To: Honorable Members of the City Council
From: Vice Mayor Sophie Hahn (Author) and Mayor Jesse Arreguín (Author); Councilmembers Susan Wengraf (Co-Sponsor) and Kate Harrison (Co-Sponsor)
Subject: Save Our Small (SOS) Business Loan Fund

RECOMMENDATION
Refer to the City Manager to rapidly explore and, if feasible, pursue the creation of a special structured financial recovery loan fund to provide a supplemental source of capital for Berkeley small businesses impacted by the COVID-19 emergency. Among other considerations, the City Manager is requested to consider whether the City of Berkeley should act as a sponsor of the fund, working with one or more financial institutions to pool capital from private investors and the City of Berkeley to lower the risk of the product and support low interest rates. The City Manager is also recommended to partner with the Haas Business School at UC Berkeley to design terms of the SOS business loan fund and build the viability assessment model on which loan decisions would depend.

SUMMARY
The shutdown of large swaths of Berkeley’s economy in response to the COVID-19 pandemic has had severe consequences for small businesses and their workers. Although the City has taken quick and important action to create a relief fund, matched by additional philanthropic dollars, we lack the resources necessary to support the capital needs of Berkeley’s small businesses caught in the wake of COVID-19. State and Federal programs to assist small businesses, while helpful, are also likely to be insufficient. Private funding for loans is another important source of capital that the City of Berkeley should help make available to small businesses, on terms that are more accessible than traditional bank loans.

Prompted by a proposal from faculty and students at the Sustainable and Impact Finance Initiative at the Haas School of Business, the City of Berkeley should explore the creation of a public/private loan product to complement local, state and federal grants and loans, expanding options for small businesses to recover from the crisis. Supporting the rebuilding of Berkeley’s small business sector will strengthen and rebuild Berkeley’s economy over the long run and, by extension, its tax base; Berkeley should pursue all avenues to access and make available the means to rebuild this sector.
BACKGROUND
The outbreak of the COVID-19 pandemic, and subsequent orders to stay at home and practice social distancing, have significantly impacted Berkeley small businesses and their workers. As of March 13, 2020, many Berkeley small businesses had already seen a 25-75% drop in gross receipts since the outbreak began as compared to the previous year. Some small businesses, lacking the financial cushion to absorb such a steep loss of revenue, have closed, reduced services, or laid off workers.

On March 17, the City Council acted quickly to meet the crisis, referring to the City Manager the creation of a tax-exempt special fund of $3 million dollars to provide gap resources to small businesses, arts organizations, and renters significantly impacted by the COVID-19 emergency. Since the launch of the Berkeley Relief Fund, Berkeley has received more than $680,000 in grants and philanthropic donations to complement the city’s initial $3 million.

On March 30, the City announced the first phase of the Berkeley Relief Fund program; the Berkeley Business Continuity Grants, an allocation of $1 million to help mitigate COVID-19 related financial losses suffered by small businesses. Through this program, grants of up to $10,000 are available to Berkeley-based small businesses and nonprofits to enable continuity through and/or beyond the COVID-19 pandemic.

As of April 7, the Office of Economic Development had received over 1000 applications for relief through the Berkeley Business Continuity Grants program, testimony to the great number of needs in Berkeley. While the Fund continues to raise philanthropic donations and will provide vital assistance to hundreds of small businesses, it is clear that the needs of our local businesses will exceed the City’s capacity.

In addition, the State of California and the U.S. Small Business Administration (SBA) are providing financial assistance to small businesses impacted by COVID-19. While these programs should be helpful, they also do not have enough funds to support the medium-term recovery of all small businesses needing help in the State or nation. Nor are the cash funds immediately ready for distribution.

As Berkeley looks to the next phase of relief, it is crucial to put in place all possible measures to help sustain our small businesses as they recover from the COVID-19 shutdown. Private capital, which is more abundant than the amount of public capital that is likely to be made available locally or nationwide, can and should be a resource for viable small businesses. The City of Berkeley can play an essential role in assuring that private capital is brought forward to support our communities and that terms for repayment of debt are not so burdensome that they threaten long term viability of our local small businesses.

