IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: KSERVICING WIND DOWN CORP., *et al.*,[1] Post-Confirmation Debtors.	Chapter 11 Case No. 22-10951 (CTG) (Jointly Administered)
KSERVICING WIND DOWN CORP. (f/k/a Kabbage, Inc.), Plaintiff, v. ROBERT FROHWEIN, KATHRYN PETRALIA, LESLIE SCOTT ASKINS, SPENCER ROBINSON, DON BUTLER, JONATHAN EBINGER, ALEX CHULACK, LAURIE HODRICK, BRYAN STOLLE, IOANNIS PIPILIS, THOMVEST VENTURES LTD., BLUERUN VENTURES IV, LP, BRV OPPORTUNITIES FUND, L.P., REVERENCE CAPITAL PARTNERS OPPORTUNITIES FUND I, L.P., REVERENCE CAPITAL PARTNERS OPPORTUNITIES FUND I (CAYMAN), L.P., RCP KICKER CO-INVEST, L.P., REVERENCE CAPITAL PARTNERS OPPORTUNITIES FUND I (AI), L.P., MDV IX, L.P., SOFTBANK VISION FUND (AIV M2) L.P., SOFTBANK PRINCEVILLE INVESTMENTS, L.P., CURIEUX LIMITED CO., BENNU HOLDINGS LIMITED CO., RAYMOND JAMES & ASSOCIATES, INC. CSDN FBO ROBERT FROHWEIN RIRA U/A/D 5/27/16 A/C 2867A298, and THE FROHWEIN FAMILY 2015 TRUST, Defendants.	Adversary Proceeding No. 25-52372 (CTG) **Re: Adv. D.I.s 92, 94, 96, 100, 103, 107**

[1] The post-confirmation Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, as applicable are: KServicing Wind Down Corp. (f/k/a Kabbage, Inc. d/b/a KServicing) (3937); KServicing Wind Down Canada Holdings LLC (f/k/a Kabbage Canada Holdings, LLC) (N/A); KServicing Wind Down Asset Securitization LLC (f/k/a Kabbage Asset Securitization LLC) (N/A); KServicing Wind Down Asset Funding 2017-A LLC (f/k/a Kabbage Asset Funding 2017-A LLC) (4803); KServicing Wind Down Asset Funding 2019-A LLC (f/k/a Kabbage Asset Funding 2019-A LLC) (8973); and KServicing Wind Down Diameter LLC (f/k/a Kabbage Diameter, LLC) (N/A). The Debtors' mailing and service address is KServicing Wind Down Corp. c/o Resolute Commercial Services, 6750 E. Camelback Road, Suite 103, Scottsdale, AZ 85251.

PLAINTIFF'S OMNIBUS MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTIONS TO DISMISS THE COMPLAINT

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Plaintiff KServicing Wind Down Corp. (f/k/a Kabbage, Inc.) ("Plaintiff" or "Kabbage") respectfully submits this omnibus opposition to the following motions to dismiss: (1) the D&O and Shareholder Defendants' Motion to Dismiss (D.I. 95) and supporting memorandum of law ("D&O Defs. Mot.") (D.I. 96);[2] (2) the Motion to Dismiss of Non-Management Director Defendants Ioannis Pipilis and Alex Chulack (D.I. 93) and supporting memorandum of law ("Add'l Dir. Defs. Mot.") (D.I. 94); (3) Certain Defendants' Motion to Dismiss (D.I. 91) and supporting memorandum of law ("Certain Defs. Mot.") (D.I. 92);[3] (4) Laurie Hodrick's Motion to Dismiss (D.I. 99) and supporting memorandum of law (D.I. 100); (5) L. Scott Askins' Motion to Dismiss (D.I. 102) and supporting memorandum of law ("Askins Mot.") (D.I. 103); and (6) Spencer Robinson's Amended Motion to Dismiss (D.I. 106) and supporting memorandum of law ("Robinson Mot.") (D.I. 107).

NATURE AND STAGE OF PROCEEDING

Plaintiff agrees with the Defendants' statement of the nature and stage of this proceeding.

SUMMARY OF ARGUMENT

This case is a textbook example of fiduciary abdication.[4] When Kabbage, a fintech lender that had staked its entire business on PPP lending during the COVID-19 pandemic, received a report highlighting a risk that Kabbage "knew or should have known it was transmitting fraudulent information to the SBA," its CEO, Defendant Robert Frohwein, did not convene its Board, demand

[2] This motion was filed by Robert Frohwein, Kathryn Petralia, Donald Butler, Jonathan Ebinger, Bryan Stolle, Thomvest Ventures Ltd., BlueRun Ventures IV, LP, BRV Opportunities Fund, L.P., Curieux Limited Co., Bennu Holdings Limited Co., Raymond James & Associates, Inc. CSDN FBO Robert Frohwein RIRA U/A/D 5/27/16 A/C 2867A298, The Frohwein Family 2015 Trust, and MDV IX, L.P.

[3] This motion was filed by SoftBank Vision Fund (AIV M2) L.P., SoftBank PrinceVille Investments, L.P., Reverence Capital Partners Opportunities Fund I, L.P., Reverence Capital Partners Opportunities Fund I (Cayman), L.P., RCP Kicker Co-Invest, L.P., Reverence Capital Partners Opportunities Fund I (AI), L.P., and Spencer Robinson.

[4] Unless otherwise stated herein, Plaintiff uses the same defined terms as in its Complaint.

remediation, or pause lending to resolve the issue. Instead, he flew into a rage, admitting that the "fucking report is going to kill" a lucrative merger of Kabbage with Amex. Rather than address the problems, he instructed his team to bury the report: "get with Scott [Askins]—keep it attorney client privileged and punch them in the fucking face to update that report and pull it back."

The Directors, meanwhile, consciously chose to remain in the dark to close the Merger with Amex that would deliver hundreds of millions of dollars to their affiliated investment funds. The Board knew that Kabbage had transitioned overnight from being a small, struggling lender to processing over $7 billion in federally guaranteed loans to more than 300,000 borrowers. Yet the Board never asked how Kabbage, which had just furloughed most of its employees (including those responsible for fraud reviews), could realistically process such volumes while conducting appropriate borrower diligence. It could not. Nor did the Board ask whether Kabbage had appropriate procedures to verify loan calculations in accordance with PPP regulations. It did not.

The Directors understood that the Merger would effectively sell Kabbage's non-PPP assets to Amex while "orphaning" its PPP liabilities at the legacy company. They knew that Amex refused to acquire the PPP portfolio because it was "very worried about legal liability" and specifically concerned about "liability flowing from fraudulent applicants, anything that would give the government, applicants and others [reason for] suing them." In fact, the Directors knew that Amex was even concerned about its exposure to fraudulent transfer claims if Kabbage did not leave enough cash behind to cover its known and foreseeable liabilities. For these reasons and others, Amex demanded and got a $37.5 million holdback as part of the Merger to protect itself.

Yet when Kabbage received a solvency opinion that—based on instructions from its management—assumed the company needed only $2 million to cover "Potential Legal Liabilities" and loan buyback obligations relating to its PPP lending, the Directors looked the other way. This

reserve was so farcically small that it became a running joke with Kabbage's outside counsel and its low-level employees who, even without direct knowledge of the solvency opinion, recognized that the Directors and Officers intended to leave the legacy company holding the proverbial bag.

The Directors and Officers could have left $120 million in cash with Kabbage to cover foreseeable legal exposure. Amex was indifferent to whether that cash was run through the Merger (because it was simply paying cash to the Shareholders equal to the amount of cash it received). But the Officers and Directors (and their affiliated investment vehicles) wanted to extract that cash immediately, which would, as they discussed, "mitigate risk" of lawsuits around PPP, believing that no one would go after the remaining shell entity following the Merger.

A fiduciary acting in good faith would have known that the SBA and the DOJ might eventually target not only fraudulent PPP borrowers, but also PPP lenders who, like Kabbage, created an environment in which inflated and fraudulent applications ran rampant. Thus, while the Directors and Officers might not have known with certainty that Kabbage would face lawsuits, they certainly knew that the natural and probable consequence of their conduct was to leave Kabbage insolvent when those foreseeable lawsuits arrived.

Predictably, only weeks after the Merger closed in October 2020, Kabbage was hit with two separate whistleblower lawsuits and claims by the SBA. A second round of PPP loans in 2021 gave Kabbage a temporary lifeline, allowing it to pay $30 million to the SBA to partially resolve claims arising from its shoddy loan approvals. But the company ultimately had no choice but to file for bankruptcy. Kabbage now owes more than $240 million to its creditors, including $120 million to the DOJ, $92 million to the SBA, and $30 million to CRB.

Defendants' motions to dismiss are baseless for the following reasons:

1. The pleaded facts establish precisely the type of egregious, conscious disregard of known illegality that Delaware courts have held gives rise to oversight liability under *Caremark*. The Officers who received warnings about Kabbage approving inflated and likely fraudulent loans responded by ordering employees to look the other way. These were not "yellow flags" of business risk, but crimson red flags of actual violations of law. That multiple reports detailing Kabbage's major compliance gaps never reached the Board is telling. Although Kabbage had some written compliance policies, those policies were not enforced. Management's conduct—burying critical reports, punishing employees who raised concerns, and prioritizing the Merger over remediation—sent an unmistakable message that compliance was to be ignored. Simply put, Kabbage utterly lacked reporting systems reasonably designed to provide the Board with "mission critical" information. The Directors and Officers were incentivized to ignore these gaps because addressing them would have jeopardized the lucrative Merger.

2. Beyond oversight failures, the Officers are separately liable for grossly negligent affirmative acts that breached their duty of care. They collectively approved Kabbage's certifications to the SBA to become a PPP lender despite knowing Kabbage's compliance systems were riddled with gaps. And they were responsible for supplying the flawed assumptions that went into the "garbage-in, garbage-out" solvency opinion that was a condition of the Merger. These grossly negligent operational decisions independently establish liability.

3. The Shareholders[5] attempt to escape fraudulent transfer liability for their receipt of hundreds of millions of dollars in Merger proceeds is groundless. The Complaint pleads an actual fraudulent transfer with particularized facts detailing how the Directors and Officers structured the

[5] The "Shareholders" are defined in the Complaint as the "Fraudulent Transfer Beneficiaries." But for simplicity and clarity here, Kabbage refers to those Defendants as the "Shareholders."

Fraudulent Transfer to orphan known and knowable liabilities at Kabbage and to maximize Shareholder payouts. The Complaint sets forth numerous badges of fraud that create a presumption of fraudulent intent. The pleaded facts also support a claim for constructive fraudulent transfer. Even a small change to the solvency opinion's assumptions regarding its PPP liabilities renders Kabbage insolvent. A good-faith estimate of those liabilities would have been far higher than $2 million (the amount that the Directors and Officers used), as demonstrated by the over $210 million in aggregate settlements that Kabbage ultimately reached with the DOJ, SBA, and others. And because the Fraudulent Transfer was a one-way distribution for no value, the entire transfer is avoidable under the Bankruptcy Code.

4. Section 550(a)(1) of the Bankruptcy Code permits recovery not only from the actual transferee—here, Amex Kabbage, the entity that Amex acquired as part of the Merger—but also from any "entity for whose benefit such transfer was made." The Fraudulent Transfer—Kabbage's October 13, 2020 asset transfer to its parent, Amex Kabbage—was an integrated step in a scheme designed to deliver hundreds of millions of dollars to the Shareholders, who received quantifiable benefits from the transfer itself, and immediately accessible cash payments just days later. Plaintiff need not pierce the corporate veil of Amex Kabbage (an entity formed just months earlier for the sole purpose of effectuating the Merger) to hold the Shareholders liable for the cash they received, especially when that was the intended purpose of the Fraudulent Transfer itself.

STATEMENT OF FACTS

A. Kabbage Doled Out Hundreds of Millions of Dollars in Fraudulent Loans.

Kabbage ultimately processed more than $7 billion in PPP loans to over 300,000 borrowers, making it one of the nation's largest PPP lenders by volume.[6] But Kabbage did so

[6] Compl. ¶¶ 1, 9, 247.

without re-hiring sufficient staff to conduct good-faith reviews of loans, updating its BSA/AML compliance program to be commensurate with its new risk profile as a PPP lender, utilizing appropriate fraud-detection tools, or testing its platform for PPP compliance. And when Kabbage identified issues concerning its compliance with PPP regulations, it ignored them so that it could continue to earn the massive fees that accompanied approving, rather than denying, loans.

1. Kabbage knowingly or recklessly approved inflated loans.

Kabbage knew that its platform allowed borrowers to receive inflated PPP loans.

First, PPP loans were generally calculated based on a business's average monthly payroll costs, but Kabbage's platform asked borrowers to add SALT withholdings (which are already included in wages) to the payroll calculation, causing thousands of borrowers to double-count. The DOJ estimated this error resulted in at ***least 53,111 loans inflated by at least $111 million***.[7]

Second, PPP regulations excluded "the compensation of an individual employee in excess of [an annual salary of] $100,000." But Kabbage knew that it was "not capping sole props/single LLCs to the appropriate $100K."[8] The lack of any cap led to absurd results. In one instance, an employee mused in Slack, "dude we got a guy whose payroll was 25,978.00. Someone put in 2597800.00. Homie got submitted for a $2mm loan."[9] When asked how Kabbage validated the amount, the employee responded "cause we removed the cap."[10] The DOJ estimated these $100,000-cap errors resulted in ***at least 1,972 loans inflated by at least $108,488,540.27***.[11]

[7] *Id.* ¶ 116.

[8] *Id.* ¶ 117.

[9] *Id.* ¶ 118.

[10] *Id.*

[11] *Id.* ¶ 119.

Third, Kabbage's platform allowed borrowers to include duplicative data from IRS Form 940 Box 4 in calculating average monthly payroll. The DOJ estimated it resulted in ***at least 783 loans inflated by at least $14 million***.[12]

2. Kabbage knowingly or recklessly approved fraudulent loans.

Kabbage certified to the SBA that, ***before engaging in PPP lending activities***, it would maintain a BSA/AML compliance program "equivalent to that of a comparable federally regulated institution."[13] A BSA/AML compliance program is the set of internal policies, procedures, and controls that a financial institution maintains to detect and prevent money laundering, terrorist financing, ***and other financial crimes***, and then report such crimes to law enforcement through the filing of Suspicious Activity Reports.

Unlike traditional banks that focused on making PPP loans to *existing customers* who had already undergone BSA/AML review, including "Know Your Customer" screening, Kabbage made more than 90% of its PPP loans to *new customers*. It did so on a largely automated and expedited basis, with a small and ill-trained BSA/AML compliance team, and without reasonable systems to verify customer identities or detect, prevent, and report fraud.[14]

From the outset, Kabbage's Officers pressured employees to prioritize automation and maximize volume.[15] But Kabbage's automated fraud review failed to flag obvious indicia of fraud.[16] Even when a loan was flagged as potentially fraudulent, Kabbage lacked the systems to

[12] *Id.* ¶¶ 120–21.

[13] *Id.* ¶¶ 2, 19, 77.

[14] *Id.* ¶¶ 4, 97, 105–12.

[15] *Id.* ¶¶ 59, 110–12, 222; Pl.'s App'x Ex. G at B000198 (DOJ Proof of Claim) ("[M]ore than 90% of the more than 260,000 loans Kabbage originated or processed on behalf of its partner banks received no human review.").

[16] Compl. ¶¶ 134–58. According to the DOJ's Proof of Claim filed in Kabbage's bankruptcy, Kabbage approved borrowers not in existence at the time of application; failed to detect falsified tax forms and mismatched TINs; approved more than 4,100 loans where borrowers shared a social security number with

handle the flags.[17] Kabbage's system allowed sales team members to delete fraud flags without informing the account review team.[18] Moreover, in many cases, Kabbage did not perform fraud checks until after submitting PPP loan guarantee applications to the SBA, if ever.[19]

The actual review team—only seven members without a permanent supervisor—was ill-equipped to handle the deluge. By late May, the team faced a backlog of 35,000 applications flagged as potentially fraudulent.[20] Understaffed, overworked, and unguided, the team sought ways to "automate more of the process."[21] This automation opened the door even wider for fraudulent applications. And rather than utilizing adequate systems to address potentially fraudulent applications, Kabbage sought ways to save costs.[22]

In total, Kabbage approved thousands—if not tens of thousands—of fraudulent and likely fraudulent loans.[23]

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another PPP borrower; and approved loans of nearly 135,000 borrowers who shared an IP address or device ID with another PPP borrower. Pl.'s App'x Ex. G at B000198 (DOJ Proof of Claim).

[17] Compl. ¶¶ 105–63.

[18] *Id.* ¶ 137.

