

NETFLIX INC
Form 10-K
January 28, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-35727

Netflix, Inc.

(Exact name of Registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

100 Winchester Circle Los Gatos, California 95032
(Address and zip code of principal executive offices)
(408) 540-3700

(Registrant's telephone number, including area code)

77-0467272

(I.R.S. Employer Identification Number)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Common stock, \$0.001 par value

Name of Exchange on which registered

NASDAQ Stock Market LLC

(NASDAQ Global Select Market)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required

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to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Non-accelerated filer

Large accelerated filer Accelerated filer (do not check if smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

As of June 30, 2015, the aggregate market value of voting stock held by non-affiliates of the registrant, based upon the closing sales price for the registrant's common stock, as reported in the NASDAQ Global Select Market System, was \$33,823,183,533. Shares of common stock beneficially owned by each executive officer and director of the Registrant and by each person known by the Registrant to beneficially own 10% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for any other purpose.

As of January 27, 2016, there were 428,081,221 shares of the registrant's common stock, par value \$0.001, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Parts of the registrant's Proxy Statement for Registrant's 2016 Annual Meeting of Stockholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

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PART I

Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws. These forward-looking statements include, but are not limited to, statements regarding: our core strategy; the growth of Internet delivery of content; the decline in our DVD memberships and the resources allocated to our DVD segment; contribution margins; contribution profits (losses); liquidity; free cash flows; revenues; net income; operating cash flows; stock price volatility; pricing changes; the impact of, and the Company's response to, new accounting standards; action by competitors; risk of material impairment of current investment portfolio; reinvestment of earnings in foreign subsidiaries; membership growth rates; timing of facilities construction; nature of our content agreements; member viewing habits; payment of future dividends; obtaining additional capital; our content and marketing investments, including investments in original programming; significance and timing of contractual obligations; realization of deferred tax assets; seasonality; method of content delivery; and international expansion. These forward-looking statements are subject to risks and uncertainties that could cause actual results and events to differ. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included throughout this filing and particularly in Item 1A: "Risk Factors" section set forth in this Annual Report on Form 10-K. All forward-looking statements included in this document are based on information available to us on the date hereof, and we assume no obligation to revise or publicly release any revision to any such forward-looking statement, except as may otherwise be required by law.

Item 1. Business

ABOUT US

Netflix, Inc. ("Netflix", "the Company", "we", or "us") is the world's leading Internet television network with over 75 million streaming members in over 190 countries enjoying more than 125 million hours of TV shows and movies per day, including original series, documentaries and feature films. Our members can watch as much as they want, anytime, anywhere, on nearly any Internet-connected screen. Members can play, pause and resume watching, all without commercials or commitments. Additionally, in the United States ("U.S."), our members can receive DVDs delivered quickly to their homes.

We are a pioneer in the Internet delivery of TV shows and movies, launching our streaming service in 2007. Since this launch, we have developed an ecosystem for Internet-connected screens and have added increasing amounts of content that enable consumers to enjoy TV shows and movies directly on their Internet-connected screens. As a result of these efforts, we have experienced growing consumer acceptance of, and interest in, the delivery of TV shows and movies directly over the Internet.

Our core strategy is to grow our streaming membership business globally within the parameters of our consolidated net income and operating segment contribution profit (loss) targets. We are continuously improving our members' experience by expanding our streaming content with a focus on a programming mix of content that delights our members. In addition, we are perpetually enhancing our user interface and extending our streaming service to more Internet-connected screens.

We continue to grow our streaming service both domestically and internationally. We began our international expansion with Canada in 2010 and have since launched our service globally, with the exception of The People's Republic of China and territories where U.S. companies are not allowed to operate. We have also expanded our streaming content offering to include more exclusive and original programming, including several Emmy, Golden Globe and Academy Award nominated original series and documentaries. Our original programming increasingly includes content that we produce.

BUSINESS SEGMENTS

The Company has three reportable segments: Domestic streaming, International streaming and Domestic DVD. The Domestic streaming segment derives revenues from monthly membership fees for services consisting solely of

streaming content to our members in the United States. The International streaming segment derives revenues from monthly membership fees for services consisting solely of streaming content to our members outside the United States. The Domestic DVD segment derives revenues from monthly membership fees for services consisting solely of DVD-by-mail. For additional information regarding our segments, including information about our financial results by geography, see Note 12 of Item 8, Financial Statements and Supplementary Data.

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COMPETITION

The market for entertainment video is intensely competitive and subject to rapid change. We compete against other entertainment video providers, such as multichannel video programming distributors ("MVPDs"), Internet-based movie and TV content providers (including those that provide pirated content), video gaming providers and DVD rental outlets and more broadly against other sources of entertainment that our members could choose in their moments of free time. We also compete against entertainment video providers in obtaining content that our members love, both for licensed streaming content and for original content projects.

While consumers may maintain simultaneous relationships with multiple entertainment sources, we strive for consumers to choose us in their moments of free time. We have often referred to this choice as our objective of "winning moments of truth." In attempting to win these moments of truth with our members, we are continually improving our service, including both our technology and our content, which is increasingly exclusive and curated, and includes our own original programming.

SEASONALITY

Our membership growth exhibits a seasonal pattern that reflects variations when consumers buy Internet-connected screens and when they tend to increase their viewing. Historically, the first and fourth quarters (October through March) represent our greatest membership growth across our Domestic and International streaming segments and the fewest membership losses in our Domestic DVD segment. Our membership growth may be impacted by the release of certain high profile original content. Internationally, we expect each market to demonstrate more predictable seasonal patterns as our service offering in each market becomes more established and we have a longer history to assess such patterns.

INTELLECTUAL PROPERTY

We regard our trademarks, service marks, copyrights, patents, domain names, trade dress, trade secrets, proprietary technologies and similar intellectual property as important to our success. We use a combination of patent, trademark, copyright and trade secret laws and confidentiality agreements to protect our proprietary intellectual property. Our ability to protect and enforce our intellectual property rights is subject to certain risks and from time to time we encounter disputes over rights and obligations concerning intellectual property. We cannot provide assurance that we will prevail in any intellectual property disputes.

EMPLOYEES

As of December 31, 2015, we had approximately 3,700 total employees. Of these employees, approximately 3,500 were full-time, including approximately 400 categorized as temporary.

OTHER INFORMATION

We were incorporated in Delaware in August 1997 and completed our initial public offering in May 2002. Our principal executive offices are located at 100 Winchester Circle, Los Gatos, California 95032, and our telephone number is (408) 540-3700.

We maintain a Web site at www.netflix.com. The contents of our Web site are not incorporated in, or otherwise to be regarded as part of, this Annual Report on Form 10-K. In this Annual Report on Form 10-K, "Netflix," the "Company," "we," "us," "our" and the "registrant" refer to Netflix, Inc. We make available, free of charge on our Web site, access to our Annual Report on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as soon as reasonably practicable after we file or furnish them electronically with the Securities and Exchange Commission ("SEC").

