

**UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF
DELAWARE**

In Re:	:	CHAPTER 11
MORTGAGE LENDERS NETWORK	:	
USA, INC.	:	CASE NO.: 07-10146(PJW)
Debtor	:	

Hearing Date: April 10, 2007 at 3:00pm

**SUPPLEMENTAL MEMORANDUM OF LAW IN SUPPORT OF MITCHELL
HEFFERNAN'S MOTION TO ENJOIN THE STATE OF CONNECTICUT
FROM COMMENCING CRIMINAL PROSECUTION PURSUANT TO 11
U.S.C. § 105**

This Supplemental Memorandum of Law is submitted in further support of the Motion of Mitchell Heffernan, former Chief Executive Officer and President of Mortgage Lenders Network USA, Inc. ("Debtor") to Enjoin the State of Connecticut from commencing criminal prosecution against Mitchell Heffernan for debts owed by the Debtor.

I. BACKGROUND

A. The Debtor

On February 5, 2007, Mortgage Lenders Network USA, Inc. ("Debtor") filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code, 11 U.S.C. § 1101 et seq. At all times relevant hereto, Mitchell Heffernan acted as Chief Executive Officer and President ("Officer") of the Debtor in accordance with the Debtor's By Laws and Delaware Business Corporation Law.

B. The Threatened Criminal Action

In its objections, the Connecticut State's Attorney admits that it has threatened to arrest Mitchell Heffernan for the Debtor's failure to pay wages pursuant to Connecticut General Statute § 31-71(b) and (g). These wages arise during the 45 day

period immediately prior to the bankruptcy filing. In its objection to Mitchell Heffernan's Motion, the State's Attorney admits that the criminal statutes under which it will arrest Mitchell Heffernan address solely wages which certain individuals claim to have earned as employees of the Debtor, not from Mitchell Heffernan, and are strict liability statutes. These statutes require no mens rea or purposeful bad act or intent on the part of the defendant. State of Connecticut v. Wilson, 83 Conn. App. 67; 848 A.2d 542 (2004).

C. Mitchell Heffernan Seeks Relief under the Bankruptcy Code

On March 27, 2007, Mitchell Heffernan had no other choice and was forced to file this Motion¹ with this Court in response to the bad faith media frenzy purposely and intentionally created by the Connecticut Department of Labor ("DOL"), the Connecticut State Attorney General ("Attorney General") and the Connecticut State's Attorney Office ("State's Attorney")².

¹ The State urges this Court not to consider this Motion because it was commenced by Motion instead of by Adversary Proceeding. It is respectfully submitted that Mitchell Heffernan followed the procedures allowed under the Bankruptcy Code in asserting this Motion before this Honorable Court. *Collier on Bankruptcy- 15th Edition Rev.* states that a moving party may seek injunctive relief from a federal bankruptcy court instituted by motion instead of adversary proceeding because "in the interests of economy of administration of justice, will; address the merits and grant the relief where warranted". (See for example, In re Capital-York Constr. Corp., 43 Bankr. 52.,55 (S.D.N.Y. 1984). See also, In re: Roy Magnus, 84 B.R. 976,978 (Bankr. E.D.Pa. 1988) treating a motion seeking injunctive relief as if an adversary complaint had been filed because such a pleading is one of form and not of substance); In re: Veseay, 43 B.R. 396,397 (Bankr. E.D.Pa., 1984) (holding that a motion filed shall be treated as a complaint for asserting rights under the Bankruptcy Code).

² The State of Connecticut cites Perez v. Ledesma, 401 U.S. 82,85; 91 S.Ct. 674, 677 (1971) for the proposition that the State has the right to issue the arrest warrant against Mitchell Heffernan. Perez provides absolutely no support to the State. In Perez, the United States Supreme Court remanded the case to the district court holding that:

Only in cases of proven harassment or prosecution undertaken by state officials in bad faith without hope of obtaining a valid conviction and perhaps in other extraordinary circumstances where irreparable injury can be shown is federal injunctive relief against pending state prosecutions appropriate.

Id. at 677.

D. The State Causes a Media Frenzy

The DOL, the Attorney General and the State's Attorney willfully, wantonly, intentionally and in bad faith started a firestorm of news reports proclaiming the imminent arrest of Mitchell Heffernan, not because of any wrongdoing of Mitchell Heffernan, but because of certain unpaid wages of the Debtor which are part of this Debtor's bankruptcy case. The DOL, the Attorney General and the State's Attorney knowingly, intentionally, wantonly and in bad faith turned to the court of public opinion to circumvent this bankruptcy case under the control and custody of this Court and tried to file their claims in the news media to force Mitchell Heffernan to pay \$2,500,000 to the State to reimburse these certain creditors. This was done even though the Attorney General, the State's Attorney and certain nameless Department of Labor officials were fully aware that their actions were in bad faith and violated and circumvented the very Congressional purpose of the Bankruptcy Code. Now that they are before the bar of this Court their defense is "we have not signed the arrest warrant"!!

As set forth in length in this Memorandum of Law, this is exactly the case here. The State of Connecticut is harassing Mitchell Heffernan in the court of public opinion without any federal or State of Connecticut precedent which allows the State's Attorney to arrest or convict Mitchell Heffernan for obligations owed by the Debtor. In fact, there is not one case the State's Attorney or State Attorney General can cite which supports an arrest or conviction of Mitchell Heffernan. This threatened criminal prosecution of Mitchell Heffernan is not for any wrongdoing by Mitchell Heffernan but is threatened only by virtue of his role as a former Officer of the Debtor in the State's hope of extorting and blackmailing Mitchell Heffernan for payment of certain monies owed by the Debtor, bypassing the Bankruptcy Code and the Debtor's Bankruptcy case. Now that they are before this Bankruptcy Court, their defense is "we have not signed the arrest warrant". This reasoning to this Court that the State's Attorney have not signed an arrest warrant is an absolute and unmitigated disgrace in light of the bad faith and public prosecution of Mitchell Heffernan to date. Therefore, it is respectfully submitted on behalf of Mitchell Heffernan that this threatened criminal prosecution is nothing more than the State's harassment and bad faith conduct in attempting to blackmail and extort monies from Mitchell Heffernan to satisfy certain debts of the Debtor outside of the Debtor's bankruptcy estate in circumvention of the Congressional mandate of federal bankruptcy law.

