


TECH

Why AI startups are still flocking to San Francisco — despite high costs and taxes

Sure, prices are steep and the streets are a mess. But for startups, San Francisco's tech community "is just unmatched."

 **Chase DiFelicianantonio**
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Employees at artificial intelligence startup Andi, including founder Angela Hoover, center, chat as they work together in an Airbnb rental in San Francisco on Aug. 8. Hoover says she moved the company to San Francisco "because the community here is just unmatched."
Gabrielle Lurie/The Chronicle

Earlier this year, Angela Hoover decided to pull up stakes and move her artificial intelligence search engine startup, Andi, to San Francisco. Her small team had been working from Mexico after getting their start in Miami in 2021, and they could have gone anywhere.

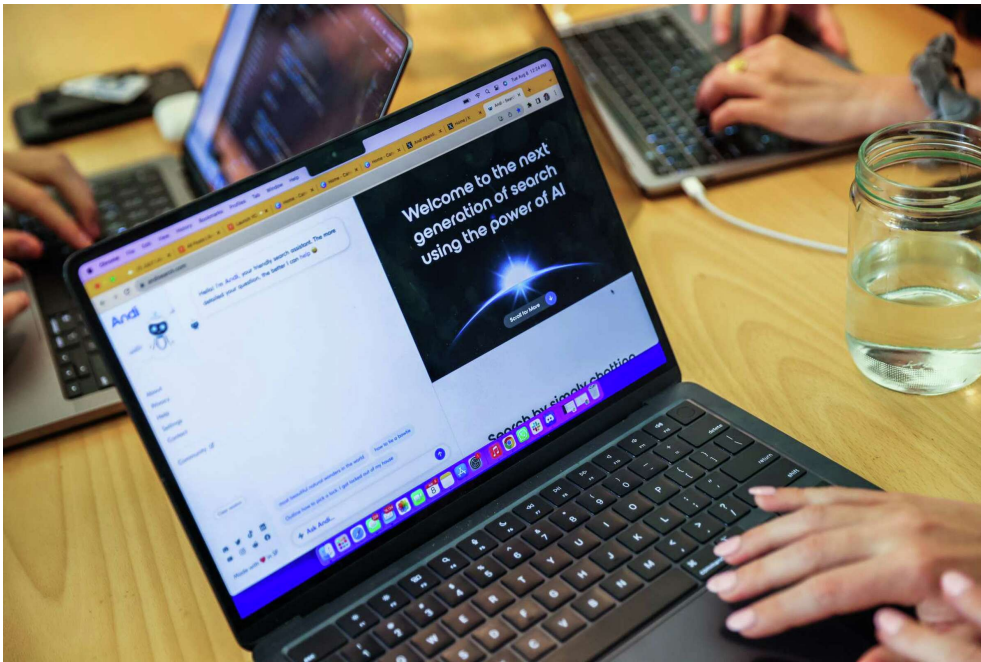
- **More on AI:** [S.F. is home of the AI revolution. Map shows where OpenAI, other major companies are located](#)

Why did they choose [San Francisco](#), particularly with its seemingly endless cycle of bad press about street conditions and political dysfunction?

“We thought of San Francisco because the community here is just unmatched,” said Hoover, citing the events, networking and fundraising opportunities in the city’s booming AI industry. Along with her team of about 10 others, she has been working out of a rented Airbnb property north of the Panhandle since relocating to the city.

San Francisco and Silicon Valley have long been the epicenter of the U.S. and global tech sector, but the pandemic pushed many techies to locales like [Miami and Austin](#) that beckoned with cheaper real estate and lower taxes.

Yet the enduring advantages of San Francisco’s startup environment continue to attract entrepreneurs, especially as events and hackathons move off Zoom and back to in person. The most [recent figures available](#) from the city controller’s office show the information and professional services sectors, which includes tech, added 6,000 jobs in June, largely offsetting the layoffs that roiled the industry starting in late 2022.



Angela Hoover shows off the Andi's artificial intelligence model and how it works. Hoover moved the company to San Francisco this year to take advantage of the events and networking and fundraising opportunities in the city's AI industry. Gabrielle Lurie/The Chronicle

For many startups that chose San Francisco, questions of taxation are at best a secondary concern when compared with the myriad benefits of being in the thick of the latest tech boom.

Nevertheless, it's true that some more established firms have blamed high taxes or other costs when opting to leave the confines of the city.

Irish American payment-processing company Stripe relocated to South San Francisco in 2019 in search of cheaper office space. And e-payments company Block, formerly known as Square, started relocating to Oakland in 2020, where it occupies the historic former downtown headquarters of the Capwell department store.