Investors and others should note that we announce material financial information to our investors using our investor relations Web site (<http://ir.netflix.com>), SEC filings, press releases, public conference calls and webcasts. We use these channels as well as social media to communicate with our members and the public about our company, our services and other issues. It is possible that the information we post on social media could be deemed to be material information. Therefore, we encourage investors, the media, and others interested in our company to review the information we post on the social media channels listed on our investor relations Web site.

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Item 1A. Risk Factors

If any of the following risks actually occur, our business, financial condition and results of operations could be harmed. In that case, the trading price of our common stock could decline, and you could lose all or part of your investment.

Risks Related to Our Business

If our efforts to attract and retain members are not successful, our business will be adversely affected.

We have experienced significant membership growth over the past several years. Our ability to continue to attract members will depend in part on our ability to consistently provide our members with compelling content choices, as well as a quality experience for selecting and viewing TV shows and movies. Furthermore, the relative service levels, content offerings, pricing and related features of competitors to our service may adversely impact our ability to attract and retain memberships. Competitors include other entertainment video providers, such as MVPDs, Internet-based movie and TV content providers (including those that provide pirated content) and DVD rental outlets. If consumers do not perceive our service offering to be of value, including if we introduce new or adjust existing features, adjust pricing or service offerings, or change the mix of content in a manner that is not favorably received by them, we may not be able to attract and retain members. In addition, many of our members are rejoining our service or originate from word-of-mouth advertising from existing members. If our efforts to satisfy our existing members are not successful, we may not be able to attract members, and as a result, our ability to maintain and/or grow our business will be adversely affected. Members cancel our service for many reasons, including a perception that they do not use the service sufficiently, the need to cut household expenses, availability of content is unsatisfactory, competitive services provide a better value or experience and customer service issues are not satisfactorily resolved. We must continually add new memberships both to replace canceled memberships and to grow our business beyond our current membership base. If growth rates slow faster than expected, given, in particular that our content costs are largely fixed in nature and contracted over several years, we may not be able to adjust our expenditures or increase our (per membership) revenues commensurate with the lowered growth rate such that our margins, liquidity and results of operation may be adversely impacted. If we are unable to successfully compete with current and new competitors in both retaining our existing memberships and attracting new memberships, our business will be adversely affected. Further, if excessive numbers of members cancel our service, we may be required to incur significantly higher marketing expenditures than we currently anticipate to replace these members with new members.

Changes in competitive offerings for entertainment video, including the potential rapid adoption of piracy-based video offerings, could adversely impact our business.

The market for entertainment video is intensely competitive and subject to rapid change. Through new and existing distribution channels, consumers have increasing options to access entertainment video. The various economic models underlying these channels include subscription, transactional, ad-supported and piracy-based models. All of these have the potential to capture meaningful segments of the entertainment video market. Piracy, in particular, threatens to damage our business, as its fundamental proposition to consumers is so compelling and difficult to compete against: virtually all content for free. Furthermore, in light of the compelling consumer proposition, piracy services are subject to rapid global growth. Traditional providers of entertainment video, including broadcasters and cable network operators, as well as Internet based e-commerce or entertainment video providers are increasing their Internet-based video offerings. Several of these competitors have long operating histories, large customer bases, strong brand recognition and significant financial, marketing and other resources. They may secure better terms from suppliers, adopt more aggressive pricing and devote more resources to product development, technology, infrastructure, content acquisitions and marketing. New entrants may enter the market or existing providers may adjust their services with unique offerings or approaches to providing entertainment video. Companies also may enter into business combinations or alliances that strengthen their competitive positions. If we are unable to successfully or profitably compete with current and new competitors, our business will be adversely affected, and we may not be able to increase or maintain market share, revenues or profitability.

The long-term and fixed cost nature of our content commitments may limit our operating flexibility and could adversely affect our liquidity and results of operations.

In connection with obtaining streaming content, we typically enter into multi-year commitments with studios and other content providers, the payment terms of which are not tied to member usage or the size of our membership base (“fixed cost”) but which may be tied to such factors as titles licensed and/or theatrical exhibition receipts. Such commitments are included in the Contractual Obligations section of Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 6, Commitments and Contingencies in Item 8. Given the multiple-year duration and largely fixed cost nature of content commitments, if membership acquisition and retention do not meet our expectations, our margins may be

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adversely impacted. Payment terms for certain content commitments, such as programming that is initially available in the applicable territory on our service (“original programming”), will typically require more up-front cash payments than other licensing agreements. To the extent membership and/or revenue growth do not meet our expectations, our liquidity and results of operations could be adversely affected as a result of content commitments and accelerated payment requirements of certain agreements. In addition, the long-term and fixed cost nature of our content commitments may limit our flexibility in planning for, or reacting to changes in our business and the market segments in which we operate. As we have expanded internationally, we have licensed content in advance of entering into a new geographical market. If we license content that is not favorably received by consumers in the applicable territory, or is unable to be shown in the applicable territory, acquisition and retention may be adversely impacted and given the long-term and fixed cost nature of our content commitments, we may not be able to adjust our content offering quickly and our results of operation may be adversely impacted.

We are devoting more resources toward the development, production, marketing and distribution of original programming, including TV series and movies. We believe that original programming can help differentiate our service from other offerings, enhance our brand and otherwise attract and retain members. To the extent our original programming does not meet our expectations, in particular, in terms of costs, viewing and popularity, our business, including our brand and results of operations may be adversely impacted.

If we are not able to manage change and growth, our business could be adversely affected.

We are expanding our operations internationally, scaling our streaming service to effectively and reliably handle anticipated growth in both members and features related to our service, ramping up our ability to produce original content, as well as continuing to operate our DVD service within the U.S. As we expand internationally, we are managing and adjusting our business to address varied content offerings, consumer customs and practices, in particular those dealing with e-commerce and Internet video, as well as differing legal and regulatory environments. As we scale our streaming service, we are developing technology and utilizing third-party “cloud” computing services. As we ramp up our original content production, we are building out expertise in a number of disciplines, including creative, marketing, legal, finance and other resources related to the development and physical production of content. If we are not able to manage the growing complexity of our business, including improving, refining or revising our systems and operational practices related to our streaming operations and original content, our business may be adversely affected.

