

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION**

**In re
HADAD DESIGN AND
CONSTRUCTION, INC.,**

Debtor.

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**No. 24-33277
Chapter 11**

**HARRIS COUNTY, TEXAS’ REPLY TO DEBTOR’S OPPOSITION TO HARRIS
COUNTY, TEXAS’ MOTION FOR DETERMINATION
THAT THE AUTOMATIC STAY DOES NOT APPLY**

TO THE HONORABLE CHRISTOPHER M. LOPEZ,

Harris County, Texas and the State of Texas by and through the Harris County Attorney, Christian D. Menefee, file this Reply to Debtor’s Opposition to Harris County, Texas’ Motion for Determination that the Automatic Stay Does Not Apply (the “Opposition”), and would show the Court as follows:

1. Harris County has asked this Court to determine that the automatic stay does not apply to its state court case enforcing the Deceptive Trade Practices Act (“DTPA”) against Debtor in *Elias Haddad et al.*, No. 2025-08779, 334th Judicial District of Harris County, Texas. Debtor responds to Harris County’s Motion by claiming that Harris County’s exercise of its police power to enforce consumer protection laws against Debtor is primarily focused “on obtaining monetary relief, including civil penalties and restitution for specific consumers, rather than forward-looking regulatory enforcement.” Opp. at ¶ 6.

2. The police and regulatory power exception contained in 11 U.S.C. § 362(b)(4) is based on the compelling need for the government to continue to protect the public when a debtor files for bankruptcy and to “prevent a debtor from ‘frustrating necessary governmental functions by seeking refuge in bankruptcy court.’” *In re Gandy*, 327 B.R. 796, 801-802 (Bankr. S.D. Tex. 2005);

see also *Commodity Futures Trading Comm'n. v. Co Petro Mktg. Group Inc.*, 700 F.2d 1279, 1283 (9th Cir. 1983) (“a fundamental policy behind the police or regulatory power exception ... is ‘to prevent the bankruptcy court from becoming a haven for wrongdoers.’”). In arguing that the exception to the automatic stay does not apply, Debtor repeatedly misconstrues the law and ignores the fact that consumer protection enforcement actions are squarely within the exception to the automatic stay outlined in 11 U.S.C. § 362(b)(4).

I.

Debtor Misstates and Misunderstands *Commonwealth Oil* and *In re Gandy*.

3. Debtor makes several misstatements and misquotes of caselaw, and fundamentally misunderstands *Commonwealth Oil* and *In re Gandy*. Both cases demonstrate that Harris County’s state court action is excepted from the automatic stay.

A. Debtor Misstates *Commonwealth Oil*. The police and regulatory power exception to the automatic stay should be construed broadly.

4. Debtor states that in *Commonwealth Oil*, the “Fifth Circuit emphasized that” the police and regulatory power exception contained in 11 U.S.C. § 362(b)(4) should be “narrowly construed.”¹ Opp. at ¶¶ 8, 10, 33. This is a misstatement of the law—the Fifth Circuit said the complete opposite. Twice. In *Commonwealth Oil*, the Fifth Circuit soundly rejected to *the debtor’s argument* that the police power exception to the automatic stay should be construed narrowly by reasoning that the Third Circuit found “that the exception to the automatic stay in § 362(b)(4) should be construed *broadly* so as not to override state laws enacted to protect some public interest.” *Matter of Commonwealth Oil Ref. Co., Inc.*, 805 F.2d 1175, 1184 (5th Cir. 1986) (citing *Penn Terra Ltd. v. Dep’t of Env’t Res., Com. of Pa.*, 733 F.2d 267, 273 (3d Cir. 1984)) (emphasis added). The Fifth

¹ Debtor misquotes *Commonwealth Oil*, nowhere in the case does the court say, “narrowly construed.”

Circuit noted that the “exception to the exception” created by § 362(b)(5), making enforcement of money judgments by governmental units subject to the automatic stay, “should be construed *narrowly* so as to leave to the States as much of their police power as a fair reading of the statute allows.” *Id.* at n. 8 (emphasis in original).

