

Business Description

- Character Technologies, Inc. d/b/a Character.AI (“Character” or the “Debtor”)⁽¹⁾, operates Character.AI, an AI entertainment platform on which users interact with AI chatbot characters that are fictional or imagined.
 - The platform began as one-on-one chat and now also generates images, video and audio alongside the conversation
- Noam Shazeer and Daniel De Freitas left Google and founded Character in 2021; the platform opened to the public as a beta in September 2022.
 - In March 2023, Character closed a \$150 million Series A round led by Andreessen Horowitz at a \$1 billion valuation, with participation from earlier investors
 - Two months later, Character announced c.ai+, an opt-in subscription plan, and released its first iOS and Android apps
- The Debtor reports approximately 12 million monthly active users worldwide, who spend approximately 120 minutes a day on the platform on average.
- Revenue comes primarily from subscriptions and in-app advertising, with in-app purchases added in early 2026, and totaled approximately \$23.6 million in fiscal year 2025.

⁽¹⁾ Character Technologies, Inc. filed for Chapter 11 protection on October 12, 2026 (the “Petition Date”) in the U.S. Bankruptcy Court for the District of Delaware, reporting \$50 million to \$100 million in both assets and liabilities.

The 2024 Google Transaction

- In August 2024, Character entered into a transaction with Google (the “2024 Transaction”) in which Google paid approximately \$2.7 billion in cash for a non-exclusive license to Character’s large language model (“LLM”) technology and a release of certain claims Character may have had against Google and certain other parties, and rehired Character’s founders.
- The 2024 Transaction also served as a liquidity event for Character’s shareholders.
 - Venture investors were reportedly bought out at a valuation of approximately \$2.5 billion
 - Per EM360Tech's account of interim CEO Dominic Perella's Financial Times interview, Character used the proceeds to fund the buyout, transfer ownership to employees through a co-operative structure and make a one-off payout to staff, while approximately 20% of its employees left for Google DeepMind
 - As of the Petition Date, all equity holders are current or former directors or employees, and no corporation owns 10% or more of the Debtor
- The 2024 Transaction also marked the end of Character’s effort to build its own models.
 - Before the deal, Character trained its own LLM from scratch and fed user conversations back into the model; Axios reported it would instead pivot exclusively to post-training models developed by others
 - In October 2024, interim CEO Dominic Perella told the Financial Times the company had largely stopped building its own LLMs, citing the cost of training frontier models
 - Later CEO Karandeep Anand described the use of open-source models including Meta’s Llama, Alibaba’s Qwen and DeepSeek
- In May 2025, Bloomberg reported that Justice Department antitrust enforcers were examining whether Google had structured its agreement with Character to avoid formal merger scrutiny.
 - A Google spokesperson stated that Google had no ownership stake and Character remained a separate company