We could be subject to economic, political, regulatory and other risks arising from our international operations. Operating in international markets requires significant resources and management attention and will subject us to regulatory, economic and political risks that may be different from or incremental to those in the U.S. In addition to the risks that we face in the U.S., our international operations involve risks that could adversely affect our business, including:

- the need to adapt our content and user interfaces for specific cultural and language differences, including licensing a certain portion of our content assets before we have developed a full appreciation for its performance within a given territory;
- difficulties and costs associated with staffing and managing foreign operations;
- management distraction;
- political or social unrest and economic instability;
- compliance with U.S. laws such as the Foreign Corrupt Practices Act, export controls and economic sanctions, and local laws prohibiting corrupt payments to government officials;
- difficulties in understanding and complying with local laws, regulations and customs in foreign jurisdictions;
- regulatory requirements or government action against our service, whether in response to enforcement of actual or purported legal and regulatory requirements or otherwise, that results in disruption or non-availability of our service or particular content in the applicable jurisdiction;
- less favorable foreign intellectual property laws;
- adverse tax consequences such as those related to repatriation of cash from foreign jurisdictions into the United States, non-income related taxes such as value-added tax or other indirect taxes, changes in tax laws or their interpretations, or the application of judgment in determining our global provision for income taxes and other tax liabilities given

intercompany transactions and calculations where the ultimate tax determination is uncertain;
fluctuations in currency exchange rates, which we do not use foreign exchange contracts or derivatives to hedge
against and which could impact revenues and expenses of our international operations and expose us to foreign
currency exchange rate risk;

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profit repatriation and other restrictions on the transfer of funds;
differing payment processing systems as well as consumer use and acceptance of electronic payment methods, such as payment cards;
new and different sources of competition;
censorship requirements that cause us to remove or edit popular content, leading to consumer disappointment or dissatisfaction with our service;
low usage and/or penetration of Internet- connected consumer electronic devices;
different and more stringent user protection, data protection, privacy and other laws;
availability of reliable broadband connectivity and wide area networks in targeted areas for expansion;
integration and operational challenges as well as potential unknown liabilities in connection with companies we may acquire or control; and
different, and often more lenient, laws and consumer understanding/attitudes regarding the illegality of piracy.
Our failure to manage any of these risks successfully could harm our international operations and our overall business, and results of our operations.

If we fail to maintain or, in new markets establish, a positive reputation with consumers concerning our service, including the content we offer, we may not be able to attract or retain members, and our operating results may be adversely affected.

We believe that a positive reputation with consumers concerning our service is important in attracting and retaining members who have a number of choices from which to obtain entertainment video. To the extent our content, in particular, our original programming, is perceived as low quality, offensive or otherwise not compelling to consumers, our ability to establish and maintain a positive reputation may be adversely impacted. Furthermore, to the extent our marketing, customer service and public relations efforts are not effective or result in negative consumer reaction, our ability to establish and maintain a positive reputation may likewise be adversely impacted. As we expand into new markets, we will also need to establish our reputation with consumers and to the extent we are not successful in creating positive impressions, our business in these new markets may be adversely impacted.

Changes in how we market our service could adversely affect our marketing expenses and membership levels may be adversely affected.

We utilize a broad mix of marketing and public relations programs, including social media sites such as Facebook and Twitter, to promote our service to potential new members. We may limit or discontinue use or support of certain marketing sources or activities if advertising rates increase or if we become concerned that members or potential members deem certain marketing practices intrusive or damaging to our brand. If the available marketing channels are curtailed, our ability to attract new members may be adversely affected.

If companies that promote our service decide that we negatively impact their business, that they want to compete more directly with our business or enter a similar business or decide to exclusively support our competitors, we may no longer have access to such marketing channels. We also acquire a number of members who rejoin our service having previously cancelled their membership. If we are unable to maintain or replace our sources of members with similarly effective sources, or if the cost of our existing sources increases, our member levels and marketing expenses may be adversely affected.

We face risks, such as unforeseen costs and potential liability in connection with content we acquire, produce, license and/or distribute through our service.

As a distributor of content, we face potential liability for negligence, copyright and trademark infringement, or other claims based on the nature and content of materials that we acquire, produce, license and/or distribute. We also may face potential liability for content used in promoting our service, including marketing materials and features on our Web site such as member reviews. As we expand our original programming, we have become responsible for production costs and other expenses, such as ongoing guild payments. We also take on risks associated with production, such as completion and key talent risk. To the extent we do not accurately anticipate costs or mitigate risks, including for content that we obtain but ultimately does not appear on our service, or if we become liable for content we acquire, produce, license and/or distribute, our business may suffer. Litigation to defend these claims could be costly and the expenses and damages arising from any liability or unforeseen production risks could harm our

results of operations. We may not be indemnified against claims or costs of these types and we may not have insurance coverage for these types of claims.

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If studios, content providers or other rights holders refuse to license streaming content or other rights upon terms acceptable to us, our business could be adversely affected.

Our ability to provide our members with content they can watch depends on studios, content providers and other rights holders licensing rights to distribute such content and certain related elements thereof, such as the public performance of music contained within the content we distribute. The license periods and the terms and conditions of such licenses vary. If the studios, content providers and other rights holders are not or are no longer willing or able to license us content upon terms acceptable to us, our ability to stream content to our members will be adversely affected and/or our costs could increase. Many of the licenses for content provide for the studios or other content providers to withdraw content from our service relatively quickly. Because of these provisions as well as other actions we may take, content available through our service can be withdrawn on short notice. As competition increases, we may see the cost of programming increase. As we seek to differentiate our service, we are increasingly focused on securing certain exclusive rights when obtaining content, including original content. We are also focused on programming an overall mix of content that delights our members in a cost efficient manner. Within this context, we are selective about the titles we add and renew to our service. If we do not maintain a compelling mix of content, our membership acquisition and retention may be adversely affected.

Music contained within content we distribute may require us to obtain licenses for such distribution. In this regard, we engage in negotiations with collection management organizations (“CMOs”) that hold certain rights to music interests in connection with streaming content into various territories. If we are unable to reach mutually acceptable terms with these organizations, we could become involved in litigation and/or could be enjoined from distributing certain content, which could adversely impact our business. Additionally, pending and ongoing litigation as well as negotiations between certain CMOs and other third parties in various territories could adversely impact our negotiations with CMOs, or result in music publishers represented by certain CMOs unilaterally withdrawing rights, and thereby adversely impact our ability to reach licensing agreements reasonably acceptable to us. Failure to reach such licensing agreements could expose us to potential liability for copyright infringement or otherwise increase our costs.

We rely upon a number of partners to make our service available on their devices.