5. The Fifth Circuit further rejected the debtor’s argument by stating that “[w]e cannot read these statements to exempt from the exception police and regulatory actions designed to protect the public health and safety. *We find no basis for reading the admonition that the exception be construed narrowly* to exclude anything but those actions which are, in fact, aimed at protecting the government’s monetary interest.” *Id.* at n. 7 (emphasis added).

6. Debtor additionally asserts that *Commonwealth Oil* stands for the proposition that exercises of a governmental unit’s police or regulatory power can only be excepted from the automatic stay if there is an “imminent threat to public health.” Opp. at ¶ 13-14. *Commonwealth Oil* explicitly rejects this argument and states the opposite—“[t]he exception from the automatic stay from proceedings to enforce police and regulatory powers is *not [] limited to those situations where imminent and identifiable harm to the public health and safety or urgent public necessity is shown.*” *Commonwealth Oil* at 1184 (internal citations omitted) (emphasis added). Indeed, the plain language of § 362(b)(4) allows for no such reading; it “does not limit the exercise of police or regulatory powers to instances where there can be shown imminent and identifiable harm or urgent public necessity.” *Id.*

7. Debtor again misstates the law by stating that “[t]he Fifth Circuit in *Commonwealth Oil* recognized that when a governmental unit’s action ‘concerns only the parties who are immediately affected the debtor is entitled to the same protection under § 362(a)(1) it would receive under the

automatic stay if the proceeding were pending instead in a judicial forum.’ 805 F.2d at 1182-86.” Opp. at ¶ 30. This quote does not appear in *Commonwealth Oil*.

8. Debtor repeatedly misstates applicable authority in asking the Court to find that Harris County’s suit against Debtor under the DTPA is not excepted to the automatic stay.

B. *In re Gandy* Mirrors Harris County’s State Court Case and Shows that Harris County Satisfies the Pecuniary Interest and Public Policy tests.

9. Debtor continues its misstatements of the law by ignoring the fact that the Court in *Gandy* held that the automatic stay did not apply to the State of Texas’ DTPA suit against one of the debtors. *Gandy* at 806.

10. Debtor states that Harris County’s reliance on *Gandy* is misplaced because *Gandy* was a suit dealing with enforcement of environmental laws. However, in *Gandy*, while the court did consider enforcement of environmental laws against debtor Ricky Lynn Gandy, the Court also considered whether the State’s DTPA suit against debtor, Elvia Diaz, was excepted from the automatic stay. In its suit against Ms. Diaz, the State of Texas alleged violations of the DTPA through her “notario fraud.”² *Id.* at 799. The *Gandy* court noted that the DTPA is a consumer protection law and that “the purpose of the Deceptive Trade Practices Act is to further the public policy of protecting Texas consumers from actions such as those alleged to have been committed by Ms. Diaz.” *Id.* at 806 (internal citations omitted).

11. In *Gandy*, as in Harris County’s state court lawsuit against Debtor, the State sought damages authorized by the DTPA in addition to injunctive relief. The *Gandy* Court held that the State’s action passed the pecuniary purpose test because the State sought injunctive relief, and all

² The State of Texas alleged that Ms. Diaz impersonated an attorney by using the title “notario” which is interpreted to mean “attorney” by the Mexican community.

penalties sought under the DTPA are specifically authorized by statute and were ancillary to the State's suit against Ms. Diaz. *Id.*

II.

Harris County's State Suit against Debtor for the Enforcement of the Deceptive Trade Practices Act Satisfies the Pecuniary Interest and Public Policy Tests.

12. Harris County determined it would be in the public interest to protect Texas consumers by bringing suit to enforce the DTPA against Debtor, by and through the Harris County Attorney, to obtain injunctive relief, and all penalties and restitution authorized under Tex. Bus. & Com. Code § 17.47.³ This suit is excepted from the automatic stay under 11 U.S.C. § 362(b)(4).

13. Harris County has already stated, and Debtor does not dispute, that the proper tests for the Court to apply in determining that the automatic stay does not apply are the “pecuniary interest” test and “public policy” test.

