the forum selection bylaws outside of 8 Del C. § 109(b)’s broad authorizing language.

Furthermore, the bylaws here are subject to the same, plus even more, controls on their misuse than the pill found valid in Moran. Like a board that has adopted a poison pill in case of some future threat and can redeem it when a tender offer poses no threat,

84 Id. (quoting Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 957 (Del. 1985)).
85 See Edgar v. MITE Corp., 457 U.S. 624, 645 (1982) (“The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation’s internal affairs—matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders . . . .”).
the boards of the companies in this case have reserved the right in the bylaw itself—as is traditional for any party affected by a contractual forum provision—to waive the corporation’s rights under the bylaw in a particular circumstance in order to meet their obligation to use their power only for proper corporate purposes. And as with all exercises of fiduciary authority, the real-world application of a forum selection bylaw can be challenged as an inequitable breach of fiduciary duty. But, as a distinguished scholar has noted, “[t]he presumption is not that the [bylaw] is invalid upon adoption because it might, under some undefined and hypothetical set of later-evolving circumstances, be improperly applied.”

And forum selection clauses have additional safeguards that poison pills do not have. For starters, unlike typical poison pills, board-adopted forum selection bylaws are subject, as will be discussed more later, to the most direct form of attack by stockholders who do not favor them: stockholders can simply repeal them by a majority vote. In addition, because the corporation must raise the forum selection clause as a jurisdictional defense if it wishes to obtain dismissal of a case filed in a different forum outside of the state selected in the bylaws, the enforceability of the forum selection bylaws will be analyzed under the Bremen test in any case where an affected stockholder plaintiff resists

86 Both bylaws begin: “Unless the Corporation consents in writing to the selection of an alternative forum . . . .” Chevron Supp. ¶ 1; FedEx Compl. ¶ 20.
89 See 8 Del. C. § 109(a).
compliance, as the court will explain in more depth later. That is, the board must voluntarily submit the forum selection clause to the scrutiny of the courts if a plaintiff does not comply with it.

Therefore, the court concludes that forum selection bylaws are statutorily valid under Delaware law, and Count I of the plaintiffs’ complaints is dismissed. The court now considers whether a forum selection bylaw is contractually invalid when adopted by the board unilaterally.

2. **The Board-Adopted Bylaws Are Not Contractually Invalid As Forum Selection Clauses Because They Were Adopted Unilaterally By The Board**

Despite the contractual nature of the stockholders’ relationship with the corporation under our law, the plaintiffs argue, in Count IV of their complaints, that the forum selection bylaws by their nature are different and cannot be adopted by the board unilaterally. The plaintiffs’ argument is grounded in the contention that a board-adopted forum selection bylaw cannot be a *contractual* forum selection clause because the stockholders do not vote in advance of its adoption to approve it. The plaintiffs acknowledge that contractual forum selection clauses are “prima facie valid” under *The Bremen v. Zapata Off-Shore Co.* and *Ingres Corp. v. CA, Inc.*, and that they are presumptively enforceable. But, the plaintiffs say, the forum selection bylaws are

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90 See *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972); *Ingres Corp. v. CA, Inc.*, 8 A.3d 1143 (Del. 2010); see also Grundfest & Savelle, *Forum Selection Provisions*, at 378 (“[F]orum selection bylaws are perhaps unique among all bylaws in that they can never be enforced by the corporation unless the corporation triggers prior judicial scrutiny designed to assure that the provision does not violate any legitimate stockholder right. This fact stands in sharp contrast to all other bylaw provisions that allow boards to act without first petitioning for judicial relief.”).

91 PIs.’ Br. in Opp’n 49-50.

92 *Bremen*, 407 U.S. at 10; *Ingres*, 8 A.3d 1143.
contractually invalid in this case, because they were adopted by a board, rather than by Chevron’s and FedEx’s dispersed stockholders. The plaintiffs argue that this method of adopting a forum selection clause is invalid as a matter of contract law, because it does not require the assent of the stockholders who will be affected by it. Thus, in the plaintiffs’ view, there are two types of bylaws: (i) contractually binding bylaws that are adopted by stockholders; (ii) non-contractually binding bylaws that are adopted by boards using their statutory authority conferred by the certificate of incorporation.93

By this artificial bifurcation, the plaintiffs misapprehend fundamental principles of Delaware corporate law. Our corporate law has long rejected the so-called “vested rights” doctrine.94 That vested rights view, which the plaintiffs have adopted as their own, “asserts that boards cannot modify bylaws in a manner that arguably diminishes or divests pre-existing shareholder rights absent stockholder consent.”95 As then-Vice Chancellor, now Justice, Jacobs explained in the Kidsco case, under Delaware law, where

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93 Although the plaintiffs’ argument suggests that a forum selection provision accomplished by a certificate amendment would be more legitimate in some normative sense because stockholders approved the amendment, the plaintiffs ignore that a certificate provision is harder for stockholders to reverse. See 8 Del. C. § 242(b)(1) (requiring a board resolution and stockholder vote for a proper amendment to the corporation’s certificate of incorporation). By contrast, in the case of a board-adopted forum selection bylaw, the stockholders can act unilaterally to amend or repeal the provision. Id. § 109(a) (“After a corporation other than a nonstock corporation has received any payment for any of its stock, the power to adopt, amend or repeal bylaws shall be in the stockholders entitled to vote.”). For present purposes, however, the issue is not whether someone might deem it more legitimate in some sense to proceed by an amendment to the certificate of incorporation rather than by a bylaw. That decision was for the Chevron and FedEx boards in the first instance, and the stockholders have multiple tools to hold the boards accountable if the stockholders disagree with it.

94 See, e.g., Fed. United Corp. v. Havender, 11 A.2d 331, 335 (Del. 1940) (holding that preferred stockholders did not have a “vested” right to accrued dividends).

a corporation’s articles or bylaws “put all on notice that the by-laws may be amended at any time, no vested rights can arise that would contractually prohibit an amendment.” 96

In an unbroken line of decisions dating back several generations, our Supreme Court has made clear that the bylaws constitute a binding part of the contract between a Delaware corporation and its stockholders. 97 Stockholders are on notice that, as to those subjects that are subject of regulation by bylaw under 8 Del. C. § 109(b), the board itself may act unilaterally to adopt bylaws addressing those subjects. 98 Such a change by the board is not extra-contractual simply because the board acts unilaterally; rather it is the kind of change that the overarching statutory and contractual regime the stockholders buy into explicitly allows the board to make on its own. 99 In other words, the Chevron and FedEx stockholders have assented to a contractual framework established by the DGCL and the certificates of incorporation that explicitly recognizes that stockholders will be bound by bylaws adopted unilaterally by their boards. 100 Under that clear contractual

96 Kidsco Inc. v. Dinsmore, 674 A.2d 483, 492 (Del. Ch. 1995) (emphasis added) (citing Roven v. Cotter, 547 A.2d 603, 608 (Del. Ch. 1988)); see also William Meade Fletcher, Fletcher Cyclopedia of the Law of Corporations § 4176 (updated 2012) (“It is presumed that a person who becomes a shareholder in, or a member of, a corporation does so with knowledge and implied assent that its bylaws may be amended.” (citations omitted)).


98 Kidsco, 674 A.2d at 492-93.

99 Stockholders likewise agree that a requisite majority of other stockholders may adopt bylaws with which they do not agree. A dissenting stockholder can no more object to the authority of a board to adopt a bylaw than it could object to the requisite majority of stockholders adopting a bylaw.

100 Kidsco, 674 A.2d at 492-93 (“[T]his Court has held that where a corporation’s by-laws put all on notice that the by-laws may be amended at any time, no vested rights can arise that would contractually prohibit an amendment.”); see also Roven, 547 A.2d at 608; accord Centaur P’rs,
framework, the stockholders assent to not having to assent to board-adopted bylaws.\textsuperscript{101}

The plaintiffs’ argument that stockholders must approve a forum selection bylaw for it to be contractually binding is an interpretation that contradicts the plain terms of the contractual framework chosen by stockholders who buy stock in Chevron and FedEx. Therefore, when stockholders have authorized a board to unilaterally adopt bylaws, it follows that the bylaws are not contractually invalid simply because the board-adopted bylaw lacks the contemporaneous assent of the stockholders.\textsuperscript{102} Accordingly, the conclusion reached by the United States District Court for the Northern District of California in \textit{Galaviz v. Berg}, a case on which the plaintiffs rely heavily—that board-adopted bylaws are not like other contracts because they lack the stockholders’ assent—rests on a failure to appreciate the contractual framework established by the DGCL for Delaware corporations and their stockholders.\textsuperscript{103}

Even so, the statutory regime provides protections for the stockholders, through the indefeasible right of the stockholders to adopt and amend bylaws themselves. “[B]y its terms Section 109(a) vests in the shareholders a power to adopt, amend or repeal bylaws that is legally sacrosanct, \textit{i.e.}, the power cannot be non-consensually eliminated or

\begin{itemize}
\item \textsuperscript{101} CA, Inc. \textit{v. AFSCME Emps. Pension Plan}, 953 A.2d 227, 231 (Del. 2008) (discussing the power of a board to adopt bylaws without stockholder assent under the contractual framework of the DGCL).
\item \textsuperscript{102} Kidsco, 674 A.2d at 492-93; \textit{see also} 8 Del. C. § 109(b).
\item \textsuperscript{103} 763 F. Supp. 2d 1170, 1174 (N.D. Cal. 2011); \textit{see Grundfest & Savelle, Forum Selection Provisions}, at 407 (“[I]f the Galaviz analysis stands then much of standard corporate law practice regarding the amendment of bylaws must fall, and much larger bodies of corporate law must be rewritten.”).
\end{itemize}
limited by anyone other than the legislature itself.”

Thus, even though a board may, as is the case here, be granted authority to adopt bylaws, stockholders can check that authority by repealing board-adopted bylaws. And, of course, because the DGCL gives stockholders an annual opportunity to elect directors, stockholders have a potent tool to discipline boards who refuse to accede to a stockholder vote repealing a forum selection clause.

Thus, a corporation’s bylaws are part of an inherently flexible contract between the stockholders and the corporation under which the stockholders have powerful rights they can use to protect themselves if they do not want board-adopted forum selection bylaws to be part of the contract between themselves and the corporation.

And, as noted, precisely because forum selection bylaws are part of a larger contract between the corporation and its stockholders, and because bylaws are interpreted using contractual principles, the bylaws will also be subject to scrutiny under the principles for evaluating contractual forum selection clauses established by the Supreme Court of the United States in *The Bremen v. Zapata Off-Shore Co.*, and adopted by our Supreme Court. In *Bremen*, the Court held that forum selection clauses are valid provided that they are “unaffected by fraud, undue influence, or overweening

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104 *CA, Inc.*, 953 A.2d at 232.
105 See 8 Del. C. § 211.
106 E.g., *MM Cos., Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1127 (Del. 2003) (“This Court has repeatedly stated that, if the stockholders are not satisfied with the management or actions of their elected representatives on the board of directors, the power of corporate democracy is available to the stockholders to replace the incumbent directors when they stand for re-election.” (citations omitted)).
107 E.g., *Airgas, Inc. v. Air Prods. & Chems., Inc.*, 8 A.3d 1182, 1188 (Del. 2010).
bargaining power,” and that the provisions “should be enforced unless enforcement is shown by the resisting party to be ‘unreasonable.’”110 In Ingres, our Supreme Court explicitly adopted this ruling, and held not only that forum selection clauses are presumptively enforceable, but also that such clauses are subject to as-applied review under Bremen in real-world situations to ensure that they are not used “unreasonably and unjustly.”111 The forum selection bylaws will therefore be construed like any other contractual forum selection clause and are considered presumptively, but not necessarily, situationally enforceable.112

In fact, U.S. Supreme Court precedent reinforces the conclusion that forum selection bylaws are, as a facial matter of law, contractually binding. In Carnival Cruise Line v. Shute, the respondent, a cruise ship passenger from Washington State, was injured during the ship’s travel between Los Angeles and Mexico.113 Mrs. Shute tried suing the company in Washington.114 But the fine print on the ticket contained a forum selection clause designating the courts of Florida as an exclusive forum for disputes.115 The Supreme Court held that the forum selection provision, although it was not subject to negotiation and was printed on the ticket she received after she purchased the passage, was reasonable, and thus enforceable.116

110 Bremen, 407 U.S. at 10 (citations omitted).
111 Ingres, 8 A.3d at 1146 (internal quotation marks and citations omitted).
112 Bremen, 407 U.S. at 15.
114 Id.
115 Id. at 587-88.
116 Id. at 594-95.
Unlike cruise ship passengers, who have no mechanism by which to change their tickets’ terms and conditions, stockholders retain the right to modify the corporation’s bylaws. That plaintiffs did not vote on the bylaws at the time of their adoption is not relevant to the question of whether the bylaws are valid or contractually binding under Delaware law. Like any other bylaw, which may be unilaterally adopted by the board and subsequently modified by stockholders, these bylaws are enforced according to their terms. Thus, they will be enforced just like any other forum selection clause.

In sum, stockholders contractually assent to be bound by bylaws that are valid under the DGCL—that is an essential part of the contract agreed to when an investor buys stock in a Delaware corporation. Where, as here, the certificate of incorporation has conferred on the board the power to adopt bylaws, and the board has adopted a bylaw consistent with 8 Del. C. § 109(b), the stockholders have assented to that new bylaw being contractually binding. Thus, Count IV of the complaints cannot survive and the bylaws are contractually valid as a facial matter.

B. The Plaintiffs’ Parade Of Horribles Are Not Facial Challenges To The Bylaws And Do Not Make The Bylaws Inconsistent With Law

The plaintiffs try to show that the forum selection bylaws are inconsistent with law and thus facially invalid by expending much effort on conjuring up hypothetical as-applied challenges in which a literal application of the bylaws might be unreasonable. For reasons the court has explained, these hypotheticals are not appropriately posed.

Rather, if a plaintiff believes that a forum selection clause cannot be equitably enforced in a particular situation, the plaintiff may sue in her preferred forum and respond to the defendant’s motion to dismiss for improper venue by arguing that, under *Bremen*, the forum selection clause should not be respected because its application would be unreasonable.  

The plaintiff may also argue that, under *Schnell*, the forum selection clause should not be enforced because the bylaw was being used for improper purposes inconsistent with the directors’ fiduciary duties. The plaintiffs argue that following regular order in this manner puts a potential plaintiff in the predicament of potentially breaching the bylaws and suffering if the court upholds the forum selection clause and dismisses her case, rendering the plaintiff liable for damages. But that predicament is the same as is faced by any party that seeks to bring a case outside the forum designated in an applicable forum selection clause. And if a potential plaintiff does not have confidence in the strength of her argument under *Bremen* that the forum selection clause does not reasonably apply to the case she seeks to bring, she can always choose to file the case in the forum designated in the bylaws.

Review under *Bremen* and its progeny is genuine, not toothless. Indeed, the *Bremen* doctrine exists precisely to ensure that facially valid forum selection clauses are

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120 See, e.g., *Doe 1 v. AOL, LLC*, 552 F.3d 1077 (9th Cir. 2009) (holding that a forum selection clause was unenforceable, because it barred plaintiffs from bringing a consumer class action under California law); *Cent. Nat’l-Gottesman, Inc. v. M.V. “Gertrude Oldendorff,”* 204 F. Supp. 2d 675 (S.D.N.Y. 2002) (holding that a forum selection clause requiring the plaintiff to litigate abroad was unenforceable because the plaintiff would be deprived of statutory remedies). See generally 14D Charles Alan Wright et al., *Federal Practice & Procedure* § 3803.1 n.5 (3d ed. updated 2013) (collecting federal cases where forum selection clauses were not enforced).
not used in an unreasonable manner in particular circumstances. Our Supreme Court and this court have in the past applied an analysis similar to *Bremen* to hold that forum selection clauses are situationally unenforceable. For example, in the *TransAmerican Natural Gas* case, Justice Berger, then-Vice Chancellor, declined to issue an injunction to enforce a forum selection clause designating this court as the exclusive forum for a contract dispute, because this court did not, as a matter of positive Delaware law, have subject matter jurisdiction over the controversy. The Supreme Court affirmed, holding that the litigation could proceed in the forum that the plaintiff in the non-Delaware action had chosen, which was a court of general jurisdiction.

But, the plaintiffs seek to undermine *Bremen* by using a facial challenge as a way to get this court to address conjured-up scenarios. Under our law, our courts do not render advisory opinions about hypothetical situations that may not occur. Rather, as

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123 *El Paso Natural Gas Co. v. TransAm. Natural Gas Corp.*, 669 A.2d 36 (Del. 1995). For other cases in which the courts of this state have declined to enforce forum selection clauses, see *Aveta, Inc. v. Colon*, 942 A.2d 603, 607 n.7 (Del. Ch. 2008), in which the Court of Chancery held that a forum selection clause was unenforceable, applying a standard “probably tantamount to the federal [Bremen] standard”; and *Brandywine Balloons, Inc. v. Custom Computer Service, Inc.*, 1989 WL 63968, at *4 (Del. Super. Ct. June 13, 1989), in which the Superior Court denied a motion to dismiss a suit under a forum selection clause, on the ground that enforcing the clause “would seriously impair the plaintiff’s ability to pursue his cause of action” (citation and internal quotation marks omitted).
124 See, e.g., *Paramount Commc’ns Inc. v. QVC Network Inc.*, 637 A.2d 34, 51 (Del. 1993) (“It is the nature of the judicial process that we decide only the case before us . . . .”); *Stroud v. Milliken Enters., Inc.*, 552 A.2d 476, 479 (Del. 1989) (“[T]his Court’s jurisdiction . . . does not require us to entertain suits seeking an advisory opinion or an adjudication of hypothetical questions . . . .” (citation and internal quotation marks omitted)); see also *Opinion of the Justices*, 314 A.2d 419 (Del. 1973) (declining to issue an advisory opinion on the ground that such an opinion was not authorized under 10 Del. C. § 141).
in other contexts, the time for a plaintiff to make an as-applied challenge to the forum selection clauses is when the plaintiff wishes to, and does, file a lawsuit outside the chosen forum. At that time, a court will have a concrete factual situation against which to apply the Bremen test, or analyze, à la Schnell,\(^{125}\) whether the directors’ use of the bylaws is a breach of fiduciary duty.

The absence of any principled basis to complete the law school hypotheticals posed by the plaintiffs is also made clear by the reality that the plaintiffs concede, as they must, that in the main, the forum selection bylaws will work without any problem.\(^{126}\) As noted earlier, in their opening brief, the defendants outlined the types of claims that the forum selection bylaws cover.\(^{127}\) Consistent with the plain language of the bylaws and the plaintiffs’ own description of the covered claims in their complaints,\(^{128}\) the defendants’ brief makes clear that the forum selection bylaws are addressed solely to internal affairs claims governed by state corporate law. In other words, the forum selection bylaws only regulate where a certain set of claims, relating to the internal affairs of the corporation and governed by the law of the state of incorporation, may be brought, not what claims.\(^{129}\)


\(^{127}\) Defs.’ Opening Br. 30-31.

\(^{128}\) Chevron Supp. ¶ 1, 28-31; FedEx Compl. ¶ 20-22; see also Pls.’ Br. in Opp’n 4-5.

\(^{129}\) See Grundfest & Savelle, Forum Selection Provisions, at 370 (“[Forum selection] provisions do not purport to regulate a stockholder’s ability to bring a securities fraud claim or any other claim that is not an intra-corporate matter, and the dominant forms of [forum selection] provisions are drafted expressly to preclude such applications.”); id. at 373 (“Because the substantive resolution of these intra-corporate disputes are, pursuant to the internal affairs doctrine, governed by the laws of the chartering state, [forum selection] provisions cannot at all influence the substantive law governing the resolution of the underlying disputes.”).
In other words, the plaintiffs cannot even reasonably contend that the bylaws are intended to do more than address where claims clearly involving the internal affairs of the corporation and thus governed by the law of the state of incorporation must be brought. And the plaintiffs fail to make any reasoned argument that the forum selection bylaws cannot operate sensibly as to the bulk of typical internal affairs cases, where the traditional defendants are the directors and top officers of the corporations, subject to jurisdiction under 10 Del. C. § 3114.130

Perhaps recognizing this weakness in their position, the plaintiffs conjure up situations where there might be a stray defendant or two who is not subject to personal jurisdiction in the state of incorporation, but may be susceptible to service elsewhere.131 In that situation, they say, the bylaws might not operate reasonably. But, of course, the plaintiffs ignore the reality that the bylaws might operate reasonably even then. For example, there may be no forum anywhere in which all possible defendants would be subject to personal jurisdiction. Nor is it apparent that it would be unreasonable to require a plaintiff to bring an internal affairs claim in the courts of the state of incorporation against the numerous corporate defendants who will be indisputably subject to the state’s personal jurisdiction, simply because a few other defendants have to be sued elsewhere. And in the case of the most common type of litigation where filing of internal affairs claims in corporate litigation occurs—those involving challenges to proposed

130 10 Del. C. § 3114 (a)-(b) (providing that nonresident directors and top officers of Delaware corporations consent to the appointment of the corporation’s agent or the Secretary of State to receive service of process).
131 Chevron Compl. ¶¶ 82-87, FedEx Compl. ¶¶ 81-86 (Count V).
mergers—the plaintiffs ignore the multiple tools that exist to allow the courts of the state of incorporation to hold parties accountable to stockholders claiming that their rights were violated. This includes the broad reach of 10 Del. C. § 3114, which now covers not only all directors, but, as mentioned, also key officers, and other jurisdictional doctrines that usually make it possible for a plaintiff to hale all the key defendants before this state’s courts. Not only that, the plaintiffs ignore that corporations such as Chevron and FedEx that have adopted forum selection bylaws will have an incentive to encourage officers, employees and affiliates not covered by § 3114 to consent to jurisdiction in the forum identified by the bylaws, and can accomplish that easily by conditioning the provision of advancement and indemnification on assent to jurisdiction in Delaware over the types of claims covered by the bylaws, or by including consent-to-jurisdiction provisions in employment agreements.