[19] *Id.* ¶¶ 153–54, 177, 183; *see also* Pl.'s App'x Ex. G at B000198 (DOJ Proof of Claim).

[20] Compl. ¶ 109.

[21] *Id.* ¶ 110.

[22] *Id.* ¶ 110–11. In May 2020, Kabbage changed fraud-detection software parameters because costs were "skyrocketing." Pl.'s App'x Ex. G at B000199 (DOJ Proof of Claim). Kabbage lowered its fraud-detection threshold and made other changes to keep costs down. *Id.* The company also "chose not to use a third-party document-reading service because 'it's expensive,' relying instead on a home-grown system which Kabbage reviewers openly complained about as having allowed significant amounts of fraud through." *Id.*

[23] *See* Compl. ¶ 283 ("At that time, the SBA was refusing to make guaranty payments to CRB on loans affected by the SALT, $100K, and IRS Form 940 issues, as well as on nearly 18,000 loans that Kabbage and CRB had flagged as potentially fraudulent."); Pl.'s App'x Ex. G at B000203 (DOJ Proof of Claim) ("The Debtor is alleged to have made at least 17,224 false claims based on loans it knew or should have known were fraudulent, resulting in potential penalties between $232,661,792 and $465,358,032.").

B. The Officers Knew of or Willfully Ignored Kabbage's Violations of the PPP Laws and Regulations.

The Officers were aware of each problem in real time, received explicit warnings, and consciously prioritized the Amex Merger over compliance remediation.

1. The Officers knew that Kabbage lacked sufficient compliance staff to perform the required KYC analyses.

From the start of the PPP, Kabbage's BSA Officer, Azba Habib, warned Defendants Frohwein, Petralia, Robinson, and Askins that the company lacked sufficient compliance staffing to perform "Know Your Customer" analyses.[24] Habib explained that many customers "have . . . never been KYB/KYC'd or . . . have not been KYB/KYC'd in years," meaning Kabbage could "see a lot of fraud (probably after the $ has left the door)."[25] Rather than hire additional personnel, the Officers pressed forward, prioritizing volume over legally mandated screening.

2. The Officers knew that Kabbage lacked sufficient controls to detect and prevent fraud.

Near the outset of PPP, Nicole Hill, then Head of Fraud, raised concerns about Kabbage's inadequate fraud controls to Robinson. Her recommendations were rejected; she was told "we do not have fraud" and instructed "not to impair investors by classifying fraud."[26] When Hill asked for additional resources, she was provided one employee and "told to be grateful."[27] On April 16, 2020, Robinson demoted Hill. The next day, Askins and Petralia received a letter from Hill detailing these concerns.[28] Hill's concerns were never addressed.[29]

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[24] Compl. ¶¶ 97–99, 126–30.

[25] *Id.* ¶¶ 97–98.

[26] *Id.* ¶ 94.

[27] *Id.* ¶¶ 95, 106

[28] *Id.* ¶ 95; Pl.'s App'x Ex. A (Email re Hill Complaint).

[29] Compl. ¶¶ 95, 196.

Similarly, on May 13, 2020, recognizing that Kabbage still did not have a formal monitoring process for KYC and other fraud controls as they related to the PPP, Habib emailed Amit Kesarwani, the new purported "Head of Fraud," and others to ask them to develop a "monitoring process" for, among other things, "KYB/KYC tickets" and "Fraud tickets." Kesarwani, however, effectively disregarded the request.[30]

The pattern continued. In June 2020, A&M, retained to audit Kabbage's PPP compliance, provided a preliminary Risk Assessment Report (the "A&M Report") to the Officers. Even though A&M reviewed only ten PPP loans out of tens of thousands, it found significant risk that "***Kabbage knew or should have known it was transmitting fraudulent information to the SBA***," especially since Kabbage was sending loans to the SBA prior to completing fraud reviews.[31] Like other warnings, the Officers disregarded A&M's findings.

By mid-June, Kabbage's already short-staffed compliance department was in disarray.[32] No one in compliance timely addressed the ongoing issues.[33] Rather, when Kabbage employees encountered fraudulent applications, the message they received from Robinson and others was, "***gotta let em through***."[34]

3. The Officers knew that Kabbage lacked appropriate systems to identify and make the required Suspicious Activity Reports.

Under the BSA, a financial institution is required to file a SAR within 30 days of learning about suspicious activity. The Officers knew that Kabbage did not have systems and procedures

[30] *Id.* ¶¶ 134–36.

[31] *Id.* ¶¶ 171–77; J.A. Ex. 9 (A&M Risk Assessment Report) at A00152.

[32] Compl. ¶¶ 126, 139.

[33] *Id.* ¶¶ 178, 187.

[34] *Id.* ¶ 157.

in place to comply with this law.[35] On April 28, 2020, Habib emailed Robinson, Askins, and others, stating she needed help identifying "what types of characteristics at onboarding and thereafter we should flag for suspicious activity referrals and reports" and establishing a process for "internal quality control and testing to ensure that our automated process is working as it should."[36] Despite these urgent warnings from Kabbage's own BSA Officer, the Officers took no meaningful action. So, on May 11, 2020, Habib explained to others at Kabbage: "I'm a bit concerned that we have identified a number of instances of suspected fraud (I think) and not yet filed any SARs."[37] A&M, unsurprisingly, also found significant risk that "***Kabbage did not have a process in place to identify and report unusual activity***."[38]

4. The Officers knew about the SALT and related calculation errors.

The Officers were aware of the inflation errors. On April 12, 2020, Kabbage's communications director sent Robinson and other executives a link to a tweet "suggesting we're doubling up on the same data points."[39] Rather than investigating, Robinson was dismissive.[40] Weeks later, the same issue was brought to Petralia and Frohwein, but there was no proper investigation, and the issue was not fixed.[41] Yet Robinson himself acknowledged concerns about Kabbage's calculations, stating: "I'm worried about our calcs."[42] Despite this worry, Robinson

[35] *Id.* ¶¶ 126–28.

[36] *Id.* ¶ 127.

[37] *Id.* ¶ 133.

[38] *Id.* ¶ 177; J.A. Ex. 9 (A&M Risk Assessment Report) at A00153.

[39] Compl. ¶ 115.

[40] *Id.* ¶¶ 115–16.

[41] *Id.*

[42] *Id.* ¶ 120.

did not ensure the methodology was corrected or inform the Board.[43] Instead, he articulated Kabbage's strategy for dealing with inflated loans as hoping the problem would never come to light: ***"[W]e just did a poor job verifying [PPP loan amounts]. . . . [It] only becomes an issue in an audit or guarantee scenario***. . . . [M]aybe they'll be auto forgiven 🤞."[44]

5. The Officers suppressed—rather than escalated—compliance issues.

The Officers made clear that Kabbage would not tolerate questions about its compliance controls. Robinson went to such lengths to suppress information that employees viewed him as an "information barrier."[45] The treatment of Hill and the A&M Report exemplifies the Officers' systematic suppression of compliance concerns. After Hill raised concerns, Robinson demoted her. And when Hill sent a letter to Askins explicitly detailing serious concerns about Kabbage's compliance program, including being told to ignore fraud, Askins did not investigate or escalate her allegations to the Board.[46] Petralia, for her part, refused to bring back more than one single furloughed employee to assist with the fraud review process.[47] Even when the Officers received the A&M Report, they did not take remedial action. Rather, Frohwein flew into a rage and instructed his team to bury the report.[48] To the extent that Askins addressed the red flags in the A&M Report, it was to push A&M to change its conclusions.[49]

[43] *Id.* ¶¶ 121–22.

[44] *Id.* ¶ 123.

[45] *Id.* ¶ 196.

[46] *Id.* ¶¶ 94–95.

[47] *Id.* ¶ 106.

[48] *Id.* ¶¶ 193, 199.

[49] *Id.* ¶¶ 200–01.

C. The Board Utterly Failed to Monitor Kabbage's PPP Compliance.

The Board knew that Kabbage had pivoted its entire business to PPP lending but turned a blind eye to whether Kabbage had the actual systems and personnel—not just written policies—to effectively perform required BSA/AML reviews and correctly calculate and submit loans to the SBA. The Board's abdication was comprehensive: it asked no questions, demanded no reports, established no committees, and took no action to ensure that Kabbage's compliance infrastructure—which it knew was already riddled with gaps—could handle the exponentially increased volume and risk of PPP lending.

First, the Board knew Kabbage's BSA/AML compliance program suffered from serious deficiencies that had not been addressed. In 2018 and 2019, Kabbage had retained Treliant to conduct "risk-based" testing of the design and effectiveness of its BSA/AML compliance program. Treliant's 2019 report, which the Board received before the PPP began, found that Kabbage's "BSA/AML Program demonstrates limited evidence of enhancement since [Treliant's] prior review" and identified "the lack of enhancements in the Company's Compliance Program operational procedures [as] an important weakness that requires prioritization."[50] Despite this warning, the Board failed to ensure these deficiencies were remediated before Kabbage certified compliance to the SBA.[51]

Second, despite PPP lending becoming Kabbage's sole new-loan business in April 2020, the Board failed to establish any formal mechanism or committee—newly formed or pre-existing, such as its audit committee—to monitor PPP compliance.[52] Even if PPP lending was only short-lived, Kabbage would have years of ongoing obligations as a lender.

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[50] *Id.* ¶¶ 88–92.

[51] *Id.* ¶ 93.

[52] *Id.* ¶¶ 202–06, 317–21.

Third, although the Board knew that Kabbage's PPP volume would be enormous, it held no discussions about compliance between the start of the PPP and one week before the program ended—when the only action was approving an updated BSA/AML Policy.[53] The meeting minutes reflect no questions and no concern regarding the timing or substance of the policy.[54]

Fourth, during the PPP, the Board did not receive any reports from the Chief Compliance Officer (Askins) or Kabbage's BSA/AML Officer (Habib and, later, Askins in an interim capacity) on compliance matters and risks.[55] There were no reports about A&M's critical review of Kabbage's PPP program. There were no reports about how many SARs had been filed by Kabbage and the general bases for such filing. There were no reports about how many loans had been made by Kabbage to borrowers that had already become subjects of criminal investigations or, relatedly, how many subpoenas had been received.[56]

Fifth, the Board did not ask basic questions, such as: (1) whether Kabbage had assessed its PPP lending practices (it had—and that assessment was not provided to the Board); (2) whether Kabbage employees had raised compliance concerns (they had—and those concerns were not escalated to the Board); or (3) how many loans had been flagged as potentially fraudulent (thousands of loans—and those flagged loans were not disclosed to the Board).[57]

Finally, the Board never set a "tone from the top" encouraging compliance reporting. With no Board oversight, management had free rein to suppress critical issues. When employees raised compliance concerns, they were marginalized, stripped of titles, or made to fear for their jobs.

[53] *Id.* ¶¶ 82, 202.

[54] *Id.* ¶¶ 202–03, 318–19.

[55] *Id.* ¶¶ 194, 318–20.

[56] *Id.* ¶¶ 21, 205, 318.

[57] *Id.* ¶¶ 202, 205, 213, 248–49, 318.

Notably, when Paul Pietschner, a Kabbage Legal Analyst, received the A&M Report, he conducted his own investigation and ***found even more serious gaps in Kabbage's fraud controls***.[58] He sent his findings to in-house counsel and senior employees.[59] Despite the red flags raised in the Kutworm Report, it took nearly two months for anyone to respond—and the only response was to leave Pietschner with the impression that he would be fired for voicing his legitimate concerns.[60]

D. Defendants Cash Out with the Amex Merger While Leaving Kabbage Hopelessly Insolvent.

1. The Directors and Officers negotiated a sale to Amex that "orphaned" the PPP liabilities at Kabbage.

Amex made it clear that it would not acquire Kabbage's loan portfolios, particularly the rapidly expanding PPP portfolio that Kabbage was churning out with minimal oversight.[61] Thus, the parties agreed to structure the sale so that Kabbage's loan portfolio and all associated liabilities remained at Kabbage. Amex would purchase Kabbage's non-loan assets—the bulk of Kabbage's assets—through a proposed multi-step merger agreement.[62] The parties signed the Merger Agreement on August 16, 2020.[63]

Not only did the Merger Agreement "orphan" Kabbage's PPP liabilities at the legacy company, but it also contained protections for Amex against PPP-related liabilities. Notably, Amex insisted on a $37.5 million holdback because it was "***very worried about legal liability***" and

[58] *Id.* ¶¶ 24–25, 179–87.

[59] *Id.* ¶¶ 187–89.

[60] *Id.* ¶¶ 188–90.

[61] *Id.* ¶¶ 208–10.

[62] *Id.* ¶¶ 211–14, 250–52.

[63] *Id.* ¶ 255.

concerned about "***liability flowing from fraudulent applicants, anything that would give the government, applicants and others [reason for] suing them***."[64]

2. The Officers dictated erroneous assumptions for a solvency opinion to increase the cash that they could extract from Kabbage.

A critical condition of the Merger Agreement was obtaining a solvency opinion for post-transaction Kabbage.[65] Amex demanded this solvency opinion because, among other reasons, it was "concerned that the burden to prove that enough money was left in legacy co [*i.e.*, Kabbage] shifts to [Amex] if they push our cash from PPP through the transaction."[66]

Rather than take a good-faith approach to determining how much cash needed to remain at Kabbage, the Officers viewed it as a "deal within a deal," pressuring Duff & Phelps to require as low a number as possible.[67] The Officers decided to reserve only $1 million for litigation—a figure Askins questioned, noting that even before the PPP, "the defense costs alone for outside litigation counsel have been higher than $1M annually in the past."[68] Even more remarkably, the Officers contemplated only $949,000 in "PPP put back liability" (later increased to $1,058,000 at closing), representing less than 0.014% of the more than $7 billion in PPP loans processed.[69] This reserve was supposed to represent a fair estimate of liability in the case where—as would ultimately happen—Kabbage was *not* able to "shield [itself] from any liability [by] relying on the

[64] *Id.* ¶¶ 226–27.

[65] *Id.* ¶¶ 229–30; J.A. Ex. 39 (Duff & Phelps Solvency Analysis).

[66] Compl. ¶ 225.

[67] *Id.* ¶ 242.

[68] *Id.* ¶ 245.

[69] *Id.* ¶¶ 247, 271. Kabbage made it clear to Duff & Phelps that these numbers were not even "estimates." Rather, as Kabbage stated in its management representation letter, "[f]or avoidance of doubt, amount ['Reserve'] represents reserved cash to fund liabilities, ***not an estimation of liabilities***." Pl.'s App'x Ex. D at B000031 (Management Rep. Letter) (emphasis added).

SBA's 'good faith' clauses with respect to actions it took reviewing borrower documents when originating and servicing loans."[70]

On October 15, in anticipation of closing, Duff & Phelps issued its "bring down" solvency opinion (the "Solvency Opinion"), which found that Kabbage was just barely solvent.[71] But, contrary to that opinion, it was almost common knowledge at Kabbage that the transfer would render it insolvent. Kabbage's attorneys joked that Duff & Phelps was "***dumb for issuing the solvency opinion***."[72] And Kabbage employees shared memes mocking Kabbage's insolvency.[73]

3. By design, the Merger stripped Kabbage of its assets and transferred their value to the Shareholders.

Pursuant to the Merger Agreement, three days before closing, on October 13, 2020, Kabbage became a wholly owned subsidiary of Amex Kabbage, with Kabbage equity holders receiving identical securities in Amex Kabbage.[74] On the same day, Kabbage made the Fraudulent Transfer, transferring substantially all of its assets to Amex Kabbage, including $120 million in cash earned through the PPP.[75] Kabbage was left with approximately $17 million—intended to service its existing loan portfolios and cover all liabilities, including massive contingent liabilities and wind-down activities.[76] Even according to Duff & Phelps, Kabbage was solvent by only around $3 million, leaving no margin for error.[77]

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[70] Pl.'s App'x Ex. E at B000053 (Duff & Phelps Oct. 15, 2020 Analysis).

[71] Compl. ¶ 271.

[72] *Id.* ¶ 272.

[73] *Id.* ¶ 30.

[74] *Id.* ¶¶ 251, 270.

[75] *Id.* ¶ 270.

[76] *Id.* ¶¶ 8, 244, 248, 271.

[77] J.A. Ex. 39 (Duff & Phelps Solvency Analysis) at A00383 (showing Net Asset Value – Kabbage LLC equal to $503,500).

