

CITY OF OAKLAND
AGENDA REPORT

FILED
OFFICE OF THE CITY CLERK
OAKLAND
2007 DEC 26 AM 10:17

TO: Office of the City Administrator
ATTN: Deborah Edgerly
FROM: Community and Economic Development Agency
DATE: January 8, 2008

RE: **A City Council Resolution Approving the Issuance of an Unsecured Loan Guaranty not to exceed Thirteen Thousand Five Hundred Dollars (\$13,500) for McKinney Griff, Inc., dba Merritt Bakery and Restaurant, As Required by One California Bank Under Its Conditions of Approval for a Two Hundred Seventy Thousand Dollars (\$270,000) Term Loan To Finance Business Expansion.**

SUMMARY

The City of Oakland has received a request by the principals of McKinney Griff, Inc., Charles and Patricia Griffis, to provide OneCalifornia Bank ("OCB") located at 1438 Webster Street, Oakland, with a loan guaranty in an amount not to exceed \$13,500. OCB has approved a 7-year term loan in the amount of \$270,000 to provide McKinney Griff, Inc., with business expansion capital for the Merritt Bakery and Restaurant ("the Merritt"). Funds will be used to purchase new restaurant equipment and provide working capital for marketing and new employee hires.

Nor-Cal State Guaranty Program has provided OCB with a loan guaranty covering 90% of the principal loan amount. The City is being asked to guaranty 5%, or \$13,500. These guaranties are required by OCB prior to funding as McKinney Griff, Inc. lacks sufficient collateral as a secondary repayment source to support the loan. OCB will take a first security interest in all equipment purchased with these loan funds, as well as a blanket security interest in all other business assets.

The City's loan guaranty will be secured by a Uniform Commercial Code (UCC-1) filing on all business assets. This filing with Alameda County will secure all business assets of McKinney Griff, Inc. and the Merritt Bakery as a possible repayment source in the event the loan guaranty is exercised by OCB. The City will also require a personal loan guaranty provided by Patricia Griffis and Charles Griffis, the principal owners of McKinney Griff, Inc. In the event of loan default, any expenses or losses associated with the loan will be allocated *pari-passu* among the State Loan Guaranty, City Loan Guaranty, and OCB participants. In any event, the City's commitment will never exceed \$13,500.

Staff recommends that the City Council approval this resolution to provide a loan guaranty as requested, supporting one of Oakland's largest retail employers to secure and expand its operations.

Item: _____
CED Committee
January 8, 2007

FISCAL IMPACT

Approval of this resolution will authorize the City Administrator to execute a Loan Guaranty with OCB, in favor of McKinney Griff, Inc., in an amount not to exceed \$13,500. Funds to cover the loan guaranty will be encumbered from the following source: HUD-CDBG (2108), One Stop Small Business (88579), Miscellaneous Contract Services (54919), OBDC Program Delivery Cost (G02200).

These funds can only be drawn upon by OCB in the event of default by their borrower, McKinney Griff, Inc. The City will share liability on a pro-rata basis with the Bank (5%), Nor-Cal State Loan Guaranty (90%) for the entire indebtedness during the entire term of the loan, including all accrued unpaid interest of the indebtedness and all collection costs, expenses and attorney fees; however, at no time will the City's liability exceed \$13,500. The loan guaranty will be secured by a blanket UCC-1 filing on all business assets; the City will be third in line behind the Small Business Administration and a shared UCC-1 filing between Nor-Cal State Loan Guaranty and OCB.

BACKGROUND

General Description

Since 1952, The Merritt Bakery and Restaurant has operated at 203 E. 18th Street in Oakland. The current owner, McKinney Griff, Inc., acquired the Merritt in 1998 after the previous owner allowed the business to fall into serious disrepair and near bankruptcy.

Since this initial acquisition, the Merritt has weathered the effects of the 2001 recession, the construction impact of the adjacent Albertson's store (2003 – 2005), and an electrical roof fire in February 2006. Sales are once again nearing 2001 levels, and the company has been consistently profitable each month since December 2006.

The Merritt owners report that they employ 86 full-time and part-time employees, 75% of whom are Oakland residents. Seventeen have been employed there for 15 to 40 years. The Merritt's owners report its kitchen, restaurant, bakery and office staff is paid at living wage levels (staff did not examine payroll to verify). The Merritt's owners informed staff that they have established a work program for high school students, as well as a scholarship program for college and college-bound employees.