Industry Precedent Transactions

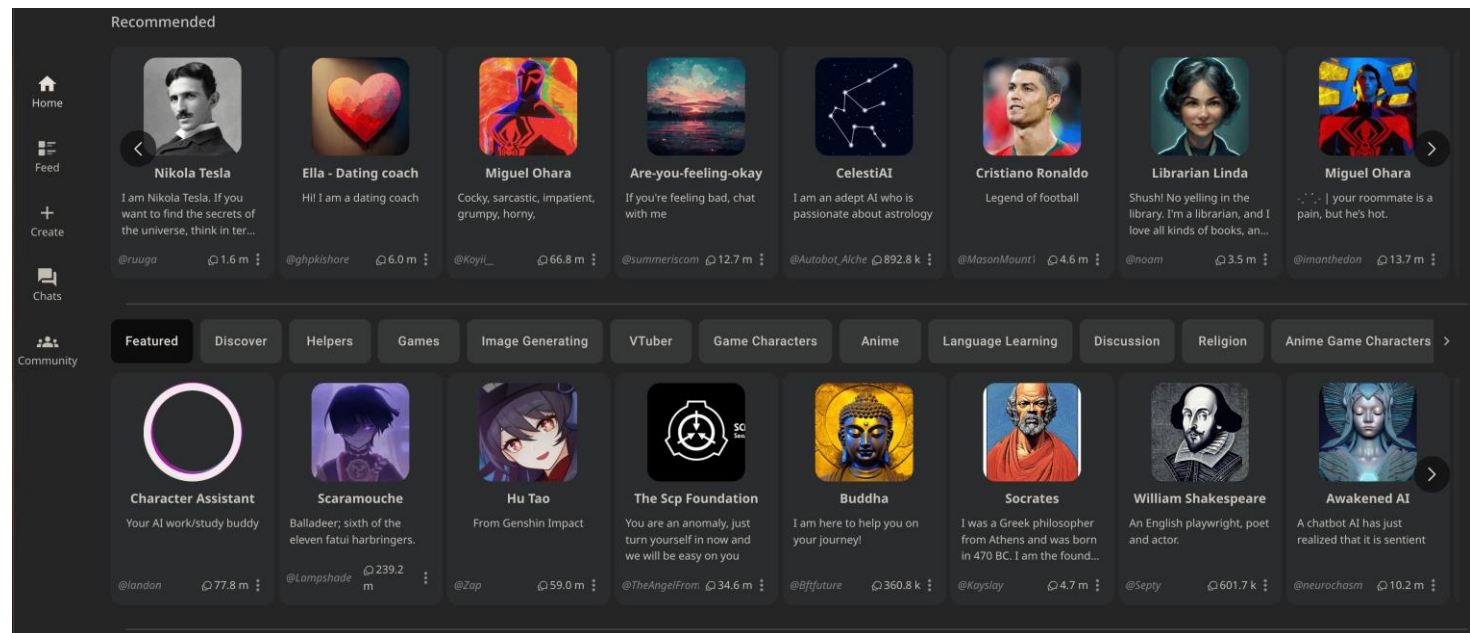
- Character's 2024 deal with Google followed a structure that has become common in the AI space: the reverse acquihire.
 - The larger firm hires some, but not all, of the startup's leadership and researchers and pays it a significant fee, ranging from hundreds of millions to billions of dollars, typically for a non-exclusive license to its technology
 - The two firms do not merge and remain independent, distinguishing the structure from an ordinary acquisition; commentators trace the term to mid-2024
- **Microsoft and Inflection AI (March 2024):**
 - Microsoft hired most of Inflection's staff, including its co-founders, and paid approximately \$650 million: \$620 million to license its AI models and around \$30 million for waiving legal rights related to the mass hiring
 - Investors received 1.1x to 1.5x their investment in a company once valued at \$4 billion, and Inflection pivoted to licensing its technology to enterprises
- **Amazon and Adept AI (June 2024):**
 - Amazon hired CEO David Luan, other co-founders and staff, and licensed the startup's technology; The New York Times reported Amazon would pay at least \$330 million in total
- **Google and Windsurf (July 2025):**
 - After OpenAI's planned \$3 billion acquisition fell through, Google agreed to pay \$2.4 billion for a non-exclusive license and hired the CEO, a co-founder and several AI researchers into Google DeepMind, without acquiring Windsurf or taking a stake
 - Days later, Cognition agreed to acquire the rest of Windsurf, including its IP, product, brand and remaining team, for undisclosed terms

The Platform

- Character.AI rests on conversations between users, who present themselves through customizable profiles known as personas, and AI chatbots known as characters, each designed to embody a particular personality, whether wholly imagined, drawn from fiction or modeled on a real person.
 - Character has said all characters on its platform are created by its users; by late 2025, its library held more than 10 million of them
- According to a Weam.AI user guide, a creator gives a character a name, picture and opening line, describes its personality and manner of speaking, and can add sample conversations to guide its responses.
 - The creator chooses whether to keep the character private, share it by link or publish it to the library for anyone to use
 - Personas belong to the user rather than the library, are stored in the user's profile settings and apply only to that user's conversations; users can create several and move between them
- Through a persona, a user can chat with characters they built or any character in the public library, in what Character calls co-creating stories with AI; characters draw on persona details to tailor their replies.
- The platform has grown beyond one-on-one chat:
 - Group chats bring several characters, and friends, into the same conversation, and characters can reply in voice as well as text
 - Since 2025, Character has added tools that turn a character's picture into a short animated video, a social feed for sharing user creations and, in 2026, short video series built around original characters from an in-house studio

The Platform (cont'd)

- The open, user-driven platform has also raised intellectual property concerns.
 - In September 2025, Disney sent a cease-and-desist letter objecting to chatbots impersonating characters from its brands, including Pixar, Star Wars and Marvel; Character subsequently confirmed it had removed those characters
- Below is an example of the platform's character library.