We currently offer members the ability to receive streaming content through a host of Internet-connected screens, including TVs, digital video players, television set-top boxes and mobile devices. We have agreements with various cable, satellite and telecommunications operators to make our service available through the television set-top boxes of these service providers. We intend to continue to broaden our capability to instantly stream TV shows and movies to other platforms and partners over time. If we are not successful in maintaining existing and creating new relationships, or if we encounter technological, content licensing, regulatory or other impediments to delivering our streaming content to our members via these devices, our ability to grow our business could be adversely impacted. Our agreements with our device partners are typically between one and three years in duration and our business could be adversely affected if, upon expiration, a number of our partners do not continue to provide access to our service or are unwilling to do so on terms acceptable to us, which terms may include the degree of accessibility and prominence of our service. Furthermore, devices are manufactured and sold by entities other than Netflix and while these entities should be responsible for the devices' performance, the connection between these devices and Netflix may nonetheless result in consumer dissatisfaction toward Netflix and such dissatisfaction could result in claims against us or otherwise adversely impact our business. In addition, technology changes to our streaming functionality may require that partners update their devices. If partners do not update or otherwise modify their devices, our service and our members' use and enjoyment could be negatively impacted.

Any significant disruption in or unauthorized access to our computer systems or those of third parties that we utilize in our operations, including those relating to cybersecurity or arising from cyber-attacks, could result in a loss or degradation of service, unauthorized disclosure of data, including member and corporate information, or theft of intellectual property, including digital content assets, which could adversely impact our business.

Our reputation and ability to attract, retain and serve our members is dependent upon the reliable performance and security of our computer systems and those of third parties that we utilize in our operations. These systems may be subject to damage or interruption from earthquakes, adverse weather conditions, other natural disasters, terrorist attacks, power loss, telecommunications failures, and cybersecurity risks. Interruptions in these systems, or with the

Internet in general, could make our service unavailable or degraded or otherwise hinder our ability to deliver streaming content or fulfill DVD selections. Service interruptions, errors in our software or the unavailability of computer systems used in our operations could diminish the overall attractiveness of our membership service to existing and potential members.

Our computer systems and those of third parties we use in our operations are vulnerable to cybersecurity risks, including cyber-attacks such as computer viruses, denial of service attacks, physical or electronic break-ins and similar disruptions. These systems periodically experience directed attacks intended to lead to interruptions and delays in our service and operations as well as loss, misuse or theft of data. Any attempt by hackers to obtain our data (including member and corporate

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information) or intellectual property (including digital content assets), disrupt our service, or otherwise access our systems, or those of third parties we use, if successful, could harm our business, be expensive to remedy and damage our reputation. We have implemented certain systems and processes to thwart hackers and protect our data and systems. To date hackers have not had a material impact on our service or systems however this is no assurance that hackers may not be successful in the future. Our insurance does not cover expenses related to such disruptions or unauthorized access. Efforts to prevent hackers from disrupting our service or otherwise accessing our systems are expensive to implement and may limit the functionality of or otherwise negatively impact our service offering and systems. Any significant disruption to our service or access to our systems could result in a loss of memberships and adversely affect our business and results of operation.

We utilize our own communications and computer hardware systems located either in our facilities or in that of a third-party Web hosting provider. In addition, we utilize third-party "cloud" computing services in connection with our business operations. We also utilize our own and third-party content delivery networks to help us stream TV shows and movies in high volume to Netflix members over the Internet. Problems faced by us or our third-party Web hosting, "cloud" computing, or other network providers, including technological or business-related disruptions, as well as cybersecurity threats, could adversely impact the experience of our members.

We rely upon Amazon Web Services to operate certain aspects of our service and any disruption of or interference with our use of the Amazon Web Services operation would impact our operations and our business would be adversely impacted.

Amazon Web Services ("AWS") provides a distributed computing infrastructure platform for business operations, or what is commonly referred to as a "cloud" computing service. We have architected our software and computer systems so as to utilize data processing, storage capabilities and other services provided by AWS. Currently, we run the vast majority of our computing on AWS. Given this, along with the fact that we cannot easily switch our AWS operations to another cloud provider, any disruption of or interference with our use of AWS would impact our operations and our business would be adversely impacted. While the retail side of Amazon competes with us, we do not believe that Amazon will use the AWS operation in such a manner as to gain competitive advantage against our service.

If the technology we use in operating our business fails, is unavailable, or does not operate to expectations, our business and results of operation could be adversely impacted.

We utilize a combination of proprietary and third party technology to operate our business. This includes the technology that we have developed to recommend and merchandise content to our consumers as well as enable fast and efficient delivery of content to our members and their various consumer electronic devices. For example, we have built and deployed our own content-delivery network ("CDN"). To the extent Internet Service Providers ("ISPs") do not interconnect with our CDN, or if we experience difficulties in its operation, our ability to efficiently and effectively deliver our streaming content to our members could be adversely impacted and our business and results of operation could be adversely affected. Likewise, if our recommendation and merchandising technology does not enable us to predict and recommend titles that our members will enjoy, our ability to attract and retain members may be adversely affected. We also utilize third party technology to help market our service, process payments, and otherwise manage the daily operations of our business. If our technology or that of third parties we utilize in our operations fails or otherwise operates improperly, our ability to operate our service, retain existing members and add new members may be impaired. Also, any harm to our members' personal computers or other devices caused by software used in our operations could have an adverse effect on our business, results of operations and financial condition.

If government regulations relating to the Internet or other areas of our business change, we may need to alter the manner in which we conduct our business, or incur greater operating expenses.

The adoption or modification of laws or regulations relating to the Internet or other areas of our business could limit or otherwise adversely affect the manner in which we currently conduct our business. In addition, the continued growth and development of the market for online commerce may lead to more stringent consumer protection laws, which may impose additional burdens on us. If we are required to comply with new regulations or legislation or new interpretations of existing regulations or legislation, this compliance could cause us to incur additional expenses or alter our business model.

Changes in laws or regulations that adversely affect the growth, popularity or use of the Internet, including laws impacting net neutrality, could decrease the demand for our service and increase our cost of doing business. The failure to adopt laws protecting strong net neutrality could also increase the cost of doing business. In the United States, on February 16, 2015, the Federal Communications Commission ("FCC") adopted net neutrality rules intended, in part, to prevent network operators from discriminating against legal traffic that transverse their networks and to prevent ISP abuses at interconnection points. The FCC's authority to adopt these rules is currently under review by the U.S. Court of Appeals for the District of

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Columbia. To the extent network operators attempt to use this ruling to extract fees from us to deliver our traffic or otherwise engage in discriminatory practices, or if the U.S. Court of Appeals for the District of Columbia invalidates the rules, our business could be adversely impacted. Regulators outside the United States, including the European Union, have adopted or may adopt Network Neutrality rules. It is also possible that network neutrality rules may be nascent or non-existent in the global markets in which we operate. Within such a regulatory environment, coupled with potentially significant political and economic power of local network operators, we could experience discriminatory or anti-competitive practices that could impede our growth, cause us to incur additional expense or otherwise negatively affect our business.

Changes in how network operators handle and charge for access to data that travel across their networks could adversely impact our business.