132 See 74 Del. Laws ch. 83, § 3 (2003) (codified at 10 Del. C. § 3114(b)).

133 These doctrines include the aiding and abetting and conspiracy theories used in conjunction with the long-arm statute, 10 Del. C. § 3104. See, e.g., Matthew v. Fläkt Woods Gp. SA, 56 A.3d 1023, 1027-28 (Del. 2012) (applying the conspiracy theory of jurisdiction in conjunction with 10 Del. C. § 3104); Hercules Inc. v. Leu Trust & Banking (Bahs.) Ltd., 611 A.2d 476, 481-82 (Del. 1992) (same); In re Am. Int’l Gp., Inc., 965 A.2d 763, 814 (Del. Ch. 2009) (“The conspiracy theory of jurisdiction has often been used by plaintiffs in concert with . . . 10 Del. C. § 3104.”); see also HMG/Courtland Props., Inc. v. Gray, 729 A.2d 300, 308 (Del. Ch. 1999) (noting that the agency, alter ego, and conspiracy theories can be used in conjunction with 10 Del. C. § 3104 “to advance Delaware’s interest in holding aiders and abettors accountable”). Many other potential defendants, such as merger partners, investment banks, and law firms, are often either domiciled in Delaware or have sufficient contacts with the state to be susceptible to personal jurisdiction. See, e.g., Sample v. Morgan, 935 A.2d 1046, 1063-65 (Del. Ch. 2007) (finding that Delaware had jurisdiction over a law firm that prepared an amendment to a Delaware corporation’s certificate that was the subject of the lawsuit); Derdiger v. Tallman, 773 A.2d 1005 (Del. Ch. 2000) (suit against target board for breach of fiduciary duty, and acquiring corporation for aiding and abetting breach of fiduciary duty); Final Order & J., In re El Paso Corp. S’holders Litig., C.A. No. 6949-CS (Del. Ch. Dec. 3, 2012) (settlement of law suit against target company board for breach of fiduciary duty, and financial advisor for aiding and abetting breach of duty, in which the financial advisor contributed to the settlement payment); Final Order & J., In re Del Monte Foods Co. S’holders Litig., C.A. No. 6027-VCL (Del. Ch. Dec. 1, 2011) (same).
Similarly, the plaintiffs’ attempts to show that there might be situations when the forum selection bylaws would not operate reasonably because they could somehow preclude a plaintiff from bringing a claim that must be brought exclusively in a federal court also is inappropriate and unconvincing as a way to show that the forum selection bylaws are facially invalid. For one thing, these arguments do not even pertain to the Chevron bylaw, which was amended to allow a filing in the federal courts of the state of incorporation. For another thing, it bears repeating that in the main, and as the plaintiffs themselves concede, the kind of cases in which claims covered by the forum selection clause predominate are already overwhelmingly likely to be resolved by a state, not federal, court. And as with the issue of personal jurisdiction, the plaintiffs ignore a number of factors that suggest that their hypothetical concern that the forum selection clause will operate unreasonably is overstated. For example, it is common for derivative actions to be filed in state court on behalf of corporations coincident to the filing of federal securities claims exclusively within the jurisdiction of the federal courts. And with good reason. The corporation is usually a defendant in the federal action. Any stockholder seeking to bring a derivative suit on behalf of the corporation has to act in the best interest of the corporation and cannot therefore sue it for damages.

134 Tr. of Oral Arg. 64:8–65:6.
simultaneously. ¹³⁶ In these situations, the derivative suits typically seek recompense from the directors on behalf of the corporation for any harm the corporation may suffer if it has to pay damages or incur other loss because the directors caused the corporation to breach the securities laws. ¹³⁷ It is not at all evident that in these situations, the application of the bylaws would operate unreasonably. Indeed, the strength of Bremen and situational fiduciary duty review is that any such argument is presented in an actual case with concrete facts.

On their face, neither of the forum selection bylaws purports in any way to foreclose a plaintiff from exercising any statutory right of action created by the federal government. Rather, the forum selection bylaws plainly focus on claims governed by the internal affairs doctrine and thus the law of the state of incorporation. In the event that a plaintiff seeking to bring a claim within the exclusive jurisdiction of the federal courts is met with a motion to dismiss because of the forum selection clause, the plaintiff will have the most hospitable forum possible to address the motion by pressing an argument that the bylaw cannot operate to foreclose her suit—a federal court. For example, if a claim under SEC Rule 14a-9 was brought against FedEx and its board of directors in federal court and the defendants moved to dismiss because of the forum selection clause, they

¹³⁶ See, e.g., Ruggiero v. Am. Bioculture, Inc., 56 F.R.D. 93, 95 (S.D.N.Y.1972) (“[I]t is difficult to see how the . . . plaintiffs can reconcile their existing duties to [the company] and its present shareholders as derivative plaintiffs with the duties which they seek to assume on behalf of a class which attacks [the company].”); see also Fed. R. Civ. Pro. 23.1(a) (“The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of shareholders or members who are similarly situated in enforcing the right of the corporation or association.”).
would have trouble for two reasons. First, a claim by a stockholder under federal law for falsely soliciting proxies does not fit within any category of claim enumerated in FedEx’s forum selection bylaw. Thus, FedEx’s bylaw is consistent with what has been written about similar forum selection clauses addressing internal affairs cases: “[Forum selection] provisions do not purport to regulate a stockholder’s ability to bring a securities fraud claim or any other claim that is not an intra-corporate matter.” Second, the plaintiff could argue that if the board took the position that the bylaw waived the stockholder’s rights under the Securities Exchange Act, such a waiver would be inconsistent with the antiwaiver provisions of that Act, codified at 15 U.S.C. § 78cc. But, the court declines to wade deeper into imagined situations involving multiple “ifs” because rulings on these situationally specific kind of issues should occur if and when the need for rulings is actually necessary.

As a distinguished scholar has pointed out, there likely are pragmatic solutions to the imagined scenarios that the plaintiffs cite, which would both respect the forum selection bylaws’ requirement that state law internal affairs claims be adjudicated in the courts of the state of incorporation, while preserving any substantive claims that must be

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141 See Moran v. Household Int’l, Inc., 500 A.2d 1346, 1357 (Del. 1985) (stating that corporate action “must be evaluated when and if the issue arises”).
brought in federal court. But, for present purposes, the key is that forum selection bylaws, like other forum selection clauses, are not facially invalid because they might operate in a problematic way in some future situation. The situational review *Bremen* requires, and the analogous protections of fiduciary duty review under cases like *Schnitt*, exist to deal with real-world concerns when they arise in real-world and extant disputes, rather than hypothetical and imagined future ones.

The wisdom of declining to opine on hypothetical situations that might or might not come to pass is evident. The waiver provision in the bylaws also counsels against the need to do that, as by that tool, the board, as the statutory instrumentality charged with advancing the corporation’s best interests, is empowered to permit a plaintiff with a claim within the exclusive jurisdiction of a federal court, but which arguably falls within the reach of the bylaw’s language, to proceed. And, the prospective plaintiff may also ask the board to waive the bylaw in a particular circumstance, and if the prospective plaintiff believes that the board’s refusal to waive amounts to a breach of fiduciary duty, the plaintiff may sue for an injunction seeking the board to be required to waive the bylaw’s application. But, under Delaware law, the presumption is not that the Chevron and FedEx directors will not use their waiver authority in good faith and for the best interests of the corporations and their stockholders; it is that they will. In view of that reality, and the fact that Chevron’s and FedEx’s stated reasons for the bylaws have nothing to do with foreclosing anyone from exercising any substantive federal rights, but only with

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channeling internal affairs cases governed by state law to the state of incorporation’s courts, there is no basis on a facial challenge to assume that the bylaws can never operate reasonably.\textsuperscript{144}

But the main point remains the mundane but important one. As with other forum selection clauses, \textit{Bremen} provides protection in the event that a plaintiff believes that the clause is operating in a situationally unreasonable or unlawful manner.\textsuperscript{145} And as with the case of bylaws generally, the board’s use of its powers under the bylaw is subject to challenge as inconsistent with its fiduciary duties in the event of an actual dispute.\textsuperscript{146}

V. Conclusion

For these reasons, the court finds that the challenged bylaws are statutorily valid under 8 \textit{Del. C.} § 109(b), and are contractually valid and enforceable as forum selection clauses. Judgment is entered for the defendants dismissing Counts I and IV of the plaintiffs’ complaints against Chevron and FedEx, with prejudice. IT IS SO ORDERED.

\textsuperscript{144} See Grundfest & Savelle, \textit{Forum Selection Provisions}, at 363-67 (discussing facial challenges to forum selection provisions).
\textsuperscript{145} \textit{The Bremen v. Zapata Off-Shore Co.}, 407 U.S. 1, 15-17 (1972).
CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA
SECOND APPELLATE DISTRICT
DIVISION SEVEN

MT. HAWLEY INSURANCE COMPANY, B234082
Plaintiff and Respondent,

v. 
RICHARD R. LOPEZ, JR.,
Defendant and Appellant.

(Los Angeles County
Super. Ct. No. BC434879)

APPEAL from a judgment of the Superior Court of Los Angeles County,

Manatt, Phelps & Phillips, Amy B. Briggs, Kenneth B. Julian, Benjamin G. Shatz,
and Amanda M. Knudsen, for Defendant and Appellant.

Morison Holden & Prough, William C. Morison and Michael D. Prough, for
Plaintiff and Respondent.
INTRODUCTION

Insurance Code section 533.5, subdivision (b),\(^1\) precludes insurers from providing a defense for certain kinds of claims. The statute provides: “No policy of insurance shall provide, or be construed to provide, any duty to defend . . . any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to” California’s unfair competition law under Business and Professions Code sections 17200 and 17500 “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel, notwithstanding whether the exclusion or exception regarding the duty to defend this type of claim is expressly stated in the policy.” In Bodell v. Walbrook Ins. Co. (9th Cir. 1997) 119 F.3d 1411 (Bodell), the Ninth Circuit held that section 533.5, subdivision (b), applies to criminal actions brought by the four listed state and local agencies but does not apply to criminal actions brought by federal prosecutors. The dissenting judge in Bodell and the trial court in this case concluded that section 533.5, subdivision (b), applies to any criminal action, including federal criminal actions. We agree with the Ninth Circuit and hold that section 533.5, subdivision (b), does not preclude an insurer from agreeing to provide a defense for criminal actions against its insured brought by federal prosecutors. Therefore, the insurer in this case, which had agreed to provide its insureds with a defense in “a criminal proceeding . . . commenced by the return of an indictment” “even if the allegations are groundless, false or fraudulent,” cannot avoid its contractual duty to defend an insured against federal criminal charges by relying on section 533.5, subdivision (b).

FACTUAL AND PROCEDURAL BACKGROUND

1. The Indictment

On January 6, 2010 the United States Attorney for the Central District of California filed a grand jury indictment charging Dr. Richard Lopez with criminal conspiracy, false statements and concealment, and falsification of records. The indictment alleged that Lopez, who was the medical director of the St. Vincent’s Medical

\(^1\) Statutory references are to the Insurance Code unless otherwise indicated.
Center Comprehensive Liver Disease Center, conspired with another doctor and other hospital employees in the liver transplant program to transplant a liver into the wrong patient.²

According to the indictment, Lopez diverted a liver designated for one patient to a different patient who was further down the list of patients waiting for a liver transplant, in violation of regulations promulgated by the United States Department of Health and Human Services under the National Organ Transplant Act, and then covered up his diversion. The indictment alleges that Lopez initially notified the United Network for Organ Sharing (UNOS) that the second patient had received the liver, but later falsely told UNOS that the first patient had received the liver. The indictment further alleges that as a result the first patient never received a liver, “was removed from the liver transplant wait list,” was “thereafter deprived of the opportunity to have this life-saving operation,” and subsequently died. The indictment alleges that Lopez engaged in a cover-up by directing his co-conspirators to restore the second patient’s name to the transplant waiting list (even though the second patient had received the liver designated for the first patient), create a false pathology report for the first patient based on data in the second patient’s pathology report, and alter medical reports to support a claim “that the transplant program had made an honest mistake confusing the names.” The eight-count indictment included alleged violations of title 18 United States Code sections 18 (conspiracy), 1001 (making false statements), and 1519 (destruction, alteration, or falsification of evidence in federal investigations).

2. The Policy

Daughters of Charity Health Systems, Inc. (DCHS), which owns St. Vincent’s, purchased a “Not For Profit Organization and Executive Liability Policy” pursuant to which Mt. Hawley agreed to “pay on behalf of the Insureds, Loss which the Insureds are

² Lopez, using a relatively expansive concept of “success,” contends that “[a]lthough the surgery was successful, the organ was transplanted into the wrong patient.”
legally obligated to pay as a result of Claims . . . against the Insured for Wrongful Acts . . . .” The policy defines “Loss” as “monetary damages, judgments, settlements, including but not limited to punitive, exemplary, multiple or non-contractual liquidated damages where insurable under applicable law, . . . and Defense Expenses which the Insureds are legally obligated to pay as a result of a covered Claim.” The policy further provides that Mt. Hawley “shall have the right and duty to defend any Claim covered by this Policy, even if any of the allegations are groundless, false or fraudulent . . . .” An endorsement defines “claim” to include “a criminal proceeding against any Insured commenced by the return of an indictment” or “a formal civil, criminal, administrative or regulatory investigation against any Insured . . . .” The policy’s definition of “insured” can include employees of St. Vincent’s like Lopez.3

3. The Action

On March 3, 2010 Lopez tendered the defense to the charges to Mt. Hawley. On April 1, 2010 Mt. Hawley, through its attorneys, sent a letter to Lopez declining to defend or indemnify Lopez, and on the same date filed this action. Mt. Hawley’s first amended complaint alleged that a doctor at St. Vincent’s, with Lopez’s “knowledge and approval,” transplanted a liver designated for one patient “who was second in line on the regional waitlist” for a liver into another patient “who was fifty-second on the waiting list,” without prior approval. Mt. Hawley alleged that Lopez “engaged in an elaborate cover-up of the ‘switch,’ which included falsification of documents and encouragement of others to participate in the cover-up.” Mt. Hawley alleged that it had no duty to defend

3 Mt. Hawley does not really contend that Lopez is not an insured under the policy. The closest Mt. Hawley comes to making such an argument is a statement in a footnote that “Dr. Lopez was a stranger to the contract and at best an incidental third-party beneficiary to the extent he qualifies as an ‘insured’ for limited purposes,” and therefore “Mt. Hawley made no representations to him, promising to defend him if he was charged with a crime or otherwise.” We do not read this cryptic sentence as an argument by Mt. Hawley that Lopez is not an insured under the policy. (See Sabi v. Sterling (2010) 183 Cal.App.4th 916, 947 [“[f]ootnotes are not the appropriate vehicle for stating contentions on appeal”].)
Lopez because of section 533.5, a “remuneration exclusion” or “personal profit exclusion,” and a “medical incident exclusion.” Mt. Hawley sought a declaration that it did not owe Lopez a duty to defend or indemnify in connection with the indictment.

Lopez filed a cross-complaint against Mt. Hawley for breach of contract, breach of the implied covenant of good faith and fair dealing, and declaratory relief.

4. The Demurrer and the Motion for Summary Judgment

Lopez filed a motion for judgment on the pleadings on Mt. Hawley’s original complaint and a demurrer to Mt. Hawley’s first amended complaint. Lopez argued in both motions that section 533.5 did not preclude an insurer from providing a defense to federal criminal charges brought by U.S. Attorney’s Office, that the remuneration/personal profit exclusion did not apply because there was no judgment or final adjudication against Lopez, and that the medical incident exclusion did not apply because it was not part of the policy. The trial court rejected Lopez’s argument that section 533.5 did not apply, granted the motion for judgment on the pleadings on the original complaint with leave to amend to allow Mt. Hawley to attach a copy of the policy to the complaint, and then overruled Lopez’s demurrer to the first amended complaint.

Mt. Hawley subsequently filed a motion for summary judgment or in the alternative for summary adjudication. Mt. Hawley argued that it had no duty to defend Lopez against the grand jury indictment “because any defense obligation is excluded by

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4 The remuneration exclusion, subdivision (c) of Exclusion 3, excluded coverage where the insured gains “any profit, remuneration or advantage to which such Insured is not legally entitled if a judgment or final adjudication adverse to such Insured establishes that such Insured gained such profit, remuneration or advantage.” The medical incident exclusion, subdivision (g) of Exclusion 3, excluded coverage for rendering or failing to render certain professional services. Mt. Hawley conceded that because of “a clerical error” the medical incident exclusion was not included in the policy, but alleged that “upon realizing the clerical error” Mt. Hawley “immediately notified [Daughters of Charity]” of the mistake and “corrected the clerical error by issuing endorsements which, on their face, are effective as [of] the inception of the insurance contracts of which they were made a part.”
California Insurance Code section 533.5 (b).” Mt. Hawley also argued that it was entitled to summary judgment on its declaratory relief causes of action and on Lopez’s cross-complaint because under section 533.5 Mt. Hawley had no duty to defend or indemnify Lopez. Although both Mt. Hawley and Lopez argued that section 533.5, subdivision (b), was unambiguous and supported their respective proposed interpretations, both sides submitted portions of the legislative history of the statute in support of their positions.

5. The Ruling

The trial court found that “section 533.5 unambiguously bars coverage for criminal actions and proceedings” and that “the plain language of section 533.5 bars Mt. Hawley’s duty to defend or indemnify Dr. Lopez against the Indictment.” The trial court acknowledged that “the legislative history seems to indicate that section 533.5 was enacted in response to difficulties that the Attorney General had encountered in settling actions under the unfair competition law due to the participation of insurance companies,” but “perceive[d] nothing in the legislative history from which it could clearly conclude that section 533.5 was intended to apply to state and local criminal actions only as opposed to all criminal actions, including federal proceedings.” The trial court concluded that “the correct interpretation of [section] 533.5 is that the enumeration of state, county and local prosecutors ought to be read as referring only to civil actions for unfair competition and false advertising. And that the prohibition against furnishing a defense in a criminal action applies regardless of the entity that commenced the criminal prosecution.” The trial court stated that the Ninth Circuit’s decision in Bodell was not binding and was unpersuasive, and concluded that the Bodell court’s “analysis of [section] 533.5, is in error.” The trial court therefore granted Mt. Hawley’s motion for summary judgment on Mt. Hawley’s first amended complaint and on Lopez’s cross-complaint.

The trial court entered judgment in favor of Mt. Hawley and against Lopez on June 23, 2011. Lopez filed a timely notice of appeal on June 29, 2011.
DISCUSSION

1. Standard of Review

We review a grant of summary judgment de novo. (Wiener v. Southcoast Childcare Centers, Inc. (2004) 32 Cal.4th 1138, 1142; see Culver Center Partners East #1, L.P. v. Baja Fresh Westlake Village, Inc. (2010) 185 Cal.App.4th 744, 749.) “On appeal from the granting of a motion for summary judgment, we examine the record de novo, liberally construing the evidence in support of the party opposing summary judgment and resolving doubts concerning the evidence in favor of that party.” (Miller v. Department of Corrections (2005) 36 Cal.4th 446, 460.) The de novo standard of review applies to issues of statutory and insurance policy interpretation. (See Bruns v. E-Commerce Exchange, Inc. (2011) 51 Cal.4th 717, 724 (Bruns) “[s]tatutory interpretation is a question of law that we review de novo”]; County of San Diego v. Ace Property & Casualty Ins. Co. (2005) 37 Cal.4th 406, 414 “[w]e apply a de novo standard of review to an order granting summary judgment when, on undisputed facts, the order is based on the interpretation or application of the terms of an insurance policy”]; Sacks v. City of Oakland (2010) 190 Cal.App.4th 1070, 1082 [where the pertinent facts are undisputed and the issue is one of statutory interpretation, “the question is one of law and we engage in a de novo review of the trial court’s determination”].)