Three days later, Amex Kabbage merged into an Amex subsidiary, with Amex Kabbage as the surviving entity. Each Amex Kabbage equity holder received the applicable per-share purchase price from Amex, and their shares were cancelled. Each equity holder (other than Reverence and holders of Series F preferred shares) then received a proportional share of common stock of Kabbage, becoming direct owners of Kabbage again.[78]

Thus, over three days and as specifically set forth in the Merger Agreement, Kabbage's Shareholders went from owning equity in Kabbage directly to owning identical equity in Amex Kabbage, and then to receiving hundreds of millions of dollars in cash. On October 16, 2020, the Merger closed, and Kabbage's former shareholders received $730,159,391 in merger consideration, including more than $500 million paid to Defendants.[79]

E. As Was Foreseeable, Kabbage Was Hit with Claims and Investigations Regarding Its PPP Lending Practices.

Shortly after the merger closed, Kabbage was hit with a wave of claims and investigations. Two separate whistleblowers filed False Claims Act lawsuits on behalf of the DOJ. The SBA asserted claims arising from Kabbage's deficient PPP lending practices, and a congressional investigation culminated in a scathing report.[80] A second round of PPP loans in 2021 gave Kabbage a temporary lifeline, allowing it to pay $30 million to the SBA to partially resolve claims. But the claims ultimately proved insurmountable.

Facing hundreds of millions of dollars in legal claims for harm caused by its role in the PPP—including, almost $800 million by the DOJ, $720 million from the SBA, $536 million from the Federal Reserve System, and $572 million from CRB—Kabbage filed for bankruptcy on

[78] Compl. ¶ 251.

[79] *Id.* ¶ 273.

[80] *Id.* ¶¶ 275–80; Pl.'s App'x Ex. F at B000064, B000121–31 (Congressional Staff Report).

October 3, 2022.[81] Plaintiff then conducted an extensive investigation and reduced these claims through protracted negotiations.[82] Plaintiff negotiated the DOJ's two FCA claims down to allowed claims totaling $120 million.[83] After resolving the DOJ claims, Plaintiff reduced the SBA's claim from $720 million to $92 million.[84]

LEGAL STANDARD

To survive a Rule 12(b)(6) motion, a complaint "must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'"[85] A claim is facially plausible when its factual allegations permit "the court to draw the reasonable inference that the defendant is liable for the misconduct alleged."[86] This standard demands only "more than a sheer possibility that a defendant has acted unlawfully."[87] Where fraud is alleged, Rule 9(b) requires particularity as to the circumstances of the misconduct, but it does not displace the required plaintiff-friendly inferences.[88] The Complaint pleads who did what, when, and why through dozens of internal emails, Slack messages, and deal documents, thereby satisfying both Rules 8 and 9(b).

As explained below, Defendants flout the motion-to-dismiss standard. Not only do they ignore the Complaint's allegations, but they also invent non-pleaded facts (*e.g.*, Frohwein claiming

[81] Compl. ¶¶ 281–82.

[82] *Id.* ¶¶ 283–85.

[83] *Id.* ¶¶ 285–86.

[84] *Id.* ¶ 287.

[85] *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)).

[86] *Id.*

[87] *Id.*

[88] *Eurand, Inc. v. Mylan Pharms., Inc.*, 266 F.R.D. 79, 82–83 (D. Del. 2010).

to have misunderstood the A&M Report)[89] and invite the Court to adopt defendant-friendly inferences from the pleaded facts (*e.g.*, Robinson arguing, based on two self-serving statements in Slack messages, that he had discussed issues with Kabbage's counsel at the time).[90]

ARGUMENT

I. The Complaint Adequately Pleads *Caremark* Claims.

Defendants invoke the familiar refrain that *Caremark* claims are "possibly the most difficult theory in corporation law."[91] But this is no ordinary case. Courts must impose heightened oversight duties when externally imposed regulations govern a company's core operations.[92] PPP lending was not merely one of Kabbage's business lines—it was effectively the company's *sole* business activity from April through October 2020. The Directors' and Officers' duty to ensure functioning compliance reporting was therefore at its apex. Yet Kabbage's compliance reporting was not merely inadequate; it was nonexistent. The Complaint alleges egregious oversight failures giving rise to *Caremark* liability under both the "information systems" and "red flags" prongs.

A. The Complaint States an "Information Systems" Claim.

Under *Caremark*'s first prong, fiduciaries are liable when they "utterly fail[] to implement any reporting or information system or controls."[93] A board must assure "that information and

[89] D&O Defs. Mot. at 39–40 n.53.

[90] Robinson Mot. at 25–26.

[91] D&O Defs. Mot. at 22 (quoting *In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996)).

[92] *See Marchand v. Barnhill*, 212 A.3d 805, 822 (Del. 2019) ("When a plaintiff can plead an inference that a board has undertaken no efforts to make sure it is informed of a compliance issue intrinsically critical to the company's business operation, then that supports an inference that the board has not made the good faith effort that *Caremark* requires."); *In re Clovis Oncology, Inc. Deriv. Litig.*, 2019 WL 4850188, at *13 (Del. Ch. Oct. 1, 2019) ("As *Marchand* makes clear, when a company operates in an environment where externally imposed regulations govern its 'mission critical' operations, the board's oversight function must be more rigorously exercised." (citing *Marchand*, 212 A.3d at 822, 824)).

[93] *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).

reporting systems exist in the organization that are reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with law and its business performance."[94] Officers "owe the same [oversight] duties as corporate directors."[95] This inquiry looks beyond paper structures, or the "trappings of oversight," to whether the board ensured that systems actually function to bring critical information to its attention.[96]

The Directors and Officers ignore the context of Kabbage's shift to PPP lending. Prior to the PPP, the Board received audit reports documenting systemic gaps in Kabbage's BSA/AML compliance infrastructure. While those gaps might not have been "mission critical" for Kabbage's typical lending operations, they became mission critical when Kabbage certified to the SBA that it had a compliance program "equivalent to that of a comparable federally regulated institution" and prepared to approve billions of dollars of loans to hundreds of thousands of borrowers.[97]

The 2018 Treliant Report identified multiple deficiencies, rating Kabbage's overall BSA/AML control environment as providing only "Limited Assurance."[98] Treliant found that "the

[94] *Caremark*, 698 A.2d at 970.

[95] *In re McDonald's Corp. S'holder Deriv. Litig.*, 289 A.3d 343, 364 (Del. Ch. 2023).

[96] *See Hughes v. Hu*, 2020 WL 1987029, at *14–16 (Del. Ch. Apr. 27, 2020) ("The mere existence of an audit committee and the hiring of an auditor does not provide universal protection against a *Caremark* claim."); *see also Marchand*, 212 A.3d at 821–22 (holding that board must ensure information systems actually function to bring critical information to its attention, not merely exist on paper); *In re Boeing Co. Deriv. Litig.*, 2021 WL 4059934, at *29–31 (Del. Ch. Sept. 7, 2021) (emphasizing that "ad hoc" communications from management do not substitute for formal compliance reporting systems).

[97] Accordingly, the fact that "Treliant found the ultimate output of the risk assessment to be reasonable and aligned to the risk profile of the Company" prior to PPP lending does not excuse Defendants' failure to take remediation measures when Kabbage changed its entire business model PPP lending. J.A. Ex. 5 at A00082; *see, e.g.*, Askins Mot. at 17 (relying on the Treliant reports while ignoring the fact that Kabbage's "risk profile" changed substantially once it became a PPP lender); D&O Defs. Mot. at 26–27, 36, 39 (same).

[98] J.A. Ex. 3 (2018 Treliant Report) at A00047. Defendants argue without much conviction that the 2018 Treliant Report may not have been "brought to the Board's attention." Add'l Dir. Defs. Mot. at 16. If

incomplete operational review process documentation is an important weakness that requires prioritization by the Company to allow for robust independent review of control effectiveness and ongoing Quality Assurance." The report warned: "Without adequate review documentation, the quality of execution of the control cannot be fully tested. This weakness affects testing of CIP, EDD, OFAC and transaction monitoring controls and is considered ***a systemic gap***."[99] The report also identified critical weaknesses in Kabbage's Quality Assurance function—one of the essential pillars of any BSA/AML program. Treliant found that "[a] formal QA/QC framework is not yet in place across all monitoring and screening processes."[100] The absence of a developed quality control reporting framework meant Kabbage had no systematic way to verify that its compliance controls were actually functioning.

The 2019 Treliant Report—provided to the Board on November 13, 2019—found that Kabbage's compliance program had deteriorated.[101] The report documented un-remediated deficiencies directly implicating Kabbage's ability to detect and prevent fraud.[102] It concluded that the "BSA/AML Program demonstrates limited evidence of enhancement since [Treliant's] prior review" and specifically warned that "the lack of enhancements in the Company's Compliance Program operational procedures [is] an important weakness that requires prioritization."[103] The overall rating remained "Limited Assurance," meaning systemic gaps identified in 2018 remained unaddressed.

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anything, this odd argument only reinforces Plaintiff's prong one claim against the Board. But it also is factually irrelevant, as the Complaint makes clear that the 2019 Treliant Report, which discusses the issues raised in the 2018 report in detail, "was provided to the Board on November 13, 2019." Compl. ¶ 89.

[99] J.A. Ex. 3 (2018 Treliant Report) at A00047.

[100] *Id.* at A00051.

[101] Compl. ¶¶ 88–89.

[102] *Id.* ¶¶ 88–92; J.A. Ex. 5 (2019 Treliant Report) at A00086-87.

[103] Compl. ¶ 90.

Defendants claim that the Treliant reports are not "red flags" of illegality because they did not explicitly state Kabbage was violating the law.[104] This argument misunderstands the information systems prong of *Caremark*. The Treliant reports are relevant because they demonstrate that the Board knew that Kabbage's compliance infrastructure was inadequate to detect or prevent violations. A board acting in good faith would have known that Kabbage needed to remediate its BSA/AML compliance program ***before*** becoming a PPP lender. But the Board took no such action, much less made any inquiry whatsoever into these known issues, despite their mission-critical importance. And as the Board knew (or willfully ignored), false statements in PPP loan submissions exposed Kabbage to liability under, among other things, the False Claims Act.

Defendants argue that "the Complaint concedes that the Directors . . . remedied any purported issues" in the Treliant reports, basing this bizarre claim on the fact that the Directors approved an updated BSA/AML Policy on July 29, 2020.[105] First, the Complaint alleges the opposite.[106] In fact, Habib told Askins in June 2020 that "corrective actions plans (remediations) from the 2019 Promontory risk assessment and the related Treliant audit are ***not complete***" and "***will require significant effort to operationalize and validate***."[107] There is no allegation (or evidence) that any effort, much less "significant effort" was undertaken in June or July to remediate the issues from the risk assessment report. Second, even if Defendants' argument was factually

[104] *See* D&O Defs. Mot. at 33–38; Add'l Dir. Defs. Mot. at 19–24 (arguing that the Treliant Reports were not red flags of illegality but "yellow flags" of business risk).

[105] D&O Defs. Mot. at 36; *see also id.* at 37 n.47.

[106] Compl. ¶ 93; *see also id.* ¶¶ 19–20.

[107] Pl.'s App'x Ex. C at B000027 (June 4, 2020 email to Askins) (referenced in Compl. ¶ 20).

accurate (it is not), the Directors did not receive an updated compliance policy until ***after*** Kabbage had already made more than $6 billion of PPP loans.[108]

Defendants point to Treliant's findings to suggest that the Board "maintain[ed] sufficient oversight" and that Treliant "did not find any material concerns or issues" with Board governance. But these statements must be read in context. Treliant was evaluating whether the Board addressed ***escalated*** issues, not whether underlying compliance controls were adequate.[109] The problem was not that the Board failed to review reports it received; it was that the compliance infrastructure necessary to generate and deliver those reports to the Board in the first place was non-existent.

In addition, while BSA/AML compliance was certainly intertwined with PPP regulations, the PPP contained additional requirements for lenders. Among other things, the PPP regulations required Kabbage to "confirm receipt of information demonstrating that a borrower had employees for whom the borrower paid salaries and payroll taxes on or around February 15, 2020," and confirm, by performing "a good faith review," "the dollar amount of average monthly payroll costs for the preceding calendar year by reviewing the payroll documentation submitted with the borrower's application."[110] When Kabbage pivoted its business to PPP lending and specifically sought to become one of the nation's largest volume lenders, the Board had a responsibility to

[108] Compl. ¶ 82. Relatedly, Defendants also argue that by April 2020, "Kabbage set upon updating its BSA/AML Policy as soon as PPP lending began." D&O Defs. Mot. at 37 n.47. What Defendants fail to mention is that the "update" to the policy in late April was for a new Kabbage Checking product (a product totally unrelated to the PPP), which gave lip-service to the PPP but clearly stated Kabbage had "implemented a CRR methodology for Offerings ***other than [PPP] loans***" and was "***still refining*** its customer risk segmentation process for [PPP] loans." Pl.'s App'x Ex. B at B000025 n.13 (April 27, 2020 Draft of Compliance Policy). Moreover, Defendants offer no proof—nor would such proof be appropriate for a motion to dismiss—that the Directors received a copy of the late April updated policy. Thus, this can hardly be an example of "the Board's chosen response [being] diligent." D&O Defs. Mot. at 37 n.47.

[109] J.A. Ex. 5 (2019 Treliant Report) at A00083.

[110] Compl. ¶ 113 (citing SBA PPP FAQ #1 (Apr. 3, 2020) and 85 Fed. Reg. 20811, 20815 (Apr. 15, 2020)).

ensure that Kabbage had a reporting and information system in place to comply with the specific PPP regulations. But no such specific system existed.

The Complaint alleges facts closely paralleling the dispositive oversight deficiencies in *Boeing* and *Marchand*. In *Boeing*, the Court of Chancery denied dismissal where the board failed to implement a system to monitor airplane safety—a "mission critical" aspect of the company's business.[111] The court held that the plaintiff had pleaded a prong-one *Caremark* claim because: (1) the board had no committee charged with direct responsibility to monitor airplane safety; (2) the board did not monitor, discuss, or address airplane safety on a regular basis; (3) the board had no regular process or protocols requiring management to apprise the board of airplane safety; and (4) management saw "red, or at least yellow, flags," but that information never reached the board.[112] Here too, compliance with PPP regulations was equally "mission critical" to Kabbage—failure would result in loss of processing fees, loss of the SBA's guaranty, billions of dollars in "put-back" liability, and False Claims Act exposure—but the Board had no committee charged with PPP oversight, did not monitor, discuss, or address PPP compliance issues, and had no functioning protocols for management to apprise the Board of PPP compliance concerns.[113]

Similar to *Boeing*, the Officers here "received reports that contained what could be considered red, or at least yellow, flags," but "the board minutes of the relevant period revealed no evidence that these were disclosed to the board."[114] The court found that this fact made it "reasonable to infer the absence of a reporting system."[115] Given the number of issues that were

[111] 2021 WL 4059934, at *26.

[112] *Id.* at *27–31.

[113] Compl. ¶¶ 202–06, 317–21.

[114] *Boeing*, 2021 WL 4059934, at *31.

[115] *Id.*

not escalated to the Board—from knowledge of the SALT double counting to the A&M Report's findings—it is reasonable to infer a lack of a reporting system from management to the Board.

The parallels with *Boeing* extend further. In *Boeing*, the court emphasized the "lack of an internal reporting system by which whistleblowers and employees could bring their safety concerns to the Board's attention."[116] The court found it significant that the board received only "certain favorable information" from management and that employees who raised safety concerns had no formal channel to escalate them to the board.[117] That failure—the absence of a reliable pipeline from employees and whistleblowers to the board—was central to the court's finding. The same deficiency pervades the Complaint's allegations here.

Kabbage had no functioning mechanism for employees to bring compliance concerns to the Board's attention. When Hill raised concerns about inadequate fraud controls, she was "derided" and stripped of her title.[118] When Pietschner prepared the Kutworm Report documenting systemic compliance failures, he feared he might be fired.[119] When Habib warned about insufficient compliance staffing and fraud risk, her concerns were ignored.[120] When employees tried to escalate concerns about inaccurate borrower data, Robinson refused even to "acknowledge that us having inaccurate borrower data is even of concern."[121] Just as in *Boeing*, employees who attempted to raise compliance concerns met a dead end—confirming that Kabbage lacked any internal reporting system by which compliance concerns could reach the Board.

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[116] *Id.* at *27.

[117] *Id.* at *27, 31.

[118] Compl. ¶¶ 95, 106.

[119] *Id.* ¶¶ 189–91.

[120] *Id.* ¶¶ 97–99.

[121] *Id.* ¶ 196.

The irony of Defendants' reliance on the BSA/AML Policy's anonymous reporting provision is difficult to overstate. The Policy states that "[t]he BSA/AML Officer ensures Kabbage employees can report violations of this Policy anonymously by telephone" and that "Kabbage never tolerates retaliation of any type against an employee who reports a potential violation."[122] Yet the allegations demonstrate the precise opposite. Rather than empowering employees to report violations, Kabbage's management systematically punished those who did.