In fact, none of this frenzy was caused by Mitchell Heffernan. The State's Attorney's contempt for this Court, its equitable powers, the federal Constitution and Congressional mandate of the Bankruptcy Code and their bad faith, wanton, unconscionable actions are demonstrated by their Objections which only reinforces, supports and furthers the very words of the various Connecticut state officials. For example, Gary Pechie, a Connecticut Department of Labor official, published in *The Hartford Courant* on March 19, 2007, stated as follows:

1. March 19, 2007 – The Hartford Courant:

Mitch Heffernan.....his old company – the now defunct Mortgage Lenders Network – could land him in plenty of trouble with the state for not paying wages earned by his former employees.

The state department of Labor confirmed Monday that is had applied for an arrest warrant in Superior Court in Middletown that would charge Heffernan – the formed President of Middletown-based Mortgage Lenders – with 61 counts of failing to pay wages.

The wages that the department alleges were unpaid total \$3 million, mostly in sales commissions. The commission range from \$5,000 to \$300,000.

Heffernan could face \$300,000 in fines, jail time or both.....

Other Mortgage Lenders executives also could be named later because the state labor department's investigation is continuing, according to Gary Pechie, director of the states' Wage and Workplace Standards Division.

* * * *

Mortgage Lenders filed for bankruptcy protection Feb. 5, after a monthlong downward spiral.....

A true and correct copy of this article is attached hereto, made a part hereof and marked Exhibit "A" hereto.

These statements by Gary Pechie published in the *Hartford Courant* set off hourly, daily and weekly news reports by the DOL and the Attorney General including print articles, internet articles and televisions reports in Connecticut and throughout the United States. In each of these published or broadcast interviews, a DOL spokesperson or Attorney General is quoted as proclaiming that a request for the issuance of an arrest warrant has been directed to the State's Attorney because this criminal prosecution **is the only way to obtain wages from the Debtor.** Attorney General Richard Blumenthal stated March 29, 2007 on the 6:00p.m. evening news on WFSB-TV, Hartford, Connecticut

there's just no way a federal bankruptcy court in Delaware is going to enjoin or stop our criminal proceeding.

See Exhibit "D" hereto).

Yet in almost each instance, the State clearly states the whole thing could be resolved if Mitchell Heffernan agreed to pay \$2,500,000 for the certain wages owed by the Debtor. Some other examples of this bad faith media frenzy undertaken by the Connecticut officials, without any hope of obtaining a valid conviction, include the following:

1. March 20, 2007 – *Eyewitness News Channel 3, WFSB-TV, Hartford, CT:*

Gary Pechie, a state Department of Labor official, was interviewed on the evening news concerning unpaid wages of the Debtor. Excerpts of this interview was published on WFSB.com, as follows:

The [Labor] department claims that the company owed its former employees wages that could top \$3,000,000.

* * * * *

Prosecutors told Eyewitness News that because the company declared bankruptcy, criminal charges may be the only way to claim the money.

“The Judge could order restitution, but if not, it’s a \$2,000 to \$5,000 fine and five years of imprisonment for each offense.” Pechie said. “And with 61 counts, you’re talking a hefty fine and a year in jail”.

A true and correct copy of this article from the website is attached hereto, made a part hereof and marked Exhibit “B” hereto.

2. March 26, 2007 – *Reuters* - Nancy Steffens, Connecticut Department of Labor spokeswoman, is quoted in a published article, as follows³:

“The company declared bankruptcy, which requires us to go through a criminal court to get former employees their money”, Steffens said **“Our real purpose is to get people money owed to them. If we can work out a settlement without criminal charges that’s great”**. (emphasis added).

A true and correct copy of the article published on *Reuters.com* is attached hereto, made a part hereof and marked Exhibit “C”.

3. March 29, 2007 – *Eyewitness News, Channel 3, WFSB-TV, Hartford, CT* - Connecticut Attorney General Richard Blumenthal was interviewed on camera and quoted at length on the 6:00p.m.Channel 3 Eyewitness News and stated, as follows:

We’re determined to fight in upholding our rights as a sovereign state to use our criminal law to punish criminal wrongdoing, and there’s just no way a federal bankruptcy court in Delaware is going to enjoin or stop our criminal proceeding.

A true and correct copy of a transcript of this television broadcast is attached hereto, made a part hereof and marked Exhibit “D”.

³ Pursuant to Federal Rule of Evidence 201 and *Benak v. Alliance Capital Management, L.P.*, 435 F.3d 396 (3rd Cir. 2006), this Court is permitted to take judicial notice of newspaper articles in the public domain.

4. April 5, 2007 – *Dow Jones News* – Connecticut Attorney General

Richard Blumenthal explained to the news media the purpose of the State's blackmail and extortion of Mitchell Heffernan in a published article"

"There is a very powerful message that employers must be held accountable to pay for work," said Connecticut Attorney General Richard Blumenthal, explaining why the state may prosecute Heffernan "or others who may have allegedly broken our criminal laws."

Connecticut can't force Mortgage Lenders to pay the employees now that it's in Chapter 11, the attorney general admitted. Unless companies provide otherwise -- and many do -- unpaid employees fall in with the rest of those waiting for a fractional recovery that may never arrive.

Connecticut has no intention of asking the bankruptcy court to order the wages paid, Blumenthal said. All the state wants to do is arrest violators of its criminal laws. However, it's not unheard of for restitution to be part of a plea deal in such cases, he admitted.