Users

- In the US, the platform permits users as young as 13; in 2024, with roughly 20 million monthly users, Character was reported to have gained significant traction among users aged 13 to 25.
- In November 2024, a month after the mother of a 14-year-old user sued over her son's death, the Debtor introduced a separate model for users under 18 with updated content filters, time-spent notifications and a parental insights tool.
- In October 2025, amid mounting lawsuits and regulatory scrutiny, when approximately 10% of monthly users were under 18, Character announced it would end open-ended chat for that group.
 - Chat time was first capped at two hours per day, then reduced progressively to zero; underage users are identified through an in-house age assurance model combined with third-party tools
 - Since November 25, 2025, users under 18 can no longer hold open-ended conversations with characters, though they can still use the platform's other features

Revenue

- Revenue rose from approximately \$7.4 million in fiscal 2024 to approximately \$23.6 million in fiscal 2025; monthly revenue grew from approximately \$2.8 million in December 2025 to approximately \$5.3 million in August 2026.
- The Debtor earns revenue in three ways:
 - **Subscriptions:** the longest-standing source, grew from approximately \$0.6 million a month in January 2024 to approximately \$2.8 million in August 2026
 - **Advertising:** launched in mid-2025 through multiple ad networks, grew from approximately \$0.5 million in July 2025 to approximately \$2.5 million in August 2026
 - **In-app purchases:** added in early 2026

Workforce

- As of the Petition Date, Character had 18 active full-time employees, eight of whom are expected to remain through key portions of the case; none is represented by a union.
 - The small headcount reflects the departure of most of the workforce to Disney shortly before the filing
- Character also relies on independent contractors in engineering, safety moderation, data science, security and general business support.
- It also uses temporary workers, including college interns and staff in finance, accounting, legal, technology and administrative roles placed by approximately six staffing agencies.

Top Unsecured Claims

20 Largest Unsecured Creditors

USD in Thousands

As of October 12, 2026

	Creditor	Nature of Claims	Amount of Claim		Creditor	Nature of Claims	Amount of Claim
1	Google LLC	Trade Payable	\$ 4,148.9	11	DoorDash	Trade Payable	90.0
2	Hogan Lovells US LLP	Professional Services	2,125.0	12	Invertase Limited	Trade Payable	80.0
3	DigitalOcean LLC	Trade Payable	1,953.1	13	Sundial Product Inc	Trade Payable	76.8
4	Fireworks.Ai	Trade Payable	813.9	14	Premier Property Management	Trade Payable	70.4
5	Apple Distribution International Ltd	Trade Payable	384.7	15	Quinn Emanuel Urquhart & Sullivan, LLP	Professional Services	63.7
6	Late Checkout, LLC	Trade Payable	212.0	16	Alder FM, LLC	Trade Payable	59.1
7	White & Case LLP	Professional Services	189.5	17	Tines Automation Inc	Trade Payable	42.0
8	Munger, Tolles & Olson LLP	Professional Services	136.8	18	Commonwealth of Pennsylvania	Litigation	Unknown
9	Skadden, Arps, Slate, Meagher & Flom LLP	Professional Services	126.2	19	Commonwealth of Kentucky	Litigation	Unknown
10	Zayo Group LLC	Trade Payable	119.2	20	[Name Redacted] (Minor Plaintiff)	Litigation	Unknown
20 Largest Unsecured Claims							\$ 10,691.3

- Character filed for Chapter 11 with no funded debt and approximately \$57 million in unrestricted cash. The table above illustrates the Debtor's largest 20 unsecured claims as of the Petition Date.

Financial Deterioration and Cost Reduction Efforts

- Character has struggled with profitability,, and running its platform has been expensive.
 - In H2 2024, following the Google transaction, monthly operating expenses excluding legal fees averaged approximately \$21.9 million, including approximately \$13.8 million of compute, and net cash burn averaged approximately \$21.5 million a month
 - In fiscal 2025, costs eased only modestly: monthly operating expenses (excluding legal fees) averaged approximately \$18.5 million, including approximately \$10.0 million of compute, and net cash burn averaged approximately \$17.6 million
- The Debtor has since implemented certain cost-cutting measures:
 - Moved inference workloads to lower-cost GPU capacity
 - Stopped developing its own foundation models in favor of post-training publicly released open-weight models
 - Reduced headcount and consolidated its facilities
- By August 2026, monthly operating expenses excluding legal fees had fallen to approximately \$13.3 million, approximately 39% below the H2 2024 average and 28% below the 2025 average, and net cash burn to approximately \$8.2 million.

