

Third Party Delivery Platforms and Virtual Kitchens: Briefing Memo

Introduction

On December 9, 2019, the Small Business Commission formally requested to schedule a special hearing to discuss the impact that third party delivery platforms and ghost/virtual kitchens are having on the economic health of the brick and mortar small business community in San Francisco. The Commission hopes to gain a better understanding of the third-party delivery platform and virtual kitchen market and how City agencies regulate those entities as compared to traditional neighborhood serving brick and mortar businesses. They also hope to hear from business owners who have been impacted by third party delivery platform and virtual kitchen entities. Findings and recommendations generated from the hearing will be presented to both the Mayor's Office and the Board of Supervisors.

Background

I. Third Party Delivery Platforms

Third Party Delivery Platform, commonly known as delivery apps, are effectively 'aggregators' which connect customers with a multitude of local restaurants and retailers via websites or apps¹. Orders placed via through these platforms are typically prepared by the restaurant or retailer and expedited by delivery workers. Popular delivery apps include Doordash, GrubHub, UberEats, and Postmates².

The delivery app market is growing rapidly, with platform sales increasing 41% in 2019³. Industry bankers forecast that two out of three restaurant deliveries will originate through a third-party platform⁴. However, customers and restaurant/retailer partners need to be aware of the financial costs and competitive risks that come with the seemingly new convenience.

Delivery apps assess sizeable commissions on orders, and some industry firms have been credibly accused of charging hidden fees to their restaurant/retail partners⁵, listing businesses on their platforms without the business' consent⁶, and "cyber-squatting." Cyber-squatting is an anti-competitive practice where the third party platform preemptively buys up web domains that look like they belong to a restaurant or retailer, creating "shadow sites"⁷. In some cases, the shadow sites list alternative menus or contact information, including phone numbers, that force customers to use the third-party platform.

¹ <https://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/the-changing-market-for-food-delivery>

² <https://fortune.com/2019/03/11/doordash-tops-grubhub-on-demand-food/>

³ <https://secondmeasure.com/datapoints/food-delivery-services-grubhub-uber-eats-doordash-postmates/>

⁴ <https://williamblair.bluematrix.com/sellside/EmailDocViewer?encrypt=1effb163-5673-4ad2-9ef3-59edcfab93c3&mime=pdf&co=williamblair&id=rlist@williamblair.com&source=mail>

⁵ <https://www.restaurantdive.com/news/delivery-by-the-numbers-how-top-third-party-platforms-compare/564279/>

⁶ <https://www.eater.com/2020/1/29/21113416/grubhub-seamless-kin-khao-online-delivery-mistake-doordash>

⁷ <https://thecounter.org/grubhub-domain-purchases-thousands-shadow-sites/>

There are benefits to doing business with delivery apps. They can provide restaurants and retailers access to new customers and can assist with brand awareness⁸. Delivery apps are also positioned to assist businesses that may not have high levels of tech literacy in leveraging consumer data that is collected relative to orders made via their platforms.

II. Ghost, virtual, dark, and cloud kitchens

Ghost, virtual, dark, and cloud kitchens are terms used to describe a significant evolution in the restaurant sector. Ghost kitchens or cloud kitchens, are *shared kitchen facilities*, where the facility is subdivided into separate kitchen facilities for use by individual tenants for food preparation with infrastructure to support those tenants' fulfillment of delivery orders placed by consumers. A ghost kitchen's "tenants" may include traditional restaurants, food trucks, catering companies, and other food businesses.

A virtual kitchen or virtual restaurant or dark kitchen is often considered to be one of the types of entities that rent from a "ghost kitchen as described above. These businesses produce and sell meals strictly via online order and not directly to members of the public. Virtual kitchens or restaurants may be run by entities that also have brick and mortar locations (not necessarily in San Francisco), or may not have a brick and mortar location at all and may strictly have an online presence.

Though the terms are often used interchangeably, there does appear to be a certain taxonomy associated with them. Where this industry phenomenon is evolving as it is growing, we can expect that the vernacular will also continue to morph with it.

