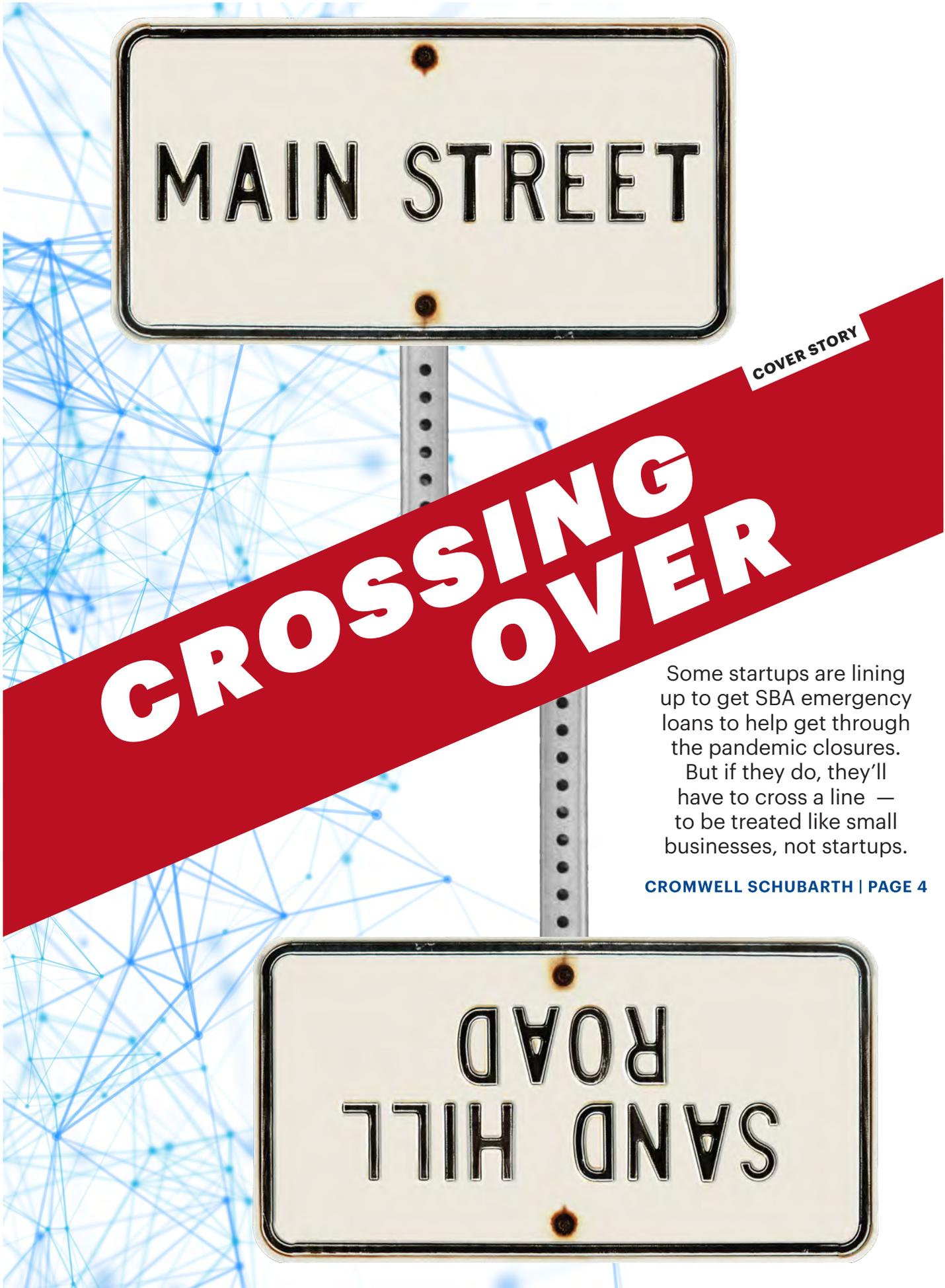


## Gear shift

Jim Leale Jr. finds opportunities to help amid pandemic fears

LYNN PEITHMAN STOCK, 23



COVER STORY

# CROSSING OVER

Some startups are lining up to get SBA emergency loans to help get through the pandemic closures. But if they do, they'll have to cross a line — to be treated like small businesses, not startups.

