



Stern v. Marshall

Core Bankruptcy Proceedings Are Not Necessarily Constitutional for a Bankruptcy Court to Finally Adjudicate

By: Rick Kuebel, III and David W. Wirt

The Supreme Court recently issued its opinion in *Stern v. Marshall* (*Stern*), Case No. 10-179, 2011 WL 2472792 (U.S. June 23, 2011), invalidating the relatively common assumption that so called “core” bankruptcy proceedings are all matters in which the bankruptcy courts are permitted to enter final judgment, and undoubtedly fostering heightened jurisdictional scrutiny in the future.

The dispute arose out of the longstanding litigation between Ms. Vickie Lynn Marshall (also known as Anna Nicole Smith, “Ms. Marshall”) and Mr. Pierce Marshall (“Mr. Marshall”), the son of her former husband. After her husband’s death, Ms. Marshall filed for bankruptcy protection and Mr. Marshall filed suit against her bankruptcy estate for defamation. Ms. Marshall counter-claimed for tortious interference with an expected gift from her late husband. Believing Ms. Marshall’s counter-claim to be a “core proceeding” under 28 U.S.C. § 157(b)(2)(C), the bankruptcy court rendered a final judgment on the counter-claim in Ms. Marshall’s favor. Appeal was taken.

On appeal to the Supreme Court, the Court was primarily concerned with whether Bankruptcy Court had both the statutory *and* Constitutional authority to render a final judgment on Ms. Marshall’s tortious interference counter-claim. Failing either prong would mean that the Bankruptcy Court would only be permitted to offer suggested findings of fact and conclusions of law to the Federal District Court, which would then have the authority to review the matter *de novo* (completely new and from the beginning) if any party objected. See 28 U.S.C. § 157(c).

Answering the first inquiry – requisite statutory authority – was relatively simple. The Court reviewed 28 U.S.C. § 157(b), which provides in pertinent part:

- (b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all *core proceedings* arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.
- (2) Core proceedings include, but are not limited to –
 - ...
 - (C) counterclaims by the estate against persons filing claims against the estate...

See 28 U.S.C. § 157(b)(2)(C) (emphasis supplied). The Court then unanimously concluded that Ms. Marshall’s tortious interference claims fell squarely within the statutory definition of a core



proceeding as a “counterclaim” to Mr. Marshall’s claim of defamation. See *Stern*, 2011 WL 2472792, at *9.

As a practical matter, a “core” finding would often end the jurisdictional inquiry. Indeed, the Supreme Court recognized as much:

In past cases, we have suggested that a proceeding’s “core” status alone authorizes a bankruptcy judge, as a statutory matter, to enter final judgment in the proceeding. See, e.g., *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989) (explaining that Congress had designated certain actions as ‘core proceedings,’ which bankruptcy judges may adjudicate and in which they may issue final judgments...) *Id.*, at *9.

But mere statutory authority is not enough, the Court ruled, in order to permit a Bankruptcy Judge to issue a final order on the matter. The Bankruptcy Court must also have Constitutional authority to enter the final judgment, and in this instance, by a 5 to 4 split decision, the Court concluded that the Bankruptcy Court did not have the requisite Constitutional authority. *Id.*, at *27.

The Court’s analysis is fairly involved, but distilled to its essence, the analysis revolves around the fact that the Constitution requires that only Article III courts – whose judges are protected with life tenure and against salary reductions – may enter final judgment on common law claims that are not otherwise “derived from a federal regulatory scheme.” In a general sense, where these “public rights” were not implicated, and where, in a bankruptcy case, the action at issue was between two private parties and did not implicate the resolution of a proof of claim, Constitutional authority would only reside in the Article III Federal District Court:

We cannot compromise the integrity of the system of separated powers and the role of the Judiciary in the system, even with respect to challenges that may seem innocuous at first blush.

Article III of the Constitution provides that the judicial power of the United States may be vested only in courts whose judges enjoy the protections set forth in that Article. We conclude today that Congress, in one isolated respect, exceeded that limitation in the Bankruptcy Act of 1984. The Bankruptcy Court below lacked the constitutional authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditors’ proof of claim. *Id.*, at * 27.

It remains to be seen as to whether the majority is correct in its prediction that removal of counterclaims like Ms. Marshall’s from the operational jurisdiction of the Bankruptcy Court will not “meaningfully change[] the division of labor in the current statute.” *Id.*, at *26. Post-*Stern*, however, bankruptcy litigants should remain keenly aware of the limited nature of the Bankruptcy Court’s jurisdiction, closely consult with counsel, and remain vigilant as to the best methods for preserving and exercising their jurisdictional rights.

Please contact any of [Locke Lord’s Bankruptcy/Restructuring attorneys](#) with questions about the *Stern v. Marshall* opinion.

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact the authors:

Rick Kuebel, III | T: 504-558-5155 | rkuebel@lockelord.com
David W. Wirt | T: 312-443-0256 | dwirt@lockelord.com