



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kim Welsh

SUBJECT: SEE BELOW

DATE: August 1, 2011

Approved

Date

8/8/11

COUNCIL DISTRICT: #3
SNI AREA: N/A

SUBJECT: PARTICIPATION AGREEMENT WITH NETFLIX

RECOMMENDATION

Staff recommends that the Council adopt a resolution authorizing the City Manager to negotiate and execute a Participation Agreement with Netflix that will provide funding to Netflix in an amount equal to 50% of the net new sales tax revenue received by the City from the Netflix operation in year one, 40% of the net new sales tax revenue received in year two, and 30% of the net new sales tax revenue received in year three, to be capped at a total of \$5,000,000 over three consecutive years.

OUTCOME

Approval of this resolution will assist Netflix in relocating and improving the site for their new DVD operations at 1732 N. First Street. Netflix will invest \$1,600,000 in improvements at their new San José facility and will locate 225 jobs to San José.

BACKGROUND

A top priority for San José is regaining jobs and City revenue as the economy recovers regionally and nationally. Staff are actively engaged with companies seeking to expand, consolidate or move to San José and have succeeded with companies like C8 Medisensors, Maxim Integrated Products, and SunPower in the last six months. San José offers quality real estate at a competitive cost and access to distinct benefits of a big city location, including proximity to transportation options, housing, workforce, and cultural/sporting amenities.

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Netflix was founded in 1997 in Scotts Valley, California and moved to their current headquarters in Los Gatos two years later. Netflix is a subscription-based service that allows users to stream movies and TV shows over the internet. Through partnerships and continuous technological improvements, users either receive DVD's via mail or stream movies through their computers, TV's, digital recorders and game consoles.

In addition to San José, Netflix studied alternative locations to expand in Silicon Valley. Location of the Netflix DVD operation in San José is a unique opportunity among Driving Industry expansions because of the associated sales tax revenue.

ANALYSIS

The Netflix headquarters is currently located at 100 Winchester Circle in Los Gatos. The company has a lease through 2018 for 86,200 square feet of office space that accommodates approximately 800 employees. Netflix is leasing 55,000 sq ft at 1732 N. First Street for an initial term of five years to relocate their DVD operation and alleviate overcrowded conditions in their Los Gatos office. The DVD operation will focus on growing the DVD service and is also responsible for software/R&D technological enhancements and improvements to the Netflix web site.

Initially the company will invest \$1,600,000 in lease improvements.

Netflix has requested financial assistance to assist with the necessary tenant improvements at 1732 N. First Street and to cover permitting fees associated with relocating the DVD operation. As a charter city under its municipal and police powers, the City of San José may provide financial assistance to Netflix in order to benefit the residents of San José. The Netflix facility will expand the number of jobs and the amount of General Fund revenue in San José and improvement of the site is necessary to accomplish these ends.

The City's proposed assistance to Netflix is as follows:

The Council may adopt a resolution authorizing the City Manager to negotiate and execute a Participation Agreement with Netflix that will provide funding to Netflix in an amount equal to 50% of the net new sales tax revenue received by the City from the Netflix operation in year 1, 40% of the net new sales tax revenue received in year two, and 30% of the net new sales tax revenue received in year three, to be capped at a total of \$5,000,000 over three consecutive years. For the remaining two years of Netflix's lease agreement, the City will retain 100% sales tax revenue allocated to the City from the Netflix operation.

It is important to note that the City can only rebate money to Netflix after Netflix generates sales tax revenue and the City receives the sales tax revenue. Netflix will submit copies of the State Board of Equalization Form 401 indicating the amount of sales tax collected for each quarter as evidence of payment of the sales tax. The City will confirm and validate the information submitted by Netflix. Such reimbursement will be made on a quarterly basis 60 days following

the quarter in which Netflix paid the State Board of Equalization. If no new sales tax revenue is generated from Netflix, the City would have no obligation to reimburse Netflix.

The final executed City documents will be filed with the City Clerk.

EVALUATION AND FOLLOW-UP

City staff will monitor Netflix's expansion and employment contributions. City staff will provide progress updates to the Community and Economic Development Committee.

PUBLIC OUTREACH/INTEREST

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

This item will be discussed at the August 23, 2011, City Council meeting.

COORDINATION

This memo has been coordinated with the City Attorney's Office and the Budget Office.

FISCAL/POLICY ALIGNMENT

The project aligns with the City's Economic Development Strategy #1 "Encourage Companies and Sectors that Can Drive the San José/Silicon Valley Economy and Generate Revenue for City Services and Infrastructure."

COST IMPLICATIONS

Funding for this agreement will be generated from General Fund sales tax revenue recognized by the City from Netflix, up to a maximum of \$5,000,000 over a three-year period. If Netflix does not generate new sales tax revenue, there will be no reimbursement.

BUDGET REFERENCE

Not applicable.

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CEQA

Not a Project, File No. PP10-069(a), Participation Agreement.

/S/
KIM WALESH
Director of Economic Development
Chief Strategist

For questions please contact Nanci Klein, Division Manager, at 408-535-8184.