In *Marchand*, the Delaware Supreme Court reversed dismissal of a *Caremark* claim where the plaintiff alleged that Blue Bell's board failed to implement any board-level system to monitor food safety—despite food safety being "mission critical" to the company's business.[123] The court found the complaint adequately alleged *Caremark* violations where: (1) no board committee addressed the mission-critical risk; (2) there was no regular process requiring management to keep the board apprised of compliance issues; (3) the board did not receive food-safety compliance information on a regular basis; and (4) the board did not act to ensure management implemented proper monitoring systems.[124] Here, the parallels are stark, and the allegations are in many respects more egregious than in *Marchand*.

The Board never set a tone from the top that would have made any reporting mechanism effective. The Board did not have a single meeting or discussion about compliance issues between the start of the PPP and approximately one week before the program ended. This silence during a period when Kabbage processed billions of dollars in highly regulated loans demonstrates conscious disregard of oversight duties. Further, for Kabbage, approving PPP loans was akin to

[122] J.A. Ex. 35 at A00362.

[123] 212 A.3d at 809, 824.

[124] *Id.* at 822–24.

entering a new, highly regulated business. Yet the Board failed to establish a dedicated committee to monitor PPP compliance. Just as the *Marchand* court found it significant that "no board committee that addressed food safety existed,"[125] this Court should find the absence of a committee addressing PPP compliance similarly concerning.

The Directors contend that the Complaint fails to allege a "sustained and systematic failure" because Kabbage's participation in the PPP spanned only approximately six months—too "short" to establish the pattern of bad faith required under *Caremark*.[126] This argument fundamentally misapprehends both the law and the facts. Delaware law does not impose a minimum durational requirement for *Caremark* claims. The "sustained, systemic, ***or*** striking" standard describes the quality of the misconduct—whether it reflects a pattern of conscious disregard rather than an isolated lapse—not the calendar duration. Total board-level oversight abandonment throughout the entire PPP period—while processing over $7 billion in federally guaranteed loans to more than 300,000 borrowers—is "striking" and "systemic" by any measure. Indeed, because Kabbage's Board knew that the PPP was going to be a short-term program, the Board consciously chose to have Kabbage enter and exist the PPP without ever implementing any of the necessary reporting systems to allow the Board to have meaningful oversight. The Directors' oversight failure was thus "sustained." Simply put, there is no durational safe harbor.

Further, the absence of a functioning BSA/AML Officer was not a mere paperwork deficiency—it was a critical gap during the period when compliance was most critical. When Kabbage's BSA/AML Officer, Habib, resigned in early June 2020—less than two months after Kabbage began processing PPP loans—Askins assumed the role on an "interim" basis without

[125] *Id.* at 822.

[126] *See* Add'l Dir. Defs. Mot. at 24.

Board approval.[127] But this interim arrangement was a compliance fiction. As BSA/AML Officer, Askins was responsible for "[m]onitoring the effectiveness of BSA/AML compliance and taking corrective action to remedy any deficiencies found"; "[p]romptly alerting the Board to any material issues of BSA/AML non-compliance"; and "[p]roviding annual reporting to the Board on the state of BSA/AML compliance and significant emerging issues."[128] Yet Askins did none of these things. Rather, she admitted that she "focused the bulk of her time on diligence matters related to the Amex Merger" rather than compliance.[129]

Defendants cite *Stone v. Ritter*, but the facts here are the inverse. In *Stone*, the Delaware Supreme Court affirmed dismissal where the board "received and approved relevant policies and procedures, delegated to certain employees and departments the responsibility for filing SARs and monitoring compliance, and exercised oversight by relying on periodic reports from them."[130] The Kabbage Board did none of these things during the entire PPP period, other than approve an updated BSA/AML Policy during the last week of PPP lending.[131] Defendants also invoke *David B. Shaev Profit Sharing Account v. Armstrong* for the proposition that a board need only engage in "diligence, not heroism" in exercising oversight.[132] But *Shaev* is inapposite. There, the plaintiff alleged that certain directors of Citigroup breached their fiduciary duties by failing to detect and prevent fraudulent activities involving the company's relationships with Enron and WorldCom.[133] The plaintiff conceded, however, that Citigroup "had a wide range of compliance systems in

[127] Compl. ¶¶ 20, 139–40.

[128] *Id.* ¶ 85.

[129] *Id.* ¶ 11.

[130] 911 A.2d at 373.

[131] Compl. ¶¶ 202–06, 318–21.

[132] Add'l Dir. Defs. Mot. at 18 (citing 2006 WL 391931, at *6 (Del. Ch. Feb. 13, 2006)).

[133] *Shaev*, 2006 WL 391931, at *1–2.

place," and that the board "had no reason to believe that these systems were not functioning in a basic sense."[134] By contrast, Kabbage's Board failed to assure the existence of reasonable reporting systems by not establishing *any* committee or other formal mechanism to monitor PPP compliance or ask *any* questions about Kabbage's PPP lending practices, at least not until *after* the company had already approved billions of dollars in federally guaranteed loans.[135]

Defendants also rely on *In re Goldman Sachs Group, Inc. Shareholder Litigation* and *In re Citigroup Inc. Shareholder Derivative Litigation* for the proposition that a board's failure to anticipate business risks or losses does not give rise to *Caremark* liability.[136] These cases are inapposite because they concern allegations that director defendants were liable "for oversight failure relating to . . . business performance."[137] The Complaint, by contrast, alleges that the Directors are liable for oversight failures relating to Kabbage's compliance with ***legal requirements***—not for any oversight failures relating to business risk. Federal law requires PPP lenders to certify compliance with BSA/AML regulations and to implement fraud controls. Kabbage failed to comply with those regulations or implement the required controls, and the Directors failed to monitor that compliance (or lack thereof). This case is not about business

[134] *Id.* at *5.

[135] *Cf. id.* (noting such oversight failure "might take the form of facts that show the company entirely lacked an audit committee or other important supervisory structures").

[136] Add'l Dir. Defs. Mot. at 24 (citing *Goldman Sachs*, 2011 WL 4826104 (Del. Ch. Oct. 12, 2011); *Citigroup*, 964 A.2d 106 (Del. Ch. 2009)). Defendants cite these cases in a section of their brief titled, "Kabbage's Board Did Not Consciously Ignore Red Flags." Defendants apparently misunderstand that the Complaint pleads only a ***prong one*** "information systems" claim—not a ***prong two*** "red flags" claim—against the Directors (other than Frohwein, who was both a Director and an Officer).

[137] *See Goldman Sachs*, 2011 WL 4826104, at *19; *Citigroup*, 964 A.2d at 130 ("What plaintiffs are asking the Court to conclude from the presence of these 'red flags' is that the directors failed to see the extent of Citigroup's business risk and therefore made a 'wrong' business decision by allowing Citigroup to be exposed to the subprime mortgage market.").

judgment regarding risk tolerance; it is about legal compliance with mission-critical regulatory requirements.

Defendants' reliance on *Bricklayers Pension Fund of Western Pennsylvania ex rel. Centene Corporation v. Brinkley* is also misplaced. The *Bricklayers* court was concerned with whether a majority of the board knew that the company's oversight framework was inadequate.[138] The court rejected plaintiff's argument that the directors "'turned a blind eye' to problems with [the company's] reporting systems or knew that [it] effectively had no controls in place" because the committees responsible for overseeing Medicaid compliance "did real work and reported to the full Board."[139] Specifically, the court found that (1) management reported to the compliance committee quarterly; (2) the committee was actually provided with updates on the company's health plan compliance program, including updates on Medicaid contracts as well as legal and regulatory compliance; (3) "the compliance committee was expressly informed of specific measures management was taking or had taken to address each of the shortcomings identified"; and (4) the plaintiff did not plead any red flags management was aware of that did not reach the Board.[140] Thus, the court concluded the proper inference from plaintiff's allegations was that "the Board oversaw improvements to Centene's Medicaid compliance systems for as long as it was aware of the deficiencies."[141]

Here, by contrast, the Complaint alleges the Board's complete abdication of oversight responsibility: zero compliance meetings during the entire PPP period; zero reports on compliance or risk from the Chief Compliance Officer or BSA/AML Officer to the Board or any Board

[138] 2024 WL 3384823, at *14 (Del. Ch. July 12, 2024).

[139] *Id.* at *15.

[140] *Id.*

[141] *Id.*

committee; no approval of a revised BSA/AML policy to address PPP lending until one week before the PPP ended; zero questions about compliance despite processing billions in federally guaranteed loans; no dedicated committee or formal mechanism to monitor PPP compliance; and multiple examples of the Board failing to address problems—such as those identified in the A&M and Kutworm Reports—that it never heard about because of its own failure to design an actual reporting system. None of that reflects a good-faith effort "to put in place a reasonable board-level system of ***monitoring and reporting***" that would amount to anything more than a chimera.[142]

Even crediting Defendants' argument that certain pre-PPP "board-level mandatory reporting protocols" existed does not mean the Directors discharged their fiduciary obligations. Courts look beyond the mere existence of a system to some indicia of ***effectiveness*** when determining whether the required good-faith efforts were made.[143] This is not a case where a functioning system failed to detect isolated wrongdoing—it is a case where the Board utterly failed to ensure that any meaningful compliance system existed at the board level.[144]

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[142] *Marchand*, 212 A.3d at 821 (emphasis added).

[143] *See Rich ex rel. Fuqi Int'l, Inc. v. Yu Kwai Chong*, 66 A.3d 963, 982–83 (Del. Ch. 2013) (shareholder plaintiffs stated information systems claim where complaint alleged that company had no "*meaningful*" controls in place, despite existence of audit committee and independent auditor, because "the mechanisms [the company] had in place appear to have been woefully inadequate"); *Hughes*, 2020 WL 1987029, at *16 ("*Caremark* envisions some degree of board-level monitoring system, not blind deference to and complete dependence on management. The board is obligated to establish information and reporting systems that 'allow management and the board, *each within its own scope*, to reach informed judgments concerning both the corporation's compliance with law and its business performance.'" (citation omitted)).

[144] *Compare Constr. Indus. Laborers Pension Fund v. Bingle*, 2022 WL 4102492, at *12–14 (Del. Ch. Sept. 6, 2022) (holding "subpar reporting system" not indicative of bad faith where prior to cyberattack, board charged two subcommittees with cybersecurity oversight, at least one subcommittee received a management presentation on cybersecurity and held a discussion, and company itself was victim of third-party crime, not a violator of positive law), *with* Compl. ¶¶ 202, 205, 319–21 (alleging that Kabbage's Board failed to establish any formal mechanism or committee to meaningfully monitor PPP compliance, as well as failed to have any substantive discussion about PPP compliance or ask management for reports regarding Kabbage's compliance with PPP regulations).

Likewise, each Officer independently failed to discharge his or her own oversight duties. Frohwein, as CEO, and Petralia, as President, had company-wide oversight responsibility and failed to ensure any compliance information reached the Board. Both failed to implement any meaningful mechanisms of PPP loan oversight when Kabbage designed its PPP platform.[145] Frohwein actively suppressed information regarding mission-critical compliance failures, like the A&M Report, from the Board. And Petralia failed to ensure that compliance concerns raised to her, such as by the former Head of Fraud, were dealt with, and that adequate reporting systems existed between herself and her reports. As a result, critical information regarding Kabbage's PPP non-compliance, such as the Kutworm Report, stopped with her subordinates.

Askins, as General Counsel and Chief Compliance Officer, also had company-wide oversight responsibility.[146] She knew that Kabbage never remediated the "systemic gaps" in its compliance program identified by Treliant—but never flagged these compliance insufficiencies in the context of PPP to the Board. She also failed to alert the Board to the A&M Report's findings and did not seek a permanent BSA/AML Officer replacement because it would not "make a lot of sense" in light of the pending transaction.[147] Moreover, Askins served as interim BSA/AML

[145] Petralia asserted her right against self-incrimination under the Fifth Amendment when asked under oath (i) whether she "approve[d] Kabbage's fraud controls for PPP" and any changes thereto; (ii) whether she "approve[d] Kabbage's BSA/AML procedures for PPP" and any changes thereto; and (iii) whether she "approve[d] the PPP loan calculation methodology that the data strategy team developed. United States Complaint in Intervention (the "Compl. in Intervention") ¶¶ 89 & n.4, 97, *United States ex rel. Pietschner v. Petralia, et al.*, C.A. No. 4:21-cv-110 (E.D. Tex. Dec. 20, 2024), ECF No. 40. Frohwein asserted his right against self-incrimination when asked "whether he approved Kabbage's fraud controls, BSA/AML process and whether he was the person who approved any changes to those controls and procedures," and if he had "oversight of individuals responsible for development and implementation of Kabbage's PPP loan calculation methodology." *Id.* ¶¶ 85 n.3, 89, 98. *See Baxter v. Palmigiano*, 425 U.S. 308, 318 (1976) (permitting adverse inference "against parties to civil actions when they refuse to testify in response to probative evidence offered against them").

[146] Compl. ¶ 11.

[147] *Id.* ¶ 40.

Officer from June 2020 until October 2020, and thus bore direct responsibility for BSA/AML compliance during this critical period of time. Despite taking on this title however, Askins showed no apparent interest in its responsibilities.

Lastly, Robinson, as de facto Head of Fraud and Head of Risk, was directly responsible for fraud detection and risk management. Yet, he stripped the Head of Fraud of her title, limited A&M's budget to ensure an inadequate review, repeatedly downplayed reports and concerns of fraud and compliance issues, and acted as an information barrier to such concerns.[148] Indeed, Robinson acted directly contrary to his oversight duties, such as when he instructed analysts to approve obviously fraudulent loans, and thus prioritized profit over compliance with the law.

Accordingly, each Officer's failure to make a good faith effort to oversee compliance within his or her area of responsibility independently supports a *Caremark* claim.

B. The Complaint States a "Red Flags" Claim.

Under the second prong of *Caremark*, directors and officers are liable if, "having implemented such a system or controls, [they] consciously fail[] to monitor or oversee [the company's] operations thus disabling themselves from being informed of risks or problems requiring their attention."[149] Plaintiff's "red flag" claim focuses on the Officers (and Frohwein in his capacity as both director and officer).[150]

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[148] Robinson argues that the Complaint's allegation he served as an "information barrier" is conclusory. It is not. The Complaint alleges the specific conduct just described. *See* Compl. ¶¶ 95, 129. Robinson also instructed fraud analysts to approve obviously fraudulent loans. *Id.* ¶ 157. And when employees tried to escalate concerns, Robinson refused to "acknowledge that us having inaccurate borrower data is even of concern." *Id.* ¶ 196. Kabbage employees recognized that Robinson was part of a system designed to ensure that "if truth can't get in, there's no duty to report it." *Id.* These are not conclusory allegations—they are specific acts of suppression that, taken together, support the inference that Robinson deliberately prevented compliance concerns from reaching senior management and the Board.

[149] *Giuliano v. Grenfell-Gardner*, 2025 WL 2502176, at *6 (Del. Ch. Sept. 2, 2025).

[150] *Id.* at *11 ("Plaintiff adequately alleges at least a red-flags claim against Grenfell-Gardner and Richardson. Just as it is reasonably conceivable that the Board failed to receive notice of red flags, it is

An officer has a duty, when confronted with red flags, to "either address them or report upward to more senior officers or to the board."[151] The Court of Chancery recently reinforced this principle in *Giuliano*, holding that officers aware of FDA compliance violations—which were mission-critical to the company's pharmaceutical operations—could be held liable for failing to report those violations to the Board.[152] Frohwein, Petralia, Askins, and Robinson each received numerous red flags regarding Kabbage's lack of compliance with PPP regulations. Yet they did nothing to address these issues.

First, while the Treliant reports are most relevant to the information systems claim, these reports also provide context for the red flags claim. Because of these reports, Frohwein, Petralia, Askins, and Robinson were "on notice of gaps in [Kabbage's] compliance" as early as 2018, "making the later red flags [of Kabbage's PPP compliance failures] all the more consequential."[153]

Second, at the outset of the PPP, Askins and Petralia received a complaint in which Kabbage's recently-demoted Head of Fraud, Hill, sounded the alarm about inadequate fraud controls and a corporate culture that squashed attempts to flag fraud issues—with Robinson specifically mentioned as being part of Hill's concerns.[154] There is no indication of any investigation into these allegations taking place.

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reasonably conceivable that Grenfell-Gardner and Richardson were aware of the red flags and failed to report them to the Board.").

[151] *McDonald's*, 289 A.3d at 362.

[152] 2025 WL 2502176, at *11.

[153] *See Teamsters Loc. 443 Health Servs. & Ins. Plan v. Chou*, 2020 WL 5028065, at *20 (Del. Ch. Aug. 24, 2020).

[154] Petralia asserted her right against self-incrimination under the Fifth Amendment when asked whether "[Nicole Hill] told you that she was fired because she had raised these concerns about fraud at Kabbage." Compl. in Intervention ¶ 239.