Legal Structure and Ownership

The Merritt is owned by McKinney Griff, Inc., a California corporation created in 1998 for the purpose of purchasing and operating the Merritt. The principals of this corporation, Patricia Tyler Griffis and Charles Griffis, have 70 years of combined business management experience. Their

Item: _____
CED Committee
January 8, 2007

extensive fast food and restaurant operational experience include Popeye's Famous Fried Chicken, Chicken Charlie's, and McDonald's. Ms. Griffis manages the strategic direction of the organization, while Mr. Griffis is responsible for daily operations, finance, business development and staff training.

See Attachment A for additional information on the company's finances and expansion plans.

KEY ISSUES AND IMPACTS

1. The City does not provide business loan guaranties as a matter of course. This request is made to support an historic Oakland business that currently has over 80 employees, generates \$4,000-\$5,000 annually in Business License Tax, provides valuable products and services in an economically expanding and ethnically diverse Oakland neighborhood, and requires this assistance to meet its business expansion goals.
2. Patricia and Charles Griffis, the current owners, have managed to keep the Merritt a going concern through difficult times. This loan guaranty offers the City an opportunity to ensure that the economic, social, and quality-of-life benefits offered by the Merritt continue and expand into the future.
3. OneCalifornia Bank Loan: McKinney Griff, Inc. has successfully self-funded the capital needs of the Merritt, replacing obsolescent and deteriorated furniture, fixtures and equipment, and offsetting revenue losses through refinancing of personal real estate. Past attempts to secure traditional business financing have been unsuccessful due to the ongoing net losses of the Merritt from 2004 through 2006. Since these losses have been financed through increased debt on most of Patricia and Charles Griffis' investment properties; insufficient equity remains in the properties to secure either the OCB loan or the State Loan Guaranty.
 - OneCalifornia Bank recently moved its headquarters to Oakland, occupying the former Oakland Athletic Club building on Webster Street. The subject loan to McKinney Griff, Inc. is an example of OneCalifornia Bank's commitment to serving growing businesses in Oakland. The Merritt's recent history of net revenue losses and lack of sufficient equity margins in business and personal assets to use as loan collateral rendered the Merritt unqualified for traditional financing until OneCalifornia Bank's commitment.
 - The \$270,000 loan commitment from OCB, which has funded \$80,000 to date, is based upon the Merritt's history of management expertise (especially given the Merritt's circumstance-driven economic challenges since 2001); excellent credit

Item: _____
CED Committee
January 8, 2007

history of the company despite the revenue challenges and existing debt; the Merritt's return to net profitability in 2007; plus the 90% loan guaranty provided by a Nor-Cal State Loan Guaranty (already approved) and the yet-to-be approved 5% loan guaranty by City of Oakland. The Bank's 5% loan liability not covered by the loan guaranties will be collateralized by the new equipment to be purchased through the loan funds.

- The Nor-Cal State Loan Guaranty will be secured through a UCC-1 filing (second position behind the Small Business Administration) and a 2nd Deed of Trust on the Griffis' personal residence. There is no remaining viable equity in any of the Griffis' other real estate assets.
 - The City's Loan Guaranty will be secured by a blanket UCC-1 filing behind the SBA and Nor-Cal State Loan Guaranty/OCB and a personal guaranty from Patricia Griffis and Charles Griffis.
4. Financial risk to the City of Oakland: Approval of the proposed loan guaranty for McKinney Griff, Inc. subjects the City to the financial risk of default by the company and the subsequent request by OCB that the City reimburse its loan loss according to the following terms:
- The loan is payable over seven years, payable monthly, and fully amortized over the term of the loan. As a result, the City's principal risk declines over the loan term.
 - Any losses associated with this loan (principle, interest, legal fees, etc.) will be allocated *pari-passu* among all three parties at risk; that is, the Nor-Cal State Loan Guaranty will assume 90% of any loss, the City of Oakland will be responsible for 5% of any loss (not to exceed \$13,500), and the Bank is at risk for 5% of any loss.
 - Both the State and City loan guaranties must remain in effect for the full seven-year term of the loan.
 - Should the loan go into default, the City's loan guaranty will be secured by a 3rd tier security interest in the business assets (it is unlikely that this will provide a viable repayment source) and a personal guaranty from Patricia and Charles Griffis. This guaranty would allow the City to pursue repayment from the Griffis' that is not restricted to liquidation of specific collateral.

