

Mass. Retailer Sues Digital Lender Over \$3.2M Arbitration Win

By **Reenat Sinay**

Law360 (September 9, 2019, 7:16 PM EDT) -- A family-owned clothing shop in Massachusetts asked a Bay State federal judge to throw out a \$3.2 million arbitration award it was ordered to pay to the operators of a purported “rent-a-bank” scheme who violated state usury laws, according to a complaint filed Monday.

NRO Boston LLC, owned and run by James Indelicato and his wife Alice, accuses digital lending platform Kabbage Inc. of using the Utah-based Celtic Bank Corp. to “front” its “loan sharking business” and skirt the Commonwealth’s usury laws. Unlike Massachusetts, which caps commercial loan interest rates at 20%, Utah has no maximum limit, NRO said.

“Kabbage with the assistance of Celtic has systematically taken advantage of NRO for years, slowly devastating an otherwise profitable business that has employed dozens of Massachusetts residents for nearly a decade,” NRO said. “It preys on the weak and desperate and extorts unconscionable terms that are expressly prohibited by the criminal laws, civil statutes, and the strong public policy of this Commonwealth.”

In a separate motion filed Monday, Celtic Bank urged the court to enforce the arbitration award against NRO and Alice Indelicato, arguing the arbitrator, Charles B. Swartwood III, is an experienced former magistrate judge who rejected all of NRO’s claims after thorough examination.

The suit brought by NRO stems from 30 loans it was issued by Kabbage between 2014 and 2016. The retail store struggled to keep up with the payments because of the high interest rates, and first **filed a suit in 2017** seeking to invalidate the loans and collect damages of \$20 million, court records show.

Celtic Bank and Kabbage filed counterclaims for breach of contract in May 2018 seeking both recovery and damages, but the suit was paused that same month when the parties agreed to arbitrate their claims.

Swartwood ultimately awarded Celtic recovery of the loans owed in the sum of over \$109,000 plus daily interest, \$2.7 million in attorney fees, and \$447,000 in costs and expenses in July.

NRO and Indelicato filed suit to challenge the \$3,285,116 award and Swartwood’s finding that the business partnership between Kabbage and Celtic Bank was legitimate. James Indelicato is not a party in either suit.

Central to the dispute is the question of who is the "true lender" taking on the risk of the loans: Kabbage, which is subject to state usury laws, or Celtic Bank, which is not subject to state usury laws as a Federal Deposit Insurance Corp. member.

According to the plaintiffs, a "rent-a-bank" scheme is carried out when a third party digital lender, like Kabbage, identifies a bank chartered in a state with high interest rate limits or no limit at all, such as Celtic, as the lender on official loan documents in an attempt to illegally charge higher rates than are allowed by the state in which the third party is issuing loans.

NRO argued the arbitrator incorrectly found that Celtic Bank was the "true lender," when in fact Kabbage originates, underwrites and finances loans to Bay State businesses, and that a Kabbage executive has admitted as much. Celtic is paid a fixed percentage for allowing its name to be used, the complaint says.

The clothing store contended its owners and employees have been subject to harassment and a string of lawsuits because of Kabbage and Celtic's actions, that its business assets have been frozen, and that Alice Indelicato has had liens placed on her home.

Celtic Bank in its Monday filing noted the arbitrator had been "sharply critical" of the Indelicatos' attempt to blame it and Kabbage for their financial struggles, instead finding that their difficulties arose from mismanagement, overeager expansion and excessive owner compensation to the tune of \$1 million more than industry standard.

NRO also accused Swartwood of being biased. It said that unbeknownst to the company, the arbitrator was close friends with an interested third party who had lent the Indelicatos money as a friend. NRO alleges that Swartwood, who did not fully disclose his personal connection to the third party, suggested that it file for bankruptcy in order to pay the man back.

"This undisclosed evident partiality helps explain the manifest disregard of the law that has fatally infected the Award," NRO said.

Leslie Rinaldi, a spokeswoman for Celtic Bank, told Law360 on Monday the bank was "gratified" with the arbitration award and that it trusts in Swartwood's decision.

"We feel the award is extremely well-reasoned and the product of diligent and conscientious hard work by our arbitrator," Rinaldi said. "Judge Swartwood is a very well-respected [former] federal magistrate and we feel confident in his reasoning."

Representatives for Kabbage did not immediately respond to requests for comment Monday.

NRO is represented by Shane R. Heskin and Justin E. Proper of White & Williams LLP.

Celtic Bank is represented by Michael Maya, Andrew Soukup and Ashley Simonsen of Covington & Burling LLP.

Counsel information for Kabbage was not available Monday.

The cases are NRO Boston LLC et al. v. Kabbage Inc. et al. and Indelicato et al. v. Kabbage Inc. et al., case numbers 1:19-cv-11901 and 1:17-cv-11976, in the U.S. District Court for the District of Massachusetts.

--Editing by Amy Rowe.

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