We rely upon the ability of consumers to access our service through the Internet. If network operators block, restrict or otherwise impair access to our service over their networks, our service and business could be negatively affected. To the extent that network operators implement usage based pricing, including meaningful bandwidth caps, or otherwise try to monetize access to their networks by data providers, we could incur greater operating expenses and our membership acquisition and retention could be negatively impacted. Furthermore, to the extent network operators create tiers of Internet access service and either charge us for or prohibit us from being available through these tiers, our business could be negatively impacted.

Most network operators that provide consumers with access to the Internet also provide these consumers with multichannel video programming. As such, many network operators have an incentive to use their network infrastructure in a manner adverse to our continued growth and success. While we believe that consumer demand, regulatory oversight and competition will help check these incentives, to the extent that network operators are able to provide preferential treatment to their data as opposed to ours or otherwise implement discriminatory network management practices, our business could be negatively impacted. In some international markets, these same incentives apply however, the consumer demand, regulatory oversight and competition may not be as strong as in our domestic market.

Privacy concerns could limit our ability to collect and leverage our membership data and disclosure of membership data could adversely impact our business and reputation.

In the ordinary course of business and in particular in connection with merchandising our service to our members, we collect and utilize data supplied by our members. We currently face certain legal obligations regarding the manner in which we treat such information. Other businesses have been criticized by privacy groups and governmental bodies for attempts to link personal identities and other information to data collected on the Internet regarding users' browsing and other habits. Increased regulation of data utilization practices, including self-regulation or findings under existing laws that limit our ability to collect and use data, could have an adverse effect on our business. In addition, if we were to disclose data about our members in a manner that was objectionable to them, our business reputation could be adversely affected, and we could face potential legal claims that could impact our operating results. As our business evolves and as we expand internationally, we may become subject to additional and/or more stringent legal obligations concerning our treatment of customer and other personal information, such as laws regarding data localization and/or restrictions on data export. Failure to comply with these obligations could subject us to liability, and to the extent that we need to alter our business model or practices to adapt to these obligations, we could incur additional expenses. For instance, in October 2015, the European Court of Justice overturned the E.U./U.S. Safe Harbor Program, under which companies were able to transfer personal data from the E.U. to the U.S. in a legally compliant manner. If other legally compliant forms of data transfer are similarly invalidated by courts or other authorities in the E.U., we may need to alter our business practices, and which may adversely affect our business.

Our reputation and relationships with members would be harmed if our membership data, particularly billing data, were to be accessed by unauthorized persons.

We maintain personal data regarding our members, including names and billing data. This data is maintained on our own systems as well as that of third parties we use in our operations. With respect to billing data, such as credit card numbers, we rely on licensed encryption and authentication technology to secure such information. We take measures

to protect against unauthorized intrusion into our members' data. Despite these measures we, our payment processing services or other third party services we use such as AWS, could experience an unauthorized intrusion into our members' data. In the event of such a breach, current and potential members may become unwilling to provide the information to us necessary for them to become members. Additionally, we could face legal claims for such a breach. The costs relating to any data breach could be material, and we currently do not carry insurance against the risk of a data breach. For these reasons, should an unauthorized intrusion into our members' data occur, our business could be adversely affected.

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We are subject to payment processing risk.

Our members pay for our service using a variety of different payment methods, including credit and debit cards, gift cards, direct debit and online wallets. We rely on internal systems as well as those of third parties to process payment. Acceptance and processing of these payment methods are subject to certain rules and regulations and require payment of interchange and other fees. To the extent there are disruptions in our payment processing systems, increases in payment processing fees, material changes in the payment ecosystem, such as large re-issuances of payment cards, delays in receiving payments from payment processors and/or changes to rules or regulations concerning payment processing, our revenue, operating expenses and results of operation could be adversely impacted. In addition, from time to time, we encounter fraudulent use of payment methods, which could impact our results of operation and if not adequately controlled and managed could create negative consumer perceptions of our service.

If our trademarks and other proprietary rights are not adequately protected to prevent use or appropriation by our competitors, the value of our brand and other intangible assets may be diminished, and our business may be adversely affected.

We rely and expect to continue to rely on a combination of confidentiality and license agreements with our employees, consultants and third parties with whom we have relationships, as well as trademark, copyright, patent and trade secret protection laws, to protect our proprietary rights. We may also seek to enforce our proprietary rights through court proceedings. We have filed and we expect to file from time to time for trademark and patent applications. Nevertheless, these applications may not be approved, third parties may challenge any copyrights, patents or trademarks issued to or held by us, third parties may knowingly or unknowingly infringe our intellectual property rights, and we may not be able to prevent infringement or misappropriation without substantial expense to us. If the protection of our intellectual property rights is inadequate to prevent use or misappropriation by third parties, the value of our brand and other intangible assets may be diminished, competitors may be able to more effectively mimic our service and methods of operations, the perception of our business and service to members and potential members may become confused in the marketplace, and our ability to attract members may be adversely affected.

We currently hold various domain names relating to our brand, including Netflix.com. Failure to protect our domain names could adversely affect our reputation and brand and make it more difficult for users to find our Web site and our service. We may be unable, without significant cost or at all, to prevent third parties from acquiring domain names that are similar to, infringe upon or otherwise decrease the value of our trademarks and other proprietary rights. Intellectual property claims against us could be costly and result in the loss of significant rights related to, among other things, our Web site, streaming technology, our recommendation and merchandising technology, title selection processes and marketing activities.

Trademark, copyright, patent and other intellectual property rights are important to us and other companies. Our intellectual property rights extend to our technology, business processes and the content on our Web site. We use the intellectual property of third parties in merchandising our products and marketing our service through contractual and other rights. From time to time, third parties allege that we have violated their intellectual property rights. If we are unable to obtain sufficient rights, successfully defend our use, or develop non-infringing technology or otherwise alter our business practices on a timely basis in response to claims against us for infringement, misappropriation, misuse or other violation of third-party intellectual property rights, our business and competitive position may be adversely affected. Many companies are devoting significant resources to developing patents that could potentially affect many aspects of our business. There are numerous patents that broadly claim means and methods of conducting business on the Internet. We have not searched patents relative to our technology. Defending ourselves against intellectual property claims, whether they are with or without merit or are determined in our favor, results in costly litigation and diversion of technical and management personnel. It also may result in our inability to use our current Web site, streaming technology, our recommendation and merchandising technology or inability to market our service or merchandise our products. As a result of a dispute, we may have to develop non-infringing technology, enter into royalty or licensing agreements, adjust our merchandising or marketing activities or take other actions to resolve the claims. These actions, if required, may be costly or unavailable on terms acceptable to us.

We are engaged in legal proceedings that could cause us to incur unforeseen expenses and could occupy a significant amount of our management's time and attention.

From time to time, we are subject to litigation or claims that could negatively affect our business operations and financial position. As we have grown, we have seen a rise in the number of litigation matters against us. These matters have included patent infringements as well as consumer and securities class actions, each of which are typically expensive to defend. Litigation disputes could cause us to incur unforeseen expenses, could occupy a significant amount of our management's time and attention and could negatively affect our business operations and financial position.