The Bank has determined:

- That this loan to the Merritt presents a reasonable risk for the reasons identified above.
- Cash flow from the business (primary repayment source) is adequate to meet the monthly loan repayment schedule.

Item: _____
CED Committee
January 8, 2007

- There is insufficient collateral to provide the Bank with a secondary repayment source should the Merritt re-experience cash flow shortfalls. Accordingly the State and City guaranties are required to provide the Bank with an adequate secondary repayment source.

Should the City Council choose not to approve the requested loan guaranty, the loan amount would be reduced by \$13,500, forcing the Merritt to cut back in its expansion plans. Working capital funds in the amount of \$80,000 have been disbursed to date.

PROGRAM DESCRIPTION

Merritt Restaurant and Bakery Expansion Plans

To better accommodate ongoing neighborhood changes and the anticipated increase in local and regional traffic to the Lake (see Attachment for details), McKinney Griff, Inc. plans a Two-Phase expansion of the restaurant products, service and facility.

1. *Phase One:* The subject term loan from OCB will provide Merritt with funds for the purchase and installation of new equipment and for working capital.
2. *Phase Two:* Renovation of the Merritt, for which funding has not yet been identified, is to include:
 - Expansion of window area directly facing Lake Merritt
 - Restructure the kitchen and server layouts
 - Continued modernization of the kitchen equipment and furnishings
 - Replace the restaurant tables
 - Upgrade the flatware, glassware and tableware
 - Construction/renovation costs are estimated at \$300,000, based upon a representative bid received from one contractor. Staff did not receive cost estimates for the new furniture and equipment identified for this phase.

Once all expansion phases are complete, it is the intention of Merritt's management to expand its hours of operation to 24 hours a day, seven days a week, representing a 24.4% increase in overall operating hours. Up to 20 new employees could be hired, including 10 restaurant and 10 bakery staff. Remodeling would increase productivity as more customers could be served using less labor per table.

Item: _____
CED Committee
January 8, 2007

As part of the City's commitment to support thriving and expanding locally-owned businesses, the Economic Development and Redevelopment staff will work with McKinney Griff, Inc. to (1) determine the specific expansion needs and costs for Phase II and (2) identify potential City and Redevelopment resources that could be used to assist and leverage Merritt's expansion and additional job creation opportunities.

SUSTAINABLE OPPORTUNITIES

Economic: The opportunity to retain and potentially expand a long-standing, iconic Oakland restaurant and bakery business that currently employs 86 full-time and part-time people. The business generates \$4,000-\$5,000 annually in Oakland business license tax. Approximately 75% of the Merritt's employees are Oakland residents.

Environmental: No significant environmental opportunities are noted.

Social Equity: The Merritt provides a quality dining experience and baked goods in a neighborhood that has significant ethnic diversity (primarily African American, Asian and Hispanic), and is experiencing increased investment and improving economic demographics. McKinney Griff, Inc., the Merritt's parent company, is a woman-owned, African American business, and one of Oakland's largest retail employers.

DISABILITY AND SENIOR CITIZEN ACCESS

The Merritt is fully compliant with all ADA access requirements.

RECOMMENDATION(S) AND RATIONALE

Staff recommends that the City Council approve the attached resolution authorizing the issuance of a Loan Guaranty not to exceed \$13,500 for McKinney Griff, Inc., dba Merritt Bakery and Restaurant, as required by One California Bank under its Conditions of Approval for a \$270,000 Term Loan to finance business expansion.

This recommendation is made based upon the existing and potential economic and social benefits to the City of Oakland in supporting the expansion of a 55-year Oakland restaurant and bakery.

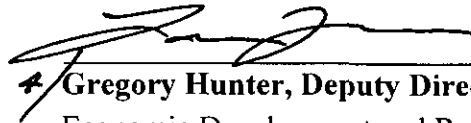
Item: _____
CED Committee
January 8, 2007

OCB has determined that the primary repayment source (cash flow from the business) is viable, and the preponderance of risk related to the secondary repayment (liquidation of collateral and/or the loan guaranties) has been assumed by the State of California through the Nor-Cal Loan Guaranty. The City of Oakland's financial risk will never exceed \$13,500, and will diminish over the seven-year loan term as this fully amortized loan is repaid.