CROMWELL SCHUBARTH | PAGE 4

### MUST KNOW

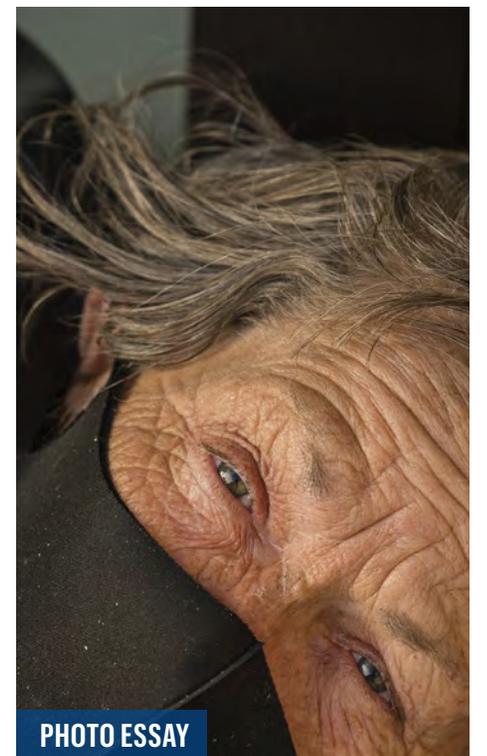


### Uncertainty is the new watchword

Ramsey Daya of Newmark Knight Frank says real estate deals are getting harder to close as more lenders pull back to protect themselves. **MATTHEW NIKSA, 10**

### Vehicular backfire

People are driving less and buying less gas — here's why that might not be a good thing for Silicon Valley roads. **JODY MEACHAM, 12**



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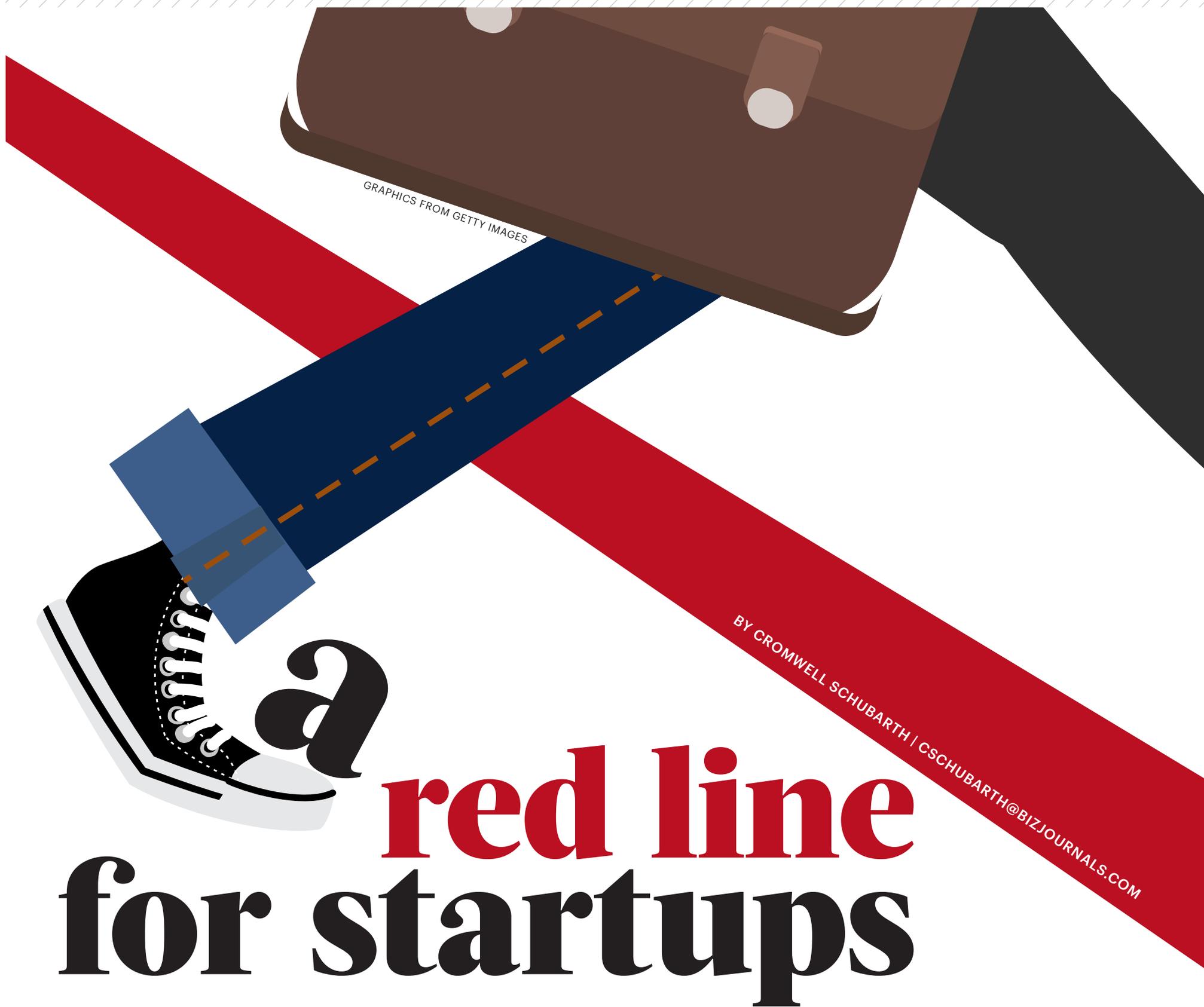
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## COVER STORY



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# a red line for startups

SMALL BUSINESSES ARE RACING TO GET EMERGENCY SBA LOANS TO KEEP THEIR WORKERS PAID. SHOULD STARTUPS JOIN THE RUSH? IT'S COMPLICATED.