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We may seek additional capital that may result in stockholder dilution or that may have rights senior to those of our common stockholders.

From time to time, we may seek to obtain additional capital, either through equity, equity-linked or debt securities. The decision to obtain additional capital will depend on, among other things, our business plans, operating performance and condition of the capital markets. If we raise additional funds through the issuance of equity, equity-linked or debt securities, those securities may have rights, preferences or privileges senior to the rights of our common stock, and our stockholders may experience dilution.

We have debt outstanding and may incur additional debt in the future, which may adversely affect our financial condition and future financial results.

As of December 31, 2015, we had \$2,400 million aggregate principal amount of senior notes outstanding. Risks relating to our long-term indebtedness include:

requiring us to dedicate a portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of cash flow to fund working capital, capital expenditures, acquisitions and investments and other general corporate purposes;

limiting our flexibility in planning for, or reacting to, changes in our business and the markets in which we operate; and

limiting our ability to borrow additional funds or to borrow funds at rates or on other terms we find acceptable.

It is possible that we may incur additional indebtedness in the future in the ordinary course of business. If new debt is added to current debt levels, the risks described above could intensify.

We may lose key employees or may be unable to hire qualified employees.

We rely on the continued service of our senior management, including our Chief Executive Officer and co-founder Reed Hastings, members of our executive team and other key employees and the hiring of new qualified employees. In our industry, there is substantial and continuous competition for highly-skilled business, product development, technical and other personnel. We may not be successful in recruiting new personnel and in retaining and motivating existing personnel, which may be disruptive to our operations.

If memberships to our Domestic DVD segment decline faster than anticipated, our business could be adversely affected.

The number of memberships to our DVD-by-mail offering is declining, and we anticipate that this decline will continue. We believe, however, that the domestic DVD business will continue to generate significant contribution profit for our business. The contribution profit generated by our domestic DVD business will help provide capital resources to fund our growth internationally. To the extent that the rate of decline in our DVD-by-mail business is greater than we anticipate, our business could be adversely affected. We do not anticipate increasing resources to our DVD operations and the technology used in its operations will not be meaningfully improved. To the extent that we experience service interruptions or other degradations in our DVD-by-mail service, members' satisfaction could be negatively impacted and we could experience an increase in DVD-by-mail member cancellations, which could adversely impact our business.

Changes in U.S. Postal rates or operations could adversely impact our operating results and member satisfaction.

We rely exclusively on the U.S. Postal Service to deliver DVDs from our shipping centers and to return DVDs to us from our members. Increases in postage delivery rates, including those resulting from changes to policies on the requirements of first class mail such as size, weight or machinability, could adversely affect our Domestic DVD segment's contribution profit. If the U.S. Postal Service were to implement other changes to improve its financial position, such as closing mail processing facilities or service reductions, such changes could lead to a decrease in customer satisfaction and our Domestic DVD segment's contribution profit could be adversely affected.

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Risks Related to Our Stock Ownership

Provisions in our charter documents and under Delaware law could discourage a takeover that stockholders may consider favorable.

Our charter documents may discourage, delay or prevent a merger or acquisition that a stockholder may consider favorable because they:

- authorize our board of directors, without stockholder approval, to issue up to 10,000,000 shares of undesignated preferred stock;
- provide for a classified board of directors;
- prohibit our stockholders from acting by written consent;
- establish advance notice requirements for proposing matters to be approved by stockholders at stockholder meetings;
- and
- prohibit stockholders from calling a special meeting of stockholders.

As a Delaware corporation, we are also subject to certain Delaware anti-takeover provisions. Under Delaware law, a corporation may not engage in a business combination with any holder of 15% or more of its capital stock unless the holder has held the stock for three years or, among other things, the board of directors has approved the transaction.

Our board of directors could rely on Delaware law to prevent or delay an acquisition of us.

In addition, a merger or acquisition may trigger retention payments to certain executive employees under the terms of our Amended and Restated Executive Severance and Retention Incentive Plan, thereby increasing the cost of such a transaction.

Our stock price is volatile.

The price at which our common stock has traded has fluctuated significantly. The price may continue to be volatile due to a number of factors including the following, some of which are beyond our control:

- variations in our operating results, including our membership acquisition and retention, revenues, contribution profits, net income and free cash flow;
- variations between our actual operating results and the expectations of securities analysts, investors and the financial community;
- announcements of developments affecting our business, systems or expansion plans by us or others;
- competition, including the introduction of new competitors, their pricing strategies and services;
- market volatility in general;
- the level of demand for our stock, including the amount of short interest in our stock; and
- the operating results of our competitors.

As a result of these and other factors, investors in our common stock may not be able to resell their shares at or above their original purchase price.

Following certain periods of volatility in the market price of our securities, we became the subject of securities litigation. We may experience more such litigation following future periods of volatility. This type of litigation may result in substantial costs and a diversion of management's attention and resources.

Financial forecasting may differ materially from actual results.

Given the dynamic nature of our business, and the inherent limitations in predicting the future, forecasts of our revenues, contribution margins, net income and number of total and paid membership additions and other financial and operating data may differ materially from actual results. Such discrepancies could cause a decline in the trading price of our common stock.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

Our corporate headquarters are located in Los Gatos, California and consist of leased space aggregating approximately 370,000 square feet. In the third quarter of 2015, the Company entered into additional lease agreements to expand its Los Gatos, California headquarters by approximately 260,000 square feet with a lease term of 10 years commencing after construction of the facilities, which is expected in late 2016.

In the United States, we lease other offices in various locations, including Beverly Hills, California for content acquisition, marketing and general and administrative operations and Fremont, California for our DVD operations. In the third quarter of 2015, the Company entered into an agreement to lease approximately 200,000 square feet in Los Angeles, California, with a lease term of 10 years commencing after the construction of the facility, which is expected to be in 2017. We also lease office space in other countries to support international streaming operations.

We believe that our existing facilities are adequate to meet current requirements, and that suitable additional or substitute space will be available as needed to accommodate any further physical expansion of operations and for any additional offices.

Item 3. Legal Proceedings

Information with respect to this item may be found in Note 6 of Item 8, Financial Statements and Supplementary Data, under the caption "Legal Proceedings" which information is incorporated herein by reference.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our common stock is traded on the NASDAQ Global Select Market under the symbol "NFLX". The following table sets forth the intraday high and low sales prices per share of our common stock for the periods indicated, as reported by the NASDAQ Global Select Market. The per share amounts are adjusted for our seven-for-one stock split that occurred in July 2015. Further information on the stock split can be found in Note 8 of Item 8, Financial Statements and Supplementary Data.

