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Litigation Regarding the CARES Act's Paycheck Protection Program

As businesses take advantage of the forgivable loans offered by the Paycheck Protection Program ("PPP"), there has been an expected increase in PPP-related litigation. Since this trend is expected to continue well into the future, it is important for borrowers and lenders participating in the Program to seek guidance from the Small Business Administration ("SBA") and counsel as to the benefits and risks of PPP related loans.

On March 27, 2020, the \$2 trillion CARES Act was signed into law to curb COVID-19's impact on the U.S. economy. An integral component of the law was the creation of the Paycheck Protection Program to be administered by the SBA. Under the Program, \$349 billion in loans were authorized to assist eligible small businesses to maintain their payroll through the crisis. The loans are potentially forgivable under certain criteria. In addition to payroll expenses, PPP loan proceeds can be used to pay rent, utilities, and interest on mortgages. However, the forgiveness amount will decrease if a business's full-time headcount declines, or if the business decreases salaries and wages. Additionally, at least 75% of the forgiven amount must have been used for payroll expenses. For a more thorough review of the elements of the PPP forgiveness process, please see this article on [how to determine loan forgiveness for PPP](#) as well as this article about [the new rules and additional guidance for PPP](#).

The PPP proved to be very popular. It only took 12 days for the initial \$349 billion to be exhausted and many applicants were unable to secure loans. Many small businesses have alleged that large companies have been unduly prioritized by lenders, resulting in PPP-related litigation against lenders, the SBA, and the U.S.

Department of the Treasury. In response to the exhaustion of funds, Congress passed additional legislation, which the President signed, authorizing an additional \$310 billion in funds to be injected into the PPP.

The most common PPP-related cases concern the bank's prioritization of certain PPP applicants during the initial round of funding. The most important prioritization case to date is *Profiles, Inc. v. Bank of America Corp.*, No. SAG-20-0894, 2020 WL 1849710 (D. Md. April 13, 2020). On April 3, following the practice of most banks, Profile Inc.'s bank began accepting online applications for PPP loans. At the time, the bank only permitted applications from customers with a preexisting borrowing relationship with the bank. Although the plaintiffs had a longstanding depository relationship with the bank, the bank refused to accept Profile Inc.'s PPP applications because it did not have an existing borrowing relationship. The bank later amended its policy to permit its depository customers to apply for PPP loans, but on the condition that those customers did not have a borrowing relationship with any other bank. The district court held that the bank's policy was consistent with the CARES Act, and was permitted to prioritize its existing borrowers for PPP applications. However, the court's most important holding was that PPP loan applicants have no private right of action to bring civil suits against PPP lenders. If this decision is adopted by other courts, banks and financial institutions will have strong defenses against PPP applicants challenging lenders' prioritization of certain PPP applications.

While the expected effect of *Profiles, Inc.*, would be a decrease in PPP-related litigation, a plaintiff has recently found success in seeking a Temporary Restraining Order ("TRO") against a PPP lender. In *Hidalgo County Emergency Service Foundation v. Jovita Carranza*, No. 19-20497, 2020 WL 2029252 (Bankr. S.D. Tex. April 25, 2020), the court issued a TRO, reasoning that the plaintiff established a substantial likelihood of success on the merits on both its claims that (1) the SBA exceeded its statutory authority in stating that PPP loans will not be approved if the applicant is involved in any bankruptcy; and (2) the SBA violated the U.S. Bankruptcy Code in excluding applicants seeking bankruptcy relief. Additionally, the court found that granting the TRO was in the public interest because the plaintiff was a front-line health care provider. It is important to note, the court did not address the issue of whether a PPP applicant has a private right of action against a PPP lender.

Litigation has extended beyond prioritization claims to those of discrimination in violation of the Fifth Amendment and Administrative Procedure Act. In *Infinity Consulting Group, LLC v. United States Department of the Treasury*, No. GJH-20-981, 2020 WL 1985040 (D. Md. April 26, 2020), plaintiffs allege that when the Treasury Department and SBA implemented guidelines governing the first round of funding for the PPP, they knowingly and intentionally discriminated against minority-owned and women-owned businesses. The guidelines delayed when nonemployee businesses could apply for a PPP loan, which the plaintiffs alleged was discriminatory because minority and women-owned businesses are overwhelmingly nonemployer.

The court held that the plaintiffs were unlikely to succeed on the merits as to their race and gender discrimination claims, finding there was not enough evidence to show that a discriminatory purpose was a motivating factor in the defendants' actions. In particular, the court noted that a high percentage of non-minority businesses also did not have employees. Additionally, the court noted that the plaintiffs may not have suffered harm because of the additional \$310 billion in funding recently introduced to the Program.

Despite the recent wins by banks and government entities, an increase in PPP litigation is expected to continue well into the future. Applicants have complained that SBA guidance has been unduly slow thus impacting the approval of their applications. Furthermore, litigation is likely to result where borrowers' loans are not fully forgiven because the SBA did not sufficiently apprise borrowers of the risks in taking a PPP loan. Thus, it is important for borrowers and lenders to continuously seek guidance from the SBA and counsel as to the terms and conditions of PPP-related loans.

For more information, please contact [Peter Cummins](#), [Jared Tully](#), [Matthew Hart](#), or any other member of Frost Brown Todd's [Financial Services](#) Industry Team.

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