A “decision to sustain or overrule a demurrer is subject to de novo review on appeal . . . .” (Montclair Parkowners Assn. v. City of Montclair (1999) 76 Cal.App.4th 784, 790.) “In reviewing an order overruling a demurrer, we accept as true all properly pleaded facts in the complaint and exercise independent judgment to determine whether the complaint states a cause of action as a matter of law.” (Caliber Bodyworks, Inc. v. Superior Court (2005) 134 Cal.App.4th 365, 373; see Boy Scouts of America National Foundation v. Superior Court (2012) 206 Cal.App.4th 428, 438 “[t]he reviewing court accepts as true all facts properly pleaded in the complaint in order to determine whether the demurrer should be overruled”].)
2. The Trial Court Erred in Granting Mt. Hawley’s Motion for Summary Judgment

   a. Section 533.5

   Section 533.5, subdivision (b), as originally enacted in 1988, provided: “No policy of insurance shall provide, or be construed to provide, any duty to defend, as defined in subdivision (c), any claim in any civil or criminal action or proceeding in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, or any city prosecutor, notwithstanding whether the exclusion or exception regarding the duty to defend this type of claim is expressly stated in the policy.”

   In 1990 the Legislature amended section 533.5, subdivision (b), to read substantially as it does now: “No policy of insurance shall provide, or be construed to provide, any duty to defend, as defined in subdivision (c), any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to Chapter 5 (commencing with Section 17200) of Part 2 of, or Chapter 1 (commencing with Section 17500) of Part 3 of, Division 7 of the Business and Professions Code in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, or any city prosecutor, notwithstanding whether the exclusion or exception regarding the duty to defend this type of claim is expressly stated in the policy.” The parties agree that the language “Chapter 5 (commencing with Section 17200) of Part 2 of, or Chapter 1 (commencing with Section 17500) of Part 3 of, Division 7 of the Business

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5 Section 533.5, subdivision (c), provides: “For the purpose of this section, ‘duty to defend’ means the insurer’s right or obligation to investigate, contest, defend, control the defense of, compromise, settle, negotiate the compromise or settlement of, or indemnify for the cost of any aspect of defending any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to Chapter 5 (commencing with Section 17200) of Part 2 of, or Chapter 1 (commencing with Section 17500) of Part 3 of, Division 7 of the Business and Professions Code in which the insured expects or contends that (1) the insurer is liable or is potentially liable to make any payment on behalf of the insured or (2) the insurer will provide a defense for a claim even though the insurer is precluded by law from indemnifying that claim.”
and Professions Code” refers to California’s unfair competition and false advertising laws, commonly referred to as the UCL and the FAL. (See Hill v. Roll Internat. Corp. (2011) 195 Cal.App.4th 1295, 1298.)

In 1991 the Legislature amended section 533.5, subdivision (b), a second time to add county counsel to the list of prosecutors in the statute. Thus, the statute currently reads: “No policy of insurance shall provide, or be construed to provide, any duty to defend, as defined in subdivision (c), any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to” the UCL or the FAL “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel, notwithstanding whether the exclusion or exception regarding the duty to defend this type of claim is expressly stated in the policy.”

No California court has addressed the issue raised by this appeal of whether section 533.5, subdivision (b), precludes an insurer from providing a defense in all criminal actions, including federal criminal actions. In Bodell, supra, 119 F.3d 1411, the Ninth Circuit held that “the phrase ‘sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel’ modifies both ‘any criminal action or proceeding’ and ‘any action or proceeding brought pursuant to [the UCL and FAL],’ and that the statute therefore only precludes the tender of a defense in all criminal actions and certain civil actions brought by state, county or city officials.” (Id. at p. 1416.) The dissent in Bodell argued that the phrase “sought by the Attorney General, any district

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6 In Bank of the West v. Superior Court (1992) 2 Cal.4th 1254, the Supreme Court stated that as originally enacted in 1988, section 533.5 “barred coverage in all civil and criminal actions, whatever the theory of liability, brought by the Attorney General, a district attorney, or a city prosecutor. [Citation.] In 1990, the Legislature limited the statute’s reach to criminal actions and actions under the Unfair Business Practices Act.” (Id. at p. 1271.) This passage suggests that the “limited reach” of the statute as a result of the 1990 amendment also applied only to actions “brought by the Attorney General, a district attorney, or a city prosecutor,” but Bank of the West did not address that issue and the court’s brief discussion of section 533.5 and its history is not conclusive.
attorney, any city prosecutor, or any county counsel” modifies only civil actions or
proceedings brought under the UCL and FAL, not criminal actions.  (ld. at p. 1421
(dis. opn. of Kozinski, J.).) The dissent noted that “the phrase ‘any criminal action or
proceeding’ is separated by the disjunctive ‘or’ from actions brought pursuant to” the
UCL and the FAL.  (Ibid.) Neither the majority nor the dissent in Bodell discussed or
engaged in the three-step analysis for statutory interpretation under California law.

b. California law for interpreting statutes

“We begin with the fundamental rule that our primary task is to determine the
lawmakers’ intent.”  (Delaney v. Superior Court (1990) 50 Cal.3d 785, 798.) “In
construing statutes, we aim ‘to ascertain the intent of the enacting legislative body so that
we may adopt the construction that best effectuates the purpose of the law.’”  (Klein v.
United States of America (2010) 50 Cal.4th 68, 77 (Klein), quoting Hassan v. Mercy
American River Hospital (2003) 31 Cal.4th 709, 715.) California courts “have
established a process of statutory interpretation to determine legislative intent that may
involve up to three steps.”  (Alejo v. Torlakson (2013) 212 Cal.App.4th 768, 786-787
(Alejo).) The “key to statutory interpretation is applying the rules of statutory
construction in their proper sequence . . . as follows: ‘we first look to the plain meaning
of the statutory language, then to its legislative history and finally to the reasonableness
of a proposed construction.’”  (MacIsaac v. Waste Management Collection &

“The first step in the interpretive process looks to the words of the statute
themselves.”  (Alejo, supra, 212 Cal.App.4th at p. 787; see Klein, supra, 50 Cal.4th at
p. 77 [“[w]e look first to the words of the statute, ‘because the statutory language is
generally the most reliable indicator of legislative intent’”].) “If the interpretive question
is not resolved in the first step, we proceed to the second step of the inquiry.  [Citation.]
In this step, courts may ‘turn to secondary rules of interpretation, such as maxims of
construction, “which serve as aids in the sense that they express familiar insights about
conventional language usage.”’  We may also look to the legislative history.  [Citation.]
‘Both the legislative history of the statute and the wider historical circumstances of its enactment may be considered in ascertaining the legislative intent.’ [Citation.] ‘If ambiguity remains after resort to secondary rules of construction and to the statute’s legislative history, then we must cautiously take the third and final step in the interpretive process. [Citation.] In this phase of the process, we apply “reason, practicality, and common sense to the language at hand.” [Citation.] Where an uncertainty exists, we must consider the consequences that will flow from a particular interpretation. [Citation.] Thus, “[i]n determining what the Legislature intended we are bound to consider not only the words used, but also other matters, ‘such as context, the object in view, the evils to be remedied, the history of the times and of legislation upon the same subject, public policy and contemporaneous construction.’ [Citations.]” These “other matters” can serve as important guides, because our search for the statute’s meaning is not merely an abstract exercise in semantics. To the contrary, courts seek to ascertain the intent of the Legislature for a reason—“to effectuate the purpose of the law.””’ (Alejo, at pp. 787-788; see MacIsaac, supra, 134 Cal.App.4th at p. 1084.)

We do not necessarily engage in all three steps of the analysis. “It is only when the meaning of the words is not clear that courts are required to take a second step and refer to the legislative history.” (Soil v. Superior Court (1997) 55 Cal.App.4th 872, 875; accord, Sisemore v. Master Financial, Inc. (2007) 151 Cal.App.4th 1386, 1411; see MacIsaac, supra, 134 Cal.App.4th at 1084 “[i]f ambiguity remains after resort to secondary rules of construction and to the statute’s legislative history, then we must cautiously take the third and final step in the interpretative process”).

c. **Step one: Section 533.5 is not clear and unambiguous**

Mt. Hawley argues that the “plain language of the statute . . . is susceptible to only one, single, reasonable interpretation regarding the defense of criminal actions: that California law bars an insurance contract from providing for the defense of ‘any criminal action or proceeding.’” According to Mt. Hawley, “the statutory language used and enacted by the Legislature has plain meaning” and “[t]here is no need to refer to extrinsic aids to interpretation, specialized rules of grammar, or legislative history.”
In order for us to agree with Mt. Hawley, its proposed interpretation of section 533.5 must be not merely *more reasonable* than any other interpretation, Mt. Hawley’s proposed interpretation must be the *only reasonable* interpretation of section 533.5. (See *Coalition of Concerned Communities, Inc. v. City of Los Angeles* (2004) 34 Cal.4th 733, 737 [“[i]f the statutory language permits more than one reasonable interpretation, courts may consider other aids, such as the statute’s purpose, legislative history, and public policy”]; accord, *Bruns, supra*, (2011) 51 Cal.4th at p. 724; see *Jones v. Lodge at Torrey Pines Partnership* (2008) 42 Cal.4th 1158, 1162-1163 (*Jones*) [“statutory language is not plain” where its “language does lend itself to plaintiff’s interpretation, but . . . that is not the only reasonable interpretation of the statutory language”]; *Chosak v. Alameda County Medical Center* (2007) 153 Cal.App.4th 549, 561-562 [where both plaintiff’s and defendant’s proposed interpretations of statute were reasonable and “the statutory language can bear either meaning,” the court proceeded “to a more detailed consideration of” the purpose and legislative history of the statute “to determine which of the proposed definitions best fits the intent of the Legislature in enacting the statute,” even though one side’s interpretation was “the most obvious” interpretation]; *Ailanto Properties, Inc. v. City of Half Moon Bay* (2006) 142 Cal.App.4th 572, 585-586 (*Ailanto Properties*) [because plaintiff’s proposed interpretation of the statute was not “wholly unreasonable,” statute was ambiguous and court would “turn to the second step of our inquiry and look to the statute’s legislative history to clarify its meaning”].) Mt. Hawley’s interpretation, however, is not the only reasonable one.

There are at least three reasonable interpretations of the statute. One reasonable interpretation, advocated by Mt. Hawley, is that section 533.5, subdivision (b), addresses “two separate and distinct types of actions: any criminal action or proceeding (unqualified), or any action or proceeding brought pursuant to certain specific statutes in which the recovery of a fine, penalty or restitution is sought by certain state and local attorneys (as distinct from such actions brought by private parties).” Under this interpretation, “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel”
modifies “any action or proceeding brought pursuant to” the UCL or FAL, but not “any criminal action or proceeding.” This interpretation precludes insurers from providing a defense in any criminal action, including a criminal action bought by federal prosecutors.

Another reasonable interpretation, advocated by Lopez and adopted by the majority in Bodell, is that section 533.5, subdivision (b), applies to “any criminal action or proceeding” “in which the recovery of a fine, penalty, or restitution is sought by” the four California state and local public agencies listed in the statute, or to “any action or proceeding brought pursuant to [the UCL or the FAL] in which the recovery of a fine, penalty, or restitution is sought by” the four state and local public agencies. Under this interpretation, “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” modifies both “any criminal action or proceeding” and “any action or proceeding brought pursuant to [the UCL and FAL].” This interpretation precludes insurers from providing a defense in criminal or civil actions brought by the state and local agencies listed in the statute, but not in criminal or civil actions brought by federal prosecuting agencies.

Yet another reasonable interpretation, urged by neither Mt. Hawley at all nor by Lopez directly, is that section 533.5, subdivision (b), applies to “any claim” in either a criminal action or proceeding or a UCL or FAL action or proceeding “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel.” Under this interpretation, “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” modifies “any claim,” whether the claim is part of a criminal, UCL, or FAL action or proceeding.

Thus, section 533.5, subdivision (b), is susceptible to at least these three reasonable interpretations. Even the dissenting judge in Bodell did not argue that the language of the statute is clear and unambiguous. (See Bodell, supra, 119 F.3d at
Therefore, we cannot conclude that the language of the statute is clear and unambiguous, and we must proceed to the second step of the interpretive analysis and consider the purpose of the statute, the legislative history, and secondary rules of interpretation.

It may be that at first glance Mt. Hawley’s proposed interpretation is more grammatically natural. Under the first step of the statutory interpretation analysis, however, that is not the test. The issue is whether Mt. Hawley’s proposed interpretation is the only reasonable interpretation. And because it is not, we proceed to step two. (See County of San Diego v. Alcoholic Beverage Control Appeals Bd. (2010) 184 Cal.App.4th 396, 401 [“[w]hen the language is reasonably susceptible of more than one meaning, it is proper to examine a variety of extrinsic aids in an effort to discern the intended meaning,” including, “for example, the statutory scheme, the apparent purposes underlying the statute and the presence (or absence) of instructive legislative history”].)

d. Step two: The statute’s legislative history, the circumstances of its enactment, and maxims of construction

As have the few courts that have considered section 533.5, we now “proceed to the second step of the inquiry,” looking to “the statute’s legislative history,” which “can be very instructive.” (People v. Nelson (2011) 200 Cal.App.4th 1083, 1101; see Ailanto Properties, supra, 142 Cal.App.4th at p. 586 [“[i]n the second step of our interpretive

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7 The dissenting judge in Bodell stated that he agreed with the insurers’ argument that the phrase “‘any criminal conduct or proceeding’ is separated by the disjunctive ‘or’ from actions brought pursuant to California’s unfair competition and false advertising statutes,” which “makes perfect sense because such actions can be brought by both the government and private parties.” (Bodell, supra, 119 F.3d at p. 1421 (dis. opn. of Kozinski, J.).) The dissent concluded that “[a]s applied to the specified civil actions, therefore, the list serves a useful function: It limits the statute’s scope to unfair competition and false advertising actions brought by the government, not those by private parties.” (Ibid.) We agree that this interpretation “makes sense” and is reasonable. But Lopez’s proposed interpretation also makes sense and is reasonable.

8 Bodell, supra, 113 F.3d at pages 1416 to 1417; Bank of the West, supra, 2 Cal.4th at pages 1270 to 1271; AIU Ins. Co. v. Superior Court (1990) 51 Cal.3d 807, 837, footnote 15.
inquiry, we examine the entire history of the Legislature’s enactment and amendment of the statute”). If a statute “is susceptible of multiple interpretations . . . we will divine the statute’s meaning by turning to a variety of extrinsic sources, including the legislative history [citation], the nature of the overall statutory scheme [citation], and consideration of the sorts of problems the Legislature was attempting to solve when it enacted the statute [citation].” (Clayworth v. Pfizer, Inc. (2010) 49 Cal.4th 758, 770.) In addition, an “examination of the original text of the statute and the evolution of the language” of a statute that has been amended is “useful in ascertaining its current meaning.” (Ailanto Properties, at p. 586.)

i. Legislative history

We look to the Legislative Counsel’s digest and other summaries and reports indicating the Legislature’s intent. “Although the Legislative Counsel’s summary digests are not binding, they are entitled to great weight.” (Van Horn v. Watson (2008) 45 Cal.4th 322, 332, fn. 11; accord, Jones, supra, 42 Cal.4th at p. 1170; see People v. Superior Court (Lavi) (1993) 4 Cal.4th 1164, 1178 [Legislative Counsel’s digest is indicative of legislative intent]; Martin v. PacifiCare of California (2011) 198 Cal.App.4th 1390, 1402.) The Legislative Counsel’s digest “constitutes the official summary of the legal effect of the bill and is relied upon by the Legislature throughout the legislative process,” and thus “is recognized as a primary indication of legislative intent.” (Souvannarath v. Hadden (2002) 95 Cal.App.4th 1115, 1126, fn. 9.) In addition, “[c]ommittee reports are often useful in determining the Legislature’s intent.” (California Teachers Assn. v. Governing Bd. of Rialto Unified School Dist. (1997) 14 Cal.4th 627, 646; see Tesco Controls, Inc. v. Monterey Mechanical Co. (2004) 124 Cal.App.4th 780, 793.) “In construing a statute, legislative committee reports, bill reports, and other legislative records are appropriate sources from which legislative intent may be ascertained.” (In re John S. (2001) 88 Cal.App.4th 1140, 1144, fn. 2; see Valley Vista Services, Inc. v. City of Monterey Park (2004) 118 Cal.App.4th 881, 889 [“[w]hen construing a statute, we may consider its legislative history, including committee and bill reports, and other legislative records”).) “Relevant material includes: legislative
committee reports; Legislative Analyst’s reports; and testimony or argument to either a house of the Legislature or one of its committees,” but “[m]aterial showing the motive or understanding of an individual legislator, including the bill’s author, his or her staff, or other interested persons, is generally not considered.” (Metropolitan Water Dist. v. Imperial Irrigation Dist. (2000) 80 Cal.App.4th 1403, 1425-1426.)

A. The 1988 enactment of section 533.5

The legislative history of section 533.5 reveals two unmistakable and undisputed facts about the 1988 statute. First, the Legislature intended the statute to apply equally to civil and criminal actions brought by the three (at the time) listed state and local public entities that seek to recover a fine, penalty or restitution, and not to actions brought by federal agencies. As originally enacted in 1988, section 533.5, subdivision (b), applied to “any claim in any civil or criminal action or proceeding in which the recovery of a fine, penalty, or restitution is sought by” the Attorney General, a district attorney, and a city prosecutor. The Legislative Counsel’s digest states that Assembly Bill No. 3920 (AB 3920), the bill that would become section 533.5, “would prohibit insurance coverage or indemnity for the payment of any fine, penalty, or restitution in any civil or criminal action or proceeding brought by specified law enforcement entities . . . .” (Legis. Counsel’s Dig., AB 3920 (1987-1988 Reg. Sess.) at p. 1.)

Committee analyses and reports confirm the Legislative Counsel’s understanding. (See Ailanto Properties, supra, 142 Cal.App.4th at pp. 589-590.) An analysis for the Assembly Committee on Finance and Insurance stated that AB 3920 would prohibit “any policy of insurance providing, or being construed to provide, coverage or indemnity for the payment of fine, penalty, or restitution in any civil or criminal action brought by the Attorney General, district attorney, or city attorney regardless of what the policy says.” (Assem. Com. on Finance and Ins., Analysis of AB 3920 (1987-1988 Reg. Sess.) Apr. 19, 1988, p. 1.) The bill also would prohibit “any insurance policy from providing, or being construed to provide, any duty to defend any claim” “in any civil or criminal action brought by” the three specified public entities. (Ibid.) Thus, as the Supreme Court noted in 1990, the original version of section 533.5 “on its face . . . [did] not apply to relief
sought by the federal government . . .” (AIU Ins. Co., supra, 51 Cal.3d at p. 837, fn. 15
[emphasis in original]; see Bank of the West, supra, 2 Cal.4th at p. 1271.)

Second, the Legislature enacted section 533.5 to address a problem the Attorney
General had encountered (only) in UCL and FAL actions and to address a specific
problem that public entities were experiencing when they brought unfair competition or
false advertising actions, whether civil or criminal, against individuals and businesses.
According to the Attorney General, the bill’s sponsor and principal supporter, section
533.5 was intended to facilitate “the consumer protection activities of our office and local
district attorneys and city attorneys.” (See Catlin v. Superior Court (2011) 51 Cal.4th
300, 305-306 [considering a letter to Senate and Assembly Committees on Public Safety
expressing the Attorney General’s concerns about proposed legislation as part of the
legislative history].)

The Attorney General argued to the Assembly Committee on Finance and
Insurance that the proposed new law would address “a problem which arises under
current law when the Attorney General or a district attorney seeks to enforce [the UCL
and FAL],” because “[i]n many instances” the defendants were claiming “that the
conduct involved is covered by their business insurance policy.” (Office of the Atty.
Apr. 19, 1988.) The Attorney General complained that defendants “tendered the defense
of the action[s] to insurers whose policies provide general liability coverage which may
include coverage for advertising and unfair competition claims.” (Office of the Atty.
public entity then found itself litigating with an insurance company, “rather than the
individual whose conduct violated provisions of the Business & Professions Code,” a
practice that made “no public policy sense.” (Office of the Atty. Gen., Stmt. AB 3920
cases became “impossible to settle because the defendants refuse[d] to make restitution of
unlawfully obtained property or to pay any civil penalty out of their own funds,” and law
enforcement agencies would not accept any settlement “paid by the insurer because such
a settlement does not impose any penalty for unlawful conduct directly on the defendant and permits the defendant to retain the ill-gotten gains . . . . [¶] As a result, the cases consume a large measure of prosecutorial resources during extensive litigation financed without cost to the defendant by the insurer which should have no obligation to pay the judgment ultimately awarded.” (Office of the Atty. Gen., Bill Proposal Summary of AB 3920, supra, at p. 1.) For this reason, the Attorney General proposed and urged the Legislature to enact section 533.5 “to hold individuals personally accountable for behavior [that] constitutes an unfair business practice or false and misleading advertising,” in order to avoid “the litigation becom[ing] a contest between the public entity and the insurance company in which the involvement of the person whose conduct is at issue is almost negligible.” (Assem. Com. on Finance and Ins., Analysis of AB 3920, supra, at p. 2.)

