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Second Circuit Expands Threshold Issues Reviewable Before Determining Complex Issues of Subject-Matter Jurisdiction

It is hornbook law that federal courts must assure themselves that they have subject-matter jurisdiction before addressing the merits of any case.[1] In *Steel Co.* v. *Citizens for a Better Environment* and *Sinochem Int'l Co.* v. *Malaysia Int'l Shipping Corp.*, the Supreme Court of the United States highlighted an exception to this general rule, holding that federal courts may sometimes, in their discretion, rule on merits issues before deciding subject-matter jurisdiction — particularly when subject-matter jurisdiction is difficult to resolve and there are "non-merits," non-jurisdictional grounds for dismissal that are more straightforward. Importantly, courts may exercise this discretion only when (1) the merits question is more readily resolved than the jurisdictional question and (2) the party prevailing on the merits question is the same as the party that would prevail party if jurisdiction were denied.[2] Since then, the lower courts have wrestled with identifying the types of "non-merits," non-jurisdictional grounds that can be considered before ruling on complex questions of subject-matter jurisdiction, including issues such as *forum non-conveniens* and abstention.

In *Phoenix Light SF Limited* v. *Bank of New York Mellon*, the Court of Appeals for the Second Circuit recently added to this list of "non-merits," non-jurisdictional issues in addressing an issue of first impression, and held that the lower court had appropriately dismissed plaintiffs' claims on the non-merits ground of collateral estoppel before determining whether plaintiffs had standing under Article III of the U.S. Constitution to bring their claims.[3] The decision confirms that there are potentially a wide array of "non-merits," non-jurisdictional grounds that federal courts can rely on to dismiss a case before addressing subject-matter jurisdiction.

The outcome of *Phoenix Light* signals that federal courts are increasingly willing to expand the list of permissible non-merits grounds for dismissal before considering complex issues of subject-matter jurisdiction. In the future, courts may be willing to further expand this list to include issues such as international comity, exhaustion, and the political-question doctrine.

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[1] *See, e.g.*, *Steel Co.* v. *Citizens for a Better Env't*, 523 U.S. 83, 95 (1998) ("[E]very federal appellate court has a special obligation to satisfy itself not only of its own jurisdiction, but also that of the lower courts in a cause under review, even though the parties are prepared to concede it.") (citing *Mitchell* v. *Maurer*, 293 U.S. 237, 244 (1934)).

[2] *Steel Co.*, 523 U.S. at 94.

[3] *Phoenix Light SF Ltd.* v. *Bank of New York Mellon*, 2023 WL 3082212, at *6 (2d Cir. Apr. 26, 2023).

Background: Prior U.S. Supreme Court Decisions

In *Steel Co* v. *Citizens for a Better Environment*, an environmental group sued a steel manufacturer under the Emergency Planning and Community Right-To-Know Act of 1986 (EPCRA) for failure to make required reporting.[4] Upon receiving the environmental group's statutory notice of intent to sue, the manufacturer filed the overdue reports and then moved to dismiss.[5] The trial court granted the motion to dismiss, but the Court of Appeals for the Seventh Circuit reversed and remanded.[6] The manufacturer petitioned for *certiorari*, which the Supreme Court granted on the issue of whether the EPCRA allowed parties to sue for a historical violation that had since been remedied.[7] The manufacturer argued that plaintiffs lacked Article III standing to bring their claims.[8]

Justice Scalia delivered the opinion of the Court, which disavowed the so-called practice of "hypothetical jurisdiction," whereby certain courts considered the merits of a case before determining the issues underlying constitutional jurisdiction.[9] The Court criticized this practice as "carr[ying] the courts beyond the bounds of authorized judicial action and thus offend[ing] fundamental principles of separation of powers." The Court held that "[w]ithout jurisdiction the court cannot proceed at all in any cause," and "[j]urisdiction is power to declare the law, and when it ceases to exist, the only function remaining to the court is that of announcing the fact and dismissing the cause."[10]

The *Steel Co*. opinion, however, provided that courts could determine other threshold issues before ruling on Article III standing — namely, whether dismissal would be appropriate under *Younger* v. *Harris*, which the Court viewed as a jurisdictional issue, or through the denial of discretionary pendant jurisdiction.[11]

Similarly, in *Ruhrgas AG* v. *Marathon Oil Co.*, the Supreme Court noted that there was no mandatory "sequencing of jurisdictional issues" and that a court could dismiss a case for lack of personal jurisdiction before determining subject-matter jurisdiction.[12] The Court noted that it was "hardly novel for a federal court to choose among threshold grounds for denying audience to a case on the merits," again citing instances where other jurisdictional issues were decided before addressing issues of Article III standing.[13] Despite this, many federal courts of appeal read *Steel Co.* as requiring issues of subject-matter and personal jurisdiction to be resolved before considering any non-merits, non-jurisdictional issues.[14]

Almost a decade after deciding *Steel Co.*, the Supreme Court took up *Sinochem Int'l Co.* v. *Malaysia Int'l Shipping Corp.*, where it considered whether it had to first establish its own subject-matter jurisdiction before dismissing a suit on grounds of *forum non conveniens*.[15] The Court clarified that federal courts have "leeway" to

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[4] *Steel Co.*, 523 U.S. at 83.