Askins now argues that Hill's complaint could not have been a red flag for her because "fraud controls did not fall within her remit."[155] As an initial matter, it is a staggering assertion that the General Counsel would claim that a complaint from the just-demoted Head of Fraud warning about inadequate fraud controls and an upper management hostile to reports of fraud was not within her purview. The argument is also completely wrong. Askins was Chief Compliance Officer, and this officer has broad company-wide oversight responsibilities under *Caremark* and progeny.[156] Additionally, Askins also became the interim BSA/AML Officer in the beginning of June, a point in time in which Kabbage was approving thousands of fraudulent or otherwise ineligible loan applications—oversight of fraud controls and ensuring management properly listened to reports of fraud was certainly "within her remit" in this role.[157]

Third, Frohwein, Petralia, and Robinson each received multiple red flags regarding Kabbage's PPP platform miscalculating—and therefore incorrectly inflating—loans.[158] No proper investigation was conducted and the issues remained unfixed, resulting in tens of thousands of PPP loans issued by Kabbage being incorrectly inflated by totals in the hundreds of millions of

[155] Askins Mot. at 18.

[156] *See McDonald's*, 289 A.3d at 369 (explaining that a company's CEO and Chief Compliance Officer typically have "company-wide oversight" responsibilities).

[157] Coupled with this meritless argument, Askins puts forth a causation argument, asserting that "independent causation deficiencies defeat the Complaint's Prong Two theory against Ms. Askins." Askins Mot. at 21. First, the Complaint more than adequately alleges a sufficient casual nexus between the failure of oversight by the Directors and Officers and the corporate trauma suffered by Kabbage, beginning as early as April 2020. *See* Compl. ¶¶ 1–5, 9–12, 15–16, 18–21, 28, 31, 95, 115–17, 119, 121, 205–06, 274–88, 303–25. Mitigation of corporate trauma extends "[e]ven after the first round of PPP loans ended in August 2020," which Defendants could have accomplished by preserving significantly more cash in Kabbage, given the known and knowable massive liabilities Kabbage faced. *Id.* ¶ 322. Second, and more importantly, Delaware law is clear that "questions of causation are fact intensive and, as such, cannot be addressed at the pleading stage." *Clovis*, 2019 WL 4850188, at *15 & n.217 (holding that "at this stage, Plaintiffs' allegation that this failure of oversight caused monetary and reputational harm to the Company is sufficient to provide a causal nexus between the breach of fiduciary duty and the corporate trauma").

[158] *See* Compl. ¶¶ 115–17, 123.

dollars.[159] Defendants argue that the Officers "took steps to resolve the issue" because Frohwein responded—internally—"let's hear what he has to say" to an email warning that Kabbage's online PPP application "has a HUGE mistake in how it figures out loan amounts that is gonna get you guys in trouble."[160] But as explained in the Complaint, the Officers did not actually conduct any substantive follow-up and no investigation occurred into these miscalculation issues. As a result, the inflation issues remained unfixed.[161] Mere words without any effective follow-up actually "support[s] the inference of a bad-faith decision not to take meaningful action, not the opposite."[162]

Fourth, Frohwein, Askins, and Robinson each received the A&M Report. A&M identified multiple weaknesses in Kabbage's policies and procedures.[163] The Officers attempt to parse the language in the report and pick conclusions that favor their position. They note that A&M found that Kabbage's PPP compliance program "generally appear[ed] to be consistent with SBA" rules.[164] But they ignore the key issues, literally highlighted in red, where A&M found "Kabbage's risk management systems do not identify and appropriately control significant risks posed by the product or process; substantial gaps exist" and "[l]osses, exceptions, and ***violations of law or regulation have occurred or are imminent and either have or predictably will result in material harm to Kabbage's earnings and capital***."[165] The Officers could not just ignore the specific

[159] *Id.* ¶¶ 116, 119, 121.

[160] D&O Defs. Mot. at 41 (citing J.A. Ex. 21 at A0015–16).

[161] *See, e.g.*, Compl. ¶¶ 116, 120–22.

[162] *Los Angeles City Emps.' Ret. Sys. v. Sanford*, 352 A.3d 276, 316–18 (Del. Ch. 2026) (concluding that minimal action taken in response to red flags was effectively inaction, and explaining that "efforts to respond to red flags are not sufficient under *Caremark* when it is reasonably conceivable that those efforts were nominal, tainted by deliberate heel-dragging, and ran parallel to a campaign of concealment").

[163] Compl. ¶ 176.

[164] J.A. Ex. 30 at A00292.

[165] *Id.* at A00299 (defining "Needs Improvement').

negative findings while accepting the overall positive conclusion that Kabbage's compliance program "generally appear[ed] to be consistent with SBA" rules. Their *Caremark* duties required them to make a good-faith inquiry into the literal red flags identified by A&M.[166] Critically, had they done so, they would have uncovered even more issues, as documented in the Kutworm Report.

Further, if the A&M Report "could not plausibly constitute a red flag,"[167] as the Officers argue, then they had no reason to suppress the report. But that is exactly what they did.[168] Frohwein remarkably claims that his frustration with the A&M Report was primarily the result of confusing "color-coding."[169] But the reasonable inference here is not that a sophisticated CEO with a law degree had trouble reading the report. Rather, it is that Frohwein wanted this report buried because A&M assigned a failing grade to three different risk categories, including the significant risk that "Kabbage knew or should have known it was transmitting fraudulent information to the SBA." And as a result, Frohwein, Askins, and Robinson made sure that the A&M Report was never elevated to the Board or shared with Amex.[170]

The circumstances of this case in many ways mirror those in *Clovis Oncology*.[171] There, a biopharmaceutical company's future depended on FDA approval and getting the drug to market

[166] *See McDonald's*, 289 A.3d at 366 (explaining that "[a] critical part of an officer's job is to identify red flags, report upward, and address them if they fall within the officer's area of responsibility"); *Sanford*, 352 A.3d at 318 (Del. Ch. 2026).

[167] D&O Defs. Mot. at 39. As part of their argument, Defendants miscomprehend the relevant legal standards, claiming that warnings of "compliance risk" cannot "constitute a red flag." *Id.* at 39 n.52. Delaware courts disagree: "A red flag for *Caremark* purposes informs the fiduciary of a central compliance risk." *Sanford*, 352 A.3d at 314 (citing *Marchand*, 212 A.3d at 824; *McDonald's*, 289 A.3d at 376). Moreover, Defendants again simply ignore the A&M finding that "violations of law or regulation have occurred or are imminent." J.A. Ex. 30 at A00299, -0306–07.

[168] Compl. ¶¶ 199–200.

[169] D&O Defs. Mot. at 39–40 n.53.

[170] Compl. ¶¶ 21, 193, 199–201.

[171] 2019 WL 4850188, at *1 (Del. Ch. Oct. 1, 2019).

faster than its competitors.[172] The company chose a specific clinical drug trial protocol but, as the directors knew, regularly departed from aspects of the protocol against FDA guidance.[173] The Court held that the complaint adequately pleaded "that the Board consciously ignored red flags that revealed a mission critical failure to comply with the [clinical trial] protocol and associated FDA regulations."[174] Here too, the Officers consciously ignored evidence that Kabbage was not in compliance with PPP regulations. Also, like here, the defendants in *Clovis* groused that "FDA guidance was not as clear as the Complaint depicts."[175] But as explained by the court, what matters is what is alleged—and "[a]s pled, these regulations . . . were not nuanced."[176]

The Officers, and Robinson in particular, devote a considerable portion of their briefs to attacking the DOJ's underlying FCA case.[177] But these arguments are inappropriate for a motion to dismiss and incorrect. Nothing in the SBA guidance suggested that lenders could recklessly approve inflated and highly suspicious loans and avoid liability for doing so. In fact, the regulations state that "*[l]enders* must comply with the applicable lender obligations"—including having a functioning BSA/AML program and conducting good-faith reviews—and that lenders would only be "held harmless for *borrowers'* failure to comply with program criteria."[178]

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[172] *Id.* at *4.

[173] *Id.* at *13.

[174] *Id.* at *15.

[175] *Id.* at *14.

[176] *Id.*; *see* Compl. ¶ 80 ("[T]he SBA made clear to program participants that a lender would remain liable in circumstances where it knowingly transmits false information to the SBA.").

[177] *See, e.g.*, Robinson Mot. at 11 (arguing how "materiality is an element of FCA liability"), 17 ("The Complaint alleges in several places that this multiple device issue was suspicious. *Not necessarily*. An accountant or other service provider *could have* been filing applications for multiple clients." (emphasis added)), & 20 (arguing that the "SBA and Kabbage were in the same boat—they knew that the PPP's need for speed and reliance on borrower certifications would allow some number of fraudulent applications to get through the system. That is why the Complaint fails to allege materiality and intent under the FCA.").

[178] 85 Fed. Reg. at 20812 (emphasis added). Tellingly, the "hold harmless" language is found in the section of the regulations pertaining to borrower forgiveness, rather than underwriting. In other words, the

Moreover, the "hold harmless" and "no enforcement action" clauses apply only to actions taken by the SBA, and not by other governmental agencies like the DOJ. The DOJ investigated and sued Kabbage (and its officers) precisely because it determined that Kabbage knowingly or recklessly made false statements to the government in connection with its PPP lending.

To try to excuse Kabbage's compliance failures, Robinson misleadingly suggests that AML policies have nothing to do with the BSA or fraud detection, and that these policies solely relate to the specific crime of money laundering.[179] Not so. The BSA requires financial institutions to have an AML program, and is designed to "assess the money laundering, terrorism finance, tax evasion, and ***fraud risks*** to financial institutions, products, or services."[180] Financial institutions are required to submit SARs for dozens of types of financial crimes and suspicious activities, including consumer and commercial loan fraud.[181] By becoming a PPP lender, Kabbage agreed to comply with these requirements.[182] The DOJ alleges how Kabbage made "false records and statements" that "Kabbage would comply with PPP lender requirements, when in fact it did not, and Kabbage attested that it applied the BSA requirements of an equivalent federally regulated institution, when in fact it did not."[183]

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regulations provided that lenders were not responsible if borrowers did not abide by program requirements and thus failed to qualify for loan forgiveness. *See id.* at 20815 ("Can lenders rely on borrower documentation for loan forgiveness? Yes. The lender does not need to conduct any verification if the borrower submits documentation supporting its request for loan forgiveness and attests that it has accurately verified the payments for eligible costs. The Administrator will hold harmless any lender that relies on such borrower documents and attestation from a borrower.").

[179] Robinson Mot. at 7–12.

[180] 31 U.S.C. § 5311(4) (emphasis added).

[181] *See* FinCEN Suspicious Activity Reporting (SAR) Filing Instructions at 32–42, *available at* https://bsaefiling.fincen.gov/resources/FinCENSARFilingInstructions.pdf.

[182] 85 Fed. Reg. at 20815 ("[PPP lenders] will also generally have to identify and report certain suspicious activity to the U.S. Department of Treasury's Financial Crimes Enforcement Network (FinCEN).").

[183] *See, e.g.*, Compl. in Intervention ¶ 341.

The remainder of the Officers' arguments are unsupported contentions about their alleged good faith that are contrary to the Complaint's allegations.[184] But this is not the juncture to debate whether, for instance, they actually relied, in good faith, on the non-existent opinion of some unidentified counsel, or their claim that the SALT error was an "innocent mistake."[185]

C. Substantial Personal Payouts to the Officers and to the Directors' Affiliated Funds Support a Bad-Faith Inference.

The Directors and Officers were personally incentivized to close the Amex Merger quickly and to avoid asking hard questions about compliance issues that might delay or derail the transaction. The *Boeing* court, in denying the motion to dismiss the *Caremark* claim, emphasized that the Board had shifted Boeing's mission from safety to profits and rapid production.[186] The Board here similarly prioritized profits over legal compliance. The Directors had a separate financial incentive to turn a blind eye to PPP regulatory issues: they could pump up PPP fees and then, pursuant to the planned Merger, quickly extract those funds for themselves and their Kabbage-shareholder affiliates.

The conduct here contains echoes of *In re Massey Energy Co.*, where fiduciaries prioritized profits over legal compliance.[187] As the *Massey* court recognized, corporate management are often incentivized to maximize profits while externalizing the risk of their operations onto others, notwithstanding laws designed to prevent such conduct.[188] Here, the Directors and Officers were highly incentivized to prioritize profits over legal compliance because "[t]he more [PPP] fees

[184] *See e.g.,* Robinson Mot. at 20–26; D&O Defs. Mot. at 33–34.

[185] *E.g.*, Robinson Mot. at 20–26.

[186] 2021 WL 4059934, at *3 ("Rather than prioritizing safety, Defendants lent their oversight authority to Boeing's agenda of rapid production and profit maximization.").

[187] 2011 WL 2176479, at *18–21 (Del. Ch. May 31, 2011).

[188] *Id.* at *29 n.185.

Kabbage earned, the more that [the Directors] and their shareholders would receive as part of the anticipated Amex Merger."[189]

Also insightful is *Walton*, in which plaintiffs brought *Caremark* claims against Walmart's directors and officers for Walmart's role in the opioid crisis.[190] Central to the court's decision to deny a motion to dismiss were the repeated examples of Walmart's directors and officers prioritizing profits over legal compliance.[191]

In the present case, the Directors and Officers "were focused on short-term profits that would assist" with closing the Amex Merger, and "neither set of Kabbage's fiduciaries was concerned about the fallout from Kabbage's lax compliance program and flagrant violations of the law."[192] Instead, as made clear by Frohwein, the priority was to "ISSUE ISSUE" more PPP loans, and Kabbage's compliance issues were downplayed, denied, and often just ignored.[193]

II. The Complaint Separately States a Duty-of-Care Claim Against the Officers.

The Officers argue that Kabbage's duty-of-care claims are merely "repackaged" *Caremark* allegations. This argument misunderstands Delaware law. While a claim based on passive oversight might not state a duty-of-care violation,[194] the duty-of-care claims here rest on affirmative, grossly negligent acts that extend well beyond the oversight context.

First, Askins signed SBA Form 3507, certifying that Kabbage had a BSA/AML compliance program "equivalent to that of a comparable federally regulated institution" when she knew or

[189] Compl. ¶¶ 309–11, 323–24.

[190] *Ontario Provincial Council of Carpenters' Pension Tr. Fund v. Walton*, 2023 WL 3093500, at *1 (Del. Ch. Apr. 26, 2023).

[191] *See, e.g.*, *id.* at *43 ("The extent of the pleading-stage record on this subject and the involvement of the directors supports an inference that they knew Walmart was sacrificing compliance for profits.").

[192] Compl. ¶¶ 5, 7, 123–25.

[193] *Id.* ¶ 125.

[194] *McDonald's*, 289 A.3d at 373–75.

should have known this certification was false.[195] This was grossly negligent. Askins argues that her certification was qualified by the phrase "to the best of my knowledge" and therefore cannot support a claim.[196] But the Complaint alleges that Askins knew that the 2019 Treliant Report found that Kabbage's BSA/AML program was "an important weakness that require[d] prioritization."[197] A certification of compliance made despite known systemic deficiencies is not a "good faith" statement of belief—it is a reckless disregard of known facts.

Frohwein, Petralia, and Robinson, though they did not physically sign the certification, participated in the collective decision to pursue PPP lending despite known compliance gaps. In particular, Robinson, as the officer responsible for fraud detection and risk management, knew better than anyone that Kabbage's controls were inadequate—yet raised no objection to Kabbage applying to become a PPP lender.[198]

Second, and more importantly, the Officers' decision to transfer $120 million in cash to Amex Kabbage while leaving only $17 million behind, knowing this was grossly insufficient to cover foreseeable liabilities, was an affirmative operational decision. The Officers controlled every variable: they selected the solvency firm Duff & Phelps (after Houlihan Lokey declined due to the "massive assumptions" Kabbage demanded), dictated the unreasonable assumptions Duff & Phelps would use, and determined how much cash to retain. At every juncture, the Officers chose the option that maximized shareholder payouts at the expense of Kabbage and its residual claimants.[199] Each Officer never explained to Kabbage's CFO, who was working the most closely

[195] Compl. ¶¶ 100, 123–25, 294.

[196] Askins Mot. at 25–26.

[197] Compl. ¶¶ 19–20, 87–93.

[198] *Id.* ¶¶ 147–57, 196, 210, 221–22, 295.