"People are often persuaded by criminal prosecutions to do the right thing," Blumenthal said. "It's a matter of simple justice."

A true and correct copy of the *Dow Jones News* article is attached hereto, made a part hereof and marked Exhibit "E".

Despite its bad faith harassment and public lynching of Mitchell Heffernan in the news media, the State's Attorney now has explained its bad faith, unconscionable, wanton, harassment and prosecution of Mitchell Heffernan to this Court and says that the arrest warrant of Mitchell Heffernan has not been signed and therefore argues that this Motion is not ripe⁴. However, it is undisputed that by his own voice State Attorney

⁴ Despite the flames of this news media frenzy fanned by the State of Connecticut and State Attorney General Blumenthal and his continued threat of the arrest and criminal prosecution of Mitchell Heffernan, the State of Connecticut argues in their Objection to this Motion that this Motion is not ripe. The State is clearly wrong on the law. A case before a federal court must involve an actual case and controversy.

General Blumenthal, the top law maker in Connecticut, has told each and every citizen of the state on public television that this very United States Bankruptcy Court is not going to stop the criminal proceeding. Attorney General Blumenthal ignores the clear

Surrick v. Killion, 449 F.3d 520, 527 (3rd Cir. 2006). There is a three part test to determine whether an action is ripe for pre-enforcement determination by the Court. Id. In Step-Saver Data Systems, Inc. v. Wyse Technology, 912 F.2d 643,647 (3rd Cir. 1990) the Third Circuit a Court must consider: (1) the parties must have adverse interests; (2) the facts must be such to allow for a legal judgment; and (3) the judgment rendered by the reviewing court must be useful to the parties. Under the first prong of this test in The Presbytery of New Jersey of the Orthodox Presbyterian Church v. Florio, 40 F.3d 1454, 1468 (3rd Cir. 1994), the Third Circuit held that a case was ripe where even a threat of criminal prosecution existed. Under the second prong, the Court must determine whether a decision at the present time would be “more than an advisory opinion based upon a hypothetical set of facts” Id. In Presbytery, relying upon Atlanta Gas Light Co. v. U.S. Dept. of Energy, 666 F.2d 1359 (11th Cir. 1982), the Third Circuit held the second prong of the ripeness standard was satisfied where (a) the parties claims would not change in future litigation, the current party was the appropriate party raising the issue; and (c) the party was subject to enforcement if the court permitted implementation. Id. The third element is satisfied, if the judgment in the instant case would be useful to the parties at bar and other parties that may be affected. Id. At 1469. In Presbytery, the Third Circuit found the case was ripe because the threat of arrest for the minister existed if and when the minister stepped off the property of the church. Id.

In the case at bar in applying the Step Saver test it is clear that this case is ripe for a ruling by this Court on Mitchell Heffernan’s Motion because:

- (1) The first prong of the ripeness test is satisfied in the case at bar because the State of Connecticut, by its own Department of Labor and its Attorney General has threatened to issue an arrest warrant for Mitchell Heffernan arising from certain unpaid debts of the Debtor;
- (2) The second prong of the ripeness test is satisfied here because (a) Mitchell Heffernan’s claims and defense would be the same in any future litigation; (b) Mitchell Heffernan is the correct party to bring this Motion because he is the party threatened with imminent criminal prosecution by the State of Connecticut; (b) and if this Court does not enjoin the State of Connecticut from prosecuting Mitchell Heffernan for certain payments owed by the Debtor, Mitchell Heffernan would be subject to enforcement of this statute for debts owed by the Debtor; and
- (3) In the case at bar, any judgment by this Court would be useful to the parties and others affected because it would rule upon whether Connecticut law trumps bankruptcy law by enforcing its statute against an individual officer or director for certain debts of a debtor.

Accordingly, Mitchell Heffernan most respectfully submits that this Motion is ripe for consideration by this Court and, therefore, the State’s argument must fail.

The State relies on NE Hub Partners, L.P. v. CNG Transmission Corp., 239 F.3d 333 (3rd Cir. 2001) to support its argument. The State’s reliance is misguided. In Hub, the Third Circuit reversed and remanded the case to the District Court finding that the case was ripe for consideration to enjoin a state enforcement action.

and unequivocal fact that any criminal prosecution of Mitchell Heffernan for debts of the Debtor clearly and unequivocally interferes with the Debtor's bankruptcy case and interferes with the rights of all of the Debtor's other creditors. And now after all of this grandstanding, the State expects this Court to believe this process is not ripe because it has not signed the arrest warrant. The State's own conduct lead directly to the opposite conclusion.

E. Mitchell Heffernan Retains Counsel

Counsel for Mitchell Heffernan contacted the DOL and the State Attorney General's Office to attempt to understand the grounds for an imminent arrest warrant for Mitchell Heffernan based solely on a debt of the Debtor. Counsel for Mitchell Heffernan discovered that the State's Attorneys' office was pursuing a criminal arrest for Mitchell Heffernan and the State Attorney General's Office was pursuing a civil complaint for the unpaid obligations of the Debtor. Mitchell Heffernan's counsel spoke to a representative of the State Attorney General's Office, Glen Woods and John Cashan from the State's Attorneys' Office, and was advised that if a negotiated financial settlement was reached with Mitchell Heffernan for payment of the Connecticut unpaid wages of the Debtor, the State's Attorney would certainly consider that in its determination of whether to approve an arrest warrant. The State Attorney General's Office then demanded that Mitchell Heffernan pay \$2,500,000 even though when the Debtor files its schedules in its bankruptcy case, Mitchell Heffernan believes that these unpaid wages by the Debtor will be referenced as \$1,700,000.