The advent of ghost and virtual kitchens is likely related to the exponential growth of and continued demand for goods via delivery, particularly meals. To meet this growing demand, restaurants and some retailers are beginning to transition to a model where the food they produce and goods that they sell are for delivery apps only. Many businesses are recognizing that utilizing a ghost or virtual kitchen model allows them to produce meals at a higher volume, significantly reduce labor costs, and requires fewer overhead costs, like rent⁹. And, for more nascent restaurants and retailers, the lower upfront costs needed to open can provide them with an opportunity to build their brand and enough capital to possibly one day open a brick and mortar¹⁰.

Delivery apps, ghost kitchens, and virtual kitchens in San Francisco:

I. Delivery apps

In the fall of 2018 the San Francisco Municipal Transportation Agency (SFMTA) conducted to better understand benefits and challenges related to delivery apps . The SFMTA refers to deliver app services as 'courier network services'. Merchants and drivers/couriers were surveyed, respectively. Of the 32 merchant responses, 80% reported that they used courier network services. Most reported that using those services to increase revenue and expand their customer base. Deliveries made between 4:00 p.m. and 8:00 p.m. were

⁸ <https://thecounter.org/grubhub-domain-purchases-thousands-shadow-sites/>

⁹ <https://www.fool.com/investing/2020/01/25/why-ghost-kitchens-are-the-next-restaurant-frontier.aspx>

¹⁰ <https://www.delish.com/food/a29462910/ghost-cloud-kitchen-trend-fast-food-chains/>

most common. Of the 61 courier responses, more than half reported to use a car to make deliveries, this was followed by biking, and then walking. Approximately half of the respondents reported that they traveled an average of three miles or less to pick up and deliver the order. Approximately a third of the respondents reported that they double parked in order to pick up an order.

Sentiments related to delivery apps were shared during a Board of Supervisors Land Use hearing held in 2019 on the State of the Restaurant Industry in San Francisco. Restaurateurs shared that demand for online ordering has placed a strain on their ability to be successfully, particularly as they have communicated other economic challenges they are facing.¹¹ Despite the costs, many restaurateurs have also reported that opting out of on-demand delivery would leave them in an even more economically precarious position.

II. Ghost and virtual kitchens

Three distinct ghost kitchen models have so far been observed in San Francisco and are described below.

A. *Model 1:*

Under this model, the ghost kitchen operator effectively serves as a landlord to a number of virtual kitchen tenants. The operator manages and maintains the physical space of the ghost kitchen facility and, outfits each virtual kitchen tenant space with commercial kitchen equipment that is ready to be used upon move-in. There appears to be one such operator currently open in the City.

The ghost kitchen facility appears to be registered with the Treasurer and Tax Collector's (TTX) Office as both a Real Estate and Rental Leasing Service and a Food Service. It also appears that the ghost kitchen facility has been permitted by the Planning Department as a Catering Service Use.

Virtual kitchen tenants appear to have been permitted with the Planning Department as Limited Restaurants. Some, but not all, virtual kitchen tenants have obtained permit through the Department of Public Health (DPH)¹². These permits include: Retail Market with Food Prep – under 5,001 square feet (H07); Restaurant – under 1,000 square feet (H24); Restaurant – 1,000-2,000 square feet (H25).

B. *Model 2*

There is little information available regarding the *exact* nature of the relationship between the ghost kitchen operator and the virtual kitchen tenant. However, there are five active locations open in the City and all are registered with TTX as a Food Service. Three are located in Neighborhood Commercial Districts.

The five locations have been permitted by the Planning Department as follows: Restaurant (1); Limited Restaurant (x3); one location's information could not be found.

One location of the five appears to have obtained a DPH permit for Restaurant – Under 1,000 square feet.

¹¹ <https://sf.eater.com/2019/9/17/20869268/sf-restaurants-meet-city-hall-board-of-supervisors-crisis>

¹² Applications for the other tenants may be in progress with DPH.

C. Model 3

This model takes the form of a mobile trailer. This type of ghost kitchen can, in theory, move more freely to meet varying consumer demands by neighborhood. It is understood that, this model is permitted as a mobile food facility level 5, which allows for the most intense level of food prep and, is served by a commissary for off-site water disposal and cleaning. This model currently operates under a Temporary Use Authorization.

