

Client Advisory

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Davis v. HSBC Bank Nevada, Best Buy Stores, L.P., et al.: Ninth Circuit Clarifies “Principal Place of Business” Test for National Corporations Seeking Removal

The Ninth Circuit's recent published decision in *Davis v. HSBC Bank Nevada, N.A., et al.* impacts all national businesses operating in California. In *Davis*, the court held that Best Buy Stores L.P., the entity that owns and operates the national chain of Best Buy consumer electronics stores, is not a citizen of California for purposes of diversity merely because it has more stores, more employees and more sales in California than in any other U.S. state. This decision is important for any national business sued in California state court that seeks to remove the case to federal court because it stands for the proposition that the mere fact that the corporation does more business in California than any other state (as would be expected given California's population and the size of its consumer market) does not mean that the corporation's principal place of business is in California. Where a corporation is deemed to be a citizen of California, even when its headquarters is located in another state, it may not be able to remove under traditional diversity standards and possibly under the Class Action Fairness Act of 2005.

Background

A limited partnership or a corporation is a citizen of (1) the state under whose laws it is organized or incorporated; and (2) the state of its “principal place of business.” 28 U.S.C. § 1332(c)(1). The Ninth Circuit applies two tests to determine a corporation's principal place of business. First, the court applies the “place of operations” test. Under that test, a corporation's principal place of business is the state having a “substantial predominance” of corporate operations. If no state contains a “substantial predominance” of corporate operations, the Ninth Circuit applies the “nerve center” test, which focuses on where the corporation's executive offices and administrative functions are performed.

Prior to *Davis*, the Ninth Circuit opinions in *Tosco Corp. v. Communities for a Better Env't*, 236 F.3d 495 (9th Cir. 2001) (*per curiam*) and *Indus Tectronics, Inc. v. Aero Alloy*, 912 F.2d 1090 (9th Cir. 1990) provided guidance for determining whether a corporation's activities “substantially predominate” in a particular state. Those courts held that substantial predominance does not require a majority of the corporation's operations in one state, but the corporation's activity must be “substantially larger” in one state than in any other state.

To measure a corporation's presence in a particulate state, the *Tosco* court held that it is appropriate to look at sales, stores and employees in the states in which the corporation does business. Neither of the decisions, however, take into account the population and size of California when measuring these criteria. This is significant because, as a practical matter, virtually any truly national business selling products and services throughout the country could be expected to have more sales, employees and stores in California. As a result, these businesses were deemed to be citizens of California, even though they were headquartered elsewhere and could not remove actions by California plaintiffs based on diversity. That was the case with defendant Best Buy Stores, which has operations in 49 states, the District of Columbia and Puerto Rico, but has its headquarters in Minnesota. Best Buy has 11% of its stores, 13% of its sales and 13% of its employees in California, compared with about 10% of its stores, and 9% of sales and employees in Texas, the next most active state. Based on these facts, the district court held that Best Buy's operations substantially predominate all California and that Best Buy is therefore a citizen of California for purposes of diversity jurisdiction.

The Holding in *Davis*

Davis v. HSBC Bank Nevada, N.A., et al., is a putative class action alleging that the defendants, HSBC Bank Nevada N.A., HSBC Finance Corporation, Best Buy Co. Inc., and Best Buy Stores L.P., did not adequately disclose the annual fee that would be charged to California consumers in their online credit card offer. The defendants removed the case to federal district court under the Class Action Fairness Act. The district court issued an order to show cause why the case should not be remanded, and sought evidence of the defendants' activities in the top five states in which they conduct business. After receiving this information, the district court held that Best Buy Stores L.P. was a citizen of California because it had more stores, more employees and more sales in California. The district court declined to consider California's disproportionately larger population and economic market, and remanded the case back to state court. The defendants then filed a petition for a discretionary appeal, which was granted; after oral argument, the Ninth Circuit issued its decision in favor of the defendants.

The court noted that Best Buy's retail activities roughly reflect California's larger population, and if "a corporation may be deemed a citizen of California on this basis, nearly every national retailer—no matter how far flung its operations—will be deemed a citizen of California for diversity purposes. Such a result is untenable."

Prior to this decision, district courts had issued conflicting opinions on the question presented in *Davis*, and one recent unpublished Ninth Circuit decision held expressly that consideration of California's population was not relevant. Under that analysis, virtually every national business with greater operations in California would be deemed to be a citizen of California, and have its access to federal court severely circumscribed, if not eliminated altogether. The Ninth Circuit has now definitively held that a national business will not be deemed to have its principal place of business in California "merely because its operations in California cater to California's larger population."

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