F. Mitchell Heffernan's Counsel Requests Legal Precedent

At all times relevant hereto, counsel for Mitchell Heffernan reminded the DOL, the State Attorney General and the State's Attorney that the Debtor had filed for bankruptcy protection under Chapter 11 of the Bankruptcy Code, that these very wages are part of this bankruptcy case and requested legal precedence supporting the State's authority to arrest and convict an Officer of a Debtor for the debts of the Debtor when the only basis for the arrest is his position as an Officer of the Debtor. To date, the State has been unable to direct counsel or this Court to any legal authority whatsoever or any other time they used this State of Connecticut statute to arrest or convict an officer of a Bankrupt Debtor⁵.

By way of illustration, counsel for Mitchell Heffernan, on March 26, 2007 and March 27, 2007, sent letters to the State Attorney General's office requesting the legal precedence the State was proceeding under which permitted the circumvention of the Bankruptcy Code. If the State was unable to provide any legal precedence for its position to arrest and convict an Officer, counsel for Mitchell Heffernan indicated he would have no choice but to seek this Court's protection.⁶ The State again was unable to point to any legal authority. True and correct copies of counsel's letters are attached hereto, made a part hereof and marked Exhibit "F".

⁵ In its Objections, the State relies upon In Matter of Davis; Davis v. Sheldon d/b/a CNC, Ins. Co., 691 F.2d 176 (3rd Cir. 1982) in support of its position that it can ignore federal Bankruptcy law and arrest Mitchell Heffernan for the debts of the Debtor. Davis is factually distinguishable. Davis concerned the prosecution of the debtor (husband and wife) for passing bad checks to pay debts which were dischargeable in bankruptcy. This is not the case here. Here, the State's Attorney seeks to arrest Mitchell Heffernan for debts owed by the Debtor.

⁶ The statute the State's Attorney seeks to enforce against Mitchell Heffernan has been in affect for at least forty (40) years. In these forty years, there is not one instance where the State's Attorney has arrested the officer or former officer of a debtor for the debts of the Debtor.

G. There is No Legal Precedent for the State's Prosecution

Instead of providing legal authority to arrest and convict an Officer for the unpaid commissions of the Debtor in accord with the Bankruptcy Code, the State continued its news media frenzy through the statements of DOL spokeswoman Nancy Steffens which were published in *Reuters* article on March 26, 2007, which clearly and unequivocally demonstrates the State's intent to circumvent the Bankruptcy Code and blackmail and extort, in bad faith through publicly threatened criminal proceedings, Mitchell Heffernan to make payments to certain creditors of the Debtor:

“The company declared bankruptcy, which requires us to go through a criminal court to get former employees their money”, Steffens said “Our real purpose is to get people money owed to them. If we can work out a settlement without criminal charges that's great”.

See Exhibit “B” hereto.

This threatened criminal prosecution is nothing more than bad faith and harassing extortion and blackmail of Mitchell Heffernan by the State to force him to personally pay certain creditors of the Debtor, which cannot be tolerated or condoned by this federal Bankruptcy Court. Now, the State argues that Mitchell Heffernan's Motion before this Court is premature because a Connecticut judge has not signed the arrest warrant yet. Simply put, the State is wrong. It is the State who has started, in bad faith, the criminal proceeding and media frenzy and firestorm. This threatened criminal proceedings and the resulting media frenzy and bottom-feeding by the press has forced Mitchell Heffernan and his family to hide from the media and has turned them into pariahs walking the dead man's walk to the death chamber. If the State had not started the bad faith prosecution of its case in the news media, on television and in the

newspaper, Mitchell Heffernan would not now be seeking this Court's protection. The State started this criminal proceeding intentionally, willfully, wantonly, unconscionably, in bad faith and has continued it and can not now be allowed to tell this Court it is temporarily taking back these willful, wanton and unconscionable bad faith harassing actions or that this Motion is not ripe now because Mitchell Heffernan rightfully seeks protection from this Bankruptcy Court. It is too late! Such unconscionable bad faith conduct cannot be tolerated or condoned.

Therefore, on behalf of Mitchell Heffernan it is most respectfully submitted that this Motion is ripe for consideration by this Court today and not after the State completes the entire circumvention of the Founding Fathers and the Congressional intent of the Bankruptcy Code by arresting Mitchell Heffernan.

II. ARGUMENT

11 U.S.C. § 105(a) provides that “the Court may issue any order, process or judgment that is necessary or appropriate to carry out the provisions of this title.”

Bankruptcy Courts throughout this country have enjoined criminal prosecution, pursuant to the Bankruptcy Court’s equitable powers of 11 U.S.C. § 105(a) when the criminal process is being used as a means of extracting a preference not accorded other creditors similarly situated. See, e.g., In re Jerzak, 47 B.R. 771 (W.D. Wis. 1985), In re Bicro Corporation, 105 B.R. 255 (M.D. Pa. 1988), In re Dettler Farms, 58 B.R. 404 (D. S.Dak. 1986) and In re Caldwell, 5 B.R. 740 (W.D. Va. 1980).

In the case at bar, Mitchell Heffernan most respectfully submits that this Honorable and Equitable Court must extend the automatic stay provisions of 11 U.S.C. § 362, or alternatively enter a permanent injunction, enjoining the Connecticut State’s Attorney from proceeding with the criminal prosecution of Mitchell Heffernan for the following reasons: (a) there is such an identity between Mitchell Heffernan and the Debtor that any proceeding against Mitchell Heffernan is in effect a proceeding against the Debtor; (b) the State of Connecticut is using the criminal process as a means of extracting a preference not accorded the creditors similarly situated; (c) pursuant to the Debtor’s By Laws, Debtor must absolutely indemnify Mitchell Heffernan for any judgment, fines or penalties rendered against him in any Connecticut action, either criminal or civil, rendering any adverse finding against Mitchell Heffernan a finding or liability of the Debtor; (d) the Debtor will be irreparably harmed by any prosecution of Mitchell Heffernan for wage claims; (e) Mitchell Heffernan will be irreparably harmed by any criminal prosecution directed to him as a former Officer of the Debtor for a debt

of the Debtor; (f) under the doctrine of collateral estoppel the Debtor would be estopped from disputing the wage claims of Connecticut employees; and (f) there is no authority under the Connecticut statute permitting the personal arrest of a corporate officer of a corporation seeking bankruptcy protection.

