Money Where Your Mouth Is
(the hidden costs of third-party delivery)

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Introduction.

Third-party delivery has, in just a few short years, changed the face of the food and beverage industry as we've known it.

This session was intended to examine the Pros, the Cons, and the hard, soft, and hidden costs of third-party delivery, with a focus on how food and beverage operators could protect themselves from additional costs, liability, and unintended consequences.

As of March 2020, however, third-party delivery became necessary for survival for both fast casual and dine-in restaurants (QSRs use them, too, but most QSR units feature drive-up/drive-through, and thus were forced to rely less on costly delivery services).

Now the most important considerations for foodservice operators are the use of tamper-resistant/tamper-evident packaging (or labels on packaging), negotiation of contractual liability/indemnity provisions, and generating enough sales to stay alive.

This paper will thus present information about third-party delivery as they existed pre-COVID, with the understanding that the data is still relevant, and will be all the more relevant when things return to normal (though whether we see a backlash against third-party delivery by foodservice operators remains to be seen).

The Pre-COVID State of Things.

In early 2020, restaurants' delivery sales were projected to outpace in-store sales by **more than three times** through 2023. As such, restaurants around the nation found themselves needful of embracing what was still an emerging and unregulated trend. App-based, third-party delivery platforms had encroached on traditional, on-premise restaurant sales, forcing companies across all facets of the foodservice industry, from QSR to fine dining, to adapt to this new and growing trend.[1]

[1] "Study: Delivery Sales to Outpace In-Restaurant Sales" – *QSR Magazine*, March 5, 2019.

“ ‘As consumers find themselves more and more pressed for time, online ordering from restaurants has captivated a diner demographic increasingly shaped by the sophisticated world of consumer ecommerce,’ says Manny Picciola, Managing Director at L.E.K. Consulting and coauthor of *Meals on Wheels: The Digital Ordering and Delivery Restaurant Revolution*. ‘And millennials are a driving force behind the growth of digital ordering and delivery. We expect them to account for a full 70 percent of the at-home delivery business by 2020.’ ”[2]

A 2019 survey of 1,053 respondents by Steritech, a provider of to-go containers to the food and beverage industry, provides important statistics on the state of delivery in the United States.[3] Respondents provided useful information, including demographic data, frequency of delivery orders, and how orders are placed. Surprisingly, older diners may be using delivery more than younger age groups:

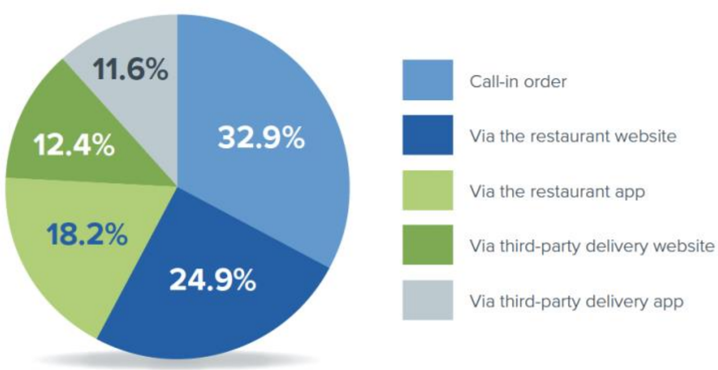
In the previous six months:

• 9% of those ages 18-27 ordered more than 10 times

• 15% of those ages 28-35 ordered more than 10 times

• 18% of those ages 36-51 ordered more than 10 times[4]

The majority of delivery orders, however, at least for now, appear to originate with the restaurants themselves:[5]



How delivery orders are placed. What methods did delivery customers use to place their orders?

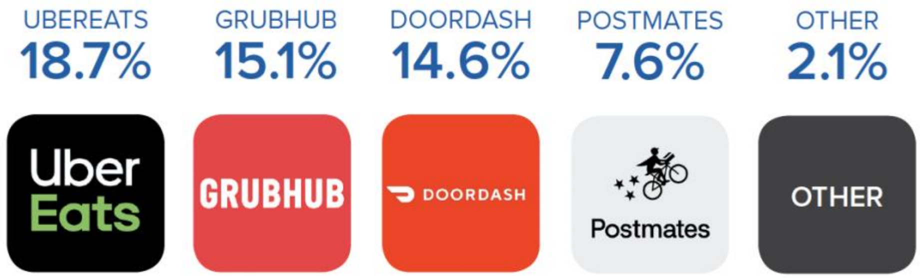
[2] Id.

[3] “Opportunity To Go – Consumer insights to drive your restaurant’s delivery experience” – available at https://deliverystudy.steritech.com/ (last visited February 20, 2020).

[4] Id, at p. 5.

[5] Id, at p. 7.

Despite these figures, third-party delivery is surging (along with the valuations of third-party delivery companies).[6] UberEats leads the pack:[7]



As a result, restaurants and other food and beverage companies had a rapidly closing window in which to come to terms with the new economy involving third-party delivery apps before late-adopters are left behind.