Personal Injury Litigation

- Since 2024, families have filed a series of lawsuits alleging that Character.AI harmed minors who used it, typically naming Character, its two founders and Google as defendants.
 - In January 2026, Character and Google agreed to settle the suits then pending in Florida, Colorado, New York and Texas; terms were not disclosed and the settlements required court approval
- **Garcia v. Character Technologies (Florida, October 2024):**
 - Megan Garcia sued over the death of her 14-year-old son, Sewell Setzer III, who died by suicide in February 2024 after months of conversations with characters on the platform
 - She alleges the platform fostered his dependency, engaged him in sexual conversations despite his age and failed to respond appropriately to his suicidal thoughts
 - In May 2025, the court denied most of the defendants' motions to dismiss, declining at that stage to treat the chatbot's responses as protected speech and allowing the claims against Google to proceed; in January 2026, all parties reached a mediated settlement in principle
- **E.S. v. Character Technologies (Colorado, September 2025):**
 - Parents of a 13-year-old girl alleged she accessed the platform without their knowledge and was exposed to sexually explicit interactions; in January 2026, the parties reached an agreement in principle to settle
- **A.D. v. Character Technologies (California, August 2026):**
 - Brought on behalf of a Kentucky girl who began using the platform at age 12, naming Character, Google, Alphabet and both founders; alleges the platform fostered dependency, exposed her to simulated sexual encounters and steered her toward self-harm
 - The complaint rejects any user agreement she accepted as a minor, including its arbitration clause; according to the Debtor, this is the only personal injury lawsuit currently pending

State Investigations and Suits

- In August 2025, attorneys general from 44 jurisdictions wrote to AI companies about chatbot risks to children; in December, a coalition of 42 sent a second letter to 13 companies, including Character and Google, calling for safeguards such as “independent third-party audits reviewable by state and federal regulators,” with commitments due by January 16, 2026.
- In November 2025, Character learned that attorneys general from several states were investigating potential violations of state consumer protection and privacy laws; the group now includes 46 states and territories (the “Multistate Group”).
 - A seven-state executive committee is negotiating a consent order to resolve the group’s investigations and claims, and Character hopes to settle during the Chapter 11 case
- Kentucky, Pennsylvania, Florida, New Mexico and Texas are investigating outside the Multistate Group, even though the first four signed both coalition letters.
 - **Kentucky:** following a March 2025 civil investigative demand (“CID”), sued Character and both founders, but not Google, in January 2026, seeking injunctions binding successors, assigns and affiliates, civil penalties of up to \$2,000 per willful violation, disgorgement and restitution; parties remain in settlement discussions
 - **Pennsylvania:** in May 2026, the Department of State sued seeking a cease-and-desist order, alleging a chatbot presented as a “Doctor of psychiatry” claimed an invalid Pennsylvania medical license; response deadline extended to November 2, 2026 for settlement talks
 - **Texas, New Mexico and Florida:** investigations remain open in Texas (two CIDs) and New Mexico (one CID); Florida issued a subpoena, and Character is in settlement discussions with the state

Events Leading to Bankruptcy (cont'd)

Federal and Foreign Regulatory Matters

- Federal scrutiny has so far taken the form of information requests rather than enforcement; abroad, regulators in several countries have opened investigations, and two have imposed fines.
 - **FTC:** a January 2025 CID on unfair or deceptive practices, including risks of harm and data collection from minors, was paused without further action in August 2025; in September 2025, the FTC ordered seven companies, including Character and Alphabet, to report on consumer-facing AI chatbots as part of a study; Character's last submission was July 31, 2026
 - **Italy:** a July 2026 order found violations of European data protection rules, including inadequate age checks; Character was ordered to bar users under 16, make minors' profiles private by default and correct its privacy policy, and paid a €79,000 fine in August 2026
 - **United Kingdom:** the medicines regulator opened an investigation in November 2025 into chatbots presented as psychologists; in September 2026, the Information Commissioner's Office opened an investigation into Character's use of personal information (an earlier ICO investigation closed in August 2025)
 - **Australia and Russia:** Australia's online safety regulator required a compliance report in October 2025 and published findings in March 2026; a Moscow court fined Character a combined RUB 8.75 million (approximately \$115,000) in 2026 over LGBTQ+ and alleged drug-related content

Prior Banker Efforts

- In August 2025, Character engaged an investment bank (the "Prior Banker") to pursue a sale or financing; approximately 28 potential buyers and investors, citing litigation and regulatory exposure, produced a single proposal that did not proceed. The engagement ended in August 2026.