Founder Jack Dorsey, who was also CEO of Twitter for about six years, [tweeted in 2019](#) about the tax squeeze from San Francisco's Proposition C, a voter-approved levy on his and other large companies to combat homelessness.

Citizens passed the tax, which applies principally to companies with at least \$50 million in San Francisco-based gross receipts, in 2018. According to a [city report that year](#), the plurality of the money raised by the tax — some 30% — was expected to come from the info-tech industry.

The report also projected that during the next 20 years, “there would be 725 to 875 fewer jobs in the city than there otherwise would be” as a result of the additional tax.

Both Stripe and Block “cited various reasons for leaving but undoubtedly the tax structure and how their gross receipts were calculated was likely a major factor in their ultimate decisions to move out of San Francisco,” said Jeff Cretan, communications chief for Mayor London Breed, in an email. “Broadly, this is why the Mayor is pursuing business tax reform.”



Sandra Dib, left, works with Andi founder Angela Hoover in San Francisco on Aug. 8. The company, which got its start in 2021, moved from Mexico to the Bay Area earlier this year.
Gabrielle Lurie/The Chronicle

Some studies have tried to prove that higher business taxes in San Francisco also pushed large, established companies out of the city. A [Bay Area Council report](#) from earlier this year found a hypothetical financial technology payment processing company with 1,000 employees and \$500 million in taxable gross receipts would pay close to \$7 million in business taxes annually, including \$2.7 million in Prop. C taxes, while the same company would pay slightly less than \$70,000 in San Jose.

The council is a public-policy and advocacy organization whose members include some of the largest Bay Area employers, such as Wells Fargo, Google and Salesforce.

The report also said it was “impossible to pinpoint a single determining factor in relocations and other corporate real estate decisions.”

With the AI boom in full swing and centered in San Francisco, many startups are just trying to find their feet and attract customers and funding. And most fall below the thresholds for various kinds of corporate taxes.

Many startups, for instance, don’t have to pay taxes under a city scheme that exempts companies with less than \$2.09 million in annual gross receipts and which is adjusted up each year. “Many startups are small and would fall under this exemption,” said

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Cretan, the mayor's spokesperson.

The catch is that if the companies stay in San Francisco and thrive, taxes start to kick in as they grow. And some investors feel the city's tax policies, approved by voters, have sent an overall hostile signal to the tech industry.



Jed White, the co-founder and Chief Technology Officer of Andi, makes tea during the workday in an S.F. Airbnb rental, where he lives and the company is based, on Aug. 8.

Gabrielle Lurie/The Chronicle

“I always view taxes as primarily as what they incentivize or disincentivize,” said Lee Edwards, an early stage tech investor at San Francisco-based Root Ventures. The city’s model of taxing gross receipts, “scales with revenue and discourages you from making more revenue,” unfairly affecting many startups whose goal at the outset is to grow their top line as fast as possible.

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Edwards said he would favor returning to a payroll tax that would not single out tech. San Francisco voters chose to eliminate payroll taxation on businesses in favor of the gross receipts model in 2020. Gross receipts are still calculated in part by determining where an employee is physically performing their job, with some commentators calling it a payroll tax in all but name.

Taxes like Prop. C may not affect startups right away, but they send a message to companies about growing in San Francisco, Edwards said. They can be particularly painful for companies that do high volumes of business at a low margin, including ride-hailing apps such as Uber and Lyft.

Asked what the mayor's office hears from startups interested in setting up shop in the city, Cretan said founders ask about plans to address public safety and street cleanliness concerns, "and they ask about our tax structure and costs."

He said the city has added permit specialists to help businesses get started, and that for companies with higher gross receipts, a plan included in the mayor's budget offers an annual tax credit of up to \$1 million on office-based gross receipts for up to three years.

For some tech founders like Emmanuel Turlay who runs Sematic AI, a South of Market startup working on software to make it easier to train AI models, taxes aren't really part of the equation at all.

"I don't even know how much I paid in taxes this year," Turlay said, pointing to the large pool of talented engineers, networking opportunities, and proximity to venture capital funding that continue to make the Bay Area the premiere place to start and grow a tech company.

But, he said, there are other drawbacks beyond just the street conditions in some parts of town.

Skilled software engineers command higher salaries here, which means a startup burns cash at a faster rate. The result is that companies have less time to nail down their business model and get revenue flowing.

"You need to figure out a way to make your company viable much faster," Turlay said.

Reach Chase DiFelicianantonio: chase.difelicianantonio@sfchronicle.com; Twitter: @ChaseDiFelice