RULES COMMITTEE: 5-6-20
ITEM: G.2

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: RULES AND OPEN GOVERNMENT COMMITTEE

FROM: Councilmember Lan Diep

SUBJECT: FEE CAP ON FOOD DELIVERY SERVICES

DATE: April 30, 2020

Approved Lan Diep

Date 4/30/20

RECOMMENDATION

Direct the City Manager to draft and enact an urgency ordinance that:

1. Limit fees third-party food-delivery services operating in San José may charge on restaurants to:

    a. 10% where food-delivery companies do not make personal protective equipment available to the employees or independent contractors who make deliveries; and
    b. 15% where food-delivery companies establish that personal protective equipment is provided at no cost to the employees or independent contractors making deliveries;

2. Sunsets the 15% cap on fees once restaurants in Santa Clara County may offer unrestricted dine-in service;

3. Grants food-delivery companies 14 days per incident to refund any fees taken in excess of these limits; and

4. Imposes a sliding scale of fines for repeated instances of exceeding the fee limits.

BACKGROUND

The food-delivery market has only existed since 2011. Four companies – DoorDash, GrubHub, Postmates, and Uber Eats – control about 95% of the market. Of the four, only GrubHub has made a profit so far, yet even it is struggling. In the third quarter of 2019, GrubHub's net income was just $1 million compared to $22.7 million in the third quarter of 2018. Postmates, DoorDash, and Uber Eats are still burning through venture capital and have yet to have a profitable quarter.

The collective efforts of these companies to make a profit are hurting the restaurant industry more than they are helping. When a restaurant makes a sale directly to a customer, the restaurant keeps all the profit. Now, as is increasingly the case while Santa Clara County is under a Shelter-In-Place Order, consumers buy food through a food-delivery app. Restaurants have little choice but to partner with a food-delivery company to have their food featured in the apps. But sales made through the apps come at a high cost.

Earlier this month a class-action lawsuit was filed in federal court in the Southern District of New York against DoorDash, GrubHub, Postmates, and Uber Eats, alleging that the companies charge "exorbitant fees" ranging from 13.5% to 40% of a restaurant's profit, while restaurants typically only make 3% to 9% off a sale. San Francisco and Seattle have limited the fees food-delivery services may charge restaurants to 15%. Los Angeles is considering the same. New York City is exploring a 10% cap. Chicago is studying a 5% cap.

ARGUMENT

For many years, food-delivery companies have made consumers accustomed to the convenience of having food brought to their doorsteps for a marginal fee. As they changed our dining habits by making ordering takeout more appealing, these companies have also made it increasingly difficult for brick-and-mortar restaurants to profit. As the covid-19 virus has shut down economies the world over, restaurants in California no longer even have the option of serving dine-in customers and can now only offer takeout options. Reliance on food-delivery services is at an all-time high. According to the research firm Second Measure, during the last week of March, credit card spending on food-delivery was up 70% compared to this time last year.

During this time, some companies have waived fees on independent restaurants or lowered their standard commission fees overall. But the fact remains that food-delivery fees add an extra cost burden to restaurants already running thin margins. As this pandemic has revealed, too many restaurants do not have money saved up to last a month. Restaurants prefer that customers purchase directly from their stores but food-delivery companies have created a captive market of hungry customers with apps already downloaded on their phones. Even restaurants with established reputations seem to have no choice but to sign up with one or more of these companies.

Restaurants in San José are hurting across the board because of covid-19. They need more customers. Yet partnering with food-delivery companies is self-defeating when fees can go as high as 40%, cutting deeply into already thin profit margins and forcing restaurants to raise prices on consumers. While it is great to have food delivered to your home, unless you are unable to go get food yourself, such a service is more a luxury than a necessity. Restaurants are a vital part of our economy and add to the vibrancy of our city. Food delivery apps expand the customer-base of restaurants but as delivery apps become more prominent, food-delivery companies have gained disproportionate bargaining power. This council should endeavor to buoy our battered restaurant community during the harsh economic realities of Shelter-in-Place.

The aim of this fee-limit is to ease the financial burden on restaurants during this crisis while not unduly burdening third-party delivery services who are providing employment opportunities in this time of high unemployment. Indeed, some of these companies have already voluntarily lowered commissions to around 15%.

COUNCLUSION

San José should enact an urgency ordinance capping food-delivery fees until restaurants may operate once again with restrictions to help them through the pandemic.

COUNCILMEMBER
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