



## Bankruptcy ADVISORY ■

**MARCH 31, 2015**

### Following *Stern*, Bankruptcy Courts Are Sending State Law Claims to the District Court for Final Review

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Bankruptcy courts appear to be increasingly sending state law claims to the district court for final review, as illustrated by a recent decision from the bankruptcy court for the Southern District of Texas. In *Gomez v. Lone Star National Bank (In re Saenz)*, Jose Gomez financed his acquisition of a restaurant from Humberto Saenz. When the restaurant failed, Gomez sued his lender and Saenz on various claims, but Saenz filed for bankruptcy protection. The lender then moved for summary judgment against Gomez's claims for common-law fraud and negligence. The bankruptcy court granted the lender summary judgment, but rather than enter a final order, it issued proposed findings of fact and conclusions of law for the district court's review. Since the claims at issue were state law claims, the bankruptcy court held that it could not enter a final order. In so ruling, the bankruptcy court followed the Supreme Court's guidance in *Stern v. Marshall* and *Executive Benefits Insurance Agency v. Arkison*.

In *Stern*, the Supreme Court held that bankruptcy courts lack constitutional authority to enter a final order on a state law counterclaim by the estate against a creditor. In *Arkison*, the Supreme Court clarified that, upon encountering a "Stern claim" over which it could not enter a final order, a bankruptcy court should instead treat the claim as a "noncore" claim under the Bankruptcy Code and issue proposed findings of fact and conclusions of law. Although the Supreme Court has yet to define what exactly a "Stern claim" is or to specify the parameters of the bankruptcy court's constitutional authority over state law claims, the *Gomez* decision shows that bankruptcy courts now have a workable method for dealing with potential *Stern* claims.

As in *Gomez*, bankruptcy courts are likely to issue proposed findings of facts and conclusions of law whenever they encounter state law claims (and other claims that are found to be *Stern* claims), thereby avoiding any constitutional pitfalls associated with *Stern*. This development means that litigants are likely to see increased costs and delay, as litigation will be handled first by the bankruptcy court and then reviewed again, in full, by the district court. Lenders and other parties at risk for litigation in bankruptcy courts should take these increased costs and delay into account when determining their litigation strategies.

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If you have questions regarding the information in this bankruptcy and restructuring update, please feel free to reach out to:

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Kit Weitnauer  
404.881.7780  
kit.weitnauer@alston.com

Kevin Hembree  
404.881.7831  
kevin.hembree@alston.com

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ATLANTA: One Atlantic Center ■ 1201 West Peachtree Street ■ Atlanta, Georgia, USA, 30309-3424 ■ 404.881.7000 ■ Fax: 404.881.7777  
BRUSSELS: Level 20 Bastion Tower ■ Place du Champ de Mars ■ B-1050 Brussels, BE ■ +32 2 550 3700 ■ Fax: +32 2 550 3719  
CHARLOTTE: Bank of America Plaza ■ 101 South Tryon Street ■ Suite 4000 ■ Charlotte, North Carolina, USA, 28280-4000 ■ 704.444.1000 ■ Fax: 704.444.1111  
DALLAS: 2828 North Harwood Street ■ 18th Floor ■ Dallas, Texas, USA, 75201 ■ 214.922.3400 ■ Fax: 214.922.3899  
LOS ANGELES: 333 South Hope Street ■ 16th Floor ■ Los Angeles, California, USA, 90071-3004 ■ 213.576.1000 ■ Fax: 213.576.1100  
NEW YORK: 90 Park Avenue ■ 15th Floor ■ New York, New York, USA, 10016-1387 ■ 212.210.9400 ■ Fax: 212.210.9444  
RESEARCH TRIANGLE: 4721 Emperor Blvd. ■ Suite 400 ■ Durham, North Carolina, USA, 27703-85802 ■ 919.862.2200 ■ Fax: 919.862.2260  
SILICON VALLEY: 1950 University Avenue ■ Fifth Floor ■ East Palo Alto, CA 94303-2282 ■ 650.838.2000 ■ Fax: 650.838.2001  
WASHINGTON, DC: The Atlantic Building ■ 950 F Street, NW ■ Washington, DC, USA, 20004-1404 ■ 202.756.3300 ■ Fax: 202.756.3333