



Brain Over Brawn

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A Corporation's Place of Business, and thus its State of Citizenship, Lies with its Brain

Strategic or tactical considerations may lead a litigant to prefer federal court over a state venue, and the most common source of federal jurisdiction is "diversity of citizenship" between the parties. Article III of the United States Constitution provides that federal judicial power shall extend to "controversies...between Citizens of different States," and Congress has empowered federal courts to hear disputes "where the matter in controversy exceeds the sum of \$75,000...and is between...citizens of different States."

While it is a fairly simple matter to determine an individual's state of citizenship, it is more complicated if the litigant is a corporation. Congress has decreed that for purposes of diversity jurisdiction, "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..." The Circuit Courts of Appeal have adopted a number of different tests to identify the principal place of a corporation's business. While some look strictly to a corporation's nerve center (brain), others look to the bulk of business activities such as production and sales (brawn). Still others have developed a two-step system that first looks at corporate structure and then decides what test to apply (brain or brawn), and some have developed hybrid tests (brain and brawn). As a result, access to federal courts has differed from circuit to circuit and even from case to case.

On February 24, 2010, the United States Supreme Court finally put an end to the inconsistency and, in a unanimous decision, adopted a simple and uniform standard: a corporation's principal place of business is the state where its "nerve center" is located. *The Hertz Corp. v. Friend*, 559 U.S. ___ (2010). The nerve center is the place where corporate "officers direct, control, and coordinate the business's activities," which normally points to the site of corporate headquarters.

The Supreme Court's goal in adopting this rule was "to find a single, more uniform interpretation of the statutory phrase ['principal place of business']." While the Court's opinion acknowledges that the "nerve center" rule is "imperfect," the Court deemed it "superior to other possibilities." Because the rule is simpler and will be uniform throughout the United States, it should be more economical to administer, reducing jurisdictional disputes and promoting predictability.

To protect against gamesmanship, the Supreme Court required that lower courts administering the nerve center test ferret out the actual place where corporate activities are being "directed, controlled, and coordinated." Thus, a corporation cannot set up a post office box and label it "corporate headquarters," nor is an office with a computer enough to create diversity and open the doors to federal courthouses in other states. The location of the company retreat or annual board meeting is not the "nerve center," even if that is the one place where the Board of Directors convenes each year. Instead, the principal place of business is where day-to-day corporate control occurs. Usually, that will be the headquarters where corporate officers go on a daily basis to direct, control, and conduct the business of the corporation.

The Supreme Court's message was clear: keep it simple, look to the brain.