While third-party delivery companies tout their marketing prowess as a benefit to restaurant companies trying to compete for dining dollars, those relationships do not come without significant costs. “Third-party delivery comes with its own cons. Commission and delivery fees can scrape away at the already small margin generated by delivery—and could be costing you customers, based on feedback in this survey. But more risk for the brand may be the quality control issues: once food leaves the restaurant, the restaurant doesn’t have any control over how long delivery takes, food temperatures, food security, and delivery personnel behavior.”[8]

Restaurants must not only negotiate the pricing of delivery service, but should, perhaps over price concerns, prioritize negotiating the indemnity and liability-shifting provisions in the services’ form contracts. Additionally, operators must take steps to protect their deliveries from tampering by delivery drivers,[9] while ensuring their delivery packaging is adequate to maintain food integrity.

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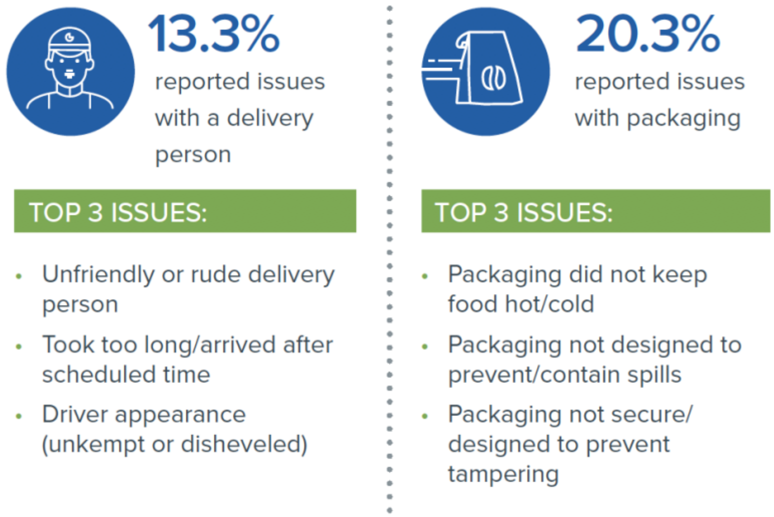
[6] Leach, Kamaron; “Grubhub Spikes After Sale Chatter Spurs Call for M&A,” *Bloomberg*, Jan. 9, 2020; available at https://www.bloomberg.com/news/articles/2020-01-09/grubhub-sale-report-spurs-calls-for-food-delivery-consolidation (last visited February 20, 2020).

[7] *See* Steritech, p. 8.

[8] Id at 9.

[9] Matias, Dani; “1 in 4 Food Delivery Drivers Admit to Eating Your Food,” *NPR*, July 30, 2019; available at https://www.npr.org/2019/07/30/746600105/1-in-4-food-delivery-drivers-admit-to-eating-your-food (last visited February 20, 2020).



Other concerns to be addressed include delivery company insurance, disclaimers of agency between the delivery service (and its drivers) and the restaurant, compliance with safe food handling procedires, and mandatory driver tracking technology (so food integrity can be monitored, and foodborne illness claims can be refuted).[10]

The major hidden cost of third-party delivery, however, may appear in another realm altogether. Restaurants with leases requiring the payment of a percentage of gross sales (usually after a breakpoint of sales have been reached) may need to either renegotiate the definition of gross sales to eliminate the inclusion of third-party delivery charges, or negotiate with the delivery company to receive payment net of delivery fees.

For example, if the restaurant pays rent equal to six percent (6%) of gross sales, all sales are used to calculate that number, unless the definition of that term in the lease allows for deductions (usual deductions include sales tax and server gratuities, among others). When an operator makes $10,000 in sales in a month via third-party delivery, all $10,000 of revenue for those sales hits the restaurant's point-of-sale system, and is consequently included in the gross sales calculation. The delivery service, however, will invoice the restaurant (usually weekly) for its share of the delivery sales (sometimes as high as thirty percent (30%), which the restaurant pays to the service. Thus, the restaurant faces the unenviable predicament of paying rent on $10,000 in sales, when it only realized $7,000 (making the effective rate of percentage rent much higher).

[10] Orato, Damien and Singer, Suzanne; "The cost of convenience: Understanding the third-party delivery dilemma," Nation's Restaurant News, April 24, 2017, available at https://www.nrn.com/operations/cost-convenience-understanding-third-party-delivery-dilemma (last visited February 20, 2020).

Conclusion.

Thus, while third-party delivery continues to grow in popularity among diners across all demographic groups, restaurants and other food and beverage operators must act now to negotiate contracts with those companies that offer competitive rates, they must also consider the soft and hidden costs, fighting for protection from liability, addressing issues that could affect a restaurant's brand, and remaining vigilant in seeking to minimize the amount of rent paid on gross sales that include delivery revenue.