

March 1, 2010 | Posted By

## United States Supreme Court Clarifies Standard For Determining Corporate Citizenship For Purposes Of Federal Court Diversity Jurisdiction

In [\*Hertz Corp. v. Friend\*](#), No. 08-1107, 2010 U.S. LEXIS 1897 (Feb. 23, 2010), the [United States Supreme Court](#) reversed the [United States Court of Appeals for the Ninth Circuit](#)'s holding that New Jersey-based Hertz Corporation ("Hertz") was a citizen of the State of California for purposes of federal court diversity jurisdiction, rejecting the Ninth Circuit's "business activities" test and instead adopting the corporate "nerve center" standard used by numerous other Circuits. In doing so, the Supreme Court established a single, uniform and clear interpretation of the phrase "principal place of business" for purposes of deciding a corporation's citizenship status in disputes over whether diversity exists among parties to a lawsuit.

Hertz was sued in California state court by two California citizens. It filed a notice seeking removal the action to federal court based upon diversity of citizenship, arguing that the state in which it had its principal place of business (as the term is used in [28 U.S.C. § 1332\(c\)\(1\)](#)) was New Jersey, not California. In support its argument, Hertz submitted a declaration attempting to demonstrate that the majority of its business occurred outside of California and that its leadership and headquarters were in New Jersey. The [United States District Court for the Northern District of California](#) applied the Ninth Circuit's "business activities" test to determine Hertz's citizenship. This test compared the amount of Hertz's business activity on a state by state basis. It found that the plurality of Hertz's business activities were in California, and thus its "principal place of business" was in that State. The Ninth Circuit affirmed.

The Supreme Court disagreed. It recognized that various Circuits have looked to numerous factors in attempting to determine the principal place of a corporation's "business activities." The factors considered by different courts, it observed, led to complicated, differing interpretations of the diversity statute. The Supreme Court addressed this by adopting the "nerve center" test, which was originally set forth in *Scot Typewriter Co. v. Underwood Corp.*, 170 F. Supp. 862, 865 (S.D.N.Y. 1959). This test provides that a corporation's "principal place of business" for purposes of diversity jurisdiction is "the place where a corporation's officers direct, control, and coordinate the corporation's activities. . . . [I]t should normally be the place where the corporation maintains its headquarters – provided that the headquarters is the actual center of direction, control, and coordination."

Three reasons were set forth by the court for adoption of the nerve center test. First, the court looked to the statutory language of 28 U.S.C. § 1332(c)(1). In doing so, it recognized that the word “place” is singular and refers to a place within a state, not to an entire state. A corporation’s main headquarters is generally located in a single place. Conversely, it held, the business activities test was improper because it looks to a corporation’s activities within an entire state. Second, the nerve center test provides for much more simplicity and uniformity than the business activities test. Noting that the rule may sometimes lead to counterintuitive results, the court stated “accepting occasionally counterintuitive results is the price the legal system must pay to avoid overly complex jurisdictional administration while producing the benefits that accompany a more uniform legal system.” Third, the Court noted that legislative history indicated that the statute was aimed at providing a “simplicity-related interpretive benchmark” for determining the principal place of business of a corporation. While the “business activities” test often led to complex investigation into a corporation’s finances and activities, the “nerve center” test provides a simple, straightforward approach.

The significance of this holding for business entities operating in multiple states is significant, especially in the California. A test that focused on and compared the relative amount of business activity among various states state was inherently biased in favor of larger states. The nerve center approach removes that bias. It also provides for greater certainty, since it is not subject to shifts in business fortunes that can occur on a quarter-by-quarter basis. The Supreme Court’s decision promises not only to lessen the burden on entities with substantive operations in states where they do not have their executive offices, but also provides a simple solution for federal courts faced diversity disputes where individual, resident plaintiffs of a state may attempt to keep a dispute in state court.

For further information, please contact [John Stigi](#) at (213) 617-5589 or [Amir Torkamani](#) at (213) 617-4180.