Considerations:

I. Land Use Permitting

At present, there is not a clear land use definition or category for ghost kitchens or virtual kitchens. It appears per the Property Information Map, that some ghost kitchens, are currently considered to be a Catering Service which is considered to be a Non-Retail Sales and Services Use. And, some virtual kitchens as described above, are considered to be Limited Kitchens.

There are a number of considerations to be contemplated regarding ghost kitchens that are currently operating in Neighborhood Commercial Districts¹³. Businesses operating in Neighborhood Commercial Districts are intended to serve the daily needs of those residents and should be places of public accommodation. Policy makers should opine on whether or not ghost kitchens fit this description. Additionally, brick and mortar restaurants operating in these Districts must comply with certain operating hour restrictions due to specified land use controls. Land use policy should be administered equitably between brick and mortar and ghost and virtual kitchens. In addition, there is also a concern that ghost kitchen operations in Neighborhood Commercial Corridors could result in an increased presence of delivery vehicles and could contribute to increased levels of traffic and noise.

There is also a need to consider formula retail restrictions as they relate to ghost and virtual kitchens. This is especially important as formula retailers like McDonalds and Starbucks have indicated interest in opening their own ghost kitchen facilities¹⁴. In addition, without a clearly defined land use policy relative to these entities, formula retailers *may* be able to open as a virtual kitchen *within* a ghost kitchen facility and as such, circumvent established formula retail restrictions.

II. Public Health Permitting

The Department of Public Health permits a variety of entities in the Retail Food space. Through the Retail Food Safety Program, their charge is to monitor compliance with local and state food safety regulations in restaurants, markets, and all other retail food operations. In late fall of 2019, a new definition relative to the Retail Food space was added to the Health Code, 'shared kitchen facilities'. It is understood that this definition applies to the models described above. However, given that many ghost and virtual kitchens appear to have been granted permits to operate as Catering Facilities, Restaurants, and Limited Restaurant, it is unclear as to how exactly they meet the definitions of those uses.

¹³ <https://www.sfgate.com/food/article/New-ghost-kitchen-opens-in-Noe-Valley-14989895.php>

¹⁴ <https://www.businessinsider.com/fast-food-chains-turn-to-ghost-kitchens-and-mobile-restaurants-2019-9>

CITY AND COUNTY OF SAN FRANCISCO
OFFICE OF SMALL BUSINESS
SMALL BUSINESS COMMISSION



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February 20, 2020

Regina Dick-Endrizzi, Executive Director
Office of Small Business
1 Dr. Carlton B. Goodlett Place
City Hall, Room 110
San Francisco, CA 94102

Subject: Small Business Commission letter dated February 10, 2020_SFMTA responses

Dear Director Dick-Endrizzi:

Following are San Francisco Municipal Transportation Agency (SFMTA) responses to the questions related to third-party online delivery platforms included in the Small Business Commission's letter dated February 10, 2020.

Does SFMTA know or have a reasonable estimate for how many third-party delivery vehicles use our roads daily?

The SFMTA does not know or have an estimate of the number of third-party delivery vehicles using San Francisco streets at this time. In an effort to better understand the benefits and challenges of app-based delivery services, referred to as courier network services, the SFMTA conducted two surveys in the fall of 2018—one for merchants and one for drivers/couriers.

A total of 32 merchants responded to the survey. Key findings from the courier survey include:

- Over 80 percent of the merchants who responded use courier network services to make deliveries.
- The most common reasons for exploring the use of courier network services were to increase revenue and expand their customer base.
- Courier deliveries are made throughout the day with 4 to 8 p.m. being the most common timeframe for deliveries reported by the merchants.

A total of 61 couriers responded to the survey. Key findings from the courier survey include:

- Over half of the couriers used a car to make deliveries, followed by biking and walking.
- About half of the couriers reported traveling an average of three miles or less to pick up and deliver the order.



- About a third of the couriers reported double parking to pick up an order.