A. There is an Identity Between Mitchell Heffernan and the Debtor Rendering Any Judgment or Penalty Against Mitchell Heffernan a Judgment or Penalty Against Debtor

The automatic stay provisions set forth at 11 U.S.C. § 362 serves several functions including, but not limited to, (a) providing the debtor a breather from all adverse collection actions; (b) protects the Debtor from an “uncontrollable scramble for its assets in a number of uncoordinated proceedings in different courts”; (c) protects creditors by preventing a creditor from acting to obtain payments from the debtor to the detriment of the other creditors of the debtor; and (d) provides “the debtor and its executives with a reasonable respite from protracted litigation, during which they may have an opportunity to formulate a plan of reorganization for the debtor. A.H. Robins Co., Inc. v. Piccinin, 788 F.2d 994, 999 (4th Cir. 1986), cert. denied, 479 U.S. 876; 107 S.Ct. 251 (1986); McCartney v. Integra National Bank North, 106 F.3d 506 (3rd Cir. 1997).

The automatic stay provisions of 11 U.S.C. § 362 read together with this Court’s equitable powers under 11 U.S.C. § 105 “empowers the bankruptcy court to enjoin parties other than the bankruptcy from commencing or continuing litigation”. Robins at 1002 (citing In re Otero Mills, Inc., 25 Bankr. 1018, 1020 (D.N.M. 1982). Protarga, Inc., v. Webb (In re: Protarga), 329 B.R. 451 (Bankr. DE 2005).

In Robins, the United States Appellate Court for the Fourth Circuit read the automatic stay provisions of Section 362 together with the equitable powers of the Bankruptcy Court under 11 U.S.C. § 105 to enjoin actions against non-debtors because of the potential impact any claim against the non-debtors would have on the bankruptcy case. Id. At 999. The Fourth Circuit held that unusual circumstances existed to extend the automatic stay to non-debtors where:

there is such identity between the debtor and the third party defendant that the debtor may be said to be the real party defendant and that a judgment against the third party defendant will in effect be a judgment or finding against the debtor.

Id.

In the Adversary Proceeding styled American Film Technologies, Inc. v. Taritero, 175 B.R. 847, 850 (Bankr. DE. 1994) this Honorable Court, in reliance upon Robins, held there was an identity of parties where an action was commenced against individual non-debtor defendants, who were directors of the debtor, only because of their capacity as directors of the debtor. This Court held that any liability found against the non-debtor directors would be because of their capacity as agents of the debtor. Id. This Honorable Court enjoined the state court fraud action against these non-debtor directors finding that any liability found against the non-debtor directors would expose the debtor to vicarious liability under the doctrine of respondent superior. Id.

B. Debtor Must Absolutely Indemnify Mitchell Heffernan for any Adverse Action in Connecticut

The Robins exception extending the automatic stay to a non-debtor third party is applicable in a proceeding against the third party non-debtor defendant where there is

an indemnity clause between the third party and the debtor making the debtor responsible for any monetary judgment which results. Id. At 999-1000. See also In RE W.R. Grace & Co., et al., Debtors; W.R. Grace & Co. et al., v. Chakarian, 2005 Bankr. LEXIS 579 Protarga, Inc., v. Webb (In re: Protarga), 329 B.R. at 479-480; accord American Film Technologies, 175 B.R. at 850. (Bankr. DE. 2004);

This Honorable Court, in reliance on Robins, extended the automatic stay to a non-debtor third party finding a close identity between the third party non-debtor and the debtor. In Re.W.R. Grace at 9. The Grace Court held that a judgment against the third party non-debtor would be a debt of the debtor because any adverse finding against the third party non-debtor would trigger an indemnification between these parties. This Court further reasoned a judgment against the third party non-debtor would essentially be a judgment against the debtor and will impair the debtor's ability to reorganize. Id. at 12.

Similarly, in In re Eagle-Picher Indus., Inc., 963 F.2d 855, 877 (6th Cir. 1992) the United States Court of Appeals for the Sixth Circuit held that the automatic stay extended to two non-debtor officers of the corporation where an absolute indemnity agreement existed because if the action against the officers was allowed to proceed it would essentially be a suit against the debtor.

a. The Indemnification Provisions

Debtor's By Laws provide such an absolute indemnification to Mitchell Heffernan from Debtor for any and all actions including criminal and civil proceedings. It is undisputed that Mitchell Heffernan is a director and former Chief Executive Officer and President of the Debtor. Article XI of the Debtor's By laws provide as follows:

Article XI – Indemnification and Insurance

Section 1 (a) Right to Indemnification. Each person who was or is made a party or is threatened to be made a party or is involved in any action, suit or proceeding, whether civil, criminal, administrative or investigative (hereinafter “proceeding”), by reason of the fact that he or she, or a person of whom he or she is the legal representative, is or was a director or officer, of the Corporation.....shall be indemnified and held harmless by the Corporation to the fullest extent authorized by the Delaware General Corporation Law, as the same exists or may hereafter be amended (but, in the case of any such amendment, only to the extent that such amendment permits the Corporation to provide broader indemnification rights than said law permitted the Corporation to provide prior to such amendment(against all expense, liability and loss (including attorneys’ fees, judgments, fines, ERISA excise taxes or penalties and amounts paid or to be paid in settlement) reasonably incurred or suffered by such person in connection therewith and such indemnification shall continue as to a person who has ceased to be a director, officer, employee or agent....

A true and correct copy of Debtor’s By Laws are attached hereto, made a part hereof and marked Exhibit “G”.

The Debtor’s By Laws comply with the indemnification provisions of the Delaware Business Corporation Law which expressly permits indemnification of corporate officers in threatened criminal actions. Del. Code § 145. Section 145 provides in pertinent part:

(a) A corporation shall have power to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the corporation) by reason of the fact that the person is or was a director, officer, employee or agent of the corporation.....