[199] *Id.* ¶ 31.

with Duff & Phelps, the specific PPP issues of which he or she was aware—from the SALT issue, to the red flags in the A&M Report, to their recognition in response to subpoenas and news reports "that seems like we let stuff through" (which is exactly what Robinson instructed Kabbage to do). The "sensitivity case" in the Solvency Opinion literally assumed a scenario in which Kabbage would be liable for "improper document review," and yet none of the Officers provided any advice to Kabbage's CFO regarding the known extent of that issue. Accordingly, the Court can easily reject, for instance, Askins' argument that she "made sure that the decision maker with respect to setting the reserve had the relevant information before finalizing that amount."[200]

This was not a business judgment call where reasonable minds might differ—it was a deliberate decision to ignore the litigation risk the Officers knew or should have known was looming because of Kabbage's failure to detect significant amounts of fraud.[201] The inadequacy of Kabbage's cash retention was so obvious that it became a running joke. Goodwin attorneys—Kabbage's outside counsel—joked on October 15, 2020, that Duff & Phelps was "dumb for issuing the solvency opinion."[202] When your own lawyers joke that your solvency opinion is indefensible, proceeding with the transaction is the epitome of gross negligence.

III. The Complaint Adequately Pleads Claims for Both Actual and Constructive Fraudulent Transfer.

A. The Pleaded Facts Support a Claim for Actual Fraudulent Transfer.

The Complaint more than sufficiently pleads an actual fraudulent transfer because it details how the Officers and Directors deliberately structured the Amex Merger to strip Kabbage of

[200] Askins Mot. at 10.

[201] Compl. ¶ 245.

[202] *Id.* ¶ 272.

substantially all its assets, including $120 million in cash earned through the PPP, while leaving only $17 million to cover known and objectively foreseeable liabilities.

An actual fraudulent transfer is a transfer made "with actual intent to hinder, delay, or defraud any" creditor.[203] The statutory language is disjunctive: any one of these intents is independently sufficient to render the transfer avoidable.[204] Courts have consistently held that a general intent to place assets beyond the reach of creditors—even without targeting a particular creditor—satisfies the statute.[205] Here, even if the Directors and Officers were unaware of exactly how Kabbage might be burdened with claims, the pleaded facts show they had the intent to place assets beyond the reach of the very class of creditors—the DOJ and SBA—that ultimately did bring claims. This is all that is required to sustain an actual intent claim at the pleading stage.

Defendants' primary retort is that actual fraudulent intent must be established for a majority of the Board who approved the transaction.[206] But this argument fails for several reasons. First, as explained herein, the Officers deliberately concealed compliance failures and other material information from the Board to prevent it from learning facts that might jeopardize the Merger. Because they concealed material information from the Board, their intent is properly imputed to

[203] 11 U.S.C. § 548(a)(1)(A).

[204] *See Wiggains v. Reed (In re Wiggains)*, 848 F.3d 655, 661 (5th Cir. 2017) (holding that the statutory phrase "hinder, delay, or defraud" is "stated in the disjunctive, which signifies that an intent to hinder or to delay or to defraud is sufficient"); *Drivetrain, LLC v. DDE Partners, LLC (In re Cyber Litig. Inc.)*, 2023 WL 6938144, at *7 (Bankr. D. Del. Oct. 19, 2023) (same).

[205] *Christian Bros. High School Endowment v. Bayou No Leverage Fund, LLC* **(***In re Bayou Grp., LLC)*, 439 B.R. 284, 304 (S.D.N.Y. 2010) (holding that "intent 'to hinder, delay, or defraud' creditors need not target any particular entity or individual as long as the intent is generally directed toward present or future creditors of the debtor"); *Faulkner v. Kornman (In re The Heritage Org., L.L.C.)*, 413 B.R. 438, 468 (Bankr. N.D. Tex. 2009) ("[I]f each of the Transfers was made by Heritage with the actual intent to hinder, delay or defraud *any* Heritage creditor, irrespective of whether that creditor can serve as a triggering creditor, the Transfer(s) is avoidable under TUFTA by the Trustee.").

[206] Certain Defs. Mot. at 18–20.

the corporation for fraudulent transfer purposes.[207] Second, the Officers determined how much cash to retain at Kabbage and selected and instructed Duff & Phelps on the solvency opinion assumptions. If the Officers had instructed Duff & Phelps to include more reserves for contingent liabilities, then the amount of the Fraudulent Transfer would have been reduced. Simply put, while the Board approved the Solvency Opinion, that opinion was based on faulty instructions from the Officers, making the Officers' intent relevant to the Fraudulent Transfer. Third, even assuming Board-level intent was required, a majority of the Board members had the requisite intent. Each outside Director (except Hodrick) was a designee of a major shareholder fund that received tens of millions of dollars from the merger, creating direct financial incentives to close the deal while ignoring known and knowable liabilities at Kabbage.[208]

The Directors and Officers knew Amex did not want the PPP portfolio because it was "very worried about legal liability" and specifically concerned about "liability flowing from fraudulent applicants, anything that would give the government, applicants and others suing them."[209] Multiple aspects of the Merger Agreement were designed to shield Amex from such liabilities. And, likewise, this recognition of PPP liabilities was why one of the major Shareholders "wanted nothing to do with ownership interest in the legacy Kabbage entity after the deal."[210] Yet the

[207] *See Cyber Litig*, 2023 WL 6938144, at *2 ("[W]hen Person A controls Person B, Person A's intent may be imputed to Person B. And there can be no stronger case for the application of that principle than where Person A tricked or deceived Person B into voting in favor of a transaction.").

[208] Indeed, even after receiving Duff & Phelps' solvency opinion on August 11, 2020—which set out management's extraordinary assumptions in plain terms, including only $1 million reserved for litigation costs—the Board never once followed up on those assumptions between August and October, despite a flood of DOJ subpoenas, bad press, and mounting evidence that Kabbage's PPP liabilities would dwarf the reserve. Compl. ¶¶ 246–48, 256–69, 271, 322. The Directors "failed to question the basis for that minimal reserve—and ask how much should reasonably be reserved—because they did not want an answer that would lead to Kabbage having to retain more of its cash." *Id.* ¶ 322. This deliberate refusal to revisit plainly inadequate assumptions is itself powerful evidence of intent to place assets beyond creditors' reach.

[209] *Id.* ¶ 227.

[210] *Id.* ¶ 228.

Directors and Officers facilitated and approved the solvency opinion knowing that it essentially ***assumed zero risk to Kabbage*** of liability flowing from fraudulent applications. The reasonable inference to draw from this conduct is that the Directors and Officers intended to extract as much cash as possible from Kabbage with little to no regard for the liabilities Kabbage faced. There is no other reasonable way to interpret Frohwein's statement that orphaning the PPP liabilities at a shell entity would "mitigate [the] risk of law suites [sic] around PPP."[211]

This case stands in stark contrast to the facts of *In re Tribune* and *In re Pack Liquidating*.[212] In *Tribune*, the Second Circuit declined to impute fraudulent intent to the debtor because the challenged transaction was approved by a fully functioning special committee of independent directors who, with the help of financial advisors, "checked" the relevant information provided to them and reached an informed decision.[213] In *Pack Liquidating,* the court rejected plaintiff's claim because it alleged only that one director acted with fraudulent intent and did not allege that his "individual intent drove the board's decisions."[214] Unlike the facts of those cases, the Complaint alleges that the CEO and other senior officers acted with fraudulent intent and actively suppressed material information to prevent the Board from making an informed decision.

In addition to this direct evidence of fraudulent intent, courts have long held that "[b]ecause proof of actual intent to hinder, delay or defraud creditors may rarely be established by direct evidence, courts infer fraudulent intent from the circumstances surrounding the transfer."[215] The

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[211] *Id.* ¶ 213.

[212] *Kirschner v. Large S'holders* (*In re Tribune Co. Fraudulent Conv. Litig.)*, 10 F.4th 147 (2d Cir. 2021); *Off. Comm. of Unsecured Creditors of Pack Liquidating, LLC v. Vagenas (In re Pack Liquidating, LLC)*, 2025 WL 2587577 (Bankr. D. Del. Sept. 5, 2025).

[213] *Tribune*, 10 F.4th at 161.

[214] *Pack Liquidating*, 2025 WL 2587577 at *7.

[215] *Brown v. Third Nat'l Bank (In re Sherman)*, 67 F.3d 1348, 1353 (8th Cir. 1995); *JLL Consultants, Inc. v. Gothner* (*In re AgFeed USA, LLC)*, 546 B.R. 318, 335 (Bankr. D. Del. 2016) ("Because direct evidence

Complaint alleges numerous "badges of fraud" supporting an inference of fraudulent intent,[216] including: (1) the transfer rendered Kabbage insolvent; (2) Kabbage received no consideration for the transfer; (3) the transfer comprised substantially all of Kabbage's assets; (4) the transfer was made to an insider (Amex Kabbage, Kabbage's sole shareholder at the time) and for the benefit of insiders (Amex Kabbage's shareholders, the former shareholders of Kabbage itself); (5) Kabbage retained insufficient assets to meet known and knowable liabilities; and (6) Kabbage made the transfer shortly after incurring massive liabilities.[217] These badges demonstrate that Kabbage's insiders deliberately structured a transaction to strip the company of its assets while leaving it saddled with known liabilities—the epitome of actual fraudulent intent.[218]

Defendants argue that the transfer was made pursuant to a valid contractual obligation (the Merger Agreement) and therefore cannot be fraudulent.[219] But a debtor can enter into a contract with the intent to use that contract as a vehicle for defrauding creditors. The Complaint alleges that the Officers and Directors structured the Merger to strip Kabbage of its assets while leaving it

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of fraudulent intent is often unavailable, courts usually rely on circumstantial evidence to infer fraudulent intent. In doing so, courts look to common law and statutory badges of fraud." (internal citations omitted)).

[216] *See AgFeed USA*, 546 B.R. at 335 ("The 'badges of fraud' that courts often refer to include, but are not limited to: (1) the relationship between the debtor and the transferee; (2) consideration for the conveyance; (3) insolvency or indebtedness of the debtors; (4) how much of the debtor's estate was transferred; (5) reservation of benefits, control or dominion by the debtor over the property transferred; and (6) secrecy or concealment of the transaction."); Ga. Code Ann. § 18-2-74(b) (listing badges of fraud).

[217] Compl. ¶¶ 252–54, 270–73, 275–77, 299–300, 331.

[218] *See Maxus Liquidating Tr. v. YPF S.A. (In re Maxus Energy Corp.)*, 641 B.R. 467, 514 (Bankr. D. Del. 2022) ("[I]t is the confluence of several [badges] in one transaction [that] generally provides conclusive evidence of an actual intent to defraud." (internal quotations omitted)); *AgFeed USA*, 546 B.R. at 335 (same). Defendants argue that the court may consider the implications of the absence of certain badges of fraud in evaluating the totality of the circumstances of the transfers. But, here, the totality of the circumstances cannot be judged on a motion to dismiss. Further, the case cited by Defendants held that "the absence of *several very significant badges* of wrongful intent may disprove actual intent to hinder, delay or defraud." *Adamson v. Bernier* (*In re Bernier)*, 282 B.R. 773, 782 (Bankr. D. Del. 2002) (emphasis added). But here, the significant badges of fraud are present.

[219] D&O Defs. Mot. at 51–55.

saddled with liabilities they knew could be massive—all while extracting hundreds of millions of dollars for themselves and their affiliated shareholders.

Moreover, contrary to Defendants' arguments, Kabbage did not satisfy an "antecedent debt" when it made the Fraudulent Transfer. "[A] contingent contractual obligation does not give rise to an 'antecedent debt' that is 'incurred' or 'owed' unless and until the payment obligations are actually triggered."[220] The Fraudulent Transfer was made pursuant to a contingent obligation under the Merger Agreement that did not crystallize until numerous other conditions were satisfied (some of which, in reality, were not, because Kabbage was insolvent).[221] In addition, the Merger Agreement was not an "antecedent debt" at the time because provided it could be terminated.[222]

The Merger Agreement also did not require Kabbage to transfer $120 million in cash through the Merger. To the contrary, it required Kabbage to be solvent as of closing, which meant that Kabbage needed to determine, in good faith, how much cash to leave with the legacy company.[223] This makes Defendants' reliance on the Merger Agreement particularly unavailing. Kabbage did not obtain the Solvency Opinion in good faith. Rather, Defendants manipulated the

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[220] *Piazza v. Pac. Maritime Indus. Corp. (In re George G. Sharp, Inc.)*, 2022 WL 1714178, at *10 (Bankr. S.D.N.Y. May 25, 2022) (citing *In re Trib. Co. Fraudulent Conv. Litig.*, 10 F.4th 147, 173 (2d Cir. 2021)).

[221] J.A. Ex. 42 (Merger Agreement) at A00509 (closing conditions include, *inter alia*, accuracy of representations and warranties "on and as of the Closing," § 6.3(a)). One of those representations was that Kabbage "at and immediately after the Effective Time (after giving effect to the Transactions . . .), will be, Solvent." *Id.* at –00482 (§ 2.28).

[222] *Id.* at A00512 (§ 7.1(a)).

[223] *Id.* at A00582 (§ 2.28) ("After giving effect to the Transactions (including the Merger and the Reorganization), at and immediately after the Effective Time, the Legacy Company, will have sufficient cash on hand and working capital, in an amount *equal to or greater than the Retained Cash*, to service the Retained Loan Assets and *to satisfy its obligations* under any of its retained Contracts or Liabilities to third-parties that are known by the Company or are *reasonably likely to exist*." (emphasis added)); *see also id.* at –00550 (definition of "Merger Consideration") ("Merger Consideration" means $625 million in cash less (i) all Unpaid Transaction Expenses, plus (ii) the Tax Opinion Credit, less (iii) the Closing Net Working Capital Shortfall, if any, plus (iv) the Closing Net Working Capital Surplus, if any, less (v) the aggregate amount of Target Company Debt, plus (vi) the *Target Company Cash, if any*." (emphasis added)).

Solvency Opinion to facilitate the Fraudulent Transfer so that they could extract more cash for themselves. It would be absurd to find that the Defendants are protected from fraudulent transfer liability based on Kabbage's breaches of the Merger Agreement, especially when those breaches are what helped facilitate the Fraudulent Transfer and increased cash payments to the Shareholders that they never should have received.

B. The Pleaded Facts Support a Claim for Constructive Fraudulent Transfer.

A constructive fraudulent transfer is a transfer made for less than reasonably equivalent value when the debtor was insolvent or became insolvent as a result.[224] The Complaint alleges that Kabbage received no value for the Fraudulent Transfer—the assets were transferred to Amex Kabbage, and the merger consideration was paid to the Shareholders, not to Kabbage.[225] The transfer rendered Kabbage insolvent because, as of the transfer date, Kabbage's liabilities (including its massive liabilities to the DOJ and SBA) exceeded the fair value of its assets.[226]

1. The Fraudulent Transfer rendered Kabbage insolvent.

Defendants rely on the Solvency Opinion to support their argument that Kabbage was solvent. But as alleged in the Complaint, the critical flaw in the Solvency Opinion is its assumption that Kabbage's PPP-related exposure was limited to approximately $2 million.[227] This figure was divorced from economic reality. First, regarding legal expenses, Kabbage was already subject to what one employee called a "subpoena tornado" relating to fraudulent borrowers.[228] Just responding to those subpoenas would likely consume much of Kabbage's $1 million legal reserve.

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[224] 11 U.S.C. § 548(a)(1)(B).

[225] Compl. ¶¶ 251–54, 270, 332–33.

[226] *Id.* ¶¶ 270–72, 274–88.

[227] *Id.* ¶¶ 29–30, 246–248, 270–72.

[228] *Id.* ¶ 257.

More importantly, it was foreseeable that the government would, at the very least, investigate whether Kabbage had submitted false claims to the SBA. The cost of an FCA investigation—even leaving aside questions of liability—would easily exceed $1 million.[229]

Second, a reserve of only $1 million for contractual "put-back liability" was not reasonable.[230] The mathematical implausibility is staggering: an approximately $1 million reserve on a $7 billion portfolio assumes only 0.014% of loans would result in put-back liability. Given the inflated loans and systemic compliance failures documented in the A&M and Kutworm Reports—and in multiple emails and Slack messages—known to the Officers before the Solvency Opinion issued, substantial put-back liability was not merely foreseeable but virtually certain.

Kabbage's actual liabilities proved orders of magnitude higher than $2 million. The DOJ and SBA settlements alone totaled approximately $212 million.[231] Caselaw holds that when a legal liability was contingent or disputed at the time of the fraudulent transfer but is later set by settlement or judgment before the court's insolvency determination, a court may permissibly use the settlement or judgment amount in valuing the liability at the time of the transfers.[232] The

[229] *See id*. ¶ 245 (alleging that the "historical benchmark" of $1 million in yearly legal expenses just for "defense costs" "pre-dated the PPP, where Kabbage originated nearly as much loan value in six months as the company had underwritten in its entire history before the PPP combined").