The Attorney General also argued to the Assembly Committee on Finance and Insurance and the Senate Insurance Committee that “[m]ost businesses purchase insurance to protect against losses arising from the operation of the business. Although existing law expressly prohibits insurance for losses incurred as a result of an insured’s willful misconduct, the Attorney General’s office frequently encounters problems enforcing [the UCL and FAL] because business defendants claim that the conduct involved is covered by their business insurance policies. If there is any ambiguity as to the potential liability of the insurance company, and there often is because there is no statute expressly dealing with this issue, the insurance company is obligated to defend the business. [¶] . . . [¶] Instead of individual accountability, the litigation becomes a contest between the public entity and the insurance company in which the involvement of the person whose conduct is at issue is almost negligible.” (Office of the Atty. Gen., letters to Assemblyman Patrick Johnston, Chair of the Assem. Com. on Finance and Ins., and Senator Alan Robbins, Chair of The Senate Ins. Com. AB 3920, Apr. 12, 1988, pp. 1-2.) The Attorney General explained that “[c]ases brought under [the UCL and FAL] do not involve the private victim’s right to compensation for losses. Rather, the public entities are seeking civil and/or criminal penalties, fines, and perhaps restitution as well. No
legitimate public purpose is served by allowing such fines and penalties to be paid by insurance companies; nor is there any valid purpose served by forcing insurance companies to provide defenses in such cases solely because the insurance policy coverage is ambiguous.” (Office of the Atty. Gen., letters to Assemblyman Patrick Johnston and Senator Alan Robbins AB 3920, Apr. 12, 1988, at p. 2.)

B. The 1990 amendment

In 1990 the Legislature amended section 533.5, subdivision (b), by enacting what was referred to as a “clean-up bill” from the Attorney General, Assembly Bill No. 3334 (AB 3334). The legislative history reveals two unmistakable and undisputed facts about the 1990 amendment.

First, the legislative history makes clear that the Legislature did not intend the 1990 amendment to the statute to expand the reach of section 533.5, subdivision (b). The Legislative Counsel’s digest stated that the bill to amend section 533.5 was designed to “restrict the civil actions to which those limitations apply . . . .” (Legis. Counsel’s Dig., AB 3334 (1989-1990 Reg. Sess.) Stats. 1990, ch. 1512.) The Assembly Committee on Finance and Insurance analysis stated that AB 3334, “like its 1988 predecessor, is sponsored by the Attorney General, to reinforce the notion that person[s] violating our unfair competition and unfair advertising law may not use their insurance coverage to evade the personal consequences of wrongdoing. This proposition is not in controversy.” (Assem. Com. on Finance and Ins., Analysis of AB 3334 (1989-1990 Reg. Sess.) Apr. 17, 1990, p. 1.) The committee analysis stated that the amendment “seeks to conform current law to its originally declared purpose while avoiding any adverse effect, one way or another, upon other issues of insurance contract coverage.” (Id. at p. 2.) There is nothing in the legislative history indicating that the Legislature intended to expand the scope of the statute. (See Donovan v. Poway Unified School Dist. (2008) 167 Cal.App.4th 567, 597 [“the absence of legislative history [can] be of significance in deciphering legislative intent”], citing Jones, supra, 42 Cal.4th at p. 1169; Starving Students, Inc. v. Department of Industrial Relations (2005) 125 Cal.App.4th 1357, 1363 [court can consider “the presence (or absence) of instructive legislative history”].)
Second, the Legislature intended the 1990 amendment to address a specific problem that state and local public entities had encountered arising from insurance companies’ use of section 533.5, subdivision (b), to avoid paying for environmental cleanup costs. The new problem arose because of “the use of the overbroad civil action reference,” which created “other insurance coverage issues . . . which were not remotely considered by the Legislature in connection with the 1988 legislation . . . .” (Assem. Com. on Finance and Ins., Analysis of AB 3334, supra, at p. 2.) This coverage issue arose because insurers were arguing in court that section 533.5 precluded and excused them from providing coverage under a “Comprehensive General Liability Policy for the cost of toxic waste cleanup when a business is sued by the state or federal government . . . .” (Ibid.) As the Assembly Finance and Insurance Committee Republican Analysis explained, the original statute “prohibited insurers from paying for fines arising from unfair business practices. Since then it has been interpreted to prevent insurers to cover [sic] certain toxics costs. That was never the author’s or the sponsor’s intent. This bill clarifies that.” (Assem. Com. on Finance and Ins., Republican Analysis of AB 3334 (1989-1990 Reg. Sess.) Apr. 10, 1990.)

The Attorney General, who proposed the 1990 amendment as he had the original 1988 legislation, argued to the Assembly Finance and Insurance Committee that “Insurance Code section 533.5 was proposed due to the concerns about insurance companies being involved, on behalf of insured businesses, in the defense and settlement of cases brought under the unfair competition and false advertising statutes.” (Office of the Atty. Gen., letter to Assemblyman Patrick Johnston, Chair of the Assem. Finance and Ins. Com. AB 3920, Apr. 10, 1990, p. 1.) The problem in 1988, the Attorney General noted, was that “businesses were unwilling to pay penalties or restitution to defrauded customers out of their own funds, as long as they had [] pending claims against insurance companies,” which meant that “unfair competition and false advertising cases were dragging out and consuming a large measure of prosecutorial resources.” (Ibid.) The Attorney General explained that, to resolve these problems, the Legislature enacted section 533.5, which “prohibits insurance coverage for fines, penalties, and restitution in
any civil or criminal action brought by the Attorney General, district attorneys, and city attorneys.” (Ibid.)

In the area of environmental cleanup costs, however, insurers were taking the position “that state agencies are precluded from arguing that damages within the meaning of the typical liability policy include environmental clean up costs because such costs are in the nature of equitable restitution.” (Office of the Atty. Gen., letter to Assemblyman Patrick Johnston, Chair of the Assem. Finance and Ins. Com. AB 3920, supra, p. 2.) Thus, insurance companies were interpreting “restitution more broadly in order to restrict their liability” for environmental cleanup costs. (Ibid.) This was not the intent of the original statute, and the Attorney General argued that “AB 3334 would clarify the original intent” of section 533.5 and “preserve the potential of maximizing recovery of public funds expended pursuant to statutory programs, such as the superfund regarding release of hazardous substances into the environment . . . .” (Ibid.)

The Assembly Finance and Insurance Committee also considered a lengthy memorandum from the Environmental Section of the Attorney General’s Office entitled “Bill Proposal: Hazardous Waste Insurance.” (See People v. Cruz (1996) 13 Cal.4th 764, 773, fn. 5 [“it is reasonable to infer that those who actually voted on the proposed measure read and considered the materials presented in explanation of it, and that the materials therefore provide some indication of how the measure was understood at the time by those who voted to enact it”].) This memorandum stated that “section 533.5 . . . prohibits insurance coverage for fines, penalties and restitution in any civil or criminal action brought the Attorney General, district attorneys and city attorneys. The Environmental Section proposes an amendment to clarify that section 533.5 is directed at criminal actions and civil law enforcement actions brought under [the UCL and FAL] and does not apply to actions filed under state and federal hazardous substance and hazardous waste control laws.” (Office of the Atty. Gen., Bill Proposal: Hazardous Waste Ins., AB 3334 (1989-1990 Reg. Sess.) undated, p. 1.) The Attorney General noted that “[t]he problem at hand is that Insurance Code section 533.5 was not intended to address the currently active issue of toxic pollution insurance coverage, yet the statute has played,
and undoubtedly will continue to play[,] a role in resolving the coverage question.” (Id. at p. 2.)

Thus, the use of the broad term “any civil action” in the 1988 statute was the problem because it covered more than just UCL and FAL civil actions. As the Attorney General noted, section 533.5 as originally drafted was “too broad, in that it affects many more regulatory activities than consumer protection . . . .” (Office of the Atty. Gen., Bill Proposal, supra, at p. 4.) The statute was supposed to solve a narrow problem in UCL and FAL actions brought by state and local agencies, but it created problems in other kinds of cases. As a result, the Legislature amended the statute so that the prohibition on providing a duty to defend applied to UCL and FAL actions, rather than all civil actions, which insurers were arguing included environmental cleanup actions. As the analysis of AB 3334 from the Assembly Committee on Finance and Insurance explained, the amendment “deletes the general references to civil actions in the 1988 Insurance Code amendments and, instead, substitutes more specific references to proceedings brought pursuant to those portions of the Business and Professions Code governing unfair competition and unfair advertising.” (Analysis of AB 3334, supra, at p. 2.)

Of course, as is often the case with legislative histories, the legislative history of AB 3334 is not always entirely consistent. For example, an analysis prepared for the Senate Committee on Insurance, Claims and Corporations stated that the bill “clarifies that the prohibition against insurance to provide coverage or indemnity for the payment of any fine, penalty or restitution shall apply only to proceedings pertaining to unfair business practices or false or misleading advertisements rather than all civil actions, in addition to criminal actions.” (Sen. Ins., Claims and Corps. Com., Analysis of AB 3334 (1989-1990 Reg. Sess.) Aug. 8, 1990, p. 1.) This fragment of the legislative history can be read to support Mt. Hawley’s position that the 1990 amendment revised section 533.5 to bar insurers from providing a defense in (1) UCL and FAL actions seeking to recover a fine, penalty, or restitution, and (2) criminal actions. As explained above, however, the vast majority of the amendment’s legislative history and the circumstances of its enactment do not support this interpretation. Indeed, the Senate committee analysis went
on to state that the amendment “is needed to avoid any adverse effects that may result as a misinterpretation of the unintended broad reference to ‘any civil action.’” (Id. at p. 2.) The committee analysis also did not discuss the issue of what agency (state or federal) was bringing the action.

Mt. Hawley relies heavily on section 2 of AB 3334, which states that the Legislature’s intent in 1988 in enacting section 533.5 was that it “shall be applicable to insurance coverage and to the duty to defend only in criminal actions and in actions or proceedings brought by the Attorney General, any district attorney, or any city prosecutor, pursuant to [the UCL and the FAL].” (AB 3334 (1989-1990 Reg. Sess.) Stat. 1990, ch. 1512, § 2, subd. (a), p. 2.) This statement suggests that the statute applies to (1) criminal actions and (2) civil actions under the UCL and FAL, as Mt. Hawley contends. This declaration in 1990 of what the Legislature had intended in 1988 is relevant to our inquiry but it is not binding. (See Apple Inc. v. Superior Court (2013) 56 Cal.4th 128, 131 [“the declaration of a later Legislature is of little weight in determining the relevant intent of the Legislature that enacted the law”]; McClung v. Employment Development Dept. (2004) 34 Cal.4th 467, 473 [“a legislative declaration of an existing statute’s meaning’ is but a factor for a court to consider and ‘is neither binding nor conclusive in construing the statute’”].) “Ultimately, the interpretation of a statute is an exercise of the judicial power the Constitution assigns to the courts.” (Western Security Bank v. Superior Court (1997) 15 Cal.4th 232, 244 (Western Security Bank); see In re Retirement Cases (2003) 110 Cal.App.4th 426, 480 [Legislature “has no legislative authority simply to say what it did mean,” but “[c]ourts do take cognizance of such declarations when they are consistent with the original intent”].) In any event, it is undisputed that section 533.5, subdivision (b), as originally enacted in 1988, unambiguously applied only to actions brought by state and local agencies, and not to actions brought by federal agencies.

Moreover, there are other indications in the 1990 legislative record confirming that the Legislature had intended in 1988 that the original statute apply to civil or criminal actions brought by the three named state and local public entities that seek to recover a
fine, penalty or restitution. (See Ailanto Properties, supra, 142 Cal.App.4th at p. 589, fn. 13 ["[w]e may properly rely on the legislative history of subsequent enactments to clarify the Legislature’s intent regarding an earlier enacted statute,” and, while the concept of “‘subsequent legislative history’ may seem oxymoronic, it is well established that ‘the Legislature’s expressed views on the prior import of its statutes are entitled to due consideration, and we cannot disregard them,’” quoting Western Security Bank, supra, 15 Cal.4th at p. 244]; City of Long Beach v. California Citizens for Neighborhood Empowerment (2003) 111 Cal.App.4th 302, 307, fn. 6 [“[a]lthough a legislative expression of the intent of an earlier act is not binding upon the courts in their construction of the prior act, that expression may properly be considered together with other factors in arriving at the true legislative intent existing when the prior act was passed,’” quoting Eu v. Chacon (1976) 16 Cal.3d 465, 470].) For example, the Legislative Counsel’s digest for AB 3334 stated that under “[e]xisting law . . . no policy of insurance shall provide any [duty to defend] any civil or criminal action or proceeding brought by the Attorney General, any district attorney, or any city prosecutor” for “the payment of any fine, penalty, or restitution.” (Legis. Counsel’s Dig., AB 3334, supra.) An analysis prepared for the Assembly Committee on Finance and Insurance stated that “California law, enacted by the adoption of Assembly Bill 3920 (Johnston) in 1988[,] provides that no policy of insurance shall provide coverage or indemnity for the payment of any fine, penalty, or restitution in any civil or criminal action brought by the Attorney General, any district attorney, or any city prosecutor . . . .” (Analysis of AB 3334, supra, at p. 1.) The committee analysis also confirmed that the purpose of AB 3920 in 1988 “was to ‘hold individuals personally accountable for behavior which constitutes an unfair business practice or false and misleading advertising.’” (Ibid.)

These declarations and statements of prior legislative intent are relevant to our inquiry, but no individual expression is determinative. Section 2 of AB 3334 does not, as Mt. Hawley argues, definitively prove that the Legislature intended (in 1988 or 1990) that “the list of attorneys who are prosecuting an action modifies only those civil actions brought pursuant to the UCL and the [FAL],” and not criminal actions. The entirety of
the legislative history and purpose of the statute show that the Legislature enacted section 533.5 in 1988 to address actions brought by state and local agencies, and then amended section 533.5 in 1990 to limit—not expand—the application of the statute.

C. The 1991 amendment

In 1991 the Legislature again amended section 533.5, subdivision (b), as part of Senate Bill No. 709 (SB 709). SB 709, sponsored by the County of San Bernardino, made a relatively minor change in the UCL by adding county counsel to the list of public entities that can bring UCL actions. The Legislative Counsel’s digest states that the bill would allow “a county counsel authorized by agreement with the district attorney in actions involving violation of a county ordinance to prosecute an action for injunction to enjoin unfair competition.” (Legis. Counsel’s Dig., SB 709 (1990-1991 Reg. Sess.) Stat. 1990, ch. 1195.) The Legislative Counsel’s digest also states that the bill would authorize the county to collect any fine recovered in such an action brought by a county counsel. (Ibid.) Although SB 709 was primarily about amending the UCL, the last section of the bill added county counsel to the group of public entities listed in section 533.5, subdivision (b). (SB 709 (1990-1991 Reg. Sess.) Stat. 1990, ch. 1195, § 4, subds. (a), (b), pp. 3-4.)

Most of the legislative history of SB 709 concerns the issue of adding county counsel to the list of public entities that can bring UCL actions. An analysis of SB 709 prepared for the Senate Committee on Judiciary explains that the bill “would provide that in addition to the Attorney General, the district attorney and the city attorney, any county counsel can bring an action for any violation of, or an injunction pursuant to, specified provisions [of the Unfair Trade Practices Act].” (Sen. Com. on Judiciary, Analysis of SB 709 (1990-1991 Reg. Sess.) May 14, 1991, p. 2.) This analysis contains one of the few references in the legislative history of SB 709 to section 533.5 and confirms that section 533.5, subdivision (b), applies to UCL actions brought by state and local agencies: “Existing law also provides that no policy of insurance shall provide, or be construed to provide[, ] coverage or indemnity of the payment of any fine, penalty, or restitution in any action brought under unfair competition laws brought by the Attorney
General, any district attorney and city attorney.” (Ibid.) There is no indication in the legislative history that the Legislature intended in 1991 to preclude insurers from providing a defense in federal criminal actions, or for that matter in any actions other than UCL and FAL actions brought by state and local public entities.

D. The takeaway

The legislative history of the original 1988 statute and the 1990 and 1991 amendments makes it clear that the purpose of the statute, the circumstances of its enactment, and the Legislature’s goal in enacting the statute, were to preclude insurers from providing a defense in civil and criminal UCL and FAL actions brought by the Attorney General, district attorneys, city attorneys, and (later) county counsel. It is undisputed that the original version of section 533.5, subdivision (b), applied only to criminal and civil actions brought by the Attorney General, a district attorney, or a city attorney seeking the recovery of a fine, penalty, or restitution, and not to actions brought by federal agencies. Although the original version of section 533.5, subdivision (b), did not specifically mention UCL and FAL claims, the Legislature enacted the original statute to address UCL and FAL actions. It was in response to a perceived defect in the wording of the original statute, which allowed insurers to use the statute as a defense in environmental cleanup cases, that the Legislature in 1990 amended the statute to make it clear that the prohibition on providing a defense applied only in UCL and FAL cases brought by the three (and in 1991 four) named state and local agencies. At no time did the Legislature ever intend section 533.5, subdivision (b), to apply to actions other than UCL and FAL actions brought by state and local agencies. 9 At no time did the Legislature ever intend section 533.5, subdivision (b), to apply to criminal actions brought by public entities other than the three and then four enumerated state and local agencies, such as criminal actions brought by the federal prosecuting authorities.

9 Indeed, one federal court stated in 1993 that section 533.5 stands for the principle that there is “no insurance coverage or duty to defend in actions brought under Unfair Business Practices Act.” (Standard Fire Ins. Co. v. Peoples Church of Fresno (9th Cir. 1993) 985 F.2d 446, 449.)
Mt. Hawley’s primary argument on the issue of legislative intent is that “there is no indication that the Legislature intended to distinguish federal from state criminal prosecutions and to permit an insurer-funded defense or indemnity for federal [crimes] while barring it for those brought by the State.” As Lopez concedes, Mt. Hawley is correct: there is nothing in the legislative history suggesting that the Legislature intended or was even thinking about a distinction between state and federal criminal actions and proceedings. (See *People v. Taylor* (2007) 157 Cal.App.4th 433, 439 [noting that the “absence from the legislative history” of a distinction “supports our conclusion that no distinction was intended by the Legislature”].) But that is because the Legislature was thinking about UCL and FAL actions and proceedings, which only state and local agencies bring. As Lopez correctly argues, “[b]ecause federal prosecutors do not enforce the UCL, the Legislature had no reason to include them within the statute’s ambit,” and there was no need to distinguish or even consider actions brought by federal prosecutors. The Attorney General’s expressed concern that UCL and FAL cases were consuming “a large measure of prosecutorial resources” was a concern about state resources, not federal resources. (Bill Proposal Summary of AB 3920, supra, at p. 1.) Indeed, the absence of any discussion regarding, concern about, or mention of federal prosecutions supports Lopez’s position that the Legislature intended the original statute and the two amendments to apply only to criminal or civil UCL actions brought by the listed state and local agencies. As the Supreme Court stated in *Van Horn v. Watson* (2008) 45 Cal.4th 322, “one would expect that, had the Legislature intended to alter the scope of” a statute, “some mention of its intent would have made it into the legislative history. The absence of any such discussion suggests the Legislature did not so intend.” (*Id.* at p. 332, fn. 12.)

**ii. Maxims of construction**

As noted above, section 533.5, subdivision (b), precludes an insurer from defending “any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to [the UCL or the FAL] in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel.” Mt. Hawley argues that the “plain grammatical structure” of
section 533.5, subdivision (b), “compels the conclusion that the list of lawyers contained within the second ‘in any’ prepositional phrase qualifies only those types of actions described within that phrase,” because of the “or” between “criminal action or proceeding” and “any action or proceeding brought pursuant to” the UCL or FAL.

Such grammatical and interpretive aids are important tools, but they are only tools. “The rules of grammar and canons of construction are but tools, ‘guides to help courts determine likely legislative intent. [Citations] And that intent is critical. Those who write statutes seek to solve human problems. Fidelity to their aims requires us to approach an interpretive problem not as if it were a purely logical game, like a Rubik’s Cube, but as an effort to divine the human intent that underlies the statute.” (Burris v. Superior Court (2005) 34 Cal.4th 1012, 1017-1018, quoting J.E.M. AG Supply, Inc. v. Pioneer Hi-Bred Intl., Inc. (2001) 534 U.S. 124, 156 [122 S.Ct. 593, 151 L.Ed.2d 508].)

“Grammar and syntax thus are a means of gleaning intent, not a basis for preventing its effectuation.” (California Redevelopment Assn. v. Matosantos (2011) 53 Cal.4th 231, 269; see Del Cerro Mobile Estates v. City of Placentia (2011) 197 Cal.App.4th 173, 183 [“[a] litigant may not make a ‘fortress out of the dictionary’ [citation], nor similarly employ the rules of grammar”].) Thus, “[w]hile punctuation and grammar should be considered in interpreting a statute, neither is controlling unless the result is in harmony with the clearly expressed intent of the Legislature.” (Zanone v. City of Whittier (2008) 162 Cal.App.4th 174, 189, fn. 16.) Similarly, the “canons of construction . . . are not to be rotely applied in disregard of other indicia of the intent and purpose of the body which enacted the statutory provision in question.” (California Chamber of Commerce v. Brown (2011) 196 Cal.App.4th 233, 258; see Renee J. v. Superior Court (2001) 26 Cal.4th 735, 744 (Renee J.) [“[p]rinciples of statutory construction are not rules of independent force, but merely tools to assist the courts in discerning legislative intent”].)