ACTION REQUESTED OF THE CITY COUNCIL

Staff recommends that the City Council approve the resolution authorizing the issuance of an unsecured Loan Guaranty not to exceed \$13,500 for McKinney Griff, Inc., dba Merritt Bakery and Restaurant, as required by One California Bank under its Conditions of Approval for a \$270,000 Term Loan to finance business expansion.

Respectfully submitted,



Gregory Hunter, Deputy Director
Economic Development and Redevelopment,
Community and Economic Development Agency

Reviewed by:
Aliza Gallo, Urban Economic Coordinator
Business Development Unit

Prepared by:
Deborah V. Acosta, Urban Economic Analyst III
Business Development Unit

APPROVED AND FORWARDED TO THE
COMMUNITY AND ECONOMIC DEVELOPMENT COMMITTEE:


OFFICE OF THE CITY ADMINISTRATOR

Item: _____
CED Committee
January 8, 2007

Financial Summary

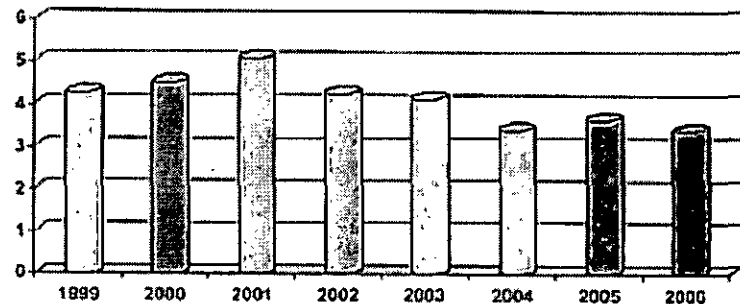
Company financial statements show that from December 1998 to September 2001, the Merritt’s sales grew from \$2 million to over \$5 million in annual sales. The period following September 11, 2001 exhibited a modest but noticeable decline in monthly sales through 2002. However, the Merritt continued to post profits both years.

In October 2003 the adjacent Albertson’s store, which shares a shopping center with the Merritt, began a comprehensive renovation project with an expected completion date of September 2004. The 11-month project actually took 27 months and was completed in August 2005. This renovation project limited customer access to much of the shared parking lot, leaving Merritt customers a minimal number of the original 265 parking spaces during the renovation period¹.

Finally, an electrical fire in the Merritt’s roof in mid-year 2006 resulted in the business working through internal re-construction issues, impacting sales and cash flow for the store through the remainder of the year.

As illustrated by the graph to the right, the Merritt’s gross revenues continued to be negatively impacted through 2006.

**Merritt Restaurant & Bakery
Annual Gross Revenue
(\$ in Millions)**



Financial statements show that the Merritt has returned to consistent monthly profitability, a trend that began in December 2006. Between April and June of 2007, net profitability before taxes increased 82%, from \$22,617 to \$40,422. Through August 2007 (8 months), net profits before taxes exceeded \$93,000, more than enough to meet the debt requirements of the loan approved by OCB.

Gross revenues between 2006 and 2007 have increased 27% when compared on an annualized basis. A return to profitability has been achieved, not solely through increased revenues, but also through a managed reduction in costs of goods sold and operating expenses between 2006 and 2007, as evidenced by the following year-to-year financial comparisons:

¹ According to the company’s 2007 business plan, only 20 spaces were available to customers during the construction period.

**Merritt Restaurant & Bakery
2004 - 2009 Financials Comparisons Summary**

	2004 (Actual)	2005 (Actual)	2006 (Actual)	2007 (6 Months Actual, 6 Months Projected)	2008 (12 Months Projected)	2009 (6 Months Projected)
Total Sales (in dollars)	\$4,345,412	\$3,621,581	\$3,366,518	\$4,910,962	\$5,424,481	\$2,629,132
COGS - Restaurant & Bakery Food/Supplies (% of sales)	34.7%	23.8%	24.9%	21.8%	26.0%	26.0%
COGS - Restaurant & Bakery Labor Cost (% of sales)	30.9%	41.8%	48.9%	40.5%	36.1%	36.1%
TOTAL COGS (% of sales)	65.6%	65.6%	73.8%	62.3%	62.1%	62.1%
Gross Profit (% of sales)	34.4%	34.4%	26.2%	37.7%	37.8%	37.9%
Total Expense (% of sales)	41.6%	46.2%	43.6%	36.9%	32.8%	31.8%
Net Other Income (% of sales)	4.4%	2.1%	12.3%	3.8%	6.1%	6.1%
Net Income (% of sales)	-2.8%	-9.8%	-5.1%	4.6%	11.2%	12.3%

Financial projections reasonably anticipate maintenance of these spreads, with increased operating efficiencies (lower repair expenses) due to the anticipated replacement of older equipment through the OCB loan proceeds.