A proposal by faculty and students at the Sustainable and Impact Finance Initiative of the Haas School of Business at the UC Berkeley -- the Save Our Small (SOS) Business Loan Fund -- would create a product that the City of Berkeley could offer in tandem with
the Berkeley Business Continuity Grants program, as well as other public grant and loan programs. The initiative is led by a group of experts in the field of small business finance and economics at the Haas School, including Adair Morse, Associate Professor of Finance; Laura D. Tyson, Distinguished Professor of the Graduate School and Faculty Director at the Institute for Business and Social Impact; and Ben Mangan, Executive Director of the Center for Social Sector Leadership.

While many details remain to be explored, the basic elements of the proposed SOS Business Loan Fund are straightforward. Private investors would pool their capital with public dollars in a ratio based on the risk associated with loans to be made. Traditional bank loans to small businesses typically have a failure rate of at least 10%. Assuming a higher failure rate for loans to be made by the SOS fund (e.g., 20%), private investors would contribute approximately 80% of funds and the City of Berkeley would contribute approximately 20%. Loans from the SOS Fund would then be made to viable small Berkeley businesses, based on pre-agreed viability and loan criteria.

Repayment of the loans would go first to private investors, with the City’s claim for repayment subordinate. This arrangement would have the effect of providing a deep cushion or “guarantee,” allowing the City (or another public agency — possibly the State) to provide a great deal of security to private investors and make possible very low interest rates for borrowers; likely between 0 and 2%.

While the City would take a significant risk with respect to these loans, participation as a quasi-guarantor in the loan pool would also support the availability of significantly more capital than the City could ever deploy on its own. In the above scenario, each Berkeley dollar invested in the fund would be matched 4:1. Should the City, for example, be able to invest $3 million, private investors would provide an additional $12 million, creating a fund with a total of $15 million available to lend to local businesses.

The City’s most significant benefit from creation of, and participation in, the loan fund would be the long-term positive impacts on the local economy and, by extension, the City’s tax base. The upside for private investors would be capped at one-time repayment of their loaned capital, with interest. By contrast, while the City may be repaid for some (but not likely all) of its own relatively small amount of loaned capital and interest, it will reap 100% of the long term benefits of the full $15 million in local investments, in perpetuity.

RECOMMENDATIONS FOR IMPLEMENTATION
The City Manager should work with partners at UC Berkeley’s Haas School of Business and other experts to evaluate the cost/benefit to local businesses, and to the City of Berkeley, of implementing an SOS Loan Fund based on this proposal, while pursuing a variety of relationships and structures that would support creation of such a Fund. Should the analysis show strong value in establishing the SOS Loan Fund, and viable

---

1 https://fsmbusiness.com/sba-statistics-lending/#California
relationships and structures be developed, the City Manager should move forward to create the SOS Loan Fund as quickly as possible.

FISCAL IMPACTS
This item is a referral to explore creation of a new low-interest loan product to support Berkeley’s small businesses as they recover from the economic crisis created by COVID-19. The only costs associated with the item at this time are staff time to rapidly explore and, if feasible, pursue the creation of a special structured financial recovery loan fund.

Should the City Manager determine that creation of the SOS Business Loan Fund is feasible and in the interests of the City, monies may be allocated to the fund through the budget process by the City Council. The amount of funds proposed for allocation to the SOS Business Loan Fund and the risk associated with repayment of loans will be determined and proposed by the City Manager. Should the fund be launched, and significant private capital attracted to leverage the City’s investment, the City will benefit from repayment of some of its loaned capital and from the full combined public/private investment in restoration of the City’s economic sector, preserving and enhancing the City’s tax base and financial viability over the long term.

CONTACT INFORMATION
Vice Mayor Sophie Hahn, Council District 5, 510-981-7150 (ofc); 510-682-5905 (cell)

ATTACHMENTS
1. Save-our Small (SOS) Business Loan Fund - A Proposal from the Sustainable and Impact Finance Initiative, Haas School of Business, University of California, Berkeley Professors Adair Morse, Laura Tyson, and Ben Mangan
2. Letter from the Berkeley Chamber, Downtown Berkeley Association, Telegraph Business Improvement District and Visit Berkeley