The human problems that the Legislature was seeking to solve with section 533.5 were first that insurers were providing their business insureds with an indemnity and a defense in UCL and FAL actions brought by state and local public entities, and then later that insurers were using section 533.5 to argue that they did not have to pay for
environmental cleanup costs. The appearance in the 1990 amendment of the second “or any” phrase does not definitively show that the Legislature intended section 533.5, subdivision (b), to apply to all criminal actions, including federal criminal actions. The legislative history is bursting with manifestations of intent to bar indemnity and defense for UCL and FAL actions brought by state and local agencies, and devoid of any indications that the bar would apply to criminal actions brought by federal agencies. We cannot allow technical rules of grammar and construction to defeat the clear legislative intent behind section 533.5. (See Payless Shoesource, Inc. v. Travelers Companies, Inc. (10th Cir. 2009) 585 F.3d 1366, 1371-1372 [“while the rules of English grammar often afford a valuable starting point to understanding a speaker’s meaning, they are violated so often by so many of us that they can hardly be safely relied upon as the end point of analysis”].)

A. The last antecedent rule

Mt. Hawley places considerable reliance on the last antecedent rule. The last antecedent rule provides that “qualifying words, phrases and clauses are to be applied to the words or phrases immediately preceding and are not to be construed as extending to or including others more remote.” (Renee J., supra, 26 Cal.4th at 743; see Genlyte Group, LLC v. Workers’ Comp. Appeals Bd. (2008) 158 Cal.App.4th 705, 717 (Genlyte Group).) Mt. Hawley argues that under the last antecedent rule the phrase “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” modifies “any action or proceeding brought pursuant to” the UCL or FAL, but not the first and more remote “any criminal action or proceeding.”

The last antecedent rule, however, “is ‘not immutable’ and should not be ‘rigidly applied’ in all cases” and has several exceptions. (People ex rel. Lockyer v. R.J. Reynolds Tobacco Co. (2003) 107 Cal.App.4th 516, 530; see In re Phelps (2001) 93 Cal.App.4th 451, 456.) One exception “provides that when several words are followed by a clause that applies as much to the first and other words as to the last, ‘the natural construction of the language demands that the clause be read as applicable to all.’” [Citation] Another
provides that when the sense of the entire act requires that a qualifying word or phrase apply to several preceding words, its application will not be restricted to the last.” (Renee J., supra, 26 Cal.4th at p. 743.) These “exceptions to a rigid or mechanical application of the last antecedent rule . . . are simply another way of stating the fundamental rule that a court is to construe a statute to effectuate the purpose of the law.” (Genlyte Group, supra, 158 Cal.App.4th at p. 717; see Anderson v. State Farm Mut. Auto. Ins. Co. (1969) 270 Cal.App.2d 346, 349-350 [“if the clear intent of the parties is opposed to the application of the rule, the rule must yield”].)

Both of these exceptions to the last antecedent rule apply here. The clause “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” applies “as much to” “any criminal action or proceeding” as to “action or proceeding brought pursuant to [the UCL and FAL].” (See Lickter v. Lickter (2010) 189 Cal.App.4th 712, 726 [last antecedent rule did not apply because qualifying phrase “is just as applicable to the more remote [words] . . . as it is to the immediately preceding term”].) With the exception of county counsel (which we discuss below), the named public entities can bring both criminal actions and civil actions under the UCL and FAL, and can seek fines and restitution in criminal actions and penalties in civil actions. (See Kasky v. Nike, Inc. (2002) 27 Cal.4th 939, 950 [“[i]n a suit under the UCL, a public prosecutor may collect civil penalties”]; People v. Pacific Land Research Co. (1977) 20 Cal.3d 10, 17 [prosecutors can seek restitution under the FAL]; People v. First Federal Credit Corp. (2002) 104 Cal.App.4th 721 [district attorney sought civil penalties under the UCL and FAL].)

In addition, the goal of the legislation that enacted and amended section 533.5, subdivision (b), was to bar insurers from providing a defense in UCL and FAL actions but not in environmental actions brought by state agencies seeking fines, penalties, and restitution. In light of this goal, the “sense” of the entire statute requires that the phrase “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” apply to the words “any
criminal action” and “not be restricted to” civil UCL and FAL actions and proceedings. (See Costco Wholesale Corp. v. Workers’ Comp. Appeals Bd. (2007) 151 Cal.App.4th 148, 154-155 [“[t]he last antecedent rule does not trump” considerations of “the spirit of the statute . . . as a whole”).) There is no indication or “sense” that the Legislature ever intended the statute to apply to criminal actions brought by federal prosecutors, who do not bring actions seeking recovery of a fine, penalty, or restitution under the UCL or the FAL. The last antecedent rule does not mandate an interpretation that section 533.5, subdivision (b), applies to federal criminal actions.10

B. Other maxims

“Statutory language is not considered in isolation. Rather, we ‘interpret the statute as a whole, so as to make sense of the entire statutory scheme.’” (Bonnell v. Medical Bd. of California (2003) 31 Cal.4th 1255, 1261.) We must also “interpret legislative enactments so as to avoid absurd results.” (People v. Torres (2013) 213 Cal.App.4th 1151, 1158.) Relying heavily on and quoting extensively from the dissenting opinion in Bodell, Mt. Hawley argues that the use of the word “recovery” in the phrase “in which the recovery of a fine, penalty, or restitution is sought” by the named public agencies “reinforces [the] insurers’ view that the list of lawyers applies only to civil actions” because a “prosecutor doesn’t seek ‘recovery’ of a conviction in a criminal case.” (Bodell, supra, 119 F.3d at p. 1421 (dis. opn. of Kozinski, J.).)

10 A third exception to the last antecedent rule is the presence of a comma between all of the antecedents and the qualifying phrase (here, between “any criminal action or proceeding” and “any action or proceeding brought pursuant to” the UCL and FAL, and “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel”). There is no comma in section 533.5, subdivision (b), between the two antecedents and the qualifying phrase. Nevertheless, just because the punctuation of a statute “[a]dmittedly . . . is not punctilious” does not justify blind adherence to the last antecedent rule. (Absher v. AutoZone, Inc. (2008) 164 Cal.App.4th 332, 344; see U.S. Nat. Bank of Oregon v. Independent Ins. Agents of America, Inc. (1993) 508 U.S. 439, 454 [113 S.Ct. 2173, 124 L.Ed.2d 402] [“a purported plain-meaning analysis based only on punctuation is necessarily incomplete and runs the risk of distorting a statute’s true meaning”].)
Prosecutors, however, do seek recovery of fines and restitution as a result of a conviction in general, and in UCL and FAL cases in particular. (See, e.g., Bus. & Prof. Code, § 17500 [violation punishable by imprisonment in county jail not to exceed six months, a fine not to exceed $2,500, or both]; People v. Holmberg (2011) 195 Cal.App.4th 1310, 1324 [prosecutor sought victim restitution].) Indeed, prosecutors can waive the imposition of a fine if they do not request it or do not object when the trial court fails to impose it. (See People v. Tillman (2000) 22 Cal.4th 300, 302-303.) And restitution hearings in criminal cases cannot proceed in the absence of the prosecutor, even if the victim is present with counsel. (See People v. Dehle (2008) 166 Cal.App.4th 1380, 1386, 1389 [“[r]estitution hearings held pursuant to section 1202.4 are sentencing hearings and are thus hearings which are a significant part of a criminal prosecution,” and the “goals of a restitution hearing . . . can only be accomplished with the participation of the district attorney acting in accordance with his responsibilities to the criminal justice system”]; see also People v. Smith (2011) 198 Cal.App.4th 415, 434 [“[t]he restitution hearing, whether for economic or noneconomic damages, is a criminal sentencing hearing, not a civil trial”].)

Moreover, the phrase “in which the recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel” cannot modify only “any action or proceeding brought pursuant to [the UCL and FAL],” because fines are not recoverable in civil UCL and FAL actions. Only public entities can prosecute a violation of the UCL and FAL as a misdemeanor and seek a fine pursuant to Business and Professions Code section 17500. (See Kasky v. Nike, Inc., supra, 27 Cal.4th at p. 950 [“[i]n a suit under the UCL . . . a private plaintiff’s remedies are ‘generally limited to injunctive relief and restitution,’” quoting Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co. (1999) 20 Cal.4th 163, 179]; Lavie v. Proctor & Gamble Co. (2003) 105 Cal.App.4th 496, 503 [“Attorney General and district attorneys . . . are authorized to prosecute violations of the UCL criminally (see Bus. & Prof. Code, § 17500) and may also seek redress through the bringing of civil law enforcement cases seeking equitable relief and civil penalties.
beyond those available to private parties (see Bus. & Prof. Code, §§ 17203, 17206, 17535, 17536); \textit{People v. Municipal Court} (1972) 27 Cal.App.3d 193, 201-202 [“crimes are considered to be offenses against the body politic for which the punishment is fine or imprisonment as distinguished from civil wrongs where private redress is obtained through individually prosecuted lawsuits for damages”].) Because fines can only be sought in criminal cases, the phrase must also modify “any criminal action or proceeding,” consistent with the maxim of construction that “our interpretation is faithful to the canon that we must ‘interpret a statute consistently with the meaning derived from its grammatical structure.’” (\textit{Moore v. Hill} (2010) 188 Cal.App.4th 1267, 1281.) If, as Mt. Hawley argues, the phrase modified only “any action or proceeding brought pursuant to [the UCL and FAL],” then the Legislature would have had no reason to include the word “fine” in the statute, thus violating another maxim of construction. (See \textit{Metcalf v. County of San Joaquin} (2008) 42 Cal.4th 1121, 1135 [“rule of statutory interpretation [is] that courts should avoid a construction that makes any word surplusage”]; \textit{Kulshretha v. First Union Commercial Corp.} (2004) 33 Cal.4th 601, 611 [“courts may not excise words from statutes”]; \textit{Moss v. Kroner} (2011) 197 Cal.App.4th 860, 879 [“[i]t is a settled axiom of statutory construction that significance should be attributed to every word and phrase of a statute, and a construction making some words surplusage should be avoided”].)

Again quoting the dissenting opinion in \textit{Bodell}, Mt. Hawley argues that the interpretation we are adopting “makes no sense because at least one of the lawyers listed (the county counsel) cannot bring criminal charges,” that the “circumstances under which ‘county counsel’ was added to the list conclusively undermines the notion that the list has any relevance to criminal prosecutions,” and that “the list only includes those lawyers who are authorized to bring unfair competition and false advertising actions, and has nothing at all to do with criminal prosecutions.” (\textit{Bodell, supra}, 119 F.3d at p. 1421 (dis. opn. of Kozinski, J.).) This argument misunderstands the 1991 amendment. The “circumstances under which ‘county counsel’ was added to the list” were that the Legislature was amending the UCL to allow county counsel to file UCL actions, and amended section 533.5, subdivision (b), accordingly. This history supports the
conclusion that the Legislature enacted section 533.5 to address the problem of insurers providing indemnification and defense in UCL and FAL actions, and to prevent insurers from litigating against state prosecutors in these kinds of cases, not to prevent insurers from providing a defense to insureds in all criminal cases. (See Wotton v. Bush (1953) 41 Cal.2d 460, 467 [“the objective sought to be achieved by a statute as well as the evil to be prevented is of prime consideration in its interpretation”]; All Angels Preschool/Daycare v. County of Merced (2011) 197 Cal.App.4th 394, 403 [where “the plain wording does not answer our question of interpretation, it is appropriate to consider extrinsic aids such as the apparent objective to be achieved and the evils to be remedied by the entire” statute].) Moreover, because county counsel can bring claims, “county counsel” can modify the first “any claim” in section 533.5, subdivision (b). In any event, when the Legislature amended the UCL and section 533.5, subdivision (b), in 1991 to add county counsel to the statute, the Legislature had to put county counsel somewhere, and with the Attorney General, district attorney, and city attorney was the only realistic place county counsel would fit in the statute.

e. Step three: Reason, practicality, and common sense

Although it is not necessary to do so, we confirm our interpretation of section 533.5, subdivision (b), by applying “reason, practicality, and common sense to the language” of the statute. (See Brown v. Valverde (2010) 183 Cal.App.4th 1531, 1552 [although “we need not reach [the] second and third steps” in the analysis, “[w]e nevertheless discuss them . . . as they lend strong support to our conclusion”]; Ailanto Properties, supra, 142 Cal.App.4th at p. 591 [“[a]lthough our review of the legislative history suffices to support our conclusion, applying ‘reason, practicality, and common sense to the language at hand’ confirms that conclusion”].)

Outside the special area of UCL and FAL actions brought by state and local prosecuting agencies, there is no public policy in California against insurers contracting to provide a defense to insureds facing criminal charges, as opposed to indemnification for those convicted of criminal charges. (See Stein v. Internat. Ins. Co. (1990) 217 Cal.App.3d 609, 615 [“[w]hile nothing would preclude [the insurer] from choosing”
to defend the insured’s criminal action, “it is a judgment call to be left solely to the insurer”]; *Ohio Casualty Ins. Co. v. Hubbard* (1984) 162 Cal.App.3d 939, 944 (*Ohio Casualty Ins. Co.*) [“[a]n insurer is not absolved from its duty to defend the lawsuit merely because it is forbidden by law or contract to indemnify the liability-causing action”].) Section 533.5 did not change that law outside of the context of certain actions brought by the listed state and local agencies.\(^{11}\)

To the contrary, courts have held that section 533, a similar but much older statute (enacted in 1935) that prohibits indemnification “for a loss caused by the wilful act of the insured,” does not extinguish an insurer’s duty to defend an insured accused of those wilful actions. (See *Gray v. Zurich Ins. Co.* (1966) 65 Cal.2d 263, 277-278 [“a contract to defend an assured upon mere accusation of a wilful tort does not encourage such wilful conduct”]; *State Farm General Ins. Co. v. Mintarsih* (2009) 175 Cal.App.4th 274, 287 [although “section 533 precluded indemnification . . . coverage” for malicious prosecution, “section 533 did not relieve the insurer of the contractual duty to defend that claim”]; *Marie Y. v. General Star Indemnity Co.* (2003) 110 Cal.App.4th 928, 959 [“[e]ven though public policy or section 533 precludes an insurer from indemnifying an insured in an underlying action the duty to defend still exists so long as the ‘insured reasonably expect[s] the policy to cover the types of acts involved in the underlying suit’”]; *Mez Industries, Inc. v. Pacific Nat. Ins. Co.* (1999) 76 Cal.App.4th 856, 878 (*Mez Industries*) [“where a denial of indemnification is based on the application of section 533, it does not necessarily follow that no duty to defend exists”]; *Downey Venture v. LMI Ins. Co.* (1998) 66 Cal.App.4th 478, 508 (*Downey Venture*) [“[o]bviously, the public policy concerns applicable to an insurer’s indemnification” of a malicious prosecution action because of section 533 “do not extend to the provision of a defense”]; *B & E*  

\(^{11}\) Indeed, the Legislative Counsel’s digest for AB 3920 stated that the new statute’s provisions did “not constitute a change in, but are declaratory of, the existing law.” (Legis. Counsel’s Dig., AB 3920, *supra*, at p. 1.) Existing law in 1988 did not preclude insurance companies from providing a defense, as opposed to indemnity, for criminal charges.

[“[p]ut another way, if the reasonable expectations of an insured are that a defense will be provided for a claim, then the insurer cannot escape that obligation merely because public policy precludes it from indemnifying [it”].) 12 So for example in Jaffe v. Cranford Ins. Co. (1985) 168 Cal.App.3d 930 (Jaffe), the insurer argued that, “since the policy excludes payment for damages resulting from criminal acts, legal defense to criminal charges is also excluded” and that section 533 was “in accord with the policy.” (Id. at p. 935 & fn. 9.) The court disagreed, concluding that, although “the policy behind section 533 would prohibit coverage for fines resulting from a criminal conviction,” section 533 only “restricts the possible liability of insurers for losses. It does not restrict the insurer’s right to contract to provide legal services. [Citation.] Nor do we think the policy behind section 533 necessarily precludes such coverage.” (Id. at p. 935, fn. 9.) Thus, while it is true, as Mt. Hawley argues, that “California law recognizes a strong public policy of discouraging certain types of conduct by barring insurance coverage for any resulting proceedings or damages,” that public policy applies to indemnification not defense. 13

12 The same is true for section 1668 of the Civil Code, assuming, as Mt. Hawley contends, that it applies to insurance policies. This section provides: “All contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law.” (See Downey Venture, supra, 66 Cal.App.4th at pp. 486, fn. 1, 492; J.B. Aguerre, Inc. v. American Guarantee & Liability Ins. Co. (1997) 59 Cal.App.4th 6, 14; Ohio Casualty Ins. Co., supra, 162 Cal.App.3d at pp. 945-946; see also St. Paul Fire & Marine Ins. Co. v. Weiner (9th Cir. 1979) 606 F.2d 864, 870.) “However, it is not at all clear that section 1668 applies to indemnity agreements such as an insurance policy.” (Downey Venture, at p. 486, fn. 1.)

13 Where section 533 precludes indemnification and there is no “reasonable expectation of a defense even though indemnification is excluded,” there is no duty to defend. (Mez Industries, supra, 76 Cal.App.4th at p. 878; see Uhrich v. State Farm Fire & Casualty Co. (2003) 109 Cal.App.4th 598, 621-622.) Where, however, there is a “separate promise to defend against an inherently intentional tort,” the insurer can still owe a duty to defend even if section 533 precludes a duty to indemnify. (See Uhrich, at p. 622; Mez Industries, at p. 878, fn. 21; Downey Venture, supra, 66 Cal.App.4th at
Mt. Hawley, quoting the dissenting opinion in *Bodell*, argues that Lopez’s interpretation of section 533.5, subdivision (b), would create a conflict with subdivision (a) of section 533.5, “which contains a parallel construction” precluding “coverage or indemnity for the payment of any fine, penalty, or restitution in any criminal action or proceeding or in any action or proceeding brought pursuant to” the UCL or FAL by the same four state agencies. Mt. Hawley argues that if we adopt Lopez’s proposed interpretation of subdivision (b), then we would have to interpret subdivision (a) to “mean that insurance coverage would be barred for indemnification for criminal fines, penalties and restitution, only for criminal actions brought by the state but not the federal government.” As the dissenting opinion in *Bodell* rhetorically asks, “Why would indemnification of criminal fines imposed under federal law create any less of a moral hazard than indemnification of fines imposed under state law?” (*Bodell, supra*, 119 F.3d at p. 1411 (dis. opn. of Kozinski, J.).)

The alleged conflict with subdivision (a) is a false issue. Section 533 precludes indemnification of criminal fines, state and federal. (See *California Casualty Management Co. v. Martochhio* (1992) 11 Cal.App.4th 1527, 1533 [§ 533 precludes coverage “for fines or restitution imposed as a result of a criminal conviction”]; *Jaffe, supra*, 168 Cal.App.3d at p. 935, fn. 9 [“policy behind section 533 would prohibit coverage for fines resulting from a criminal conviction”].) Our interpretation of section 533.5, subdivision (b), has no effect on that rule. The Legislature enacted section 533.5, subdivision (a), provides: “No policy of insurance shall provide, or be construed to provide, any coverage or indemnity for the payment of any fine, penalty, or restitution in any criminal action or proceeding or in any action or proceeding brought pursuant to Chapter 5 (commencing with Section 17200) of Part 2 of, or Chapter 1 (commencing with Section 17500) of Part 3 of, Division 7 of the Business and Professions Code by the Attorney General, any district attorney, any city prosecutor, or any county counsel, notwithstanding whether the exclusion or exception regarding this type of coverage or indemnity is expressly stated in the policy.”
to address the problem the Attorney General had been experiencing in UCL and FAL cases, not to allow indemnification of federal criminal fines. Our conclusion that subdivision (b) does not preclude an insurer from providing a defense to federal criminal charges does not create any disharmony with subdivision (a). (See *Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4th 205, 218 [“[r]elated provisions ‘should be read together and construed in a manner that gives effect to each, yet does not lead to disharmony with others’”]; *Elsner v. Uveges* (2004) 34 Cal.4th 915, 933 [“when interpreting a statute, we must harmonize its various parts if possible, reconciling them in the manner that best carries out the overriding purpose of the legislation”].)