Revenue Sources

Eighty percent of the Merritt's revenue is derived from restaurant, bakery and catering sales. In the first half of 2007, percentage of sales for each revenue source averaged as follows:

- Restaurant sales → 65%
- Bakery → 16%
- Lottery & Scratchers → 19%
- Potential Growth Areas → Primarily catering. The company plans to expand this line of business.

In addition to these revenue sources, several local doughnut and bakery shops purchase some of their products from the Merritt for sale in their retail shops. As a result, Merritt Bakery owners are examining the potential profitability of expansion into the wholesale bakery business.

Neighborhood Characteristics

Expansion plans intend to capture the economic benefits of changing neighborhood conditions, including:

- *The Lake Merritt Park Master Plan (Measure DD)*: Approved by the City Council in 2002 and funded by bond issuance approved by Oakland voters under Measure DD, the Lake Merritt Master Plan will enhance the beauty, safety and use of Lake Merritt. The project is expected to increase foot, motor and bicycle traffic to the area, which will increase traffic to the Merritt as it is, at present, the only restaurant located adjacent to the Lake.
- *Changing Demographics*: There are dramatic demographic changes taking place within a 15-minute drive-time around the Merritt², with a large increase in the Asian and Hispanic populations recorded through the U.S. Census between 1990 and 2000 (23% and 49%, respectively) with further increases projected through 2012.

Similarly, changes are taking place for Household Incomes within a 15-minute drive time of the Merritt:

HH Income Categories	1990		2000		2007		2012		Percent Change	
	Census	%	Census	%	Estimate	%	Projection	%	1990 to 2000	2007 to 2012
\$0 - \$15,000	52,005	25.5%	37,088	17.4%	31,381	14.9%	29,037	13.8%	-28.7%	-7.3%
\$15,000 - \$24,999	34,573	16.9%	24,789	11.6%	20,539	9.8%	19,364	9.2%	-28.3%	-6.0%
\$25,000 - \$34,999	31,540	15.2%	25,063	11.8%	20,722	9.8%	17,343	8.2%	-19.3%	-16.3%
\$35,000 - \$49,999	33,249	16.3%	32,469	15.2%	28,427	13.5%	26,672	12.6%	-2.3%	-6.2%
\$50,000 - \$74,999	29,504	14.5%	37,830	17.8%	37,047	17.6%	36,924	17.5%	28.2%	-0.3%
\$75,000 - \$99,999	12,072	5.9%	21,828	10.2%	24,425	11.6%	24,103	11.4%	80.9%	-1.3%
\$100,000 - \$149,999	7,498	3.7%	19,964	9.4%	25,575	12.1%	29,395	13.9%	166.3%	14.9%
\$150,000 +	4,199	2.1%	14,074	6.6%	22,565	10.7%	23,097	13.3%	235.2%	24.5%
Average Hhld Income	\$40,057		\$61,648		\$89,248		\$76,251		53.9%	10.1%
Median Hhld Income	\$29,807		\$43,377		\$52,220		\$57,843		45.5%	10.6%
Per Capita Income	\$16,036		\$23,844		\$27,369		\$29,931		46.7%	9.4%

The growing household income levels and changing food tastes resulting from the changing ethnic populations are creating a greater demand for local restaurants that offer a varied food menu, quality, cleanliness, service and value, characteristics that the Merritt owners take pride in providing.

² DemographicsNow.com, December 7, 2007

2007 DEC 26 AM 10:17

OAKLAND CITY COUNCIL

RESOLUTION No. _____ C.M.S.

INTRODUCED BY COUNCILMEMBER PAT KERNIGHAN

A City Council Resolution Approving the Issuance of a Loan Guaranty not to exceed Thirteen Thousand Five Hundred Dollars (\$13,500) for McKinney Griff, Inc., dba Merritt Bakery and Restaurant, As Required by One California Bank Under Its Conditions of Approval for a Two Hundred Seventy Thousand Dollars (\$270,000) Term Loan To Finance Business Expansion.