Venture-backed startup founders and mom-and-pop business owners usually operate in entirely different universes.

But in the age of COVID-19, thousands of them have sought to avert job cuts – or even shutting down – by getting help from the same source: the Small Business Administration. That's the traditional place where businesses that are considered too risky for banks to lend to without government guarantees go for small business loans.

Nearly \$350 billion made available in an emergency Paycheck Protection Program because of the pandemic, though, is erasing a red line that VC-backed businesses have largely refused to cross until now.

On one side of that line are the barber shops, restaurants and store owners

who do their banking on Main Street. On the other are the tech and online startups that are financed by venture capital firms, many of which are based around Sand Hill Road in Menlo Park and Palo Alto.

That's raising questions about whether founders who raise millions and think in terms of one- or two-year "runways" before running out of cash belong in the same program as small businesses who often need regular cash flow to get them to the next month.

Even if the answer to that question is "yes," it also raises questions about whether it makes sense for startup founders to seek the SBA loans. And even if they decide to go for it, will there be money left in PPP by the time the startup-focused banks they usually work with process their applications?

## Are VC-backed startups SBA businesses?

Congressman Ro Khanna, who represents a significant slice of Silicon Valley, believes venture-backed companies deserve a share of the \$350 billion that have been made available in the PPP program.

"The country stands to lose hundreds of thousands of jobs at the moment we need innovation and entrepreneurial ingenuity the most," the Democratic lawmaker, who is now in his second term, told the Business Journal. "Startups can't get left behind as the nation moves through the ongoing public health crisis."

Khanna joined forces with House Speaker Nancy Pelosi, who represents San Francisco in Congress, to make access to the SBA program for startup

founders a part of the \$2 trillion Coronavirus Aid, Relief, and Economic Security (CARES) Act.

The pandemic has caused the loss of more than 23,000 jobs at over 200 venture-backed U.S. businesses between March 11 and April 14, according to the Layoffs.fyi website that has been tallying the daily toll. About a quarter of those job losses were attributed to startups based in the Bay Area.

Khanna also backs adding hundreds of millions more to the PPP program, as well as opening more SBA programs to venture-backed businesses in the future.

"I support increasing funding for SBA programs, as well as ensuring that startups have access to these small business relief programs," he said. "We have seen some progress in the additional clarification issues by Treasury, but more must be

done to ensure startups can access the relief they need to keep workers on their payrolls.”

The National Venture Capital Association also lobbied for including startups backed by its members in PPP: “It’s not about the companies. It’s about the jobs,” said Justin Field, senior vice president of government affairs at NVCA.

“Workers at startups are every bit as vulnerable as workers at other types of small businesses across the country,” Field said. “I don’t see any reason why there should be a delineation between trying to protect jobs at innovative companies with equity backing versus other types of small businesses that are independently owned.”

**Weighing the risks**

The pandemic-induced business shutdown came at a time that angel and

seed investing had already dropped to its lowest level in the first quarter since early 2013, according to the Venture Monitor report. The appearance of a lifeline as business abruptly disappeared and venture funding becomes harder to win has reportedly attracted lots of founder interest and applications for loans from the startup community.

“We saw about 180 or 190 posts asking questions about PPP in the space

of a few days when startups were made eligible for the program,” said Joseph Huang, CEO of StartX, a Stanford University-affiliated accelerator. “Nobody ever thought that figuring out how to do an SBA loan would be one of the things that you would need to figure out how to do as a founder.”

Mark Suster of Upfront Ventures said in a blog that he fielded a flood of questions from founders about the program: “There is so much confusion and misinformation out there about the government sponsored ‘payroll protection plan’ loans to companies that the heads of every small business CEO in the country must be spinning,” he wrote.

One question he recounted was, “I am hearing from all of my peers that everybody’s applying – shouldn’t I?”

“The short answer is ‘no,’” Suster wrote. “Applying for a government loan that was created to serve U.S. small businesses and employees in the times of an economic crisis is not something you should do just because your peers are telling you that you should. It is not ‘free money.’”

Amit Bhatti, a principal at the 500 Startups accelerator, said two key questions are whether a business has a high payroll cost and whether its investors are willing to relinquish some control.