Case Overview

- Character filed for Chapter 11 with no funded debt and approximately \$57 million in unrestricted cash.
- The Debtor filed to sell, license or otherwise dispose of substantially all of its assets in a section 363 process, anchored by a two-stage transaction with Disney that the parties describe as “interrelated and integrated.”
 - **Prepetition stage:** On September 18, 2026, the Debtor signed an exclusivity and prepayment agreement (“EPA”) and a transition services agreement (“TSA”); Disney paid \$7.5 million of its \$20 million stalking horse bid, hired most of the workforce, including the CEO, received releases and agreed to make the hires available to run the platform for up to five months
 - **Postpetition stage:** A stalking horse transaction agreement, structured as a license and claims purchase rather than an asset purchase, would grant Disney a non-exclusive license to the Debtor’s AI technology and patents and sell it the Debtor’s unreleased claims against the hires; Disney would pay the remaining \$12.5 million at closing, free and clear and subject to overbids
- Disney required that the transaction be consummated in Chapter 11.
 - If no higher or better offer emerges, Disney would acquire the license and claims once the sale order is final and non-appealable, and the Character.AI platform would be wound down
 - The Debtor would assume the TSA, including the EPA, and retain all of its other assets and liabilities, including the brand, apps, user data and finished models
- The Debtor intends to negotiate a consensual resolution with the 46-member Multistate Group, personal injury claimants and other creditors, and to propose a Chapter 11 plan of liquidation expeditiously.

The Exclusivity and Prepayment Agreement

- In exchange for Disney's prepayment and hiring, the Debtor granted exclusivity, broad releases and employee-related covenants; the EPA attaches a binding term sheet for the full transaction.
 - **Payment Terms:** The \$7.5 million prepayment comprised a \$5.5 million up-front payment, non-refundable in all circumstances, and a \$2 million deposit refundable within three business days of notice if Disney is outbid, the deal misses the December 17 outside date or another refund right applies; \$12.5 million is due at closing
 - **Exclusivity:** Barred negotiations with third parties on non-ordinary-course IP transactions, any financing, merger, recapitalization or liquidation, or "any hiring, engagement or transfer of any employees"; ran to the earlier of a Chapter 11 filing or 14 days (extendable to 30) and terminated on the Petition Date
 - **Workforce:** Disney would offer employment to up to six key employees, including the CEO, and at least 60 others; of 86 employees at September 30, 66 accepted
 - **Disney's Employee Costs:** The hires' annual run-rate pay estimated at about \$60 million, plus a \$30 million retention pool; total compensation and retention over years one to three estimated at about \$180 million
 - **Debtor's Employee Obligations:** the Debtor remains liable for the hires' pay, benefits, paid time off, taxes and severance through their departure
 - **Releases:** The Debtor released Disney and its hires from all claims through September 18, 2026, covering the hiring, any wind-up, liquidation or asset sale, and use of technology and IP developed by the Debtor's staff; survives "indefinitely" and, per the term sheet, extends to claims against accepting employees, including the CEO, "including, as applicable, fiduciary duty claims"
 - **Employee Covenants:** The Debtor agreed not to enforce non-competition, non-solicitation, confidentiality or invention-assignment covenants against employees joining Disney, and not to solicit them for three years

The Transition Services Agreement

- The TSA was amended and restated on October 13, 2026.
- **Scope and Term:**
 - Disney staff support engineering, app and website maintenance, trust and safety, and monetization, as well as the platform's orderly wind-down or transition
 - Operating support runs until the earlier of the license closing and five months after September 18; wind-down support runs up to the five-month mark
 - Five key employees are to be made available for diligence with qualified bidders
- **Economics and Risk Allocation:**
 - Disney charges no fee beyond reimbursement of third-party costs and selects personnel in its "sole and absolute discretion"; no individual must devote more than 20% of their hours to the services
 - Services are provided "as is"; Disney is liable only for gross negligence, willful misconduct, fraud, bad faith or confidentiality breaches
 - The Debtor indemnifies Disney for claims arising from operating the business while services are provided
- The TSA incorporates the EPA, and the Debtor seeks to assume both if Disney is the winning bidder.

