

Identifying A Principal Place Of Business For Diversity Jurisdiction: Supreme Court Settles The Debate

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In the recent United States Supreme Court decision, *Hertz Corp. v. Friend*, 175 L. Ed. 2d 1029, 1034 (U.S. 2010), Justice Breyer posed a question worthy of a law school exam: If the bulk of a company's business activities visible to the public takes place in factories in New Jersey, while its top officers direct those activities from offices just across the river in New York, where is the company's "principal place of business" for purposes of federal diversity jurisdiction?

The Supreme Court concluded that the phrase "principal place of business" for purposes of federal diversity jurisdiction refers to "the place where the corporation's high-level officers direct, control, and coordinate the corporation's activities," and not – as some circuits have held – a more in-depth state-by-state analysis of such factors as manufacturing and sales office locations.¹ In establishing a unitary "principal place of business" definition, the Court resolved an unwieldy split in the circuits as to the applicable test, settling on what has often been referred to as the "nerve center" test.

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"Principal Place Of Business" And Its Importance

The phrase "principal place of business" derives from the federal diversity jurisdiction statute: "a corporation shall be deemed to be a citizen of any State by which it has been incorporated *and of the State where it has its principal place of business.*" 28 U.S.C. § 1332(c)(1) (emphasis added). Determining "principal place of business" under the federal diversity statute is important because it is the first step in analyzing whether a corporation can remove a case to federal court based on diversity jurisdiction – a common goal for corporate defendants. A corporation will be foreclosed from removing a state action to federal court if its "principal place of business" (or incorporation) is in a state where any plaintiff is also a "citizen." Accordingly, one must determine a corporation's "principal place of business" before removal papers are filed. Not only does the party removing a state court action to federal court on the basis of diversity have the burden of establishing its "principal place of business,"² the district court, *sua sponte*, may demand "competent proof" that the "principal place of business" alleged is correct.³

The Split In The Circuits

The concept of "principal place of business" has proven harder to apply than the statute's drafters may have anticipated. Where a corporation operates in a single state, there is no dispute as to the principal place of business. But in modern commerce, corporations often have offices and facilities, of varying degrees of importance, in multiple states. With little guidance from the statute, federal courts have applied varying formulas to determine a corporation's "principal place of business."

The Second Circuit has employed a "two-part test" involving an initial determination as to whether "a corporation's activities are centralized or decentralized" followed by an application of either the "place of operations" or "nerve center" test.⁴ If corporate operations are centralized, courts within the Second Circuit have de-emphasized the concentration on the corporate "nerve center" and instead focused on the state in which a corporation has its "most extensive contacts with, or greatest impact on, the general public."⁵ The Fifth,⁶ Ninth⁷ and Eleventh⁸ Circuits have applied comparable tests.

The Third Circuit employs the "center of corporate activities" test, which requires courts to ascertain "the headquarters of day-to-day corporate activity and management."⁹ The Fourth Circuit recognizes both the "nerve center" and "place of operations" tests, applying the "nerve center" test when the corporation has "multiple centers of manufacturing, purchasing, or sales."¹⁰ The Tenth Circuit has looked to the "total activity of the company considered as a whole,"¹¹ while the Seventh Circuit has long applied the

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simpler “nerve center” test, recognizing the benefit of protecting parties from “the prospect that their litigation may be set at naught because they made a wrong guess about jurisdiction.”¹²

The Circuits’ differing and increasingly complicated tests for defining “principal place of business” have resulted in inconsistent application of the federal diversity jurisdiction statute, making the issue ripe for Supreme Court consideration. For example, in *Inland Rubber Corp. v. Triple A Tire Service, Inc.*, 220 F. Supp. 490 (S.D.N.Y. 1963), the U.S. District Court for the Southern District of New York analyzed the “principal place of business” of plaintiff corporation chartered and headquartered in Ohio. While all corporate officers were located in Ohio, most employees and sales were centered in New York. Defendants, citizens of New York, moved to dismiss on grounds that diversity jurisdiction was lacking. The court acknowledged that although corporate activities were controlled out of Ohio, since its principal operations were conducted in New York, the corporation was a citizen of New York. Accordingly, there was no diversity jurisdiction. Had a similar fact pattern been before a court in the Seventh Circuit, applying the “nerve center” test, it is likely plaintiff’s “principal place of business” would have been deemed Ohio, the location of all corporate officers.

***Hertz* Drives Supreme Court To Consider Issue**

In *Hertz*, California citizens sued Hertz in a California state court for claimed violations of the state’s wage and hour laws. Hertz sought removal to federal court under 28 U.S.C. §§ 1332(d)(2) and 1441(a), claiming the federal court had diversity jurisdiction because plaintiffs were California citizens and Hertz was a citizen of Delaware, its state of incorporation, and New Jersey, its purported “principal place of business.” To show that its “principal place of business” was in New Jersey, Hertz submitted a declaration stating that California accounted for only a portion of its business activity in the 44 states in which it operated, that its leadership is at its corporate headquarters in New Jersey, and that its core executive and administrative functions are primarily carried out there. Plaintiffs opposed

removal claiming lack of diversity jurisdiction because Hertz was also a “citizen” of California since its business activities were most significant in California as compared to its operations in other states.

