

BUSINESS TORTS & RICO NEWS

UNTANGLING DIVERSITY JURISDICTION: THE SUPREME COURT'S CONSIDERATION OF *HERTZ CORP. V. FRIEND*

By Michael J. Hahn and Kristin A. Muir¹

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I. Introduction

For purposes of establishing diversity jurisdiction in federal court, a corporation is deemed to be a citizen of "the State where it has its principal place of business."² While this language appears rather simple, its interpretation by the various circuit courts has been anything but. Indeed, circuit courts currently apply four different tests to determine a corporation's principal place of business. Application of these tests can cause a corporation to be deemed a citizen of different states. Such inconsistency caused the United States Supreme Court to grant certiorari in *Hertz Corp. v. Friend*, a case that the Court will likely use to resolve this conflict when it hears argument on November 10, 2009. If the Court does so, it will bring greater predictability to all corporations that are sued for business torts, and will be particularly helpful to those corporations sued for business torts in multiple jurisdictions.³

II. *Hertz Corp. v. Friend*

Hertz Corporation ("Hertz") is an international car rental company incorporated in Delaware that operates "on-airport" and "off-airport" rental facilities in 44 of the 50 states.⁴ Hertz is headquartered in Park Ridge, New Jersey.⁵

On September 6, 2007, plaintiffs filed a putative class action against Hertz in California state court, seeking damages for alleged violations of California's wage and hour laws.⁶ Hertz removed the action to the United States District Court for the Northern District of California on diversity grounds pursuant to the removal provisions of the Class Action Fairness Act of 2005.⁷ In support of its removal application, Hertz submitted a sworn declaration that it is incorporated in Delaware and that it maintains its corporate headquarters in Park Ridge, New Jersey; accordingly, Hertz asserted that it is a citizen of Delaware

where it is incorporated, and New Jersey where it claims to have its principal place of business.⁸ Thereafter, plaintiffs filed a motion to remand the case, arguing that Hertz is a citizen of California because it conducts one-fifth of its business in California – nearly two times more than any other state.⁹ Thus, plaintiffs contend that there is no diversity of citizenship to confer federal jurisdiction.¹⁰

The district court granted plaintiffs' motion, applying the Ninth Circuit's "place of operations" test for determining a corporation's principal place of business.¹¹ Under that framework, the court compared Hertz's business activities in the two states containing the largest amount of business activity – California and Florida: 1) 17% of Hertz' rental facilities are located in California and 9.7% are located in Florida; 2) 18.2% of Hertz' vehicle rentals are transacted in California

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and 10.7% are transacted in Florida; 3) 18.6% of Hertz' revenues are generated in California and 11.6% are generated in Florida; and 4) 20.5% of Hertz' employees are employed in California and 14.3% are employed in Florida.¹² The court found the differential between the activities conducted in California and Florida to be "significant" and thus determined that California is Hertz' principal place of business.¹³ In doing so, the court rejected Hertz' argument that its "nerve center" is located in New Jersey because its senior management is located there. The Ninth Circuit affirmed the district court's order.¹⁴

III. Tests for Determining a Corporation's "Principal Place of Business"

1. Nerve Center Test

The Seventh Circuit utilizes the "nerve center test" in determining a corporation's principal place of business. That test focuses exclusively on locating the corporation's "brain," generally found where the corporation's headquarters is located.¹⁵ The Seventh Circuit noted that other circuits "use a vaguer standard . . . [and] look not just to where the corporation has its headquarters but also to the distribution of the corporation's assets and employees . . . [but w]e prefer [a] simpler test. Jurisdiction ought to be readily determinable."¹⁶ Under the Seventh Circuit's test, the amount of business that a corporation transacts in other states is irrelevant to locating a corporation's principal place of business.¹⁷

2. Center of Corporate Activities Test

The Third Circuit utilizes the "center of corporate activities" test in determining a corporation's principal place of business for purposes of diversity jurisdiction.¹⁸ This test requires a court to examine "the headquarters of day-to-day corporate activity and management."¹⁹ "The center of corporate activities test is similar to the

nerve center test in the sense that it looks for a headquarters, albeit of day-to-day corporate activities and management."²⁰ Unlike the nerve center test, this test considers factors such as the physical location of employees and property.²¹