Moreover, the Legislature has enacted statutes authorizing insurance that provides a defense to individual defendants in various kinds of proceedings, including criminal proceedings. For example, Corporations Code section 317 authorizes a corporation to indemnify certain of its agents against “expenses, judgments, fines, settlements, and other amounts,” including “expenses actually and reasonably incurred by that person in connection with the defense or settlement of the action . . . .” (Corp. Code, § 317, subds. (b), (c).) Corporations Code section 317 applies to criminal proceedings against the agent as long as “that person acted in good faith and in a manner the person reasonably believed to be in the best interests of the corporation and, in the case of a criminal proceeding, had no reasonable cause to believe the conduct of the person was unlawful.” (Corp. Code, § 317, subds. (a), (b); see *P. S. & S. Inc. v. Superior Court* (1971) 17 Cal.App.3d 354, 359 [predecessor to Corp. Code, § 317]; 1 Marsh’s Cal. Corporate Law (4th ed. 2006) §11.22.) The statute further provides that the corporation

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15 Similar to an insurer’s right to provide a defense subject to a reservation of rights, the corporation is entitled to condition the advance of defense costs on behalf of its agent on the filing by the agent of a bond in case it is subsequently determined that the agent was not entitled to indemnification and defense under the statute. (See Corp. Code, § 317, subd. (f) [“[e]xpenses incurred in defending any proceeding may be advanced by the corporation prior to the final disposition of the proceeding upon receipt of an undertaking by or on behalf of the agent to repay that amount if it shall be determined ultimately that the agent is not entitled to be indemnified as authorized in this section”].)
“shall have power to purchase and maintain insurance on behalf of any agent of the corporation against any liability asserted against or incurred by the agent in that capacity or arising out of the agent’s status . . . .” (Corp. Code, § 317, subd. (i).) Thus, Corporations Code section 317 embodies a policy decision by the Legislature to allow insurers in certain circumstances to provide a defense in criminal actions or proceedings. (See Wilshire-Doheny Associates Ltd. v. Shapiro (2000) 83 Cal.App.4th 1380, 1388-1389 [“[t]he policy considerations behind [Corp. Code §] 317 ‘are that persons who serve the corporation in good faith should, in the absence of certain conduct (fraud, breach of fiduciary duties, etc.) be free from liability for corporate acts; indemnification encourages capable persons to perform their duties, secure in the knowledge that expenses incurred by them despite their honesty and integrity will be borne by the corporation”’]; Channel Lumber Co. v. Porter Simon (2000) 78 Cal.App.4th 1222, 1231 [by enacting Corp. Code, § 317 the Legislature made a policy decision “to encourage capable individuals to act for and in the place of the corporation by affording them indemnification for the expenses of defending against lawsuits to which they are made parties because they are agents of the corporation”].)

Similarly, Government Code section 990 provides that a local public entity may “[i]nsure, contract or provide against the expense of defending a claim against the local public entity or its employee . . . where such liability arose from an act or omission in the scope of his employment, and an insurance contract for such purpose is valid and binding notwithstanding Section 1668 of the Civil Code, Section 533 of the Insurance Code, or any other provision of law.” (Gov. Code, § 990, subd. (c).) Government Code section 995.8 provides that “a public entity may provide for the defense of a criminal action or proceeding . . . brought against an employee or former employee if” the “criminal action or proceeding is brought on account of an act or omission in the scope of his employment as an employee of the public entity . . . .”16 (Gov. Code, § 995.8; see Los Angeles Police

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16 The public entity must also determine that such a defense would be in its best interest and that “the employee or former employee acted, or failed to act, in good faith,
Protective League v. City of Los Angeles (1994) 27 Cal.App.4th 168, 176 [Gov. Code, § 995.8 “declares that public entities are not required to provide for the defense of criminal actions brought against their employees, but instead permits the entities to provide defenses in certain circumstances”].

Our interpretation of section 533.5 allows insurers to contract to provide a defense to certain kinds of criminal charges, as the Legislature has said insurers can do in the cases of corporate agents and government employees charged with crimes. Interpreting section 533.5, subdivision (b), as Mt. Hawley proposes and as the trial court did would create a potential conflict with statutes in the Corporations Code and the Government Code. (See Broughton v. Cigna Healthplans (1999) 21 Cal.4th 1066, 1086 [“[w]hen we construe potentially conflicting statutes, our duty is to harmonize them if reasonably possible”]; Walters v. Weed (1988) 45 Cal.3d 1, 9 [“[s]tatutes that are apparently in conflict should, if reasonably possible, be reconciled [citation], even when the court interprets provisions in different codes”]; Ailanto Properties, supra, 142 Cal.App.4th at p. 591 [refusing to adopt an interpretation of Gov. Code section that “would negate other statutory provisions” in the Water Code]; In re Marriage of Paddock (1971) 18 Cal.App.3d 355, 359 [“[s]tatutes should be construed so as to harmonize the various sections, and wherever possible seemingly conflicting provisions should be reconciled to avoid the declaration of an irreconcilable conflict”].

Our interpretation is also consistent with the goal of encouraging individuals to serve on boards of directors and trustees of corporations and charities. Allowing insurers to provide for defense costs in criminal cases against corporate agents enhances the ability of for-profit and non-profit organizations to attract directors, trustees, and volunteers who otherwise might hesitate or decline to serve because of a fear of lawsuits and criminal prosecutions. (See In re WorldCom, Inc. Securities Litigation (S.D.N.Y. 2005) 354 F.Supp.2d 455, 469 [“[u]nless directors can rely on the protections without actual malice and in the apparent interests of the public entity.”] (Gov. Code, § 995.8, subd. (b).)
given by D & O policies, good and competent men and women will be reluctant to serve on corporate boards’]; Homestore, Inc. v. Tafeen (Del. 2005) 888 A.2d 204, 211
[“[i]ndemnification encourages corporate service by capable individuals by protecting their personal financial resources from depletion by the expenses they incur during an investigation or litigation that results by reason of that service”]; Griffith, Uncovering a Gatekeeper: Why the SEC Should Mandate Disclosure of Details Concerning Directors’ and Officers’ Liability Insurance Policies (2006) 154 U.Pa. L.Rev. 1147, 1171
[“[c]orporate managers insist on D&O insurance to protect their personal wealth from the risk of shareholder litigation, making such coverage necessary to attract qualified persons to board service and executive-level employment”].)

Our interpretation that insurers may pay for defense costs in federal and some state criminal actions is also consistent with the principle that insureds charged with crimes begin with a presumption of innocence. (See Wiley v. County of San Diego (1998) 19 Cal.4th 532, 541 [presumption of innocence is “that bedrock ‘axiomatic and elementary’ principle whose ‘enforcement lies at the foundation of the administration of our criminal law,’” quoting In re Winship (1970) 397 U.S. 358, 363 [90 S.Ct. 1068, 25 L.Ed.2d 368]]; Gong v. Firemen’s Ins. Co. (1962) 202 Cal.App.2d 686, 691 [insured accused of criminal acts enters “upon the trial clothed with the presumption of innocence,” “one of the strongest disputable presumptions known to the law”]; see also U.S. v. Stein (2d Cir. 2008) 541 F.3d 130, 156 [“the Sixth Amendment protects against unjustified governmental interference with the right to defend oneself using whatever assets one has or might reasonably and lawfully obtain”]; Associated Elec. & Gas Ins. Services v. Rigas (E.D.Pa. 2004) 382 F.Supp.2d 685, 700 [insureds under D&O policy involved in a criminal prosecution “[u]ntil and unless they are found guilty, they are presumed innocent and must enjoy the constitutionally-based prerogatives of any citizen who stands merely accused, but not convicted, of a crime”]; CGU Ins. v. Tyson Assoc. (E.D.Pa. 2001) 140 F.Supp.2d 415, 421 [public policy precluding insurance coverage for willful criminal acts or for intentional torts “is not appropriately considered during the duty to defend analysis,” particularly where insureds “have not been found guilty of any
wrongdoing”). The law punishes individuals convicted of crimes, not those accused of crimes.

Finally, Mt. Hawley points to the statement in the dissenting opinion in Bodell that “no California court has ever construed an insurance policy to cover criminal defenses.” (Bodell, supra, 119 F.3d at p. 1421 (dis. opn. of Kozinski, J.).) No California court, however, has ever construed an insurance policy like this one not to cover criminal defenses, nor has any California court ever held that it is against public policy for an insurer to agree to provide a defense to criminal charges. The two cases cited by the dissent in Bodell, Perzik v. St. Paul Fire & Marine Ins. Co. (1991) 228 Cal.App.3d 1273 (Perzik), and Jaffe, supra, 168 Cal.App.3d 930, involved medical malpractice general liability policies that provided a defense to claims for damages and did not include an express provision providing for a defense against criminal charges. (See Perzik, at p. 1275; Jaffe, at p. 933.) The policy here, unlike the policies in Perzik and Jaffe, provides that a covered claim includes “a criminal proceeding against any Insured commenced by the return of an indictment” and that Mt. Hawley has a duty to defend such a claim.

f. Breach of the implied covenant of good faith and fair dealing

The trial court granted Mt. Hawley’s motion for summary adjudication on Lopez’s second cause of action for breach of the implied covenant of good faith and fair dealing on the ground that section 533.5 precluded a duty to defend. The trial court ruled:

17 Actually, only the policy in Perzik contained an express duty to defend provision. The insured in Jaffe argued that the duty to defend arose because of the potential for coverage. (See Jaffe, supra, 169 Cal.App.3d at pp. 933-934.)

18 Mt. Hawley makes the entirely circular argument that it did not contract to provide Lopez with a defense because the policy states that “Loss shall not include . . . (5) matters (other than punitive or exemplary damages) which are uninsurable under the law pursuant to which the Policy shall be construed,” and section 533.5, subdivision (b), precludes any duty to defend. Because we conclude that section 533.5, subdivision (b), does not preclude Mt. Hawley’s duty to defend, exclusion (5) from the definition of loss for uninsurable matters does not apply.
“Having found that Mt. Hawley did not breach the insurance contract by refusing to defend against the Indictment because Insurance Code section 533.5 bars coverage for his defense, the Court holds that Dr. Lopez’s claim for breach of the implied covenant of good faith and fair dealing fails as a matter of law.” The trial court did not reach Mt. Hawley’s alternative argument that it was entitled to summary adjudication on Lopez’s bad faith claim because “Mt. Hawley’s denial was reasonable and based on a genuine dispute” regarding its duty to defend Lopez against the criminal charges and the application of section 533.5, subdivision (b). Mt. Hawley argues on appeal that, even if section 533.5, subdivision (b), does not preclude it from providing Lopez with a defense, it is still entitled to summary adjudication on Lopez’s bad faith “because its position has been at least reasonable.”

It is doubtful that the so-called “genuine dispute doctrine” applies in third party\(^\text{19}\) duty to defend\(^\text{20}\) cases like this one. Here, assuming the reasonableness of Mt. Hawley’s

\(^{19}\) (See Yan Fang Du v. Allstate Ins. Co. (9th Cir. 2012) 697 F.3d 753, 758 [collecting cases and concluding that whether the genuine dispute doctrine applies to duty to settle third party claims under California law is “unsettled”]; Howard v. American National Fire Ins. Co. (2010) 187 Cal.App.4th 498, 530 [“it has never been held that an insurer in a third party case may rely on a genuine dispute over coverage to refuse settlement”]; Croskey et al., Cal. Practice Guide: Insurance Litigation (The Rutter Group 2012) ¶ 12:618, p. 12B-104 (rev. #1, 2011) [“[t]he extent to which the ‘genuine dispute’ doctrine may apply in third party cases is presently unclear”].)

\(^{20}\) (See Harbison v. American Motorists Ins. Co. (E.D.Cal. 2009) 636 F.Supp.2d 1030, 1040 [“[b]ecause the existence of a genuine dispute as to the insurer’s liability indicates that there is at a potential for coverage, the existence of a genuine dispute is itself enough to trigger the insurer’s duty to defend,” and therefore “the genuine dispute doctrine appears wholly incompatible with duty to defend cases”]; Century Surety Co. v. Polisso (2006) 139 Cal.App.4th 922, 951 [noting that the insurer in that case “has failed to cite any cases that apply the genuine dispute doctrine to the duty to defend and our research has not disclosed any” and that the “doctrine has been applied primarily in first-party coverage cases”]; but see Gaylord v. Nationwide Mut. Ins. Co. (E.D.Cal. 2011) 776 F.Supp.2d 1101, 1125 [“the Court must respectfully disagree with Harbison’s conclusion that the ‘genuine dispute doctrine’ cannot apply in all bad faith duty to defend cases”]; Croskey et al., Cal. Practice Guide: Insurance Litigation, supra, ¶¶ 12:618.5 to 12:618.10, pp. 12B-105 to 12B-106 (rev. #1, 2012) [suggesting that whether the
position is a defense to Lopez’s claim that Mt. Hawley refused to provide Lopez with a
defense in bad faith, material factual issues precluded Mt. Hawley from prevailing on this
claim on summary adjudication.

The reasonableness of an insurer’s conduct is ordinarily a question of fact, except
in the “exceptional instance when ‘only one reasonable inference can be drawn from the
evidence.’” (Lee v. Fidelity Nat. Title Ins. Co. (2010) 188 Cal.App.4th 583, 599; see
where bad faith is alleged, a jury is empowered to resolve conflicting evidence regarding
5 Cal.App.4th 1445, 1454-1455.) While we agree that Mt. Hawley’s legal position on the
interpretation of section 533.5, subdivision (b), was reasonable (see above), Lopez
presented other evidence that created factual issues regarding the reasonableness of
Mt. Hawley’s conduct in refusing to provide Lopez with a defense to the indictment. For
example, at least two years before Mt. Hawley refused to defend Lopez against the
criminal investigation and indictment for allegedly covering up the liver transplant
diversion under the “Not For Profit Organization and Executive Liability Policy,”
Mt. Hawley had “promptly” and “[i]mmediately following notification of the claims”
agreed to defend DCHS against the same criminal investigation under the same policy.21
At one point Mt. Hawley had even “advanced some $600,000 under a reservation of
existence of a genuine dispute as to coverage precludes bad faith liability for refusing to
provide a defense depends on whether the dispute is factual or legal].

21 This evidence came from evidentiary admissions in Mt. Hawley’s litigation with
DCHS. “A pleading in a prior civil proceeding may be offered as an evidentiary
admission against the pleader” on summary judgment. (Magnolia Square Homeowners
(rev. #1, 2011), 10:150.1, p. 10-59 (rev. #1, 2011).) Such an admission is an evidentiary
admission, not a judicial admission, and may be rebutted with explanatory evidence from
the party against whom the admission is offered. (Deveny v. Entropin, Inc. (2006)
139 Cal.App.4th 408, 426; Magnolia Square, at p. 1061; Dolinar v. Pedone (1944)
63 Cal.App.2d 169, 177.)
rights” to DCHS.\textsuperscript{22} Mt. Hawley never explained why it treated St. Vincent’s so differently from Lopez and why it denied Lopez the same defense it provided to St. Vincent’s for charges arising out of the same events.

Lopez also alleged and presented evidence that Mt. Hawley refused to provide Lopez with a defense based on an exclusion, the medical incident exclusion, that according to Lopez was not part of the policy. (See \textit{Tomaselli v. Transamerica Ins. Co.} (1994) 25 Cal.App.4th 1269, 1281-1282 [insurer’s continued reliance on endorsement insureds claimed they never received was “indicia of bad faith” and “one for the jury to decide”]; \textit{Logan v. John Hancock Mut. Life Ins. Co.} (1974) 41 Cal.App.3d 988, 992 [insurer may “not rely on uncommunicated exclusions in a policy not yet issued”].) A jury could reasonably infer from this evidence that Mt. Hawley’s conduct toward its insured Lopez was unreasonable and without proper cause. Indeed, Mt. Hawley’s motion for summary adjudication did not even address Lopez’s allegation that Mt. Hawley breached the implied covenant of good faith and fair dealing by “[d]enying coverage based on an exclusion that cannot be found in the Policy.” (See Civ. Proc. Code, § 437c, subd. (f)(1); \textit{McCaskey v. California State Automobile Assn.} (2010) 189 Cal.App.4th 947, 975 [“there can be no summary adjudication of less than an entire cause of action”]; \textit{Hindin v. Rust} (2004) 118 Cal.App.4th 1247, 1259 [summary judgment must dispose of an entire cause of action].) Mt. Hawley is not entitled to summary adjudication on Lopez’s claim for breach of the implied covenant of good faith and fair dealing.

3. \textit{The Trial Court Properly Overruled Lopez’s Demurrer}

Mt. Hawley’s first amended complaint asserted two causes of action for declaratory relief, one on the issue of Mt. Hawley’s duty to defend and the other on Mt. Hawley’s duty to indemnify. Both causes of action were based on Mt. Hawley’s allegations that it had no coverage obligations because of (1) section 533.5, (2) the medical incident exclusion, and (3) the remuneration/personal profit exclusion. Lopez

\textsuperscript{22} Mt. Hawley later sought reimbursement of the “substantial sums” it had paid DCHS and St. Vincent’s.
demurred to the first cause of action only. Lopez argues that the trial court erred by overruling his demurrer.

The trial court properly overruled Lopez’s demurrer because his argument that the two exclusions do not apply is based on evidence that was outside the pleadings and not subject to judicial notice on demurrer. For example, Lopez’s argument that the medical incident exclusion does not apply depends on factual statements contained in his requests for judicial notice of documents in other cases, such as the declaratory relief action between Mt. Hawley and DCHS. (See *Oiye v. Fox* (2012) 211 Cal.App.4th 1036, 1055 [“court may take judicial notice that pleadings were filed containing certain allegations and arguments [citation], but a court may not take judicial notice of the truth of the facts alleged”]; *Williams v. Wraxall* (1995) 33 Cal.App.4th 120, 130, fn. 7 [court “cannot take judicial notice of the truth of hearsay statements in decisions or court files, including pleadings”].) The factual issue of whether the medical incident exclusion is part of the policy can be resolved perhaps on summary judgment and certainly at trial, but the issue cannot be resolved on demurrer. Because Mt. Hawley’s allegations stated a viable claim for declaratory relief on at least on a portion of its first cause of action for declaratory relief, the trial court properly overruled the demurrer. (See *Pointe San Diego Residential Community, L.P. v. Procopio, Cory, Hargreaves & Savitch, LLP* (2011) 195 Cal.App.4th 265, 274 [a “demurrer challenges a cause of action and cannot be used to attack a portion of a cause of action”]; *Chazen v. Centennial Bank* (1998) 61 Cal.App.4th 532, 542 [demurrer “may be sustained only if the complaint lacks any sufficient allegations to entitle the plaintiff to relief”].)

Finally, Lopez argues for the first time in his reply brief that issue preclusion bars Mt. Hawley’s declaratory relief cause of action. We decline to address this issue. (See *Habitat & Watershed Caretakers v. City of Santa Cruz* (2013) 213 Cal.App.4th 1277, 1292, fn. 6 [“arguments presented for the first time in an appellant’s reply brief are considered waived”]; *Holmes v. Petrovich Development Co.* (2011) 191 Cal.App.4th 1047, 1064, fn. 2 [“argument is forfeited” where “it is raised for the first time in [appellant’s] reply brief without a showing of good cause”].)
DISPOSITION

The June 21, 2011 order granting Mt. Hawley’s motion for summary judgment is reversed. The October 18, 2010 order overruling Lopez’s demurrer to Mt. Hawley’s first amended complaint is affirmed. The judgment is reversed. Lopez’s request for judicial notice of the Judgment of Discharge in his federal criminal case is granted. Lopez is to recover his costs on appeal.

SEGAL, J.*

We concur:

WOODS, Acting P. J.

ZELON, J.

* Judge of the Los Angeles Superior Court assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.
SUPREME COURT OF THE UNITED STATES

Syllabus

SALINAS v. TEXAS

CERTIORARI TO THE COURT OF CRIMINAL APPEALS OF TEXAS


Petitioner, without being placed in custody or receiving Miranda warnings, voluntarily answered some of a police officer’s questions about a murder, but fell silent when asked whether ballistics testing would match his shotgun to shell casings found at the scene of the crime. At petitioner’s murder trial in Texas state court, and over his objection, the prosecution used his failure to answer the question as evidence of guilt. He was convicted, and both the State Court of Appeals and Court of Criminal Appeals affirmed, rejecting his claim that the prosecution’s use of his silence in its case in chief violated the Fifth Amendment.

Held: The judgment is affirmed.

369 S. W. 3d 176, affirmed.

JUSTICE ALITO, joined by THE CHIEF JUSTICE and JUSTICE KENNEDY, concluded that petitioner’s Fifth Amendment claim fails because he did not expressly invoke the privilege in response to the officer’s question. Pp. 3–12.

(a) To prevent the privilege against self-incrimination from shielding information not properly within its scope, a witness who “desires the protection of the privilege . . . must claim it” at the time he relies on it. Minnesota v. Murphy, 465 U. S. 420, 427. This Court has recognized two exceptions to that requirement. First, a criminal defendant need not take the stand and assert the privilege at his own trial. Griffin v. California, 380 U. S. 609, 613–615. Petitioner’s silence falls outside this exception because he had no comparable unqualified right not to speak during his police interview. Second, a witness’ failure to invoke the privilege against self-incrimination must be excused where governmental coercion makes his forfeiture of the privilege involuntary. See, e.g., Miranda v. Arizona, 384 U. S. 436, 467–468, and n. 37. Petitioner cannot benefit from this principle.
because it is undisputed that he agreed to accompany the officers to
the station and was free to leave at any time. Pp. 3–6.