[230] Under its contracts with its lending partners, Kabbage was obligated to repurchase any PPP loan for which the SBA denied forgiveness or a guaranty due to non-compliance. The same exposure applied to PPP Liquidity Facility loans. Compl. ¶¶ 102–04. The Solvency Opinion reserved only $1.058 for "put-back" liability and assumed that a "percentage of [PPP] loans [are] projected to be 'put-back' as a result of improper document review, or as a result of a change to the SBA's view on 'Safe Harbor.'" Pl.'s App'x Ex. E at B000048 (Duff & Phelps Oct. 15, 2020 Analysis). This statement suggests management subsumed Kabbage's direct liability to the SBA—*i.e.*, the risk that the SBA would claw back forgiveness and guaranty payments on fraudulent or inflated loans—within its definition of "put-back" liability, making the miniscule reserve even more inadequate. If instead management treated "put-back" liability as limited to Kabbage's contractual repurchase obligations, the result is no better: management reserved nothing at all for what ultimately became a $720 million proof of claim. Compl. ¶ 282.

[231] Compl. ¶¶ 285–87.

[232] *See Canney v. Fisher & Strattner, LLC (In re Turner & Cook, Inc.)*, 507 B.R. 101, 109 (Bankr. D. Vt. 2014) ("In determining the proper amount of disputed or contingent liabilities to include in the insolvency calculation, courts should generally value contingent liabilities based upon the probability of the occurrence

settlement amounts thus constitute probative evidence of Kabbage's liabilities at the time of the Fraudulent Transfer, especially on a motion to dismiss.

Defendants invoke *In re R.M.L., Inc.* for the proposition that solvency must be assessed based on "the circumstances as they appeared to the debtor."[233] But *In re R.M.L.* has no application here. As the Delaware bankruptcy court explained in *In Re W.R. Grace & Co.*, the *R.M.L* case does not apply to tort and regulatory claims because such claims are not contingent on a "future event" in the relevant sense.[234] The distinction is critical. Although legal liabilities are often called "contingent liabilities" in common parlance, such liabilities are better characterized as disputed liabilities. This is because a contingent claim is one "which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event," and whether a plaintiff asserts a claim or is successful on a claim against a debtor are not extrinsic events.[235] Kabbage's liabilities arose from conduct that had already occurred—its submission of false claims to the SBA. As the *W.R. Grace* court observed: "To say that the act of making the claim was the extrinsic event stretches the meaning of that phrase too far; the formal claim is not extrinsic to the underlying liability, nor is it an event creating liability where none existed before."[236]

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of the liability. When a liability was contingent at the time of the challenged transfers but is reduced to judgment before the court's insolvency determination, however, a court may permissibly use the judgment amount in valuing the contingent liability at the time of the transfers." (internal citations omitted)); *SEC v. Antar*, 120 F. Supp. 2d 431, 443 (D.N.J. 2000), *aff'd*, 44 F. App'x 548 (3d Cir. 2002) ("It is now clear that the value of the SEC's unliquidated claim against Sam M. was, and is, approximately $15 million."); *Off. Comm. of Asbestos Pers. Inj. Claimants v. Sealed Air Corp. (In re W.R. Grace & Co.)*, 281 B.R. 852, 869 (Bankr. D. Del. 2002) (summarizing the "governing principle" that courts "may consider information originating subsequent to the transfer date if it tends to shed light on a fair and accurate assessment of the asset or liability as of the pertinent date" (quotations and citation omitted)).

[233] *See Mellon Bank, N.A. v. Off. Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.)*, 92 F.3d 139, 156 (3d Cir. 1996).

[234] *See W.R. Grace*, 281 B.R. at 862–63.

[235] *Id.*

[236] *Id.* at 863.

Under the Bankruptcy Code, a "claim" encompasses any "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."[237] A claim based on tort or regulatory liability arises when the underlying wrong is committed, not when litigation commences. Kabbage's liabilities to the DOJ, SBA, and lending partners existed as of October 13, 2020.[238] Even if the final settlement amounts of these claims are not evidence of their discounted amounts at the time of the Fraudulent Transfer, even recognizing the liabilities at fractions of their asserted amounts renders Kabbage woefully insolvent.

On August 11, 2020, the Board received a presentation from Duff & Phelps showing Kabbage solvent ***by less than $1 million***:

Balance Sheet Test
($ in thousands)

Cash (1)	$15,850.0
Contractual Servicing Obligation (2)	($15,046.5)
Potential Reimbursement of Launch Support if Mastercard Terminates Co-Brand Agreement (3)	($300.0)
Additional Contingent and Other Liabilities (3)	$0.0
Net Asset Value - Kabbage, LLC	**$503.5**

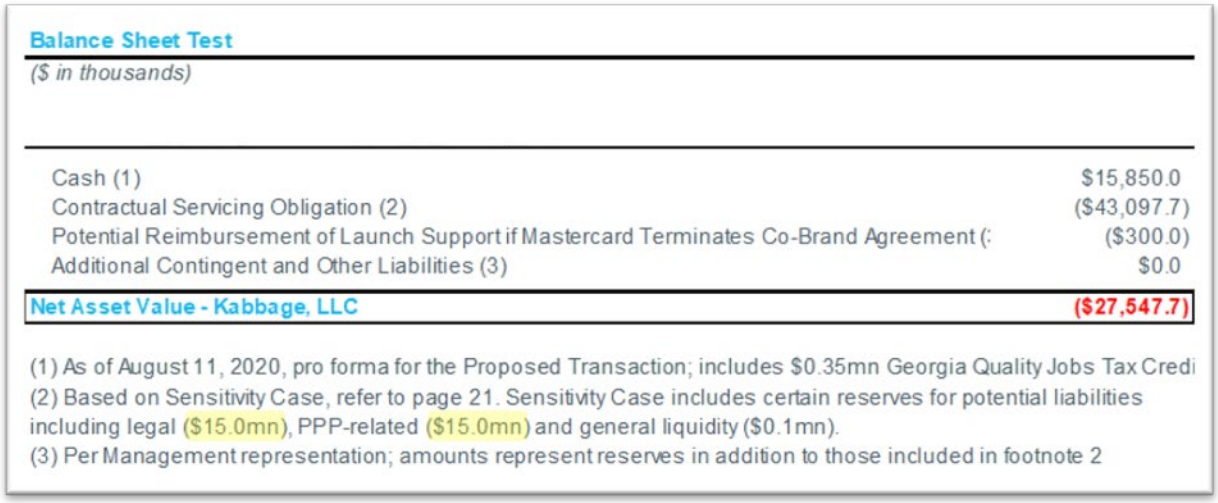
(1) As of August 11, 2020, pro forma for the Proposed Transaction; includes $0.35mn Georgia Quality Jobs Tax Credit
(2) Based on Sensitivity Case, refer to page 21. Sensitivity Case includes certain reserves for potential liabilities including legal ($1.0mn), PPP-related ($0.95mn) and general liquidity ($0.1mn).
(3) Per Management representation; amounts represent reserves in addition to those included in footnote 2

As set forth in the footnotes to this "balance sheet test," the total estimated PPP-related liabilities were less than $2 million, even assuming all "legal" liabilities would relate to the PPP. Because

[237] 11 U.S.C. § 101(5)(A).

[238] *See Bayou Grp.*, 439 B.R. at 335 ("[I]n tort cases[,] the relationship of debtor and creditor arises the moment the cause of action accrues."); *Antar*, 120 F. Supp. 2d at 443 ("Because the SEC's claim was based on Sam M.'s securities fraud in the 1980s, Sam M. possessed this debt at the time of all of the 1991 and 1997 transfers."); *W.R. Grace*, 281 B.R. at 862–63; *see also Turner & Cook*, 507 B.R. at 109; *Drenis v. Haligiannis*, 452 F. Supp. 2d 418, 428 (S.D.N.Y. 2006); *Mansfield v. Pierce*, 153 F.3d 721 (4th Cir. 1998); *Indiana Bell Tel. Co., Inc. v. Lovelady*, 2008 WL 11408781, at *5 (W.D. Tex. Mar. 5, 2008).

Kabbage's margin for remaining solvent was so thin, even a modest change in the assumptions regarding Kabbage's PPP liabilities would render Kabbage insolvent.[239] For instance, if legal and PPP put-back liabilities were each increased to $15 million, Kabbage would be balance-sheet insolvent by nearly $28 million, as shown below:



Balance Sheet Test

($ in thousands)

Cash (1)	$15,850.0
Contractual Servicing Obligation (2)	($43,097.7)
Potential Reimbursement of Launch Support if Mastercard Terminates Co-Brand Agreement (:	($300.0)
Additional Contingent and Other Liabilities (3)	$0.0
Net Asset Value - Kabbage, LLC	**($27,547.7)**

(1) As of August 11, 2020, pro forma for the Proposed Transaction; includes $0.35mn Georgia Quality Jobs Tax Credi
(2) Based on Sensitivity Case, refer to page 21. Sensitivity Case includes certain reserves for potential liabilities including legal ($15.0mn), PPP-related ($15.0mn) and general liquidity ($0.1mn).
(3) Per Management representation; amounts represent reserves in addition to those included in footnote 2

Duff & Phelps's bring-down opinion changed little from August 2020. According to that analysis, Kabbage was balance-sheet solvent by only approximately $3 million.[240]

Defendants argue that Kabbage's post-transaction operations, including nearly two years of continued business and $65 million in revenue, undermine the insolvency allegations.[241] But,

[239] Defendants contend the Complaint lacks allegations about the value of assets remaining at Kabbage following the Fraudulent Transfer, relying on *Jalbert v. Souza (In re F-Squared Inv. Mgmt., LLC)*, 2019 WL 4261168 (Bankr. D. Del. Sept. 6, 2019). Unlike in *F-Squared*, the Complaint specifically pleads how Kabbage was insolvent, and the documents incorporated by reference, including the Solvency Opinion, further show that Kabbage needed $17 million in cash just to cover the liabilities related to normal servicing costs. Compl. ¶¶ 242–43, 270–71. And, as set forth herein, just small changes to the Solvency Opinion prove that Kabbage was balance-sheet insolvent.

[240] Pl.'s App'x Ex. E at B000043 (Duff & Phelps Oct. 15, 2020 Analysis). While the October 15 bring-down analysis presented the value of Kabbage's assets in more detail than the August presentation, footnote two continued to represent that the "Sensitivity Case include[d] certain reserves for potential liabilities including legal ($1.0mn), [and] PPP-related ($0.95mn)[.]" The Bringdown Sensitivity Case Summary in the presentation actually reflected a minor increase in the PPP Put Back amount to $1.058 million. *Id.* at B000049.

[241] Certain Defs. Mot. at 33 n.24.

as alleged in the Complaint, Kabbage survived only because of the second round of PPP lending in 2021, an unknown lifeline at the time of the merger.[242] That Kabbage required a federal emergency program to delay bankruptcy confirms—rather than negates—that the Fraudulent Transfer rendered Kabbage insolvent and left it with unreasonably small capital.

2. Kabbage received no value, much less reasonably equivalent value, from the Fraudulent Transfer.

Defendants recognize that dividends and LLC distributions, like the Fraudulent Transfer, provide no value to the entity that makes them: they are a one-way transfer of value. Defendants thus argue that Kabbage received "reasonably equivalent value" by satisfying its contractual obligations under the Merger Agreement. But Kabbage had the obligation to deliver a Solvency Opinion at closing. Had it been unable to do so—as it would have been had it appropriately accounted for its PPP-related liabilities—Amex would not have had to close on the Merger. There is no allegation or reason to believe that Amex would have waived this condition. It is nonsensical for Defendants to argue that Kabbage received "value" by delivering a bogus Solvency Opinion that enabled Defendants to extract more cash from Kabbage than they otherwise would have.

In sum, the Complaint adequately pleads a claim for constructive fraudulent transfer. Kabbage received no value for the Fraudulent Transfer; its contingent liabilities vastly exceeded the $1 million assumed in the solvency opinion; and the transfer rendered Kabbage insolvent or left it with unreasonably small capital. The Solvency Opinion is no shield at the pleading stage.

IV. The Complaint States Viable Claims for Recovery of the Fraudulent Transfer under Section 550.

The Shareholders argue that the Complaint fails to state a claim for recovery because they were neither initial nor subsequent transferees and the Complaint does not plead grounds for veil

[242] Compl. ¶ 278–79.

piercing. These arguments misapprehend section 550's purpose—which grants bankruptcy trustees broad power to recover fraudulent transfers from entities who benefited from, but did not receive, the transfer—and ignore the facts demonstrating the Merger was an integrated transaction that delivered direct, quantifiable, and accessible benefits to the Shareholders.

A. Section 550's Text and Purpose Support Recovery from the Shareholders.

Section 550(a)(1) permits recovery not only from the "initial transferee" but also from the "entity for whose benefit such transfer was made."[243] This "transfer beneficiary" liability reflects Congress's recognition that fraudulent transfers can benefit parties other than those who actually receive the debtor's property.[244] While the paradigmatic example of a transfer beneficiary is a guarantor, courts do not narrowly construe the statutory language.[245] Instead, courts have articulated a three-part test for transfer-beneficiary liability: the benefit must be (1) actually received, (2) quantifiable, and (3) accessible.[246] The Complaint satisfies each element.

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[243] 11 U.S.C. § 550(a)(1).

[244] *See Bonded Fin. Servs., Inc. v. European Am. Bank*, 838 F.2d 890, 895–96 (7th Cir. 1988) (noting that the structure of the Code "distinguishes transferees (those who receive the money or other property) from entities that get a benefit because someone else received the money or property").

[245] *See Henry v. Off. Comm. of Unsecured Creditors of Walldesign, Inc. (In re Walldesign, Inc.)*, 872 F.3d 954, 966–68 (9th Cir. 2017) (holding that a principal who directs a fraudulent transfer for personal gain is "the entity for whose benefit" the transfer was made under § 550(a)(1), even without receiving the transferred property directly); *Senior Transeastern Lenders v. Off. Comm. of Unsecured Creditors* (*In re TOUSA, Inc.)*, 680 F.3d 1298, 1313 (11th Cir. 2012) ("To be sure, we have stated that the paradigm case of a benefit under § 550(a) is the benefit to a guarantor by the payment of the underlying debt of the debtor. . . . Although this relationship may be the paradigmatic case, it is not the only circumstance that can give rise to 'for whose benefit' liability." (internal quotations and citations omitted)).

[246] *See Baldi v. Lynch (In re McCook Metals, L.L.C.*), 319 B.R. 570, 590 (Bankr. N.D. Ill. 2005) (articulating a three-part test requiring that the benefit to a transfer beneficiary under § 550(a)(1) be actually received, quantifiable, and accessible); *Halperin v. Moreno (In re Green Field Energy Servs., Inc.)*, 594 B.R. 239, 287–88 (Bankr. D. Del. 2018) (applying the three-part test for transfer-beneficiary liability under § 550(a)(1)); *FTX Recovery Tr. v. Farmington State Corp. (In re FTX Trading Ltd.)*, 676 B.R. 131, 140–41 (Bankr. D. Del. 2025) ("As this Court explained in *In re Samson Res. Corp.*, the test for determining if a defendant is an entity 'for whose benefit the transfer was made' is whether that defendant received an 'actual, quantifiable, and accessible benefit.'").

The benefit was actually received. Prior to the pre-merger reorganization, the Shareholders owned shares in Kabbage directly. Because Kabbage had incurred massive liabilities from its reckless PPP lending, the value of the Shareholders' equity was a fraction of what Amex agreed to pay. Even after Amex Kabbage became Kabbage's sole shareholder, the value of Shareholders' equity was still negatively impacted by the massive liabilities at Kabbage. Kabbage's assets and liabilities sat together in a single entity (Kabbage), which was now a wholly owned subsidiary of Amex Kabbage. But when Kabbage transferred its assets to Amex Kabbage on October 13, the value of the Shareholders' equity immediately increased because the PPP liabilities were orphaned at Kabbage. Kabbage's creditors could no longer look to those assets for payment of their claims because those assets were no longer owned, directly or indirectly, by Kabbage. The Fraudulent Transfer thus conferred an immediate and actual benefit on the Shareholders.

The benefit was quantifiable. Each Shareholder received a specific, identifiable amount of merger consideration based on its percentage ownership of Amex Kabbage. The Complaint identifies the precise amounts. Contrary to Defendants' arguments, this is not a case where the alleged benefit is speculative or impossible to measure—it can be calculated with mathematical precision to the dollar: each of the Shareholders received a precise sum in Merger consideration. Further, to the extent that the benefit conferred on the Shareholders was the difference between the value of their shares in the Kabbage enterprise pre- and post-Fraudulent Transfer, that benefit can and will be quantified by expert analysis: it is, at a minimum, the amount by which the Fraudulent Transfer rendered Kabbage insolvent multiplied by each Shareholders' ownership interests in Kabbage.