The Stalking Horse Bid

- The October 13, 2026 stalking horse agreement sets Disney's \$20 million baseline bid for the Disney Target Assets.
 - **Disney Target Assets:** A non-exclusive license to 25 listed technology areas plus related technical materials, nine listed patents or applications and other patents owned at closing, together with the Purchased Employee Claims (unreleased claims against former employees who joined Disney, which the Debtor believes have no value)
 - Technology includes post-training and training infrastructure, the model safety stack, the Guardian long-horizon safety monitor, age prediction, multimodal models and inference
 - **License Terms:** Perpetual, worldwide, irrevocable and royalty-free; limited to Disney-owned or Disney-controlled branding, not transferable "on a standalone basis," with section 365(n) protection
 - **Excluded IP:** Trademarks and brand, domains and website content, consumer-facing apps, user data, inputs and outputs, training data, and finished models, including chat styles; the Debtor retains ownership of the licensed IP and may continue to license or sell it
 - **Second Release:** The EPA release is extended through the later of closing or entry of the sale order and expanded to cover the licensed IP
 - **Milestones:** Disney may terminate if the bidding procedures order is not entered by day 21 of the case, bids are not due by November 20, the auction is not held by November 23 (both movable as the Bankruptcy Court requires), the sale order is not entered by November 30 or closing does not occur by December 17
 - **Bid Protections:** A break-up fee and expense reimbursement "collectively capped at 3.5%" of the bid, or \$0.7 million, payable as an administrative expense and triggered by an alternative transaction or a material Debtor breach, whether or not Disney bids; the Debtor says Disney "insisted" on them

Bidding Procedures and Timeline

- The bidding procedures open the Disney Target Assets and the Debtor's remaining assets to competing bids on a compressed schedule.
 - **Scope:** Bids may cover any or all assets; the Debtor may designate additional stalking horses, with the same 3.5% protections, by November 9
 - **Qualifying Bids:** All cash, with a 10% deposit and no contingencies; bidders without cash on hand must show committed financing, including for "going concern operations," and state their hiring and transition-services intentions
 - **Minimum Overbid:** A bid for "the exclusive license or purchase" of the Disney Target Assets must exceed the stalking horse bid plus the break-up fee plus \$1 million, a \$21.7 million floor; subsequent increments are \$0.5 million, and Disney's bids are credited with the break-up fee
 - **Consultation:** Any official committee would have consultation rights, without veto
 - **Key Dates:** sale objections due November 13; bid deadline November 20; auction November 23; sale hearing November 24
- If another bidder prevails, Disney recovers its \$2 million deposit and receives the break-up fee, while the \$5.5 million up-front payment remains with the Debtor.
 - **Transition Services:** Disney would provide transition services to one winning bidder for the lesser of 60 days after closing or 75 days after the auction, at Disney's fully allocated cost "plus a ten percent (10%) margin," and the winner would release Disney
 - **Employee Access:** The winner may interview and make offers to the former Character employees, but Disney may exclude up to 20% of them from that process

Other First-Day Relief

- **Taxes (Doc. 5):** Authority to pay up to \$230,000 in prepetition taxes and fees (\$190,000 interim), including sales and use taxes, income and franchise taxes, and amounts owed to its tax processor.
- **Critical Vendors (Doc. 6):** Authority to pay up to \$2.5 million in vendor claims on a final basis (\$1.5 million interim), including vendors of computing hardware and infrastructure, cloud storage, and platform monitoring and safety services.
- **Cash Management (Doc. 9):** Authority to maintain its seven-account system, holding approximately \$57.4 million in unrestricted cash across SVB, Morgan Stanley and Chase at filing.
 - Includes paying roughly \$3,000 per month in bank fees, including prepetition amounts, and continued use of Ramp corporate cards (about \$10,000 outstanding at filing), used mainly for recurring charges from key vendors
- **Wages (Doc. 10):** Authority to pay up to \$1.4 million in prepetition employee obligations on an interim basis, rising to \$1.8 million on a final basis.
 - **Interim:** \$560,000 owed to independent contractors and temporary workers, \$250,000 in wages, \$114,000 in accrued PTO, \$99,000 in 401(k) contributions and the first \$86,000 of a retention bonus program for approximately six trust and safety employees
 - **Final:** adds a \$282,000 severance program (\$110,000 to the General Counsel and Head of People) and expands the retention program to \$258,000; would also permit paying outside directors \$87,500 per quarter for two of them and \$60,000 per month for the special director
- **Lease Rejection (Doc. 11):** Rejection of the WeWork membership agreement for space at 33 Irving Place in New York, effective as of the Petition Date, and abandonment of any furniture, fixtures and supplies left behind.
 - The Debtor has already vacated the space and says the lease's costs outweigh any value it could get from assigning it