A. Harris County's State Court Suit Passes the Pecuniary Interest Test.

14. Debtor argues that Harris County's state court action to enforce the DTPA fails the pecuniary interest test because Harris County requests all relief available under the statute, including civil penalties and restitution. Debtor relies on *In re RGV Smiles by Rocky L. Salinas D.D.S. P.A.*, to support this argument – this reliance is misplaced and reflects a fundamental misunderstanding of the case.⁴ 626 B.R. 278, 285 (Bankr. S.D. Tex. 2021). In *RVG Smiles*, the State of Texas requested that the Court determine that the automatic stay did not apply to its state court suit to enforce the Texas Medicaid Fraud Prevention Act (“TMFPA”) against the debtors.

³ Harris County has affirmatively pled that the proceedings are in the public interest. See Ex. A at ¶¶ 16, 41.

⁴ Debtor misstates the holding of *RVG Smiles* in ¶ 12 of its Opposition. It erroneously states that “the court held that ‘when a governmental unit acts primarily to further its financial interests, rather than to protect public health and safety, the action is considered pecuniary and the automatic stay applies.’” In *RVG Smiles*, the Court held that the State of Texas' state court lawsuit against debtors for enforcement of the TMFPA was exempted from the automatic stay after determining that it was a governmental unit and satisfied the pecuniary interest and public policy tests. *RVG Smiles* at 289.

RVG Smiles at 282. In the State’s action, it sought restitution and penalties in the amount of any payment provided under the Medicaid program, directly or indirectly, as a result of their unlawful acts, plus interest from the date of the payment, plus two times the amount of the payment and civil penalties in the amount prescribed by the TMFPA for each unlawful act committed.⁵

15. In granting the State’s motion, the court pointed to the legislative history of § 362(b)(4) which states that it “excepts commencement or continuation of actions and proceedings by governmental units to enforce police or regulatory powers. Thus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, *consumer protections*, safety, or similar police or regulatory laws, *or attempting to fix damages for violations of such law*, the action or proceeding is not stayed under the automatic stay.” *RVG Smiles* at 287 (citing H.R. REP. NO. 95-595, at 343, reprinted in 1978 U.S.C.C.A.N. 5963, 6299) (emphasis added). The Court held that the steep penalties sought by the State were ancillary to its police and regulatory powers and thus, the State’s action passed the pecuniary interest test.

16. Like *RVG Smiles*, Harris County is seeking only relief expressly authorized by the relevant statute, Tex. Bus. & Com. Code § 17.47. This requested relief is ancillary to the enforcement of its public interest suit against Debtor. Therefore, the County’s suit passes the pecuniary interest test.

B. Harris County’s State Court Action for the Enforcement of Consumer Protection Laws Against Debtor Satisfies the Public Policy Test.

17. Debtor argues that Harris County’s state court action is not brought in the public interest. This statement is contrary to the explicit purpose of both the DTPA and the exception to the

⁵ *Ex. A to State of Texas’ Expedited Motion to Determine Nonapplicability of the Automatic Stay Pursuant to 11 U.S.C. § 362(b)(4)*, *In re RVG Smiles*, No. 20-70209 (ECF No. 85).

automatic stay. The purpose of § 362(b)(4) is to exempt “situations where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, ***consumer protection***, safety, or similar police or regulatory laws, ***or attempting to fix damages for violation of such a law***” from the automatic stay. *See* H.R.Rep. No. 95–595, at 343 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6299; S.Rep. No. 95–989, at 52, reprinted in 1978 U.S.C.C.A.N. 5787, 5838 (emphasis added). The Texas legislature has explicitly stated that the DTPA was created for a public purpose, “to protect consumers against false, misleading, and deceptive business practices, unconscionable actions, and breaches of warranty and to provide efficient and economical procedures to secure such protection.” Tex. Bus. & Com. Code § 17.44(a). The Southern District of Texas has determined that actions brought by a governmental entity for the enforcement of the DTPA are brought for a public purpose. *Gandy* at 806.