WHEREAS, the Merritt Bakery and Restaurant (Merritt Bakery), with its location at 203 East 18th Street directly adjacent to Lake Merritt, has been in operation for fifty five years in the City of Oakland, is one of Oakland's largest retail employers, and has a special place in the minds and hearts of many Oakland residents and visitors; and

WHEREAS, the current owner, McKinney Griff, Inc., has invested in and guided the business through significant economic challenges, including a roof fire in 2006, over the past 27 month period of time; and

WHEREAS, Merritt Bakery is now ready to manage an expansion of the store, intended to increase both the profitability of the operation and the number of full and part time employees working there; and

WHEREAS, Merritt Bakery desires to borrow \$270,000 from OneCalifornia Bank, FSB, located at 1438 Webster St., Suite 100, Oakland, and currently has sufficient cash flow to pay the debt service on the loan, but lacks adequate collateral as a secondary repayment source; and

WHEREAS, approval of the private, 7-year term loan from OneCalifornia Bank is contingent upon the Bank's receipt of two loan guaranties covering 95% of the loan amount, including a 5% loan guaranty from the City of Oakland in an amount not to exceed \$13,500, and a 90% Nor-Cal State Loan Guaranty; and

WHEREAS, McKinney Griff, Inc. has requested that the City provide a loan guaranty of \$13,500 for seven years, plus extension periods, so that it may access the Bank loan; and

WHEREAS, approval of this guaranty provides the City the opportunity to retain and expand a long-standing, iconic Oakland restaurant and bakery business that currently employs 86 full-time and part-time people, 75% of who are Oakland residents, and generates \$4,000-\$5,000 annually in Oakland business license tax; and

WHEREAS, the loan guaranty will be secured by a UCC-1 filing on all business assets and the personal loan guaranties of Patricia Griffis and Charles Griffis, the principal owners of McKinney Griff, Inc.; and

WHEREAS, no other reasonable means of private or commercial financing of the loan guaranty, other than the City's Small Business loan fund, has been identified; and

WHEREAS, the requirements of CEQA, the CEQA Guidelines as prescribed by the Secretary for Resources, and the provisions of the Environmental Review Regulations of the City of Oakland have been satisfied; now, therefore, be it

RESOLVED: That the City Administrator is authorized to negotiate and execute a Loan Guaranty with OneCalifornia Bank, FSB, in favor of McKinney Griff, Inc., in an amount not to exceed \$13,500; and be it

FURTHER RESOLVED: That the City Administrator or her designee is hereby authorized to approve any subsequent amendments to, or extensions of, said Loan Guaranty except those involving compensation or the allocation of additional funds; and be it.

FURTHER RESOLVED: That City funds totaling \$13,500 will be encumbered for payment of said Loan Guaranty in the event of default of the loan extended by OneCalifornia Bank to McKinney Griff, Inc. as follows: HUD-CDBG (2108), One Stop Small Business (88579), Miscellaneous Contract Services (54919), OBDC Program Delivery Cost (G02200); and be it

FURTHER RESOLVED: That the City loan guaranty will be secured by a UCC-1 filing on all business assets and the personal loan guaranties of Patricia Griffis and Charles Griffis, the principal owners of McKinney Griff, Inc.;

FURTHER RESOLVED: *City funds can only be drawn upon by OneCalifornia Bank in the event of default by their borrower, McKinney Griff, Inc. The City will share liability on a pro-rata basis with the Bank (5%) and Nor-Cal State Loan Guaranty (90%) for the entire indebtedness during the entire term of the loan, including all accrued unpaid interest on the indebtedness and all collection costs; however, at no time will the City's liability exceed \$13,500; and be it*

FURTHER RESOLVED: That the City Council had independently reviewed and considered this environmental determination, and the City finds and determines, based upon the information provided in the staff report accompanying this Resolution, that this action complies with CEQA because the project is exempt from CEQA pursuant to Section 15301 (existing facilities) of the CEQA Guidelines; and be it

FURTHER RESOLVED: That the City Attorney shall review and approve as to form and legality, all agreements related to the Guaranty, and all such agreements shall be filed with the City Clerk.

IN COUNCIL, OAKLAND, CALIFORNIA, _____, 2008

PASSED BY THE FOLLOWING VOTE:

AYES- BROOKS, BRUNNER, CHANG, KERNIGHAN, NADEL, QUAN, REID and
 PRESIDENT DE LA FUENTE

NOES-

ABSENT-

ABSTENTION-

ATTEST: _____
 LATONDA SIMMONS
 City Clerk and Clerk of the Council
 of the City of Oakland, California