Based on Article IX of the Debtor’s By Laws and Section 145 of Delaware’s Business Corporation Law, it is clear and unequivocal that the Debtor is required to

indemnify Mitchell Heffernan in defending the threatened Connecticut action, criminal or civil. Further, there is no doubt that any action by the State of Connecticut against Mitchell Heffernan is a way “to get people [of the State of Connecticut] money owed to them” by the Debtor. See Exhibit “C” hereto. There are absolutely no allegations by the State’s Attorney that there was any wrongdoing on the part of Mitchell Heffernan other than the allegations that certain former employees of the Debtor claim they are owed money by the Debtor. Therefore, the indemnification provisions of the Debtor’s By Laws apply to the threatened criminal action by the Connecticut State’s Attorney.

In Protarga v. Webb, supra., this Court considered the claim of a former officer and director in a Pennsylvania state court action for unpaid wage claims against individual directors. Id at 479-480. There was an indemnity agreement between the corporation and the directors. This Bankruptcy Court found that because of this indemnification, any judgment rendered in the Pennsylvania state court was a judgment against the debtor which would significantly reduce the funds in the bankruptcy case available to pay the claims of other creditors. Id. This Court authorized the Debtor to file a motion for an injunction to enjoin the Pennsylvania state court action ruling:

In my view, such a result produces a clear conflict between state law and the Bankruptcy Code. The relevant case law clearly supports the conclusion that in this matter the Bankruptcy Code trumps the state law.

Id. At 480-481.

However, for some reason, the Connecticut State’s Attorney and its Attorney General feel they are above the United States Constitution, the Congressional intent of the Bankruptcy Code and federal laws by stating on television that:

there's just no way a federal bankruptcy court in Delaware is going to enjoin or stop our criminal proceeding.

See Exhibit "D" hereto. He is wrong! Under the Supremacy Clause of the United States Constitution, the federal Bankruptcy Code trumps the State of Connecticut law.

In accordance with Robins, Protarga, Grace, and American Film Technologies, the indemnification provisions of Debtor's By Laws support a finding that any adverse finding against Mitchell Heffernan in Connecticut, will be a liability against him as an agent of the Debtor and impair the Debtor's ability to reorganize. Accordingly, these alleged claims versus Mitchell Heffernan are a liability/debt of the Debtor which requires this Court, in accordance with the aforementioned case law, to extend the automatic stay to enjoin the Connecticut action to protect the Debtor's bankruptcy case. The State of Connecticut cannot use this threatened criminal arrest as a means to extract a preference not accorded other creditors..

C. Debtor Will be Irreparably Harmed by Any Prosecution of Mitchell Heffernan for Unpaid Liability of the Debtor

Pursuant to 11 U.S.C. § 105(a), this Honorable Court has the equitable powers to enter an injunction to permanently enjoin the Connecticut State's Attorney from proceeding with its threatened criminal action against Mitchell Heffernan. In reviewing a request for an injunction, a Court must consider the following elements: (1) likelihood of success on the merits; (2) the irreparable harm to petitioner by the conduct; (3) the extent of irreparable harm to the potential enjoined party; and (4) consideration of the public interest. Opticians Ass'n of America v. Independent Opticians of America, 920 F.2d 187, 191-192 (3rd Cir. 1990).

1. Likelihood of Success on the Merits and Irreparable Harm to Mitchell Heffernan

In the context of bankruptcy, this Court has recognized that the likelihood of Mitchell Heffernan's success on the merits depends upon the adverse affect of the Connecticut action on Debtor. Robins at 999-1000. Protarga, 329 B.R. at 479-480; American Film Technologies, 175 B.R. at 850.

Connecticut seeks to pursue its threatened arrest for alleged unpaid wages owed by the Debtor based solely on the fact that Mitchell Heffernan is a former Officer of the Debtor. The Connecticut State's Attorney articulates no other reason for its threatened criminal arrest. This Court has recognized in a bankruptcy context, this element turns on whether the Debtor will be adversely affected if an automatic stay or injunction is not extended to Mitchell Heffernan in the Connecticut threatened action. American Film Technologies at 849.

In the case at bar, there is no doubt that the Debtor will be adversely affected if an automatic stay or injunction is not extended to Mitchell Heffernan in the Connecticut action during the pendency of this case for the following reasons:

a. Connecticut threatens arrest of Mitchell Heffernan based solely on his former capacity as the former CEO and President of the Debtor (Robins, American Film Technologies);

b. There is an identity between Mitchell Heffernan and the Debtor which effectively makes the Connecticut action against the Debtor (Robins);

c. There is an indemnity between the Debtor and Mitchell Heffernan which requires the Debtor to be responsible for any liability arising out of the threatened Connecticut action (Robins, Grace, American Film Technologies ;

d. This indemnification requires the Debtor to defend the Connecticut action because any liability against Mitchell Heffernan essentially is a liability of the Debtor; (Robins, Protarga, American Film Technologies);

e. The Debtor must defend the Connecticut action as a party or be estopped from challenging the Connecticut wage issues in this case under the doctrine of collateral estoppel (American Film Technologies);

f. Vicarious liability attaches to the Debtor for any actions of Mitchell Heffernan in his capacity as a former director and officer of the Debtor under the doctrine of respondeat superior and, therefore, Debtor is the correct party in any action by the State of Connecticut (American Film Technologies);

g. Any other result would produce a clear conflict between the State of Connecticut and the Bankruptcy Code and will impair the Debtor's ability to reorganize and any judgment against Mitchell Heffernan is essentially a judgment against the Debtor (Robins);

h. The relevant case law clearly supports the conclusion that in this matter, the federal Bankruptcy Code trumps the State Law (Protarga);

i. Mitchell Heffernan will be publicly humiliated and forced to defend a criminal action based solely on the Debtor's inability to allegedly pay commissions which may or may not be due. This issue is challenged and must be litigated in this bankruptcy litigation;

j.. The very intent of bankruptcy law will be permanently damaged if an injunction is not entered because the alleged debt may receive a payment priority

ahead of other creditors (Robins, Protarga). This is clearly illustrated because the State Attorney General has stated publicly on television:

there's just no way a federal bankruptcy court in Delaware is going to enjoin or stop our criminal proceeding.