18. Debtor cites *In re D.M. Barber, Inc.* to support its argument that Harris County is attempting to adjudicate private rights rather than effectuate public policy. 13 B.R. 962, 963 (Bankr. N.D. Tex. 1981).⁶ Harris County’s state court enforcement action against Debtor is not attempting to adjudicate private rights. Harris County’s suit is expressly brought for a public purpose and is not focused on the vindication of private monetary interests. Harris County requests only relief that is expressly authorized by the public enforcement provisions of the DTPA, Tex. Bus. & Com. Code § 17.47 and does not name any individual consumers in its petition.⁷ Indeed,

⁶In that case, the court was determining whether the police power exception to the automatic stay applied to an NLRB proceeding for violations of the Fair Labor Standards Act. The Court held that the NLRB’s action was excepted from the automatic stay because, while the proceedings were “commenced by the initiative of aggrieved individual persons and thus ha[d] characteristics of private litigation, [] case law reflects that the proceedings by the Board are not to adjudicate private rights but to effectuate public policy.” *Id.* at 936.

⁷ Despite Debtor’s assertion that the suit is brought on behalf of specific individual consumers, Harris County brings suit on behalf of itself and the State of Texas, by and through the Harris County Attorney, Christian Menefee, as authorized by the DTPA.

the Harris County Attorney is prohibited by law from serving as any individuals' private attorney.⁸ Harris County is not attempting to gain "preferential treatment to the detriment of all other creditors," as Debtor contends. It is attempting to effectuate the public purpose of the DTPA by protecting consumers against false, misleading, and deceptive business practices.

19. Additionally, "seeking damages and entry of a money judgment does not abrogate an enforcement action of its police power function because levying financial penalties can be used to deter certain behavior." *In re Bloomfield Nursing Operations, LLC*, 609 B.R. 185, 194 (N.D. Tex. 2019). Harris County seeks only the relief available to it under the DTPA, including injunctive relief, restitution, and penalties to deter future consumer fraud throughout the State.

20. Debtor argues that Harris County's state court action for the enforcement of the DTPA against Debtor focuses on obtaining penalties and restitution for past actions and lacks any imminent threat to public health. Opp. at ¶ 14. This argument was soundly rejected in *Commonwealth Oil* and *Gandy*.⁹ *Commonwealth Oil* at 1184; *Gandy* at 806 ("simply because a defendant has ceased the alleged offensive conduct does not remove a governmental unit's ability to prosecute under its police and regulatory power.").

21. For all the reasons stated above, Harris County's state court suit to enforce the DTPA against Debtor satisfies the public policy test.

III.

Harris County Should Be Permitted to Proceed with Its Case and Obtain, But Not Enforce, A Judgement for All Relief Requested.

22. Debtor argues that Harris County's state court enforcement action goes "far beyond merely liquidating a claim." Opp. at ¶ 36. This is absurd because Harris County has not yet obtained a

⁸ See generally Tex. Govt. Code § 45.201.

⁹ In *Gandy*, the court rejected the debtor's argument that the State was not in fact seeking injunctive relief because she had ceased her violations of the DTPA and did not plan to resume them in the future. *Gandy* at 806.

judgement and agrees that the collection of a monetary judgement obtained pursuant to its police power in enforcing the DTPA is subject to the automatic stay.

23. Debtor concludes by stating that “even if certain aspects of Harris County’s action could qualify under the police power exception, Fifth Circuit precedent clearly establishes that monetary components should be stayed.” If Debtor is suggesting that Harris County may proceed with its state court case with regard to injunctive relief but not with regard to penalties, that is incorrect and would frustrate the purpose of the exception to the automatic stay. Harris County may not *enforce* a monetary judgement obtained through its police power at this time, but it may *obtain* it.

24. Therefore, Harris County respectfully requests that this Court issue an Order determining that the case styled *State of Texas and Harris County, Texas v. Elias Haddad et al.*, No. 2025-08779, 334th Judicial District of Harris County, Texas is excepted from the bankruptcy automatic stay in its entirety. Harris County further prays it receive such other and further relief to which it is justly entitled.

Respectfully submitted,

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**ATTORNEYS FOR THE STATE OF
TEXAS AND HARRIS COUNTY,
TEXAS**

Certificate of Service

I hereby certify that a true and correct copy of the above Notice of Hearing has been served on the persons listed below and in accordance with federal and local rules for electronic filing and service on this 9th day of May 2025:

All counsel/parties of record who have made an electronic appearance via the Court's CM/ECF system.

/s/ Eleanor Matheson
Eleanor Matheson