[5] *Id.*

[6] *Id.*

[7] *Id.*

[8] *Id.* at 88.

[9] *Id.* at 93-102.

[10] *Id.* at 95 (citing *Ex parte McCardle*, 7 Wall. 506, 514, 19 L.Ed. 264 (1868)).

[11] *Id.* at n. 3, (citing *Moor* v. *County of Alameda*, 411 U.S. 693 (1973) and *Ellis* v. *Dyson*, 421 U.S. 426 (1975)).

[12] 526 U.S. 574, 575 (1999).

[13] *Id.* at 585.

[14] *See, e.g.*, *Patrickson* v. *Dole Food Co.*, 251 F.3d 795, 800 n.3 (9th Cir. 2001); *Kamel* v. *Hill-Rom Co.*, 108 F.3d 799, 805 (7th Cir. 1997).

[15] 549 U.S. 422 (2007).

dismiss cases before determining Article III standing, not just on other jurisdictional grounds, but also on the basis of non-merits issues.[16] In so holding, the Court reasoned that, regardless of the "threshold ground[] for denying an audience on the merits," a "[d]ismissal short of reaching the merits means that the court will not 'proceed at all' to an adjudication of the cause."[17] Citing the Seventh Circuit's opinion in *Intec USA, LLC* v. *Engle*,[18] the Court reasoned that the general rule requiring that determinations of jurisdictional questions be made first allowed for this exception because "[j]urisdiction is vital only if the court proposes to issue a judgment on the merits."[19]

The *Sinochem* opinion found that a *forum non conveniens* determination in the relevant context was an allowable "threshold, nonmerits" issue and provided that the"[t]he critical point" in this decision was "simply [that]: Resolving a *forum non conveniens* motion does not entail any assumption by the court of substantive 'law-declaring power.'"[20]

Sinochem has provided the lower courts with apparent license to determine a broad variety of non-merits grounds on which to dismiss claims before determining Article III standing.

The Second Circuit's Decision in *Phoenix Light*

In *Phoenix Light*, issuers of collateralized debt obligations secured by residential mortgage-backed securities (RMBS) trust certificates sought to recover losses from their RMBS investments in the wake of the 2008 collapse of the housing market, bringing various suits against RMBS trustees, including U.S. Bank, BNY Mellon, and Deutsche Bank.[21] The suit against U.S. Bank was ultimately dismissed on the ground that plaintiffs' claims were barred by the defense of champerty and that neither prudential nor Article III standing existed.[22] After the Second Circuit affirmed that dismissal, the district court in the BNY Mellon action dismissed the case, finding that plaintiffs were collaterally estopped from relitigating the issue of prudential standing by the U.S. Bank action's decision on the champerty defense, and would in any case lack prudential standing even "under a fresh analysis."[23] Roughly a month later, the trial court in the Deutsche Bank action arrived at the same conclusion.[24]

In reaching these decisions, the trial courts "assumed that Plaintiffs had Article III standing." Plaintiffs appealed, arguing that the courts had to rule on the Article III standing issue before considering collateral estoppel because the standing issue presented a question of subject-matter jurisdiction.[25]

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[16] *Id.* at 431.

[17] *Id.*

[18] 467 F.3d 1038, 1041 (7th Cir. 2006).

[19] 549 U.S. at 431.

[20] *Id.* at 433.

[21] *Phoenix Light SF Ltd.*, 2023 WL 3082212, at *1.

[22] *Id.* "Champerty" refers to a relationship where third parties uninvolved with a litigation provide support to litigants in exchange for consideration dependent on the outcome of that litigation. *See Ehrlich* v. *Rebco Ins. Exch.*, Ltd., 225 A.D.2d 75, 77 (1996). In this instance, plaintiffs had previously conveyed all right, title, and interest in the RMBS certificates to third parties. *Phoenix Light SF Ltd.*, 2023 WL 3082212, at *1. These third parties assigned litigation rights associated with the certificates back to plaintiffs in order to allow them to pursue these actions. *Id.* The trial court found that the assignment of litigation rights was champertous and therefore invalid; plaintiffs accordingly lacked the purportedly assigned rights and, consequently, standing to sue.

[23] *Id.*

[24] *Id.*

[25] *Id.* (citing *Snoqualmie Indian Tribe* v. *Washington*, 8 F.4th 853 (9th Cir. 2021)).