	2015		2014	
	High	Low	High	Low
First quarter	\$69.50	\$45.26	\$65.43	\$45.58
Second quarter	100.89	58.46	64.40	42.79
Third quarter	129.29	85.50	69.90	58.93
Fourth quarter	133.27	96.26	66.86	45.08

Holders

As of January 27, 2016, there were approximately 237 stockholders of record of our common stock, although there is a significantly larger number of beneficial owners of our common stock.

Dividends

We have not declared or paid any cash dividends, and we have no present intention of paying any cash dividends in the foreseeable future.

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Stock Performance Graph

Notwithstanding any statement to the contrary in any of our previous or future filings with the Securities and Exchange Commission, the following information relating to the price performance of our common stock shall not be deemed “filed” with the Commission or “soliciting material” under the Securities Exchange Act of 1934 and shall not be incorporated by reference into any such filings.

The following graph compares, for the five year period ended December 31, 2015, the total cumulative stockholder return on the Company’s common stock, as adjusted for the Stock Split, with the total cumulative return of the NASDAQ Composite Index, the S&P 500 Index and the S&P North American Technology Internet Index. The Company was added to the S&P 500 Index on December 18, 2010. Measurement points are the last trading day of each of the Company’s fiscal years ended December 31, 2010, December 31, 2011, December 31, 2012, December 31, 2013, December 31, 2014 and December 31, 2015. Total cumulative stockholder return assumes \$100 invested at the beginning of the period in the Company’s common stock, the stocks represented in the NASDAQ Composite Index, the stocks represented in the S&P 500 Index and the stocks represented in the S&P North American Technology Internet Index, respectively, and reinvestment of any dividends. The S&P North American Technology Internet Index is a modified-capitalization weighted index of stocks representing the Internet industry, including Internet content and access providers, Internet software and services companies and e-commerce companies. Historical stock price performance should not be relied upon as an indication of future stock price performance.

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Item 6. Selected Financial Data

The following selected consolidated financial data is not necessarily indicative of results of future operations and should be read in conjunction with Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations and Item 8, Financial Statements and Supplementary Data. The following amounts related to earnings per share and shares outstanding have been adjusted for the Stock Split for all periods reported, see Note 8 of Item 8, Financial Statements and Supplementary Data for further detail on the Stock Split.

Consolidated Statements of Operations:

	Year ended December 31,				
	2015	2014	2013	2012	2011
	(in thousands, except per share data)				
Revenues	\$6,779,511	\$5,504,656	\$4,374,562	\$3,609,282	\$3,204,577
Operating income	305,826	402,648	228,347	49,992	376,068
Net income	122,641	266,799	112,403	17,152	226,126
Earnings per share:					
Basic	\$0.29	\$0.63	\$0.28	\$0.04	\$0.61
Diluted	\$0.28	\$0.62	\$0.26	\$0.04	\$0.59
Weighted-average common shares outstanding:					
Basic	425,889	420,544	407,385	388,648	369,926
Diluted	436,456	431,894	425,327	412,327	380,585

Consolidated Statements of Cash Flows:

	Year Ended December 31,				
	2015	2014	2013	2012	2011
	(in thousands)				
Net cash (used in) provided by operating activities	\$(749,439)	\$16,483	\$97,831	\$21,586	\$317,712
Free cash flow (1)	(920,557)	(126,699)	(16,300)	(58,151)	186,550

(1) See “Liquidity and Capital Resources” for a definition of “free cash flow” and a reconciliation of “free cash flow” to “net cash (used in) provided by operating activities.”

Consolidated Balance Sheets:

	As of December 31,				
	2015	2014	2013	2012	2011
	(in thousands)				
Cash, cash equivalents and short-term investments	\$2,310,715	\$1,608,496	\$1,200,405	\$748,078	\$797,811
Total content assets, net (1)	7,218,815	4,939,460	3,838,364	2,934,099	2,022,650
Working capital (1)	1,902,216	1,263,899	883,049	553,887	595,780
Total assets (1)	10,202,871	7,042,500	5,404,025	3,961,781	3,062,111
Long-term debt (1)	2,371,362	885,849	491,462	195,782	195,123
Long-term debt due to related party (1)	—	—	—	198,109	197,792
Non-current content liabilities	2,026,360	1,575,832	1,345,590	1,076,622	739,628
Total content liabilities	4,815,383	3,693,073	3,121,573	2,443,469	1,674,664
Total stockholders’ equity	2,223,426	1,857,708	1,333,561	744,673	642,810

(1) Certain prior year amounts have been reclassified to conform to the current year presentation in the consolidated financial statements. See Note 1 and Note 2 in Item 8, Financial Statements and Supplementary Data for further detail.

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Other Data:

	As of / Year Ended December 31,				
	2015	2014	2013	2012	2011
	(in thousands)				
Net global streaming membership additions during period (1)	17,371	13,041	11,083	9,738	—
Global streaming memberships (1)	74,762	57,391	44,350	33,267	23,529

Prior to July 2011, in the U.S., our streaming and DVD-by-mail operations were combined and members could receive both streaming content and DVDs under a single “hybrid” plan. In July 2011, we separated the combined plans, making it necessary for members who wish to receive both DVDs-by-mail and streaming content to have two separate membership plans. Prior to these changes to our pricing and plan structure in 2011, we did not separately track streaming memberships.

A membership (also referred to as a subscription or a member) is defined as the right to receive the Netflix service following sign-up and a method of payment being provided. Memberships are assigned to territories based on the geographic location used at time of sign-up as determined by our internal systems, which utilize industry standard geo-location technology. We offer free-trial memberships to new and certain rejoining members. Total members include those who are on a free-trial as long as a method of payment has been provided.

- (1) A membership is canceled and ceases to be reflected in the above metrics as of the effective cancellation date. Voluntary cancellations become effective at the end of the prepaid membership period, while involuntary cancellation of the service, as a result of a failed method of payment, becomes effective immediately except in limited circumstances where a short grace period is offered to ensure the streaming service is not interrupted for members who are impacted by payment processing delays by our banks or integrated payment partners. The number of members in a grace period at any given point is not material.

Table of ContentsItem 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
Overview and Results of Operations

The following represents our consolidated performance highlights:

	As of/ Year Ended December 31,			Change			
	2015	2014	2013	2015 vs. 2014	2014 vs. 2013		
	(in thousands, except revenue per membership and percentages)						
Global streaming memberships	74,762	57,391	44,350	30	% 29		%
Global streaming average monthly revenue per paying membership	\$8.15	\$8.20	\$8.03	(1))% 2		%
Revenues	\$6,779,511	\$5,504,656	\$4,374,562	23	% 26		%
Operating income	\$305,826	\$402,648	\$228,347	(24))% 76		%
Net income	\$122,641	\$266,799	\$112,403	(54))% 137		%

Consolidated revenues for 2015 and 2014 increased as compared to prior years due to growth in global streaming average paying memberships, the majority of which was growth in our international memberships reflecting our expansion and focus on Netflix as a global Internet TV network. For the year ended December 31, 2015, the impact from membership growth was slightly offset by a decrease in average monthly revenue per paying streaming membership resulting from unfavorable foreign currency fluctuations impacting our International streaming segment. This was partially offset by increases resulting from price changes and plan mix. The decrease in operating income for the year ended December 31, 2015 as compared to the year ended December 31, 2014 is due primarily to increased marketing and headcount costs to support our international expansion in addition to increased content expenses as we continue to acquire, license and produce content, including more Netflix originals. Net income is further impacted by the increase in interest expense associated with our debt issuance in the first quarter of 2015 as well as to an increase in losses on foreign currency denominated transactions.