The San Francisco County Transportation Authority has conducted studies to understand the impacts of Transportation Network Companies (TNCs), primarily Uber and Lyft in San Francisco. The TNCs Today report (2017) provided estimates of TNC trips within San Francisco, where these trips occurred, and the time of day and day of week trips were made. The TNCs and Congestion report (2018) analyzed the impact that TNCs have on congestion within San Francisco as measured by vehicle hours of delay, vehicle miles traveled and average speed.

As third-party delivery app and virtual kitchen markets grow, can SFMTA estimate how many more vehicles may be on our roads?

At this time there is insufficient information to estimate the growth of third-party delivery app and virtual kitchen markets and how it would impact the number of vehicles operating on city streets. From the 2018 courier survey described above, over half of the couriers surveyed reported using cars to make their deliveries.

How are third-party delivery app vehicles affecting traffic and parking in San Francisco?

Deliveries facilitated by apps or online platforms are relatively new but appear to be growing quickly. As such the traffic and parking impacts of vehicles associated with third party delivery apps is unknown at this time. The regulatory authority of these services is unclear, but one area that SFMTA can seek to address the impacts of services like these is through curb management. In response to increasing demand for limited curb space the SFMTA developed the Curb Management Strategy which includes a framework for how the SFMTA will manage and allocate the City's curb space in a way that is both responsive to current demands and anticipates future needs, and a set of recommendations for changes to policies, processes, and existing law. The Curb Management Strategy was adopted by the SFMTA Board of Directors at its February 18, 2020 meeting. Included in the strategy is an objective to provide for goods loading in non-commercial vehicles. Recommendations include:

- Encourage people who use personal vehicles for goods delivery to register for commercial license plates
- Consider removing attended vehicle requirement for noncommercial vehicles in yellow and white zones
- Initiate a communications and marketing effort to inform drivers that loading is permitted for up to three minutes in yellow zones if the vehicle remains attended



Does SFMTA know if public garages/parking spaces have been converted/permitted for use by delivery platforms? If yes, how many? For context, see this article from the Chronicle.

At this time there are no kitchens or designated third-party parking spaces for use by delivery platforms in any public garage. All public garages offer monthly/daily parking options. A number of vehicle share platforms, including Zipcar, Getaround, Maven, and Scoot, reserve parking spaces in public garages.

If you have additional questions or would like clarification on any of these responses, please do not hesitate to contact Darton Ito, Planning Deputy Director/Office of Innovation Manager at darton.ito@sfmta.com.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Jeffrey Tumlin'.

Jeffrey Tumlin
Director of Transportation

From: [Degrafinried, Alaric \(DPW\)](#)
To: [Dick-Endrizzi, Regina \(ECN\)](#)
Cc: [Gordon, Rachel \(DPW\)](#); [Donovan, Dominica \(ECN\)](#); [Spitz, Jeremy \(DPW\)](#)
Subject: RE: Small Business Commission Request for Presentation- Special Hearing 2/26/2020
Date: Thursday, February 20, 2020 7:39:49 PM
Attachments: [image004.png](#)

Director Dick-Endrizzi,

Thank you for your message. Per your request, I am providing a written response ahead of the February 26, 2020 Small Business Commission special hearing.

Upon reviewing the Chronicle article provided in your email, the Department has determined that none of the identified restaurants noted are operating within the public right-of-way. The restaurants are all located within public parking lots, and therefore do not fall under the permitting authority or jurisdiction of Public Works.

Please find the Department's official, written response to the two questions posed by your office:

1. The Department has determined, in coordination with other City Agencies, that the restaurants cited in the Chronicle article are all located within public parking lots, and therefore do not fall under the permitting authority or jurisdiction of Public Works.

The Public Works Code does not explicitly prohibit the operation of virtual kitchens under the Mobile Food Facility (MFF) permit. However, in order to determine acceptability, each MFF application is reviewed for compliance with the Public Works Code, Public Works Director's Orders, any other applicable codes. Additionally, the Department of Public Health and Fire Department must provide approvals prior to MFF operation.