(b) Petitioner seeks a third exception to the express invocation re-
quirement for cases where the witness chooses to stand mute rather
than give an answer that officials suspect would be incriminating,
but this Court's cases all but foreclose that argument. A defendant
normally does not invoke the privilege by remaining silent. See Rob-
erts v. United States, 445 U. S. 552, 560. And the express invocation
requirement applies even when an official has reason to suspect that
the answer to his question would incriminate the witness. See Mur-
phy, supra, at 427–428. For the same reasons that neither a witness' silence nor official suspicion is sufficient by itself to relieve a witness
of the obligation to expressly invoke the privilege, they do not do so
together. The proposed exception also would be difficult to reconcile
with Berghuis v. Thompkins, 560 U. S. 370, where this Court held in
the closely related context of post-Miranda silence that a defendant
failed to invoke his right to cut off police questioning when he re-
mained silent for 2 hours and 45 minutes. Id., at ___.

Petitioner claims that reliance on the Fifth Amendment privilege is
the most likely explanation for silence in a case like his, but such si-
lence is "insolubly ambiguous." See Doyle v. Ohio, 426 U. S. 610, 617.
To be sure, petitioner might have declined to answer the officer's
question in reliance on his constitutional privilege. But he also might
have done so because he was trying to think of a good lie, because he
was embarrassed, or because he was protecting someone else. Not
every such possible explanation for silence is probative of guilt, but
neither is every possible explanation protected by the Fifth Amend-
ment. Petitioner also suggests that it would be unfair to require a
suspect unschooled in the particulars of legal doctrine to do anything
more than remain silent in order to invoke his "right to remain si-
 lent." But the Fifth Amendment guarantees that no one may be
"compelled in any criminal case to be a witness against himself," not
an unqualified "right to remain silent." In any event, it is settled
that forfeiture of the privilege against self-incrimination need not be

(c) Petitioner's argument that applying the express invocation re-
quirement in this context will be unworkable is also unpersuasive.
The Court has long required defendants to assert the privilege in or-
der to subsequently benefit from it, and this rule has not proved diffi-
cult to apply in practice. Pp. 10–12.

JUSTICE THOMAS, joined by JUSTICE SCALIA, concluded that peti-
tioner's claim would fail even if he invoked the privilege because the
prosecutor's comments regarding his precustodial silence did not
compel him to give self-incriminating testimony. Griffin v. Califor-
nia, 380 U. S. 609, in which this Court held that the Fifth Amend-
ment prohibits a prosecutor or judge from commenting on a defend-
ant’s failure to testify, should not be extended to a defendant’s silence
during a precustodial interview because Griffin “lacks foundation in
the Constitution’s text, history, or logic.” See Mitchell v. United

ALITO, J., announced the judgment of the Court and delivered an
opinion, in which ROBERTS, C. J., and KENNEDY, J., joined. THOMAS, J.,
filed an opinion concurring in the judgment, in which SCALIA, J., joined.
BREYER, J., filed a dissenting opinion, in which GINSBURG, SOTOMAYOR,
and KAGAN, JJ., joined.
JUSTICE ALITO announced the judgment of the Court and delivered an opinion in which THE CHIEF JUSTICE and JUSTICE KENNEDY join.

Without being placed in custody or receiving Miranda warnings, petitioner voluntarily answered the questions of a police officer who was investigating a murder. But petitioner balked when the officer asked whether a ballistics test would show that the shell casings found at the crime scene would match petitioner’s shotgun. Petitioner was subsequently charged with murder, and at trial prosecutors argued that his reaction to the officer’s question suggested that he was guilty. Petitioner claims that this argument violated the Fifth Amendment, which guarantees that “[n]o person . . . shall be compelled in any criminal case to be a witness against himself.”

Petitioner’s Fifth Amendment claim fails because he did not expressly invoke the privilege against self-incrimination in response to the officer’s question. It has long been settled that the privilege “generally is not self-executing” and that a witness who desires its protection “must claim it.” Minnesota v. Murphy, 465 U. S. 420, 425, 427 (1984) (quoting United States v. Monia, 317 U. S.
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424, 427 (1943)). Although “no ritualistic formula is necessary in order to invoke the privilege,” Quinn v. United States, 349 U. S. 155, 164 (1955), a witness does not do so by simply standing mute. Because petitioner was required to assert the privilege in order to benefit from it, the judgment of the Texas Court of Criminal Appeals rejecting petitioner’s Fifth Amendment claim is affirmed.

I

On the morning of December 18, 1992, two brothers were shot and killed in their Houston home. There were no witnesses to the murders, but a neighbor who heard gunshots saw someone run out of the house and speed away in a dark-colored car. Police recovered six shotgun shell casings at the scene. The investigation led police to petitioner, who had been a guest at a party the victims hosted the night before they were killed. Police visited petitioner at his home, where they saw a dark blue car in the driveway. He agreed to hand over his shotgun for ballistics testing and to accompany police to the station for questioning.

Petitioner’s interview with the police lasted approximately one hour. All agree that the interview was noncustodial, and the parties litigated this case on the assumption that he was not read Miranda warnings. See Miranda v. Arizona, 384 U. S. 436 (1966). For most of the interview, petitioner answered the officer’s questions. But when asked whether his shotgun “would match the shells recovered at the scene of the murder,” App. 17, petitioner declined to answer. Instead, petitioner “[l]ooked down at the floor, shuffled his feet, bit his bottom lip, cl[enched] his hands in his lap, [and] began to tighten up.” Id., at 18. After a few moments of silence, the officer asked additional questions, which petitioner answered. Ibid.

Following the interview, police arrested petitioner on outstanding traffic warrants. Prosecutors soon concluded
that there was insufficient evidence to charge him with the murders, and he was released. A few days later, police obtained a statement from a man who said he had heard petitioner confess to the killings. On the strength of that additional evidence, prosecutors decided to charge petitioner, but by this time he had absconded. In 2007, police discovered petitioner living in the Houston area under an assumed name.

Petitioner did not testify at trial. Over his objection, prosecutors used his reaction to the officer’s question during the 1993 interview as evidence of his guilt. The jury found petitioner guilty, and he received a 20-year sentence. On direct appeal to the Court of Appeals of Texas, petitioner argued that prosecutors’ use of his silence as part of their case in chief violated the Fifth Amendment. The Court of Appeals rejected that argument, reasoning that petitioner’s prearrest, pre-Miranda silence was not “compelled” within the meaning of the Fifth Amendment. 368 S. W. 3d 550, 557–559 (2011). The Texas Court of Criminal Appeals took up this case and affirmed on the same ground. 369 S. W. 3d 176 (2012).

We granted certiorari, 568 U. S. ___ (2013), to resolve a division of authority in the lower courts over whether the prosecution may use a defendant’s assertion of the privilege against self-incrimination during a noncustodial police interview as part of its case in chief. Compare, e.g., United States v. Rivera, 944 F. 2d 1563, 1568 (CA11 1991), with United States v. Moore, 104 F. 3d 377, 386 (CADC 1997). But because petitioner did not invoke the privilege during his interview, we find it unnecessary to reach that question.

II

A

The privilege against self-incrimination “is an exception to the general principle that the Government has the right
to everyone’s testimony.” Garner v. United States, 424 U. S. 648, 658, n. 11 (1976). To prevent the privilege from shielding information not properly within its scope, we have long held that a witness who “‘desires the protection of the privilege . . . must claim it’” at the time he relies on it. Murphy, 465 U. S., at 427 (quoting Monia, 317 U. S., at 427). See also United States ex rel. Vajtauer v. Commissioner of Immigration, 273 U. S. 103, 113 (1927).

That requirement ensures that the Government is put on notice when a witness intends to rely on the privilege so that it may either argue that the testimony sought could not be self-incriminating, see Hoffman v. United States, 341 U. S. 479, 486 (1951), or cure any potential self-incrimination through a grant of immunity, see Kastigar v. United States, 406 U. S. 441, 448 (1972). The express invocation requirement also gives courts tasked with evaluating a Fifth Amendment claim a contemporaneous record establishing the witness’ reasons for refusing to answer. See Roberts v. United States, 445 U. S. 552, 560, n. 7 (1980) ("A witness may not employ the privilege to avoid giving testimony that he simply would prefer not to give"); Hutcheson v. United States, 369 U. S. 599, 610–611 (1962) (declining to treat invocation of due process as proper assertion of the privilege). In these ways, insisting that witnesses expressly invoke the privilege “assures that the Government obtains all the information to which it is entitled.” Garner, supra, at 658, n. 11.

We have previously recognized two exceptions to the requirement that witnesses invoke the privilege, but neither applies here. First, we held in Griffin v. California, 380 U. S. 609, 613–615 (1965), that a criminal defendant need not take the stand and assert the privilege at his own trial. That exception reflects the fact that a criminal defendant has an “absolute right not to testify.” Turner v. United States, 396 U. S. 398, 433 (1970) (Black, J., dissenting); see United States v. Patane, 542 U. S. 630,
637 (2004) (plurality opinion). Since a defendant’s reasons for remaining silent at trial are irrelevant to his constitutional right to do so, requiring that he expressly invoke the privilege would serve no purpose; neither a showing that his testimony would not be self-incriminating nor a grant of immunity could force him to speak. Because petitioner had no comparable unqualified right during his interview with police, his silence falls outside the Griffin exception.

Second, we have held that a witness’ failure to invoke the privilege must be excused where governmental coercion makes his forfeiture of the privilege involuntary. Thus, in Miranda, we said that a suspect who is subjected to the “inherently compelling pressures” of an unwarned custodial interrogation need not invoke the privilege. 384 U. S., at 467–468, and n. 37. Due to the uniquely coercive nature of custodial interrogation, a suspect in custody cannot be said to have voluntarily forgone the privilege “unless [he] fails to claim [it] after being suitably warned.” Murphy, supra, at 429–430.

For similar reasons, we have held that threats to withdraw a governmental benefit such as public employment sometimes make exercise of the privilege so costly that it need not be affirmatively asserted. Garrity v. New Jersey, 385 U. S. 493, 497 (1967) (public employment). See also Lefkowitz v. Cunningham, 431 U. S. 801, 802–804 (1977) (public office); Lefkowitz v. Turley, 414 U. S. 70, 84–85 (1973) (public contracts). And where assertion of the privilege would itself tend to incriminate, we have allowed witnesses to exercise the privilege through silence. See, e.g., Leary v. United States, 395 U. S. 6, 28–29 (1969) (no requirement that taxpayer complete tax form where doing so would have revealed income from illegal activities); Albertson v. Subversive Activities Control Bd., 382 U.S. 70, 77–79 (1965) (members of the Communist Party not required to complete registration form “where response to
any of the form’s questions . . . might involve [them] in the admission of a crucial element of a crime"). The principle that unites all of those cases is that a witness need not expressly invoke the privilege where some form of official compulsion denies him “a ‘free choice to admit, to deny, or to refuse to answer.’” Garner, 424 U. S., at 656–657 (quoting Lisenba v. California, 314 U. S. 219, 241 (1941)).

Petitioner cannot benefit from that principle because it is undisputed that his interview with police was voluntary. As petitioner himself acknowledges, he agreed to accompany the officers to the station and “was free to leave at any time during the interview.” Brief for Petitioner 2–3 (internal quotation marks omitted). That places petitioner’s situation outside the scope of Miranda and other cases in which we have held that various forms of governmental coercion prevented defendants from voluntarily invoking the privilege. The dissent elides this point when it cites our precedents in this area for the proposition that “[c]ircumstances, rather than explicit invocation, trigger the protection of the Fifth Amendment.” Post, at 7–8 (opinion of BREYER, J.). The critical question is whether, under the “circumstances” of this case, petitioner was deprived of the ability to voluntarily invoke the Fifth Amendment. He was not. We have before us no allegation that petitioner’s failure to assert the privilege was involuntary, and it would have been a simple matter for him to say that he was not answering the officer’s question on Fifth Amendment grounds. Because he failed to do so, the prosecution’s use of his noncustodial silence did not violate the Fifth Amendment.

B

Petitioner urges us to adopt a third exception to the invocation requirement for cases in which a witness stands mute and thereby declines to give an answer that officials suspect would be incriminating. Our cases all but
foreclose such an exception, which would needlessly burden the Government’s interests in obtaining testimony and prosecuting criminal activity. We therefore decline petitioner’s invitation to craft a new exception to the “general rule” that a witness must assert the privilege to subsequently benefit from it. *Murphy*, 465 U. S., at 429.

Our cases establish that a defendant normally does not invoke the privilege by remaining silent. In *Roberts v. United States*, 445 U. S. 552, for example, we rejected the Fifth Amendment claim of a defendant who remained silent throughout a police investigation and received a harsher sentence for his failure to cooperate. In so ruling, we explained that “if [the defendant] believed that his failure to cooperate was privileged, he should have said so at a time when the sentencing court could have determined whether his claim was legitimate.” *Id.*, at 560. See also *United States v. Sullivan*, 274 U. S. 259, 263–264 (1927); *Vajtauer*, 273 U. S., at 113. 1 A witness does not expressly invoke the privilege by standing mute.

We have also repeatedly held that the express invocation requirement applies even when an official has reason to suspect that the answer to his question would incriminate the witness. Thus, in *Murphy* we held that the defendant’s self-incriminating answers to his probation officer were properly admitted at trial because he failed to invoke the privilege. 465 U. S., at 427–428. In reaching that conclusion, we rejected the notion “that a witness

1 The dissent argues that in these cases “neither the nature of the questions nor the circumstances of the refusal to answer them provided any basis to infer a tie between the silence and the Fifth Amendment.” *Post*, at 5–6 (opinion of Breyer, J.). But none of our precedents suggests that governmental officials are obliged to guess at the meaning of a witness’ unexplained silence when implicit reliance on the Fifth Amendment seems probable. *Roberts* does not say as much, despite its holding that the defendant in that case was required to explain the Fifth Amendment basis for his failure to cooperate with an investigation that led to his prosecution. 445 U. S., at 559.
must ‘put the Government on notice by formally availing himself of the privilege’ only when he alone ‘is reasonably aware of the incriminating tendency of the questions.’”

Id., at 428 (quoting Roberts, supra, at 562, n.* (Brennan, J., concurring)). See also United States v. Kordel, 397 U. S. 1, 7 (1970).2

Petitioner does not dispute the vitality of either of those lines of precedent but instead argues that we should adopt an exception for cases at their intersection. Thus, petitioner would have us hold that although neither a witness’ silence nor official suspicions are enough to excuse the express invocation requirement, the invocation requirement does not apply where a witness is silent in the face of official suspicions. For the same reasons that neither of those factors is sufficient by itself to relieve a witness of the obligation to expressly invoke the privilege, we conclude that they do not do so together. A contrary result would do little to protect those genuinely relying on the Fifth Amendment privilege while placing a needless new burden on society’s interest in the admission of evidence that is probative of a criminal defendant’s guilt.

Petitioner’s proposed exception would also be very difficult to reconcile with Berghuis v. Thompkins, 560 U. S. 370 (2010). There, we held in the closely related context of post-Miranda silence that a defendant failed to invoke the

2Our cases do not support the distinction the dissent draws between silence and the failure to invoke the privilege before making incriminating statements. See post, at 7 (Breyer, J., dissenting). For example, Murphy, a case in which the witness made incriminating statements after failing to invoke the privilege, repeatedly relied on Roberts and Vajtauer—two cases in which witnesses remained silent and did not make incriminating statements. 465 U. S., at 427, 429, 455–456, n. 20. Similarly, Kordel cited Vajtauer, among other cases, for the proposition that the defendant’s “failure at any time to assert the constitutional privilege leaves him in no position to complain now that he was compelled to give testimony against himself.” 397 U. S., at 10, and n. 18.
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privilege when he refused to respond to police questioning for 2 hours and 45 minutes. 560 U. S., at ___ (slip op., at 3, 8–10). If the extended custodial silence in that case did not invoke the privilege, then surely the momentary silence in this case did not do so either.

Petitioner and the dissent attempt to distinguish Berghuis by observing that it did not concern the admissibility of the defendant’s silence but instead involved the admissibility of his subsequent statements. Post, at 8–9 (opinion of BREYER, J.). But regardless of whether prosecutors seek to use silence or a confession that follows, the logic of Berghuis applies with equal force: A suspect who stands mute has not done enough to put police on notice that he is relying on his Fifth Amendment privilege.3

In support of their proposed exception to the invocation requirement, petitioner and the dissent argue that reliance on the Fifth Amendment privilege is the most likely explanation for silence in a case such as this one. Reply Brief 17; see post, at 9–10 (BREYER, J., dissenting). But whatever the most probable explanation, such silence is “insolubly ambiguous.” See Doyle v. Ohio, 426 U. S. 610, 617 (1976). To be sure, someone might decline to answer a police officer’s question in reliance on his constitutional privilege. But he also might do so because he is trying to think of a good lie, because he is embarrassed, or because he is protecting someone else. Not every such possible explanation for silence is probative of guilt, but neither is every possible explanation protected by the Fifth Amendment. Petitioner alone knew why he did not answer the officer’s question, and it was therefore his “burden . . . to

3Petitioner is correct that due process prohibits prosecutors from pointing to the fact that a defendant was silent after he heard Miranda warnings, Doyle v. Ohio, 426 U. S. 610, 617–618 (1976), but that rule does not apply where a suspect has not received the warnings’ implicit promise that any silence will not be used against him, Jenkins v. Anderson, 447 U. S. 231, 240 (1980).

At oral argument, counsel for petitioner suggested that it would be unfair to require a suspect unschooled in the particulars of legal doctrine to do anything more than remain silent in order to invoke his “right to remain silent.” Tr. of Oral Arg. 26–27; see post, at 10 (BREYER, J., dissenting); Michigan v. Tucker, 417 U. S. 433, 439 (1974) (observing that “virtually every schoolboy is familiar with the concept, if not the language” of the Fifth Amendment). But popular misconceptions notwithstanding, the Fifth Amendment guarantees that no one may be “compelled in any criminal case to be a witness against himself”; it does not establish an unqualified “right to remain silent.” A witness’ constitutional right to refuse to answer questions depends on his reasons for doing so, and courts need to know those reasons to evaluate the merits of a Fifth Amendment claim. See Hoffman, 341 U. S., at 486–487.4

In any event, it is settled that forfeiture of the privilege against self-incrimination need not be knowing. Murphy, 465 U. S., at 427–428; Garner, supra, at 654, n. 9. Statements against interest are regularly admitted into evidence at criminal trials, see Fed. Rule of Evid. 804(b)(3), and there is no good reason to approach a defendant’s silence any differently.

C

Finally, we are not persuaded by petitioner’s arguments

4The dissent suggests that officials in this case had no “special need to know whether the defendant sought to rely on the protections of the Fifth Amendment.” Post, at 4 (opinion of BREYER, J.). But we have never said that the government must demonstrate such a need on a case-by-case basis for the invocation requirement to apply. Any such rule would require judicial hypothesizing about the probable strategic choices of prosecutors, who often use immunity to compel testimony from witnesses who invoke the Fifth Amendment.
that applying the usual express invocation requirement where a witness is silent during a noncustodial police interview will prove unworkable in practice. Petitioner and the dissent suggest that our approach will “unleash complicated and persistent litigation” over what a suspect must say to invoke the privilege, Reply Brief 18; see post, at 11–12 (opinion of Breyer, J.), but our cases have long required that a witness assert the privilege to subsequently benefit from it. That rule has not proved difficult to apply. Nor did the potential for close cases dissuade us from adopting similar invocation requirements for suspects who wish to assert their rights and cut off police questioning during custodial interviews. Berghuis, 560 U. S., at ___ (slip op., at 8–10) (requiring suspect to unambiguously assert privilege against self-incrimination to cut off custodial questioning); Davis v. United States, 512 U. S. 452, 459 (1994) (same standard for assertions of the right to counsel).

Notably, petitioner’s approach would produce its own line-drawing problems, as this case vividly illustrates. When the interviewing officer asked petitioner if his shotgun would match the shell casings found at the crime scene, petitioner did not merely remain silent; he made movements that suggested surprise and anxiety. At precisely what point such reactions transform “silence” into expressive conduct would be a difficult and recurring question that our decision allows us to avoid.

We also reject petitioner’s argument that an express invocation requirement will encourage police officers to “‘unfairly ‘tric[k]’” suspects into cooperating. Reply Brief 21 (quoting South Dakota v. Neville, 459 U. S. 553, 566 (1983)). Petitioner worries that officers could unduly pressure suspects into talking by telling them that their silence could be used in a future prosecution. But as petitioner himself concedes, police officers “have done nothing wrong” when they “accurately stat[e] the law.”
Brief for Petitioner 32. We found no constitutional infirmity in government officials telling the defendant in Murphy that he was required to speak truthfully to his parole officer, 465 U. S., at 436–438, and we see no greater danger in the interview tactics petitioner identifies. So long as police do not deprive a witness of the ability to voluntarily invoke the privilege, there is no Fifth Amendment violation.

* * *

Before petitioner could rely on the privilege against self-incrimination, he was required to invoke it. Because he failed to do so, the judgment of the Texas Court of Criminal Appeals is affirmed.

It is so ordered.
JUSTICE THOMAS, with whom JUSTICE SCALIA joins, concurring in the judgment.