The Second Circuit disagreed, holding that estoppel was a non-merits, threshold ground "suitable for resolution before addressing a difficult or novel question of constitutional jurisdiction."[26] It noted that "the ordinary rule" required courts to address constitutional standing first, but that courts retained "leeway" to dismiss actions based on non-jurisdictional, non-merits grounds, "particularly where the constitutional-jurisdiction question is difficult to determine and dismissing on the threshold issue is the less burdensome course."[27]

The Second Circuit noted that this was a question of first impression in the Second Circuit but also recognized that the Court of Appeals for the Ninth Circuit had addressed this same question in *Snoqualmie Indian Tribe* v. *Washington*.[28] In *Snoqualmie*, the Ninth Circuit concluded that estoppel could be considered before Article III standing, and the Second Circuit expressly adopted that decision's rationale that "issue preclusion is a non-merits inquiry because it 'does not require the court to assume substantive law-declaring power.'"[29] It agreed with the rationale that "just as a *forum-non-conveniens* dismissal is a determination that the merits should be adjudicated by a different court, an issue-preclusion dismissal is a determination that the merits (of at least one issue) have already been adjudicated by a different court." The Second Circuit went on to explain that "because jurisdiction is vital only if the court proposes to issue a judgment on the merits . . . and an issue-preclusion dismissal is not a judgment on the merits, courts are permitted to dismiss on the basis of issue preclusion without reaching harder Article III standing questions."[30]

Separately addressing whether collateral estoppel was appropriately decided by the lower courts, the Second Circuit considered that the champerty-based prudential standing issue in the BNY Mellon and Deutsche actions was decisive and "identical to the one decided in the U.S. Bank Action," as the parties had never disputed that materially identical transactions were at issue in all the actions.[31] The court also declined to find error in the lower courts' determinations that plaintiffs had had a full and fair opportunity to litigate the issue of champerty in the U.S. Bank action.[32] The court rejected each of plaintiffs' arguments that (1) the prudential-standing issue decided in the U.S. Bank action was a purely legal one that could not have preclusive effect under New York law, noting that the district courts had considered the factual determination of the purpose behind the plaintiffs' acquisition of rights in considering the champerty claims; (2) invalidation of the assignments was unfair, finding that plaintiffs had waived this argument but that it was in any case incorrect; (3) defendants had unclean hands and thus could not assert the equitable doctrine of collateral estoppel, finding this to be irrelevant; and (4) BNY Mellon had failed to originally plead, and thus had waived, the issue of champerty, finding that the lower courts had the power to raise the issue *sua sponte*.[33]

Ultimately, the Second Circuit "fully agree[d] with the district courts that Plaintiffs were not entitled to a second bite at the prudential-standing apple" and that they had not erred in taking a "straightforward, if not textbook path to dismissal" before considering Article III standing.[34]

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[26] *Id.* at *3.

[27] *Id.* (internal citations omitted).

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] *Id.* at *4.

[32] *Id.*

[33] *Id.* at *4-5.

[34] *Id.* at *6.

Conclusion

Since the Supreme Court's ruling in *Steel Co.*, the lower courts have wrestled with determining which types of non-merits, non-jurisdictional issues can be resolved without addressing subject-matter jurisdiction. The Second Circuit's opinion in *Phoenix Light* finding that collateral estoppel may be considered before the issue of Article III standing, however, appears to be part of a growing trend among the lower courts to adopt a broad understanding of the types of non-merits issues that can be considered before courts rule on complex questions of subject-matter jurisdiction. Opinions from other federal appellate courts in recent cases have similarly signaled greater comfort with asserting discretion in determining the order in which to consider non-merits issues.[35]

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Joel Kurtzberg (partner) at 212.701.3120 or jkurtzberg@cahill.com; Adam Mintz (counsel) at 212.701.3981 or amintz@cahill.com; or Caroline Neville (associate) at 212.701.3286 or cneville@cahill.com; or email publications@cahill.com.

[35] *See, e.g., Kimberly Regenesis, LLC* v. *Lee Cnty.*, 64 F.4th 1253, 1258 (11th Cir. 2023) (stating that an appeal raised many jurisdictional and other threshold questions, and that the court "had the option of choosing which path to go down"); *The Fla. Wildlife Fed'n Inc.* v. *United States Army Corps of Engineers*, 859 F.3d 1306, 1321 (11th Cir. 2017) (describing the confusion of courts tasked with applying the "jurisdictional-sequencing trilogy" cases); *see also Lopez* v. *Griswold*, 2023 WL 1960802, at *1 (10th Cir. Feb. 13, 2023) (asserting the court's discretion under *Sinochem* to dismiss an appeal on prudential mootness grounds before consideration of constitutional issues); *Khadr* v. *United States*, 67 F.4th 413, 418 (D.C. Cir. 2023) (dismissing case for failure to meet exhaustion requirements and declining to first consider issues of subject-matter jurisdiction); *In re Douse*, 2023 WL 2965594, at *1, n. 1 (Fed. Cir. Apr. 17, 2023) (dismissing petition for *mandamus* absent consideration of jurisdiction where petitioner had failed to show that *mandamus* relief was the only adequate path to the requested relief).