



Bankruptcy ADVISORY ■

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

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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