We offer three types of streaming membership plans. In the U.S. our basic plan is priced at \$7.99 per month and includes access to standard definition quality streaming on a single screen at a time. Our most popular streaming plan is priced at \$9.99 per month and includes access to high definition quality streaming on two screens concurrently. Our premium plan is priced at \$11.99 per month and includes access to high definition and ultra-high definition quality content on four screens concurrently. Internationally, the membership plans are structured similarly to the U.S. and range in price from the U.S. dollar equivalent of approximately \$5.00 to \$18.00 per month.

We expect that from time to time the prices of our membership plans in each country may change. For instance, in the second half of 2015, we increased the price of our two-screen high definition plan in the U.S. and several European countries. In May 2014, in the U.S., we increased the price of our high definition plan from \$7.99 per month to \$8.99 per month with existing memberships grandfathered for a two year period. In October 2015, in the U.S., we increased the price of this same high definition plan from \$8.99 per month to \$9.99 per month with existing memberships grandfathered for a one year period. In 2016, the grandfathered pricing period will expire for a substantial number of U.S. memberships and the members will have the option of electing the basic streaming plan at \$7.99 or continuing on the high definition plan at the higher price of \$9.99.

The following represents the key elements to our segment results of operations:

We define contribution profit (loss) as revenues less cost of revenues and marketing expenses incurred by the segment. We believe this is an important measure of our operating segment performance as it represents each segment's performance before global corporate costs.

For the Domestic and International streaming segments, content expenses, which include the amortization of the streaming content assets and other expenses associated with the licensing and acquisition of streaming content, represent the vast majority of cost of revenues. Streaming content rights were generally obtained for our current

geographic regions. As we expanded internationally, we obtained additional rights for the new geographies. With our global expansion, we now aspire to obtain global rights for our new content. We allocate this content between the Domestic and International segments based on estimated fair market value. Other cost of revenues such as streaming delivery expenses, customer service and payment processing fees, including those we pay to our integrated payment partners, tend to be lower as a percentage of total cost of revenues as compared to content licensing expenses. We have built our

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own global content delivery network ("Open Connect") to help us efficiently stream a high volume of content to our members over the Internet. Streaming delivery expenses, therefore, also include equipment costs related to our content delivery network and all third-party costs, such as cloud computing costs, associated with delivering streaming content over the Internet. Cost of revenues in the Domestic DVD segment consist primarily of delivery expenses, content expenses, including amortization of DVD content assets and revenue sharing expenses, and other expenses associated with our DVD processing and customer service centers. Delivery expenses for the Domestic DVD segment consist of the postage costs to mail DVDs to and from our members and the packaging and label costs for the mailers.

For the Domestic and International streaming segments, marketing expenses consist primarily of advertising expenses and payments made to our affiliates and device partners. Advertising expenses include promotional activities such as digital and television advertising. Payments to our affiliates and device partners include fixed fee and /or revenue sharing payments. Marketing expenses are incurred by our Domestic and International streaming segments given our focus on building consumer awareness of the streaming offerings and in particular our original content. Marketing expenses incurred by our International streaming segment have been significant and fluctuate dependent upon the number of international territories in which our streaming service is offered and the timing of the launch of new territories. We do not incur marketing expenses for the Domestic DVD segment.

We have demonstrated our ability to grow domestic streaming contribution margin as evidenced by the increase in contribution margin from 17% in 2012 to 33% in 2015. As a result of our focus on growing the streaming segments, contribution margins for the Domestic and International streaming segments are lower than for our Domestic DVD segment.

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Segment Results

Domestic Streaming Segment

	As of/ Year Ended December 31,			Change		2014 vs. 2013			
	2015	2014	2013	2015 vs. 2014					
	(in thousands, except revenue per membership and percentages)								
Memberships:									
Net additions	5,624	5,694	6,274	(70) (1)%	(580) (9)%
Memberships at end of period	44,738	39,114	33,420	5,624	14	%	5,694	17	%
Paid memberships at end of period	43,401	37,698	31,712	5,703	15	%	5,986	19	%
Average monthly revenue per paying membership	\$8.50	\$8.14	\$7.97	\$0.36	4	%	\$0.17	2	%
Contribution profit:									
Revenues	\$4,180,339	\$3,431,434	\$2,751,375	\$748,905	22	%	\$680,059	25	%
Cost of revenues	2,487,193	2,201,761	1,863,376	285,432	13	%	338,385	18	%
Marketing	317,646	293,453	265,232	24,193	8	%	28,221	11	%
Contribution profit	1,375,500	936,220	622,767	439,280	47	%	313,453	50	%
Contribution margin	33	%	27	%	23	%			

Year ended December 31, 2015 as compared to the year ended December 31, 2014

In the Domestic streaming segment, we derive revenues from monthly membership fees for services consisting solely of streaming content to our members in the United States. Our two screen high definition plan continues to be the most popular plan choice for new memberships. The increase in our domestic streaming revenues was due to a 17% growth in the average number of paid memberships and a 4% increase in average monthly revenue per paying membership resulting from our price changes and plan mix.

The increase in domestic streaming cost of revenues was primarily due to a \$208.1 million increase in content expenses relating to our existing and new streaming content, including more exclusive and original programming. In addition, we had a \$37.9 million increase in streaming delivery expenses and a \$39.4 million increase in other costs, such as payment processing fees and customer service call centers, due to our growing member base.

Domestic marketing expenses increased primarily due to an increase in advertising and public relations spending. Our Domestic streaming segment had a contribution margin of 33% for the year ended December 31, 2015, which increased as compared to the contribution margin of 27% for the year ended December 31, 2014 due to growth in paid memberships and revenue, which continued to outpace content and marketing spending. Our 2020 domestic streaming contribution margin target remains at 40%.

Year ended December 31, 2014 as compared to the year ended December 31, 2013

The increase in our domestic streaming revenues was due to the 22% growth in the average number of paid memberships, as well as to the 2% increase in average monthly revenue per paying membership resulting from our price increase for new members in the second quarter of 2014 and introduction of the higher priced plan in 2013.