



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Kim Welsh

SUBJECT: SEE BELOW

DATE: May 23, 2011

Approved

Date 5/31/11

SUBJECT: APPLICATION TO THE U.S. FOREIGN-TRADE ZONES BOARD TO ESTABLISH A FOREIGN TRADE SUBZONE AT TESLA MOTORS, INC.

RECOMMENDATION

Adoption of a resolution:

- (a) Authorizing the City Manager to submit an application to the U.S. Foreign-Trade Zones Board to establish a Foreign Trade Subzone at Tesla Motors, Inc. facilities in Palo Alto and Fremont.
- (b) Authorizing the City Manager to negotiate and execute an agreement with Tesla Motors, Inc. for management and operation of the Subzone upon the U.S. Foreign-Trade Zones Board's approval of the application.

OUTCOME

Approval by the Council will allow the City Manager to submit the Tesla Motors Foreign-Trade Subzone application to the U.S. Foreign-Trade Zones Board and to negotiate and execute an operating agreement upon approval of the Subzone application.

BACKGROUND

Although this project is not located in San Jose, the City's Foreign Trade Zone grant of authority from the federal government extends beyond the City boundary to include Santa Clara, Monterey, San Benito, and Santa Cruz Counties and the southern region of Alameda and San Mateo Counties. The Foreign Trade Zone is an important component of the City's economic development offering and generates revenue for the City through application and annual fees.

The U.S. Congress enacted the Foreign Trade Zone Program into law in 1934 to stimulate economic development and U.S. exports. Today over 250 communities in the United States have received Foreign Trade Zone designation from the federal government. Pursuant to State of California Government Code, the City is authorized to apply for and accept a grant to establish, operate and maintain Foreign Trade Zones and Subzones, subject to the requirements of federal

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law and regulations of the Foreign- Trade Zones Board and to take other actions necessary to establish, operate and maintain Foreign Trade Zones or Subzones. In addition to San Jose, Foreign Trade Zones are located in 17 other California cities, including Oakland, San Francisco, Sacramento, Long Beach, Los Angeles and San Diego. Larger cities often have the grant of authority for their metropolitan area. In November 1974, San Jose received authority from the U.S. Department of Commerce Foreign Trade-Zones Board to operate Foreign Trade Zone #18.

A Foreign Trade Zone is a space-designated site outside of U.S. Customs & Border Protection territory. Merchandise stored, manufactured or assembled in a Foreign Trade Zone is considered to be in international commerce. Companies utilizing a Foreign Trade Zone are able to delay, reduce or eliminate the payment of duties to the U.S. Government, and realize operational efficiencies and cost savings. Foreign Trade Zone sites and facilities remain within the jurisdiction of local, state and federal governments or agencies.

The City's Foreign Trade Zone grant of authority includes the designation of a General Purpose Zone which is located at 2055 South Seventh Street, Suite A, in the Monterey Corridor. Under an operating agreement, the City has delegated the administration and operation of the General Purpose Zone to San Jose Distribution Services, which operates a 330,000 square-foot warehouse facility. In addition to the General Purpose Foreign Trade Zone, the City can apply to create a Subzone for a single company engaged in manufacturing or large-scale distribution.

Tesla Motors seeks to establish a Foreign Trade Subzone at sites in Palo Alto and Fremont.

Tesla Motors, headquartered in Palo Alto, designs and manufactures a new product line of electric vehicles and powertrain technologies. Founded in 2003, Tesla Motors has sold over 1,500 electric vehicles to consumers in the U.S. and 30 nations. Tesla has over 800 employees today and plans to employ over 2,000 in 2012 and grow beyond that number in future years. The company went public on June 29, 2010 and is an important element of Silicon Valley's green technology cluster.

Tesla recently leased space in San Jose at Santana Row to allow customers an interactive experience with Tesla vehicles and to configure their Model S in the Design Studio.

ANALYSIS

The Foreign Trade Subzone designation is necessary to allow Tesla Motors, Inc. to compete in the global automotive industry. The Foreign Trade Subzone is an important part of the company's strategy to become a market leader in the rapidly growing global market for electric vehicles and to maintain and increase its presence in the United States. Cost savings associated with the Foreign Trade Subzone will likely result in employment growth at Tesla Motors and enhance future business opportunities. The company's success will benefit the clean tech and green mobility sector throughout the Valley.

Tesla Motors imports battery cells, battery pack components and electric motor components, as well as components sourced from U.S. suppliers. Tesla combines the imported and U.S. parts and manufactures into completed battery packs and electric motor transmission assemblies. Tesla stores components and finished goods in its warehouse until they are sold to U.S. and foreign destinations. Tesla exports finished goods to nations in Europe and Asia, so that the products may be used in European and Asian electric vehicles. Tesla uses finished goods in the U.S. for further manufactured process to be used in electric vehicles produced by Tesla in other U.S. facilities, such as the Fremont site.

Tesla will receive various financial benefits by receiving the designation and operating a Foreign Trade Zone. The company's U.S. manufacturing process will increase cash flow savings; avoid duty for certain merchandise, scrap or waste; enhance security requirements; and streamline its import and export operations in adherence to stringent Foreign Trade Zone regulations.

The Subzone application will include leased and owned sites in Palo Alto and Fremont. The Palo Alto site, located at 3500 Deer Creek Road, encompasses 25.28 acres and a 350,000 square-foot building. The Fremont site is located at 45500 Fremont Boulevard (formerly the NUMMI Foreign Trade Subzone), with activity in up to 15 buildings on 5.5 million square-feet.

All security requirements of U.S. Customs & Border Protection will be met prior to activation of the Subzone. Tesla will establish procedures to maintain records required by the Foreign Trade Zones-Board and U.S. Customs & Border Protection. Activation of the Subzone by U.S. Customs and Border Protection will occur after Tesla has executed an Operating Agreement with the City.

EVALUATION AND FOLLOW-UP

As this project will occur outside of the City of San Jose, staff does not anticipate follow-up with the Council.

PUBLIC OUTREACH

The Office of Economic Development notified the cities of Palo Alto and Fremont of Tesla's intention to seek the Subzone authority at the facilities in their cities.

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or

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a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

COORDINATION

This resolution has been in prepared in consultation with the Office of the City Attorney.

COST IMPLICATIONS

Under terms of the City's Foreign Trade Zone Fee Schedule, Tesla Motors will pay the City of San Jose an application fee of \$3,000 at the time of the application submission and an annual fee of \$5,000 at the time the Subzone is activated by U.S. Customs & Border Protection. If the proposed fees and charges for FY 2011-12 are approved by the Council, the application fee will be increased to \$5,000 and the annual Subzone fee will increase to \$15,000.

CEQA

Not a project, File #PP10-068 3(a). Federal Application

/s/

Kim Walesh
Director of Economic Development
Chief Strategist

Please contact Joseph Hedges, International Program Manager, at 535-8186 if there are any questions.