3. Place of Operations Test

In contrast to the Seventh and Third Circuits, the Ninth Circuit considers the location of a corporation's physical property, employees, and assets to be the predominant factors in identifying its principal place of business.²² The Ninth Circuit's test is essentially a two-part inquiry – a party must first prove that "no single state contains a substantial predominance of its business activities before the district court can consider the location of the corporation's nerve center or its headquarters of day-to-day corporate activities and management."²³ This test does not consider *all* of a corporation's activities; rather, it only considers whether these activities are "significantly larger" in one state as compared to the state with the next largest amount of such activities.²⁴ The Ninth Circuit also made clear that in considering the relative amount of business activities in each state, courts need not consider the relative populations of the two states being compared.²⁵

4. Total Activities Test

The Fifth, Sixth, Eighth, Tenth and Eleventh Circuits apply the "total activities test" in order to determine a corporation's principal place of business.²⁶ This test does not focus on one particular factor; rather it considers the activities of the company as a whole.²⁷ Specifically, a court must consider not only the location of the corporation's headquarters, "and the locations of its business activities, but also the totality of the surrounding circumstances, including things like the character of the corporation, its purposes and the kind of business in which it is engaged."²⁸ Courts applying the total activity test consider a virtually limitless array of factors, including, for example, "the

locations in which the corporation is qualified to do business," . . . "the location of the corporation's principal bank account," . . . "the location of the corporation's work force," . . . "the location of corporate records," . . . and "the location where the corporation's shareholders are citizens and residents".²⁹

IV. Impact of the *Hertz* Case

Hertz is one of the most important cases to be decided by the Supreme Court this term because it will affect nearly every corporation with operations reaching into multiple jurisdictions. Indeed, the case will likely result in a uniform standard for determining a corporation's principal place of business for diversity purposes. This will assist corporations in better predicting the consequences of their business operations. It will also dispense with forum shopping for jurisdictions having more favorable legal standards.

The particular standard that the Court ultimately adopts is paramount for corporations. Out of the four approaches utilized by the various circuit courts in determining a corporation's principal place of business, only the Seventh Circuit's "nerve center" test is a bright-line rule that provides corporations with maximum predictability in assessing exposure to lawsuits in unfavorable state court forums. Having such a bright-line test would also provide clear guidance to counsel in deciding where to properly initiate suit in federal court or in determining whether removability is a viable option when a corporation is sued in state court.³⁰

In comparison, tests employed by the other circuits have less predictable outcomes because they require courts to partake in fact-intensive and sometimes subjective analyses of changing corporate operations.³¹ "And, unlike the deliberate and readily-ascertainable choice of a corporate headquarters, the operations of a corporation must constantly change and respond to the vagaries of markets and

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demographics, and may move in and out of states on a year-by-year, or even month-by-month basis.”³² Under these tests, prospective litigants are left with little certainty that a corporation’s principal place of business will not move itself somewhere else overnight due to changes in the economy or the corporation’s business.³³ A test that concerns itself with the operations or total activities of a corporation yields different results over times as corporations continually reallocate their resources to meet changing market demands and economic conditions.³⁴ “This requires counsel to hit an ever-moving target just to make what should be the simple decision of where to file or remove a case. Even if a corporation’s principal place of business has been determined in one case, it may well be different in the next.”³⁵

Additionally, the *Hertz* case highlights one of the significant pitfalls associated with the Ninth Circuit’s place of operations test. Many corporations with nationwide operations often have one or more of its places of businesses located in California simply because California is the most populous state. For example, if a retailer has operations in all states proportional to the population, and predominance between the two largest states is the relevant determination, “California would be the principal place of business for virtually every corporation because of its larger population.”³⁶ For example, “Starbucks Corporation – world famous as a Seattle, Washington-based corporation – was nevertheless found to be a citizen of California under the Ninth Circuit’s test.”³⁷ This result completely contradicts the underlying purposes of removal, which is to protect out-of-state citizens against the prejudices of certain local courts and juries by making available the benefits the benefits and safeguards of federal courts.³⁸