We granted certiorari to decide whether the Fifth Amendment privilege against compulsory self-incrimination prohibits a prosecutor from using a defendant's pre-custodial silence as evidence of his guilt. The plurality avoids reaching that question and instead concludes that Salinas' Fifth Amendment claim fails because he did not expressly invoke the privilege. Ante, at 3. I think there is a simpler way to resolve this case. In my view, Salinas' claim would fail even if he had invoked the privilege because the prosecutor's comments regarding his pre-custodial silence did not compel him to give self-incriminating testimony.

In Griffin v. California, 380 U. S. 609 (1965), this Court held that the Fifth Amendment prohibits a prosecutor or judge from commenting on a defendant's failure to testify. Id., at 614. The Court reasoned that such comments, and any adverse inferences drawn from them, are a "penalty" imposed on the defendant's exercise of his Fifth Amendment privilege. Ibid. Salinas argues that we should extend Griffin's no-adverse-inference rule to a defendant's silence during a pre-custodial interview. I have previously explained that the Court's decision in Griffin "lacks foundation in the Constitution's text, history, or logic" and should not be extended. See Mitchell v. United States, 526
Thomas, J., concurring in judgment


Griffin is impossible to square with the text of the Fifth Amendment, which provides that “[n]o person . . . shall be compelled in any criminal case to be a witness against himself.” A defendant is not “compelled . . . to be a witness against himself” simply because a jury has been told that it may draw an adverse inference from his silence. See Mitchell, supra, at 331 (SCALIA, J., dissenting) (“[T]he threat of an adverse inference does not 'compel' anyone to testify. . . . Indeed, I imagine that in most instances, a guilty defendant would choose to remain silent despite the adverse inference, on the theory that it would do him less damage than his cross-examined testimony”); Carter v. Kentucky, 450 U. S. 288, 306 (1981) (Powell, J., concurring) (“[N]othing in the [Self-Incrimination] Clause requires that jurors not draw logical inferences when a defendant chooses not to explain incriminating circumstances”).

Nor does the history of the Fifth Amendment support Griffin. At the time of the founding, English and American courts strongly encouraged defendants to give unsworn statements and drew adverse inferences when they failed to do so. See Mitchell, supra, at 332 (SCALIA, J., dissenting); Alschuler, A Peculiar Privilege in Historical Perspective, in The Privilege Against Self-Incrimination 204 (R. Hemholz et al. eds. 1997). Given Griffin’s indefensible foundation, I would not extend it to a defendant’s silence during a precustodial interview. I agree with the plurality that Salinas’ Fifth Amendment claim fails and, therefore, concur in the judgment.
JUSTICE BREYER, with whom JUSTICE GINSBURG, JUSTICE SOTOMAYOR, and JUSTICE KAGAN join, dissenting.

In my view the Fifth Amendment here prohibits the prosecution from commenting on the petitioner’s silence in response to police questioning. And I dissent from the Court’s contrary conclusion.

I

In January 1993, Houston police began to suspect petitioner Genovevo Salinas of having committed two murders the previous month. They asked Salinas to come to the police station “to take photographs and to clear him as [a] suspect.” App. 3. At the station, police took Salinas into what he describes as “an interview room.” Brief for Petitioner 3. Because he was “free to leave at that time,” App. 14, they did not give him Miranda warnings. The police then asked Salinas questions. And Salinas answered until the police asked him whether the shotgun from his home “would match the shells recovered at the scene of the murder.” Id., at 17. At that point Salinas fell silent. Ibid.

Salinas was later tried for, and convicted of, murder. At closing argument, drawing on testimony he had elicited earlier, the prosecutor pointed out to the jury that Salinas, during his earlier questioning at the police station, had remained silent when asked about the shotgun. The prosecutor told the jury, among other things, that “[a]n
innocent person’” would have said, “‘What are you talking about? I didn’t do that. I wasn’t there.’” 368 S. W. 3d 550, 556 (Tex. Ct. App. 2011). But Salinas, the prosecutor said, “‘didn’t respond that way.’” Ibid. Rather, “[h]e wouldn’t answer that question.” Ibid.

II

The question before us is whether the Fifth Amendment prohibits the prosecutor from eliciting and commenting upon the evidence about Salinas’ silence. The plurality believes that the Amendment does not bar the evidence and comments because Salinas “did not expressly invoke the privilege against self-incrimination” when he fell silent during the questioning at the police station. Ante, at 1. But, in my view, that conclusion is inconsistent with this Court’s case law and its underlying practical rationale.

A

The Fifth Amendment prohibits prosecutors from commenting on an individual’s silence where that silence amounts to an effort to avoid becoming “a witness against himself.” This Court has specified that “a rule of evidence permitting ‘commen[t] . . . by counsel’ in a criminal case upon a defendant’s failure to testify ‘violates the Fifth Amendment.’” Griffin v. California, 380 U. S. 609, 610, n. 2, 613 (1965) (internal quotation marks omitted). See also United States v. Patane, 542 U. S. 630, 637 (2004) (plurality opinion); Turner v. United States, 396 U. S. 398, 433 (1970) (Black, J., dissenting). And, since “it is impermissible to penalize an individual for exercising his Fifth Amendment privilege when he is under police custodial interrogation,” the “prosecution may not . . . use at trial the fact that he stood mute or claimed his privilege in the face of accusation.” Miranda v. Arizona, 384 U. S. 436, 468, n. 37 (1966) (emphasis added).

Particularly in the context of police interrogation, a
Breyer, J., dissenting

contrary rule would undermine the basic protection that the Fifth Amendment provides. Cf. Kastigar v. United States, 406 U. S. 441, 461 (1972) (“The privilege . . . usually operates to allow a citizen to remain silent when asked a question requiring an incriminatory answer”). To permit a prosecutor to comment on a defendant’s constitutionally protected silence would put that defendant in an impossible predicament. He must either answer the question or remain silent. If he answers the question, he may well reveal, for example, prejudicial facts, disreputable associates, or suspicious circumstances—even if he is innocent. See, e.g., Griffin, supra, at 613; Kassin, Inside Interrogation: Why Innocent People Confess, 32 Am. J. Trial Advoc. 525, 537 (2009). If he remains silent, the prosecutor may well use that silence to suggest a consciousness of guilt. And if the defendant then takes the witness stand in order to explain either his speech or his silence, the prosecution may introduce, say for impeachment purposes, a prior conviction that the law would otherwise make inadmissible. Thus, where the Fifth Amendment is at issue, to allow comment on silence directly or indirectly can compel an individual to act as “a witness against himself”—very much what the Fifth Amendment forbids. Cf. Pennsylvania v. Muniz, 496 U. S. 582, 596–597 (1990) (definition of “testimonial” includes responses to questions that require a suspect to communicate an express or implied assertion of fact or belief). And that is similarly so whether the questioned individual, as part of his decision to remain silent, invokes the Fifth Amendment explicitly or implicitly, through words, through deeds, or through reference to surrounding circumstances.

B

It is consequently not surprising that this Court, more than half a century ago, explained that “no ritualistic formula is necessary in order to invoke the privilege.”
Quinn v. United States, 349 U. S. 155, 164 (1955). Thus, a prosecutor may not comment on a defendant’s failure to testify at trial—even if neither the defendant nor anyone else ever mentions a Fifth Amendment right not to do so. Circumstances, not a defendant’s statement, tie the defendant’s silence to the right. Similarly, a prosecutor may not comment on the fact that a defendant in custody, after receiving Miranda warnings, “stood mute”—regardless of whether he “claimed his privilege” in so many words. Miranda, supra, at 468, n. 37. Again, it is not any explicit statement but, instead, the defendant’s deeds (silence) and circumstances (receipt of the warnings) that tie together silence and constitutional right. Most lower courts have so construed the law, even where the defendant, having received Miranda warnings, answers some questions while remaining silent as to others. See, e.g., Hurd v. Terhune, 619 F. 3d 1080, 1087 (CA9 2010); United States v. May, 52 F. 3d 885, 890 (CA10 1995); United States v. Scott, 47 F. 3d 904, 907 (CA7 1995); United States v. Canterbury, 985 F. 2d 483, 486 (CA10 1993); Grieco v. Hall, 641 F. 2d 1029, 1034 (CA1 1981); United States v. Ghiz, 491 F. 2d 599, 600 (CA4 1974). But see, e.g., United States v. Harris, 956 F. 2d 177, 181 (CA8 1992).

The cases in which this Court has insisted that a defendant expressly mention the Fifth Amendment by name in order to rely on its privilege to protect silence are cases where (1) the circumstances surrounding the silence (unlike the present case) did not give rise to an inference that the defendant intended, by his silence, to exercise his Fifth Amendment rights; and (2) the questioner greeted by the silence (again unlike the present case) had a special need to know whether the defendant sought to rely on the protections of the Fifth Amendment. See ante, at 4 (explaining that, in such cases, the government needs to know the basis for refusing to answer “so that it may either argue that the testimony sought could not be self-
incriminating or cure any potential self-incrimination through a grant of immunity” (citation omitted)). These cases include Roberts, Rogers, Sullivan, Vajtauer, and Jenkins—all of which at least do involve the protection of silence—and also include cases emphasized by the plurality that are not even about silence—namely, Murphy and Garner.

In Roberts and Rogers, the individual refused to answer questions that government investigators (in Roberts) and a grand jury (in Rogers) asked, principally because the individual wanted to avoid incriminating other persons. Roberts v. United States, 445 U. S. 552, 553–556 (1980); Rogers v. United States, 340 U. S. 367, 368–370, and n. 4 (1951). But the Fifth Amendment does not protect someone from incriminating others; it protects against self-incrimination. In turn, neither the nature of the questions nor the circumstances of the refusal to answer them provided any basis to infer a tie between the silence and the Fifth Amendment, while knowledge of any such tie would have proved critical to the questioner’s determination as to whether the defendant had any proper legal basis for claiming Fifth Amendment protection.

In Sullivan, the defendant’s silence consisted of his failure to file a tax return—a return, he later claimed, that would have revealed his illegal activity as a bootlegger. United States v. Sullivan, 274 U. S. 259, 262–264 (1927). The circumstances did not give rise to an inference of a tie between his silence (in the form of failing to file a tax return) and the Fifth Amendment; and, if he really did want to rely on the Fifth Amendment, then the government would have had special need to know of any such tie in order to determine whether, for example, the assertion of privilege was valid and, perhaps, an offer of immunity was appropriate.

In Vajtauer, an alien refused to answer questions asked by an immigration official at a deportation proceeding.
United States ex rel. Vajtauer v. Commissioner of Immigration, 273 U. S. 103, 113 (1927). Here, the circumstances gave rise to a distinct inference that the alien was not invoking any Fifth Amendment privilege: The alien’s lawyer had stated quite publicly at the hearing that he advised his client to remain silent not on Fifth Amendment grounds; rather, the lawyer “‘advise[d] the alien not to answer any further questions until the evidence upon which the warrant is based will be presented here.’” Id., at 106–107 (quoting the lawyer). This statement weakened or destroyed the possibility of a silence-Fifth Amendment linkage; the Government could not challenge his right to invoke the Fifth Amendment; and this Court described its later invocation as “evidently an afterthought.” Id., at 113.

Perhaps most illustrative is Jenkins, a case upon which the plurality relies, ante, at 9, n. 3, and upon which the Texas Court of Criminal Appeals relied almost exclusively, 369 S. W. 3d 176, 178–179 (2012). Jenkins killed someone, and was not arrested until he turned himself in two weeks later. Jenkins v. Anderson, 447 U. S. 231, 232 (1980). On cross-examination at his trial, Jenkins claimed that his killing was in self-defense after being attacked. Id., at 232–233. The prosecutor then asked why he did not report the alleged attack, and in closing argument suggested that Jenkins’ failure to do so cast doubt on his claim to have acted in self-defense. Id., at 233–234. We explained that this unusual form of “prearrest silence” was not constitutionally protected from use at trial. Id., at 240. Perhaps even more aptly, Justice Stevens’ concurrence noted that “the privilege against compulsory self-incrimination is simply irrelevant” in such circumstances. Id., at 241 (footnote omitted). How would anyone have known that Jenkins, while failing to report an attack, was relying on the Fifth Amendment? And how would the government have had any way of determining whether his
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claim was valid? In Jenkins, as in Roberts, Rogers, Sullivan, and Vajtauer, no one had any reason to connect silence to the Fifth Amendment; and the government had no opportunity to contest any alleged connection.

Still further afield from today’s case are Murphy and Garner, neither of which involved silence at all. Rather, in both cases, a defendant had earlier answered questions posed by the government—in Murphy, by speaking with a probation officer, and in Garner, by completing a tax return. Minnesota v. Murphy, 465 U. S. 420, 422–425 (1984); Garner v. United States, 424 U. S. 648, 649–650 (1976). At the time of providing answers, neither circumstances nor deeds nor words suggested reliance on the Fifth Amendment: Murphy simply answered questions posed by his probation officer; Garner simply filled out a tax return. They did not argue that their self-incriminating statements had been “compelled” in violation of the Fifth Amendment until later, at trial. Murphy, supra, at 425, 431; Garner, supra, at 649, 665. The Court held that those statements were not compelled. Murphy, supra, at 440; Garner, supra, at 665. The circumstances indicated that the defendants had affirmatively chosen to speak and to write.

Thus, we have two sets of cases: One where express invocation of the Fifth Amendment was not required to tie one’s silence to its protections, and another where something like express invocation was required, because circumstances demanded some explanation for the silence (or the statements) in order to indicate that the Fifth Amendment was at issue.

There is also a third set of cases, cases that may well fit into the second category but where the Court has held that the Fifth Amendment both applies and does not require express invocation despite ambiguous circumstances. The Court in those cases has made clear that an individual, when silent, need not expressly invoke the Fifth Amend-
ment if there are “inherently compelling pressures” not to do so. *Miranda*, 384 U. S., at 467. Thus, in *Garrity v. New Jersey*, 385 U. S. 493, 497 (1967), the Court held that no explicit assertion of the Fifth Amendment was required where, in the course of an investigation, such assertion would, by law, have cost police officers their jobs. Similarly, this Court did not require explicit assertion in response to a grand jury subpoena where that assertion would have cost two architects their public contracts or a political official his job. *Lefkowitz v. Turley*, 414 U. S. 70, 75–76 (1973); *Lefkowitz v. Cunningham*, 431 U. S. 801, 802–804 (1977). In *Leary v. United States*, 395 U. S. 6, 28–29 (1969), the Court held that the Fifth Amendment did not require explicit assertion of the privilege against self-incrimination because, in the context of the Marihuana Tax Act, such assertion would have been inherently incriminating. In *Albertson v. Subversive Activities Control Bd.*, 382 U. S. 70, 77–79 (1965), we held the same where explicit assertion of the Fifth Amendment would have required, as a first step, the potentially incriminating admission of membership in the Communist Party. The Court has also held that gamblers, without explicitly invoking the Fifth Amendment, need not comply with tax requirements that would, inherently and directly, lead to self-incrimination. *Marchetti v. United States*, 390 U. S. 39, 60–61 (1968); *Grosso v. United States*, 390 U. S. 62, 67–68 (1968). All told, this third category of cases receives the same treatment as the first: Circumstances, rather than explicit invocation, trigger the protection of the Fifth Amendment. So, too, in today’s case.

The plurality refers to one additional case, namely *Berghuis v. Thompkins*, 560 U. S. 370 (2010). See ante, at 8. But that case is here beside the point. In *Berghuis*, the defendant was in custody, he had been informed of his *Miranda* rights, and he was subsequently silent in the face of 2 hours and 45 minutes of questioning before he
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offered any substantive answers. *Id.*, at ___–___ (slip op., at 2–4). The Court held that he had waived his Fifth Amendment rights in respect to his *later speech*. The Court said nothing at all about a prosecutor’s right to comment on his preceding silence and no prosecutor sought to do so. Indeed, how could a prosecutor lawfully have tried to do so, given this Court’s statement in *Miranda* itself that a prosecutor cannot comment on the fact that, after receiving *Miranda* warnings, the suspect “stood mute”? 384 U. S., at 468, n. 37.

We end where we began. “[N]o ritualistic formula is necessary in order to invoke the privilege.” *Quinn*, 349 U. S., at 164. Much depends on the circumstances of the particular case, the most important circumstances being: (1) whether one can fairly infer that the individual being questioned is invoking the Amendment’s protection; (2) if that is unclear, whether it is particularly important for the questioner to know whether the individual is doing so; and (3) even if it is, whether, in any event, there is a good reason for excusing the individual from referring to the Fifth Amendment, such as inherent penalization simply by answering.

C

Applying these principles to the present case, I would hold that Salinas need not have expressly invoked the Fifth Amendment. The context was that of a criminal investigation. Police told Salinas that and made clear that he was a suspect. His interrogation took place at the police station. Salinas was not represented by counsel. The relevant question—about whether the shotgun from Salinas’ home would incriminate him—amounted to a switch in subject matter. And it was obvious that the new question sought to ferret out whether Salinas was guilty of murder. See 368 S. W. 3d, at 552–553.

These circumstances give rise to a reasonable inference
that Salinas’ silence derived from an exercise of his Fifth Amendment rights. This Court has recognized repeatedly that many, indeed most, Americans are aware that they have a constitutional right not to incriminate themselves by answering questions posed by the police during an interrogation conducted in order to figure out the perpetrator of a crime. See *Dickerson v. United States*, 530 U. S. 428, 443 (2000); *Brogan v. United States*, 522 U. S. 398, 405 (1998); *Michigan v. Tucker*, 417 U. S. 433, 439 (1974). The nature of the surroundings, the switch of topic, the particular question—all suggested that the right we have and generally know we have was at issue at the critical moment here. Salinas, not being represented by counsel, would not likely have used the precise words “Fifth Amendment” to invoke his rights because he would not likely have been aware of technical legal requirements, such as a need to identify the Fifth Amendment by name.

At the same time, the need to categorize Salinas’ silence as based on the Fifth Amendment is supported here by the presence, in full force, of the predicament I discussed earlier, namely that of not forcing Salinas to choose between incrimination through speech and incrimination through silence. That need is also supported by the absence of any special reason that the police had to know, with certainty, whether Salinas was, in fact, relying on the Fifth Amendment—such as whether to doubt that there really was a risk of self-incrimination, see *Hoffman v. United States*, 341 U. S. 479, 486 (1951), or whether to grant immunity, see *Kastigar*, 406 U. S., at 448. Given these circumstances, Salinas’ silence was “sufficient to put the [government] on notice of an apparent claim of the privilege.” *Quinn, supra*, at 164. That being so, for reasons similar to those given in *Griffin*, the Fifth Amendment bars the evidence of silence admitted against Salinas and mentioned by the prosecutor. See 380 U. S., at 614–615.
I recognize that other cases may arise where facts and circumstances surrounding an individual’s silence present a closer question. The critical question—whether those circumstances give rise to a fair inference that the silence rests on the Fifth Amendment—will not always prove easy to administer. But that consideration does not support the plurality’s rule-based approach here, for the administrative problems accompanying the plurality’s approach are even worse.

The plurality says that a suspect must “expressly invoke the privilege against self-incrimination.” Ante, at 1. But does it really mean that the suspect must use the exact words “Fifth Amendment”? How can an individual who is not a lawyer know that these particular words are legally magic? Nor does the Solicitor General help when he adds that the suspect may “mak[e] the claim ‘in any language that [the questioner] may reasonably be expected to understand as an attempt to invoke the privilege.’” Brief for United States as Amicus Curiae 22 (quoting Quinn, supra, at 162–163; alteration in original). What counts as “making the claim”? Suppose the individual says, “Let’s discuss something else,” or “I’m not sure I want to answer that”; or suppose he just gets up and leaves the room. Cf. Davis v. Mississippi, 394 U. S. 721, 727, n. 6 (1969) (affirming “the settled principle that while the police have the right to request citizens to answer voluntarily questions concerning unsolved crimes[,] they have no right to compel them to answer”); Berkemer v. McCarty, 468 U. S. 420, 439 (1984) (noting that even someone detained in a Terry stop “is not obliged to respond” to police questions); Florida v. Royer, 460 U. S. 491, 497–498 (1983) (plurality opinion). How is simple silence in the present context any different?

The basic problem for the plurality is that an effort to have a simple, clear “explicit statement” rule poses a serious obstacle to those who, like Salinas, seek to assert
their basic Fifth Amendment right to remain silent, for they are likely unaware of any such linguistic detail. At the same time, acknowledging that our case law does not require use of specific words, see ante, at 2, leaves the plurality without the administrative benefits it might hope to find in requiring that detail.

Far better, in my view, to pose the relevant question directly: Can one fairly infer from an individual’s silence and surrounding circumstances an exercise of the Fifth Amendment’s privilege? The need for simplicity, the constitutional importance of applying the Fifth Amendment to those who seek its protection, and this Court’s case law all suggest that this is the right question to ask here. And the answer to that question in the circumstances of today’s case is clearly: yes.

For these reasons, I believe that the Fifth Amendment prohibits a prosecutor from commenting on Salinas’s silence. I respectfully dissent from the Court’s contrary conclusion.