The District Court sided with plaintiffs, concluding it lacked diversity jurisdiction because Hertz was a California citizen under Ninth Circuit precedent, which asks, *inter alia*, whether the amount of the corporation’s business activity is “significantly larger” or “substantially predominates” in one state.¹³ Finding that California was Hertz’s “principal place of business” under that test because a “plurality of each of the relevant business activities” was in California, the District Court remanded the case.¹⁴ The Ninth Circuit affirmed,¹⁵ and Hertz filed a successful petition for certiorari.

The “Nerve Center” Test

The Supreme Court granted certiorari for the purpose of establishing a single interpretation of “principal place of business.”¹⁶ After a thorough survey of the split among the circuit courts, the Supreme Court concluded that “principal place of business” refers to the state where a corporation’s officers “direct, control, and coordinate the corporation’s activities,” metaphorically called its “nerve center.”¹⁷ The “nerve center” will likely be “where the corporation maintains its headquarters – provided that the headquarters is the actual center of direction, control, and coordination ... and not simply an office where the corporation holds its board meetings (for example, attended by directors and officers who have traveled there for the occasion).”¹⁸

This holding certainly simplifies “principal place of business” analysis. The Court specifically rejected a more complex analysis of the total amount of business activities that a corporation conducts in a state and the need to determine whether they are “significantly larger” than in the next-ranking state.¹⁹ Thus, courts should no longer have to engage in the difficult task of weighing corporate functions, assets, or revenues different in kind, one from the other.²⁰

***Hertz* Will Likely Limit – Not End – Principal Place Of Business Disputes**

While the *Hertz* decision likely limits disputes regarding “principal place of

business,” it probably will not end them. In today’s complex business world, issues are likely to arise involving corporations with more decentralized management, where direction, control, and coordination of activities emanate from multiple locations. For example, a subsidiary corporation with most of its officers and production facilities located in one state, but also with officers located at the corporate parent’s headquarters in another, may present challenges even under the “nerve center” test. Where officers wear multiple hats, serving both the subsidiary and the parent simultaneously, the chance that control and coordination of corporate activities comes from multiple states is highly plausible. Anticipating such scenarios, the Court admits the test is not “perfect” but nonetheless instructs district courts to lean “towards the center of *overall* direction, control, and coordination.”²¹

¹ *Hertz Corp. v. Friend*, 175 L. Ed. 2d 1029 at *1034 (2010).

² *McNutt v. General Motors Acceptance Corp.*, 298 U.S. 178, 189 (1936); *R. G. Barry Corp. v. Mushroom Makers, Inc.*, 612 F.2d 651, 655 (2d Cir. N.Y. 1979).

³ *Wisconsin Knife Works v. National Metal Crafters*, 781 F.2d 1280, 1282 (7th Cir. 1986); see also, *Armstrong Holdings, Inc. v. Armstrong Blue Sky Partners., L.P.*, 2010 U.S. Dist. LEXIS 12036 (W.D. Pa. Feb. 11, 2010).

⁴ *R.G. Barry Corp. v. Mushroom Makers, Inc.*, 612 F.2d 651, 655 (2d Cir. 1979).

⁵ *Id.*

⁶ See, e.g., *Teal Energy USA, Inc. v. GT, Inc.*, 369 F.3d 873, 877 (5th Cir. 2004).

⁷ See, e.g., *Tosco Corp. v. Cmty. for a Better Env’t*, 236 F.3d 495, 500 (9th Cir. 2001).

⁸ See, e.g., *MacGinnitie v. Hobbs Group, LLC*, 420 F.3d 1234, 1239 (11th Cir. 2005).

⁹ See, e.g., *Mennen Co. v. Atl. Mut. Ins. Co.*, 147 F.3d 287, 291 (3d Cir. N.J. 1998).

¹⁰ *Athens Auto. v. Digregorio*, 166 F.3d 288, 290 (4th Cir. 1999).

¹¹ See, e.g., *Gadlin v. Sybron Int’l Corp.*, 222 F.3d 797, 799 (10th Cir. 2000).

¹² *Dimmitt & Owens Financial, Inc. v. United States*, 787 F.2d 1186, 1191 (7th Cir. 1986).

¹³ *Hertz Corp.*, 175 L. Ed. 2d at 1035.

¹⁴ *Id.*

¹⁵ *Friend v. Hertz Corp.*, 297 Fed. Appx. 690, 2008 U.S. App. LEXIS 22592 (9th Cir. 2008).

¹⁶ *Hertz Corp.* 175 L. Ed. 2d at 1041.

¹⁷ *Id.*

¹⁸ *Id.* at 1041-1042.

¹⁹ *Id.* at 1042.

²⁰ *Id.* at 1043.

²¹ *Id.*