V. Conclusion

In *Hertz*, the Supreme Court will likely select a single test for determining a corporation’s principal place of business for diversity purposes. Doing so will provide corporations with greater clarity concerning their exposure to lawsuits in unfriendly state court forums. Additionally, if the Seventh Circuit’s nerve center test is selected by the Supreme Court as the operable standard, it will provide trial courts with an easily administrable bright-line rule and corporations with sufficient certainty to plan their business activities.

¹ Michael J. Hahn and Kristin A. Muir are attorneys in the Roseland, N.J. office of Lowenstein Sandler PC.

² 28 U.S.C. § 1332(c)(1).

³ 297 Fed. Appx. 90 (9th Cir. 2008), *cert. granted*, 129 S. Ct. 2766 (2009).

⁴ Petition for Writ of Certiorari at 6-7, *Hertz Corp. v. Friend*, 129 S. Ct. 2766 (2009) (No. 08-1107).

⁵ *Id.*

⁶ Brief of Petitioner at 6, *Hertz Corp. v. Friend*, 129 S. Ct. 2766 (2009) (No. 08-1107).

⁷ *Id.*

⁸ *Id.*

⁹ Brief in Opposition to Petition for Writ of Certiorari at 3, *Hertz Corp. v. Friend*, 129 S. Ct. 2766 (2009) (No. 08-1107).

¹⁰ *Id.* at 6-7.

¹¹ Petition for Writ of Certiorari, *supra* note 4, at 7.

¹² *Id.* at 7-8.

¹³ Brief of Petitioner, *supra* note 6, at 8.

¹⁴ *Id.* at 9.

¹⁵ Petition for Writ of Certiorari, *supra* note 4, at 9-10 (citing *Wis. Knife Works v. Nat. Metal Crafters*, 781 F.2d 1280, 1282 (7th Cir. 1991) (“... a corporation has a single principal place of business where its executive headquarters are located”).

¹⁶ *Id.* at 10 (quoting *Wis. Knife Works*, 781 F.2d at 1282).

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ Brief of Petitioner, *supra* note 6, at 38-39 (quoting *Kelly v. U.S. Steel Corp.*, 284 F.2d 850, 852-54 (3d Cir. 1960).

²⁰ *Id.* (internal quotation marks omitted).

²¹ *Id.*

²² Petition for Writ of Certiorari, *supra* note 4, at 11.

²³ *Id.* at 11.

²⁴ *Id.* at 12.

²⁵ *Id.*

²⁶ Brief of Petitioner, *supra* note 6, at 35.

²⁷ Petition for Writ of Certiorari, *supra* note 4, at 13.

²⁸ *Id.*

²⁹ Brief of Petitioner, *supra* note 6, at 36-37.

³⁰ Brief for Chamber of Commerce of the U.S.A., et al. as Amici Curiae Supporting Petitioner, *Hertz Corp. v. Friend*, 129 S. Ct. 2766 (2009) (No. 08-1107), 2009 WL 2509218, *11 (“[P]arties ought to know definitely what court they belong in, and not face the prospect that their litigation may be set at naught because they made a wrong guess about jurisdiction.”).

³¹ *Id.* at 12-13.

³² *Id.* at 13-14.

³³ *Id.* at 15.

³⁴ *Id.* at 15.

³⁵ Brief for Amici Curiae, *supra* note 30, at 15.

³⁶ Brief for Chamber of Commerce of the U.S.A., et al. as Amici Curiae in Support of Petition for Writ of Certiorari, *Hertz Corp. v. Friend*, 129 S. Ct. 2766 (2009) (No. 08-1107), 2009 WL 924260, *13.

³⁷ *Id.*

³⁸ Petition for Writ of Certiorari, *supra* note 4, at 18.