The benefit was accessible. The Shareholders directly accessed the benefits they obtained from the Fraudulent Transfer by receiving the Merger consideration within three days of that

transfer. Unlike an indirect increase in the value of privately held stock—which a shareholder cannot spend and which might change in the future—the Shareholders received cash in hand. The Shareholders could immediately use the merger consideration as they wished. This is the key factor that distinguishes this case from other cases in which trustees have sought to hold shareholders liable under section 550.[247]

Defendants' reliance on *In re Alta Mesa* is misplaced.[248] In that case, the trustee sought to recover from shareholders of a company that received assets from the debtor, based on the theory that the asset transfer increased the value of the shareholders' equity.[249] Critically, the only alleged "benefit" was that shares theoretically became more valuable for a sale *three years later*.[250] The court dismissed the claim because the "benefit" was too "attenuated":

> Here, the sale price does not correspond to the value of the transfers in any ascertainable way. It is an incidental, indirect benefit from agreements that were entered into years before the Business Combination and sale of [the transferee] occurred. [The trustee] cannot directly quantify the amount that the transfers increased the sales price. The sales price alone does not directly reflect the corresponding benefit from the value of the transfers. The benefit received by the shareholders is merely an indirect benefit from business agreements.[251]

Here, conversely, the sale price directly reflected the benefit from the value of the transfers. Further, unlike in *Alta Mesa*, the purpose of the Fraudulent Transfer was to pay the Shareholders not at some indefinite point in the future, but a mere three days later.

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[247] *See, e.g.*, *Bodenstein v. Univ. of N. Iowa* (*In re Peregrine Fin. Grp., Inc.)*, 589 B.R. 360, 381 (Bankr. N.D. Ill. 2018) (holding that trustee had not proven his claims because the defendant "had only the right to benefit from the funds in the future" if "the funds were still available").

[248] *Dunn v. HPS Inv. Partners (In re Alta Mesa Res., Inc.)*, 2024 WL 4379801, at *1–2 (Bankr. S.D. Tex. Oct. 1, 2024).

[249] *Id*.

[250] *See id.* at *6 ("The Business Combination occurred in February 2018, approximately three years after the first of a series of conveyances that [the trustee] seeks to avoid.").

[251] *Id.*

Defendants also rely on *Cleveland-Cliffs Burns Harbor LLC v. Boomerang Tube, LLC*, another factually inapposite case.[252] In *Cleveland-Cliffs*, a creditor sought to hold the owner of the transferee liable under Delaware's fraudulent transfer statute.[253] The Delaware court rejected the claim because the owner "was not a party to the sale" in which the fraudulent transfer was made and there was no allegation that the owner actually accessed any of the benefits from the fraudulent transfer.[254] The facts at issue here are demonstrably different. The Shareholders were named and intended beneficiaries of the Merger Agreement.[255] The purpose of that agreement was to transfer the value of Kabbage's non-PPP assets to the Shareholders and to convert that value to immediate cash in the Shareholders' pockets.

Defendants further contend that transfer-beneficiary liability under section 550(a)(1) requires pleading grounds for piercing the corporate veil between Amex Kabbage and its shareholders.[256] But section 550 of the Bankruptcy Code does not require veil piercing; it provides an independent basis for recovery from "the entity for whose benefit such transfer was made."[257] The veil-piercing cases cited by Defendants where courts dismissed claims involve factual scenarios where the shareholders' only alleged benefit was, at best, an amorphous and unrealized increase in equity value.[258] But no veil piercing is necessary here. The Fraudulent Transfer did

[252] 2023 WL 5688392 (Del. Ch. Sept. 5, 2023).

[253] *See id.* at *13.

[254] *See id.*

[255] Compl. ¶¶ 251, 273, 333; J.A. Ex. 42 (Merger Agreement) at A00431–32.

[256] *E.g.*, Certain Defs. Mot. at 13–15; D&O Defs. Mot. at 47–49.

[257] *Kravitz v. Samson Energy Co.* (*In re Samson Res. Corp.*), 2022 WL 3135288 (Bankr. D. Del. Aug. 4, 2022), cited by Defendants, does not hold that veil piercing is required to establish liability. *Id.* at *7–8. Further, in that case, the trustee appeared to allege that defendant was really a subsequent transferee, as opposed to the facts here, where the Merger Agreement contemplated Kabbage transferring its assets to Amex Kabbage to confer an actual, quantifiable, and accessible benefit on the Shareholders. *See id.*

[258] *See, e.g.*, *Green Field*, 594 B.R. at 287–89 (rejecting claim at trial because the evidence showed that the transferees, which the defendant partially controlled, "generated no profit, and there is no evidence that [the

not merely increase the value of the Shareholders' equity in Amex Kabbage—it enabled them, pursuant to a contract in which they were intended beneficiaries, to immediately convert that increase in equity value into hundreds of millions of dollars in cash. The Fraudulent Transfer was necessary for the merger to close; absent it, the Shareholders would have received nothing. This causal connection between the Fraudulent Transfer and the Shareholders' receipt of value is precisely what section 550(a)(1) targets.

B. The Collapsing Doctrine Further Supports Transfer-Beneficiary Liability.

Courts routinely "collapse" a series of formally distinct but interrelated transactions into a single transaction for fraudulent transfer analysis. As the Second Circuit explained, "an allegedly fraudulent conveyance must be evaluated in context; where a transfer is only a step in a general plan, the plan must be viewed as a whole with all its composite implications."[259] This doctrine is particularly applicable to leveraged buyouts and similar multi-step transactions where the segments, in reality, comprise a single integrated scheme.[260] Courts generally consider three

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defendant] drew any form of a salary, dividend or distribution from any of them" or otherwise had "had access to the funds transferred"); *Schechter v. 5841 Bldg. Corp. (In re Hansen)*, 341 B.R. 638, 645–46 (Bankr. N.D. Ill. 2006) (holding that "[s]omething more than *mere status* as a shareholder, officer, or director must be shown" and rejecting plaintiff's claim because it was solely that the defendant was "an officer and majority shareholder" of the transferee and "*nothing more*" (emphasis added)); *Weiss v. Arabella Expl. Inc.* (*In re Arabella Petrol. Co.)*, 647 B.R. 851, 872–73 (Bankr. W.D. Tex. 2022) (rejecting § 550 claim because the primary basis for recovery against the defendant was his status as a shareholder of the transferee, without identifying any quantifiable benefit that the defendant actually received and which was accessible); *Turner v. Phoenix Fin., LLC (In re Imageset, Inc.)*, 299 B.R. 709, 718 (Bankr. D. Me. 2003) (holding that "individuals' rights as interest holders in the LLC is not *alone* sufficient to qualify them as persons 'for whose benefit [the] transfer[s were] made'" (emphasis added)). *Yu v. GSM Nation, LLC*, 2018 WL 2272708 (Del. Super. Apr. 24, 2018), is even less on point because the plaintiff did not allege any facts the defendant benefited from the transfers. *See id.* at *13.

[259] *Orr v. Kinderhill Corp.*, 991 F.2d 31, 35 (2d Cir. 1993) (internal quotations and alterations omitted).

[260] *See Off. Comm. of Unsecured Creditors of Hechinger Inv. Co. of Del. Inc. v. Fleet Retail Fin. Grp.* (*In re Hechinger Inv. Co. of Del.)*, 274 B.R. 71, 89–91 (D. Del. 2002) ("Regardless of the various complex structures of leveraged buyouts, which often involve various loans, stock purchases, mergers, and repayment obligations, courts have found that a set of transactions may be viewed as one integrated transaction if the transactions 'reasonably collapse into a single integrated plan and either defraud creditors or leave the debtor with less than equivalent value post-exchange.'" (citation omitted)).

factors in determining whether to collapse transactions: "(1) whether all of the parties involved had knowledge of the multiple transactions; (2) whether each transaction would have occurred on its own; and (3) whether each transaction was dependent or conditioned on other transactions."[261] All three factors support collapsing the Fraudulent Transfer with the payment of the merger consideration pursuant to the Merger Agreement.

First, the Shareholder Defendants knew that the Fraudulent Transfer was one step in a series of transfers designed to deliver value to them while leaving liabilities at Kabbage. Second, the Fraudulent Transfer would not have occurred on its own; it occurred solely because it was a condition of the Merger Agreement. Third, each step of the merger was explicitly conditioned on the other steps. When the transactions are properly viewed as part of an integrated transaction, the Shareholder Defendants' receipt of the Merger consideration is directly traceable to the Fraudulent Transfer of Kabbage's assets.

V. The Complaint States Viable Claims for Disallowance and Subordination.[262]

Defendants argue that Counts V–VII—seeking disallowance under sections 502(d) and 502(e) and equitable subordination under section 510(c)—must be dismissed because the Complaint fails to plead the elements of each provision and because these claims are "derivative" of Plaintiff's substantive claims. These arguments fail for the reasons explained below.

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[261] *See, e.g.*, *Adelphia Recovery Tr. v. FPL Grp., Inc.* (*In re Adelphia Commc'ns Corp.)*, 512 B.R. 447, 491 (Bankr. S.D.N.Y. 2014); *see also Hechinger*, 274 B.R. at 91 ("Courts thus focus 'not on the structure of the transaction but the knowledge and intent of the parties involved in the transaction.'" (citation omitted)); *United States v. Tabor Ct. Realty Corp.*, 803 F.2d 1288, 1302–03 (3d Cir. 1986).

[262] The Complaint alleges that the Officers (Frohwein, Petralia, Askins, Robinson) and certain Directors (Frohwein, Butler, Ebinger, Stolle, and Hodrick) filed proofs of claim in the Kabbage bankruptcy. Compl. ¶¶ 339–46, 351–57. Kabbage's disallowance and equitable subordination claims are therefore directed against these defendants and their respective proofs of claim.

A. The Section 502(e) Disallowance Claim Is Adequately Stated Against the Officers (Count V).

Section 502(e)(1)(B) of the Bankruptcy Code provides that the court "shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on . . . the claim of a creditor, to the extent that" such claim "is contingent as of the time of [its] allowance or disallowance."[263] Disallowance requires three elements: (i) the claim is for reimbursement or contribution; (ii) the claim is contingent; and (iii) the claimant and the debtor are co-liable on a creditor's claim.[264] The Complaint satisfies each element.

First, the Officers' claims are for reimbursement. Each Officer filed a proof of claim asserting a right to indemnification from Kabbage.[265] Indemnification is one type of reimbursement within the meaning of section 502(e).[266]

Second, the claims are contingent. The Officers' indemnification rights depend on whether they actually incur liability in connection with third-party claims arising from their service to Kabbage, including in connection with the DOJ's FCA action against certain former Officers individually.[267] Because their ultimate liability—and thus their right to indemnification—remains unresolved, their claims are contingent "as of the time of allowance or disallowance."[268]

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[263] 11 U.S.C. § 502(e)(1)(B).

[264] *In re Touch Am. Holdings, Inc.*, 409 B.R. 712, 715–16 (Bankr. D. Del. 2009).

[265] Compl. ¶¶ 339–46 (alleging that D&O Defendants filed proofs of claim in the Kabbage bankruptcy alleging right to indemnification from Kabbage).

[266] *See Touch Am.* at 716.

[267] Moreover, under Delaware law, Kabbage cannot indemnify the Officers or Directors for judgments or settlements of claims brought by the company or on its behalf. 8 Del. C. § 145(b).

[268] Compl. ¶ 348. In addition, the Plan itself rejected "any obligations of the Debtors … to indemnify, reimburse, or limit the liability of any Former Officer and Director." *Id.* ¶ 347. The rejection of these obligations further underscores the contingent nature of any remaining indemnification claims.

Third, the Officers are co-liable with Kabbage on a creditor's claim. Defendants protest that the Complaint "does not even attempt to allege the co-liability or security relationship that is the foundation of Section 502(e) disallowance."[269] Wrong. Count V incorporates by reference the Complaint's preceding 337 paragraphs of factual allegations, which establish co-liability as follows: the DOJ settled its FCA claims against Kabbage for allowed claims totaling $120 million.[270] The DOJ intervened in two FCA *qui tam* actions and is "continuing its pursuit" of those claims against certain Officers individually.[271] The FCA imposes liability on "any person" who "knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval."[272] The Complaint alleges the Officers knowingly caused Kabbage to submit fraudulent and inflated PPP loan applications.[273] Because both the Officers and Kabbage face liability to the same government creditor for the same underlying conduct, they are co-liable within the meaning of section 502(e)(1). Permitting the Officers to recover indemnification related to this shared liability would produce exactly "the double payment by the estate" that section 502(e) prohibits.[274]

Defendants' reliance on *In re Wedtech Corp.* is misplaced. *Wedtech* held only that the debtor "obviously cannot be co-liable with [defendants] on the causes of action asserted in adversarial proceedings brought by [itself]."[275] Plaintiff does not contend otherwise. The relevant co-liability here is not on the adversary proceeding claims Kabbage brings against the Officers,

[269] D&O Defs. Mot. at 57.

[270] Compl. ¶¶ 275–86, 338.

[271] *Id.* ¶ 17.

[272] *Id.* ¶ 4 n.5 (quoting 31 U.S.C. § 3729(a)(1)(A)).

[273] *Id.* ¶¶ 296, 306.

[274] *See Touch Am.*, 409 B.R. at 719.

[275] 5 B.R. 285, 290 (Bankr. S.D.N.Y. 1988).

but on the *government's* claims, on which both Kabbage and its former Officers face independent liability for the same fraudulent PPP lending conduct.

B. The Section 502(d) Disallowance Claim Is Adequately Pleaded Against the Officers (Count VI).

As Defendants themselves frame it, to survive a motion to dismiss Plaintiff's disallowance claim under section 502(d), Plaintiff must have alleged facts establishing: (1) an avoidable transfer occurred, and (2) the defendant from whom property is recoverable has not satisfied its liability.[276] As discussed in Part III above, the Complaint more than sufficiently alleges that an avoidable fraudulent or constructive transfer occurred. The Complaint further alleges that the Officers were among the "intended and actual beneficiaries," and specifies the precise dollar amounts each received as merger consideration.[277] As explained in Part IV, property is recoverable from each of the Officers under section 550(a)(1) as entities "for whose benefit" the transfer was made. Each Officer has filed a proof of claim in Kabbage's bankruptcy, and none has paid the amount for which they are liable.[278] Thus, at the pleading stage, Plaintiff has stated a plausible section 502(d) claim against the Officers.[279]

C. The Equitable Subordination Claim Is Adequately Pleaded Against the Officers and Directors (Count VII).

As discussed above, the Complaint adequately pleads claims against the Officers (Count II) and Directors (Count III) for breaching their fiduciary duties of loyalty and good faith, resulting in hundreds of millions of dollars in damages to the estate and its creditors. Because the

[276] *See* 11 U.S.C. § 502(d); *see also* D&O Defs. Mot. at 55.

[277] Compl. ¶¶ 333–35.

[278] *Id.* ¶ 360.

[279] At bottom, the section 502(d) analysis boils down to whether the Count IV fraudulent transfer claim survives the motion to dismiss.

Defendants' inequitable conduct—their conscious disregard of oversight duties, their suppression of compliance reports, and their self-interested extraction of hundreds of millions of dollars while leaving the estate insolvent—caused injury to Kabbage's creditors, equitable subordination is appropriate to prevent them from asserting indemnification claims *pari passu* with the creditors they harmed. Moreover, "determining whether a creditor's claim should be subordinated is a fact-intensive inquiry which should not necessarily be determined on a motion to dismiss."[280] The Complaint's allegations of bad faith, self-dealing, and injury to creditors more than provide the predicate for Plaintiff's claim for equitable subordination to survive the motions to dismiss.

VI. While Kabbage Believes that Complaint More than Sufficiently Pleads the Claims, Kabbage Is Prepared to Buttress Its Allegations.

The Complaint is already very detailed. But, as demonstrated by some of the materials affixed by the parties, there is additional evidence supporting Plaintiff's allegations. If the Court finds that additional allegations are necessary, or that the Complaint should specifically respond to some of Defendants' arguments, Plaintiff is prepared to file an amended complaint.

CONCLUSION

Plaintiff has more than sufficiently pleaded each of its claims. All these claims present fact-intensive issues—the Directors' and Officers' knowledge and state of mind, the effectiveness of compliance systems, the reasonableness of the assumptions in the Solvency Opinion, and the integrated structure of the Merger—that are paradigmatically unsuited to resolution on the pleadings. Accordingly, the motions should be denied in full.

[280] *Autobacs Strauss, Inc. v. Autobacs Seven Co. (In re Autobacs Strauss, Inc.)*, 473 B.R. 525, 583 (Bankr. D. Del. 2012).

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