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HERTZ CORP. v. FRIEND: THE SUPREME COURT ENDORSES THE "NERVE CENTER" TEST FOR CORPORATE CITIZENSHIP

Few legal questions are more fundamental than a court's ability to hear a case. For 50 years, however, federal courts have disagreed about when federal district courts may hear cases involving corporations in which federal jurisdiction is predicated solely on the parties' differing state citizenship. A federal district court may exercise jurisdiction if there is complete diversity of citizenship between the parties. But the court must first determine each party's state citizenship. Until the Supreme Court's recent decision in *Hertz Corp. v. Friend*, the resolution of this basic question varied where corporate parties were involved.

For diversity jurisdiction purposes, "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). The first prong of this statute is uncontroversial. As for the second prong, federal courts have employed a variety of conflicting approaches to determine the state in which a corporation has its principal place of business.

Some courts adopted the "nerve center" approach, wherein a corporation has a single principal place of business where its executive headquarters are located. Others focused on the corporation's "place of operations" rather than its headquarters. Still others first determined whether the corporation's activities were centralized or decentralized, before applying either the "nerve center" or "place of operations" tests. Several other circuits adopted a "total activities" test, whereby courts were directed to consider both the location of the corporation's "nerve center" and the locations of its operations. Finally, the Ninth Circuit looked to the "state which contains a substantial predominance of corporate operations" first, and only considered the "nerve center" when the initial inquiry did not resolve the issue.

The Ninth Circuit's approach led to particularly anomalous results for corporations operating in California. Because of California's disproportionately large population—approximately 12 percent of the United States population—corporations with widely

dispersed operations were at times found to be California corporations, despite the fact that they were headquartered in other states and conducted the overwhelming majority of their business outside of California.

The complexity and unpredictability of the Ninth Circuit's approach became plain in recent years. In October 2008, the Ninth Circuit affirmed a district court's decision that Hertz Corp., which argued it was headquartered in New Jersey, was a California corporation because 17 percent of its facilities, 18.6 percent of its revenues, and 21.5 percent of its employees were located in California. But in February 2009, the Ninth Circuit reversed a district court's decision concluding that Best Buy Co., Inc., which argued it was headquartered in Minnesota, was a California corporation merely because 11 percent of its retail stores, 13 percent of its revenues, and 13 percent of its employees were located in California. In June 2009, the Supreme Court granted Hertz's petition for a writ of certiorari.

In its subsequent decision in *Hertz Corp. v. Friend* (No. 08-1107), the Supreme Court unanimously endorsed the "nerve center" approach for determining the state in which a corporation has its principal place of business. The Court concluded "that the phrase 'principal place of business' refers to the place where the corporation's high level officers direct, control, and coordinate the corporation's activities," adding that "the 'nerve center' will typically be found at a corporation's headquarters."

Although the Court's decision addressed the statute's text and legislative history, the Court placed particular emphasis on the administrative simplicity of the "nerve center" approach. It noted that complex jurisdictional rules "encourage gamesmanship" and waste judicial resources. Simple jurisdictional rules, however, promote greater predictability for "corporations making business and investment decisions" and for "plaintiffs deciding whether to file suit in a state or federal court." Although the Court acknowledged that the "nerve center" test will not always be precise, it is comparatively simpler than tests focusing on a corporation's operations.

The Court also affirmed that the burden of persuasion remains on the party asserting diversity jurisdiction and emphasized that the "nerve center" approach does not permit jurisdictional manipulation. A party challenged in its assertion of jurisdiction must support its allegations by competent proof. For example, the Court noted that the mere filing of a form like the Securities and Exchange Commission's Form 10-K listing a corporation's "principal executive offices" would not, on its own, establish the corporation's "nerve center." Nonetheless, even if the record shows manipulation, courts do not revert to the corporation's "place of operations." Rather, the court must identify the place of actual direction, control, and coordination of the corporation, in the absence of such manipulation.

Hertz has a variety of implications for corporations. First, all federal courts will be required to apply the same test when locating the state in which the corporation has its principal place of business. Anomalous results between courts should be virtually eliminated, and corporations should no longer be considered citizens of more than one state under the "principal place of business" prong of the federal diversity jurisdiction statute.

Second, many corporations that were previously considered citizens of more populous states in which the "nerve center" test was not employed, particularly California, will now have the opportunity to remove state court actions to federal courts in those states. For instance, corporations that long have been considered California citizens on the basis of their operations will have a new opportunity to reevaluate their California citizenship for diversity jurisdiction purposes.

Third, some corporations may find that they are unable to remove state-court cases in states in which they previously were able to do so. For instance, a corporation with its headquarters in California and the bulk of its operations in Arizona may have been able to remove a case from California state court to federal court under the previous Ninth Circuit approach, but it would no longer be able to exercise that option.

Finally, a corporation must be prepared to support its jurisdictional allegations with proof of the place from which it actually is directed, controlled, and coordinated. Although the body of case law applying the "nerve center" approach will be slight in jurisdictions that previously employed the "place of operations" test, courts that previously applied the "nerve center" approach, such as those in the Seventh Circuit, should provide a valuable source of persuasive precedent while other courts develop their jurisprudence.

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