“This is really most helpful to companies that have high payroll costs, and that is what is causing them trouble right now,” Bhatti said, adding that there has been a lot of interest in PPP from 500 Startups’ founders. “If revenue is going to zero and you have a high payroll that you need to keep going, that is a perfect scenario for getting a PPP loan.”

Two big deterrents that kept venture-backed startup founders from turning to the SBA for help are “affiliation” rules and personal liability, he said.

SBA loans are for businesses with fewer than 500 employees. Startups that have an investor who holds positions in companies that collectively employed more than that number were previously ineligible for SBA loans under the affiliation rule, if they could also block a founder from doing what they want.

Founders are now

**WHAT IS PPP?**

The Paycheck Protection Program of the U.S. Small Business Administration was created to help entrepreneurs avoid job cuts during the COVID-19 pandemic. There was about \$350 billion allocated to it, which was expected to be fully committed by Friday. A \$250 billion addition to that allocation has been proposed. Here are the basics of the program:

- ▶ The loan is designed to protect workers from losing their jobs.
- ▶ A business can apply to get 2.5 times its average monthly payroll cost from the prior year, up to \$10 million.
- ▶ Only \$8,333 of the salaries of employees who earn over \$100,000 a year can be applied to the PPP calculation.
- ▶ Businesses can be forgiven up to eight weeks of payroll, rent and utilities from the time of origination (or up to June 30). The rest is treated as a loan.
- ▶ The amount of the loan will be reduced if the business cuts jobs or reduces salaries.
- ▶ As of Monday, California businesses had been approved for more than 54,922 PPP loans that are worth a combined \$20.85 billion.

allowed to get SBA loans if their investors agree to relinquish that control. PPP loans don’t make the founders personally liable for their debt, either, another factor that previously kept them from away from seeking SBA loans.

“It was prohibitive for a startup founder who is working on a risky idea and has to make a personal guarantee on these loans,” Bhatti said.

In the end, though, he said the transparency of taking an SBA loan may be the biggest hurdle.

Founders should ask themselves if they could defend taking a PPP loan if called before Congress to do so, he said.

“If you can very clearly and with no shame say you have been affected by the pandemic, clearly you should be looking into this,” he said. “If you are a remote video conferencing company – a type of business that has been boosted by all of this – you shouldn’t.”

**First come, first served**

A venture-backed founder who decides that it is OK to stand in the PPP line with Main Street business owners has one last hurdle to overcome in the way the program was designed.



Ro Khanna

Most of them bank with financial institutions like Silicon Valley Bank and First Republic that tailored their services to businesses that didn’t need or want an SBA loan. So these banks have had to create units on the fly to serve the new demand at a time when their staffs are working from home.



Joseph Huang

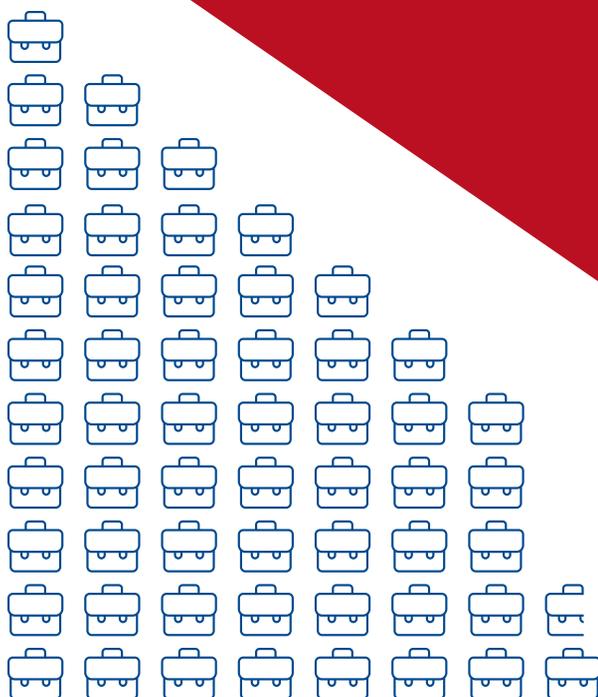
A number of venture-backed founders complained that since PPP was designed to get money committed as fast as possible, the days it took their banks to get their programs up and running put them at the end of the line when there may not be money left.

“We saw a lot of the non-traditional lenders and fintechs get involved, to help in these situations,” Bhatti of 500 Startups said. “Companies like Lendio and Womply helped thousands of founders by taking PPP applications and shopping them around to lenders.” (500 Startups is an investor in San Francisco-based Womply.)

NVCA government affairs expert Field said there is likely to be another round of funding added to the PPP program that was expected to run dry by Friday.

Both parties in Congress want to add another \$250 billion to PPP. That’s been held up by demands from Democrats for another \$250 billion to be added for states, hospitals and emergency services, as well.

“There should pretty soon be follow-on funding for these businesses,” he said. ✎



SOURCE: LAYOFFS.FYI