2. Public Works has not issued any permits to virtual kitchens, through the Mobile Food Facility Permit or any other permit type, to allow their operation. Currently, there are no requests from any company or companies for Public Works to permit virtual kitchens.

Please let us know if you have any additional questions.

Best,

Alaric

Alaric Degrafinried
San Francisco Public Works
1 Dr. Carlton B. Goodlett Place
City Hall, Room 348
San Francisco, CA 94102
(415) 554-6920
www.sfpw.org

From: Spitz, Jeremy (DPW)
Sent: Tuesday, February 11, 2020 11:12 AM
To: Donovan, Dominica (ECN) <dominica.donovan@sfgov.org>; Degrafinried, Alaric (DPW) <alaric.degrafinried@sfdpw.org>

Cc: Dick-Endrizzi, Regina (ECN) <regina.dick-endrizzi@sfgov.org>; Gordon, Rachel (DPW) <rachel.gordon@sfdpw.org>
Subject: RE: Small Business Commission Request for Presentation- Special Hearing 2/26/2020

Hi Dominca,

Thanks for your email. We will work on a response and follow up with you before next Thursday.

Thanks,

Jeremy Spitz

Policy and Government Affairs

San Francisco Public Works | City and County of San Francisco

City Hall, Room 348 | 1 Dr. Carlton B. Goodlett Place | San Francisco, CA 94102

Office: (415) 554-6972

sfpublicworks.org · twitter.com/sfpublicworks

From: Donovan, Dominica (ECN) <dominica.donovan@sfgov.org>
Sent: Monday, February 10, 2020 4:30 PM
To: Degrafinried, Alaric (DPW) <alaric.degrafinried@sfdpw.org>
Cc: Spitz, Jeremy (DPW) <Jeremy.Spitz@sfdpw.org>; Dick-Endrizzi, Regina (ECN) <regina.dick-endrizzi@sfgov.org>; Gordon, Rachel (DPW) <Rachel.Gordon@sfdpw.org>
Subject: Small Business Commission Request for Presentation- Special Hearing 2/26/2020

Dear Acting Director Degrafinried:

On December 9, 2019, the Small Business Commission (the Commission or SBC) formally requested to schedule a special hearing to discuss the impact that third-party online delivery platforms and virtual kitchens are having on the economic health of the brick and mortar small business community in San Francisco. The Commission hopes to gain a better understanding of the third-party delivery platform and virtual kitchen market and how City agencies regulate those entities. They also hope to hear from business owners who have been impacted by the delivery app and virtual kitchen entities. Findings and recommendations generated from this hearing will be presented to both the Mayor's office and the Board of Supervisors.

Accordingly, per Article XVI Sec.2A.240(a)(10) of the Administrative Code, the Commission is requesting the Department of Public Works (DPW) to provide written responses to the following questions:

- There are certain virtual kitchen types, like [Reef Technologies](#), who operate similarly to a Mobile Food Facility. Are these types of virtual kitchens permitted to operate, as described in [this Chronicle article](#), via a Mobile Food Facility permit or another permit?
- If they are permitted to operate through DPW, how many permits have been issued? Can you describe the permitting process?

The hearing has been scheduled for Wednesday February 26, 2020 a 1:00pm and will be held in Room 408, City Hall. Ahead of that hearing, the Commission is requesting that DPW's **written responses be submitted by end of day Thursday February 20, 2020**. The Commission also invites DPW to attend the hearing.

Please confirm your receipt of this request by end of day Wednesday February 12, 2020. Please send DPW's written responses or any questions you may have to Dominica Donovan, Small Business Commission Secretary, at dominica.donovan@sfgov.org.

Thank you in advance for your attention to this.

Sincerely,

A handwritten signature in black ink, appearing to read "Regina Dick-Endrizzi".

Regina Dick-Endrizzi
Director, Office of Small Business

Dominica Donovan

Senior Policy Analyst
Small Business Commission Secretary
Pronouns: She, Her, Hers

Office of Small Business
City and County of San Francisco
City Hall, Room 140
Direct: (415) 554-6489 | Office: (415) 554-6134

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