See Exhibit "D" hereto;

k. The threatened Connecticut arrest is being used as a means to extract a preference for the Connecticut employees not accorded the other creditors similarly situated (Protarga);

l. This conflict is even more obvious as demonstrated in the statements of the Connecticut DOL spokeswoman, Nancy Steffens:

"The company declared bankruptcy, which requires us to go through a criminal court to get former employees their money", Steffens said **"Our real purpose is to get people money owed to them. If we can work out a settlement without criminal charges that's great"**. (emphasis added).

See Exhibit "C" hereto.

Therefore, there is a likelihood of success on the merits and Mitchell Heffernan will be irreparably harmed if an injunction is not entered.

2. No Irreparable Harm to the State

This threatened case is nothing more than the State's Attorney's bad faith, strong arm tactics, blackmail and attempt to extort monies from the former Officer of the Debtor through public humiliation, embarrassment and the threat of arrest. This is contrary to the Congressional intent of the Bankruptcy Code. These strong arm tactics are demonstrated by numerous statements and leaks to the press by officials of the State of Connecticut, as follows:

1. On March 20, 2007, on live television, Gary Pechie an official of the Connecticut Department of Labor told reporters that the only way to obtain the alleged commission owed to these employees because of the bankruptcy was to arrest Mitchell Heffernan and have a Connecticut State judge order restitution for these alleged commissions owed by the Debtor. Excerpts of this March 20, 2007 story published with quotes from Pechie from the website of WFSB.com follows:

The [Labor] department claims that the company owed its former employees wages that could top \$3,000,000.

* * * *

Prosecutors told Eyewitness News that because the company declared bankruptcy, criminal charges may be the only way to claim the money.

“The Judge could order restitution, but if not, it’s a \$2,000 to \$5,000 fine and five years of imprisonment for each offense.” Pechie said. “And with 61 counts, you’re talking a hefty fine and a year in jail”.

See Exhibit “B” hereto.

2. On March 26, 2007, Nancy Steffens, the Connecticut Department of Labor spokeswoman, explained the Connecticut Department of Labor’s position in an article published by *Reuters* on March 26, 2007:

“The company declared bankruptcy, which requires us to go through a criminal court to get former employees their money”, Steffens said **“Our real purpose is to get people money owed to them. If we can work out a settlement without criminal charges that’s great”**. (emphasis added).

See Exhibit “A” hereto.

3. On March 29, 2007, Connecticut Attorney General Richard Blumenthal stated on the 6:00p.m.Channel 3 Eyewitness News:

We're determined to fight in upholding our rights as a sovereign state to use our criminal law to punish criminal wrongdoing, and there's just no way a federal bankruptcy court in Delaware is going to enjoin or stop our criminal proceeding.

A true and correct copy of a transcript of this television broadcast is attached hereto, made a part hereof and marked Exhibit "D".

In the very words of the Connecticut officials given to the news media including television and newspapers, there is no doubt the Connecticut State's State, on behalf of the Department of Labor, is attempting to impair and interfere with the Debtor's bankruptcy case in order to obtain priority payment for certain creditors. There is no irreparable harm to Connecticut! There is just the opposite. This irreparably harms the federal Constitution and the Congressional intent of the Bankruptcy Code on how each and every debtor in each and every bankruptcy case in the United States is treated. Therefore, Mitchell Heffernan most respectfully submits that an injunction will not irreparably harm the State of Connecticut.

Further, the "wages" the Connecticut State's Attorney is seeking to collect are all disputed by the Debtor. Pursuant to the Bankruptcy Code, the employees with any type of wages claims are required to file proof of claims in the bankruptcy estate and receive payment as a creditor once a reorganization plan is approved. The Bankruptcy Code also provides these former employees with wage claims an opportunity to approve or object to the Debtor's plan of reorganization. As stated in its objections, the State Attorney General has the opportunity to bring its threatened action against the Debtor in the Bankruptcy case for twice the amount of the unpaid wages, plus costs and reasonable attorneys' fees, if applicable.

3. Public Interest

This Honorable Court has recognized that the public interest is served in a bankruptcy context by “the promoting of a successful reorganization”. American Film Technologies at 849 (quoting Gathering Restaurant, Inc. v. First National Bank of Valparaiso (In re Gathering Restaruant, Inc.), 79 Bankr. 992, 999 (Bankr. N.D. Ind. 1986). This is a proceeding under Chapter 11 of the Bankruptcy Code with reorganization as the goal of the Debtor. Therefore, the public interest is served by its efforts to reorganize, not by any bad faith, harassing attempt to impair the ability to reorganize by an arrest warrant of a former Officer of debts owed by the Debtor.

In summary, in the case at bar, Mitchell Heffernan most respectfully submits that this Honorable Court must permanently enjoin the State’s Attorney of Connecticut from proceeding with its threatened arrest of Mitchell Heffernan based on the factors enunciated by the Third Circuit in Opticians Ass’n.

D. The Doctrine of Collateral Estoppel Bars the Connecticut Action

The doctrine of collateral estoppel is invoked when the parties, the issues and the subject matter is the same. Parklane Hosiery Co., Inc. v. Shore, 439 U.S. 322; 99 S.Ct. 645 (1979). In a bankruptcy context involving an action against director or officer non-debtors, the Courts have issued preliminary injunctions under 11 U.S.C. § 105 enjoining the actions because the Debtor will be irreparably harmed by its ability to defend the same action if the same issue is implicated in the bankruptcy estate. American Film Technologies at 850-851; In re: Ionosphere Clubs, Inc., 111 Bankr. 324, 435 (Bankr. S.D.N.Y. 1990)(enjoining action against directors because any finding against the directors would extend to the debtor under the doctrine of collateral

estoppel); Sudbury, Inc. v. H. Escott, 140 Bankr. 461 (Bankr. N.D. Ohio (1992)(enjoining fraud action against former officers and directors until after reorganization because the doctrine of collateral estoppel would require the debtor to defend the fraud action as if the debtor was a party) .

In the case at bar, the doctrine of collateral estoppel prevents the Connecticut State's Attorney from proceeding on its threatened arrest of Mitchell Heffernan by virtue of his capacity as a former Officer of the Debtor because:

1. The parties in the threatened Connecticut action and Debtor's bankruptcy case are exactly the same. The State's Attorney seeks to arrest Mitchell Heffernan solely by reason of his capacity as a former Officer of the Debtor. The indemnification provisions of the Debtor's By Laws require the Debtor to be liable for the outcome which in essence requires that the Debtor actually defend any action against Mitchell Heffernan (See Robins at 999-1000, Protarga at 480; Sudbury at 463);

2. The issues of the debts the State's Attorney seeks to litigate in the threatened Connecticut criminal action are the same debts of the Debtor's in the bankruptcy case – unpaid wages. The State's Attorney seeks to arrest Mitchell Heffernan for unpaid wages the Debtor did not pay to former employees. The threatened arrest is solely by reason of Mitchell Heffernan's former capacity as the former Chief Executive Officer and President of the Debtor and not because of any misconduct or wrongdoing on his part. The same unpaid wages are debts in the Debtor's bankruptcy case and the amounts owed, if any, are in dispute. Debtor would then be required to defend its rights in the Connecticut action or be estopped in this bankruptcy case by the findings in Connecticut thus impairing Debtor's ability to

challenge these wages. Therefore, a finding in Connecticut against Mitchell Heffernan would estop the Debtor from disputing these wages in the bankruptcy estate and violates the automatic stay provisions of 11 U.S.C. §362.

3. The subject matter in this case and the threatened Connecticut action are exactly the same. The subject matter of the Connecticut action is solely an action for unpaid wages/commission that the Debtor did not pay Debtors's Connecticut employees. These alleged unpaid commissions are disputed by the Debtor in this case at bar. Therefore, the subject matter in this case and the Connecticut action are exactly the same.

Therefore, in accordance with Parklane Hosiery, Protarga, American Film Technologies and Sudbury, the doctrine of collateral estoppel bars the threatened Connecticut arrest from preceding. Accordingly, Mitchell Heffernan most respectfully submits that this Honorable Court must enter an injunction enjoining the State's Attorney of Connecticut from proceeding with the threatened arrest of Mitchell Heffernan pursuant to this Court's equitable powers under 11 U.S.C. § 105(a).

E. The State Attorney General Has No Authority Under Connecticut Statutes or Federal Law to Seek the Arrest of a Corporate Officer of a Corporation Seeking Bankruptcy Protection

Connecticut General Statutes §§ 31-71(b),(g) and 31-72 provide both civil and criminal remedies for the same act - failure to pay wages. This is identical to the Jerzak case. The instant threatened criminal arrest of Mitchell Heffernan in a civil action dressed in "criminal" clothes- a civil action to collect wages. This statute the State's Attorney seeks to enforce is arguably a quasi-civil statute because it impose strict

criminal liability on a defendant without any showing of mens rea, bad acts or intent. State of Connecticut v. Wilson, 83 Conn. App. 67; 848 A.2d 542 (2004). All that is required to arrest is a bold face allegation by the State's Attorney that wages are not paid. Id.

Additionally, the purpose of this statute is to allow the arrest of an employer who wrongfully and allegedly refuses to pay rightful earned wages; not to arrest an officer of a bankrupt debtor.

The State's own words uttered through its spokesperson Nancy Steffens clearly demonstrate that this threatened arrest is nothing more than the State's Attorney's attempt to circumvent the federal Constitution and the Bankruptcy Code to the detriment of Mitchell Heffernan. As demonstrated by Exhibit "C" hereto, the State's Attorney's Purpose for pursuing its threatened arrest of Mitchell Heffernan is clear:

"Our real purpose is to get people money owed to them. If we can work out a settlement without criminal charges that's great". (emphasis added).

Further, there is no federal or state precedent, including Connecticut precedent, that permits the prosecution of an officer or director of a corporation that has filed for protection from its creditors under the Bankruptcy Code like the Debtor in this case. In fact, the case law in Connecticut which addressed this issue concerns the voluntary and willful failure to pay wages by an individual employer or corporate employer, as follows:

1. Butler, Commission of Labor Ex REL. Marjorie Skidmore v. Hartford Technical Institute, Inc., et al., 243 Conn. 454; 704 A.2d 222 (Sup. Ct. Conn. 1997) –

No bankruptcy pending. Corporation and president were defendants. Employee claimed she was not paid overtime for which she was worked and was awarded double pay;

2. State of Connecticut v. Merkinger, 27 Conn. App. 379; 655 A.2d 1167 (App. Ct. Conn. 1995) – employer not in bankruptcy;

3. State of Connecticut v. Wilson, 83 Conn. App. 67; 848 A.2d 542 (App. Ct. Conn. 2004) – employer not in bankruptcy;

4. State v. Lattanzio, 2001 Conn. Super. LEXIS 2830 – employer not in bankruptcy

Therefore, there is no Connecticut precedent authorizing the Connecticut State's Attorney to willfully ignore the federal Bankruptcy Code in seeking the arrest of Mitchell Heffernan based on this strict liability statute. Therefore, the Connecticut State Attorney must be enjoined from proceeding with the threatened criminal action against Mitchell Heffernan.

