

TESTIMONY

BY

COMMISSIONER

GREGG BISHOP

NEW YORK CITY

DEPARTMENT OF SMALL BUSINESS SERVICES

BEFORE

THE COMMITTEE ON SMALL BUSINESS

OF THE

NEW YORK CITY COUNCIL

THURSDAY, FEBRUARY 6th, 2020

Good morning **Chair Gjonaj** and members of the Committee on Small Business.

My name is Gregg Bishop, and I am the Commissioner at the New York City Department of Small Businesses Services ("SBS"). At SBS, we aim to unlock economic potential and create economic security for all New Yorkers by connecting them to quality jobs, building stronger businesses, and fostering thriving neighborhoods across the five boroughs. I am joined by my colleague, Steven Picker, the Executive Director of SBS's food service industry partnership and Corinne Schiff, Deputy Commissioner of Environmental Health with the New York City Department of Health and Mental Hygiene (DOHMH).

New York City is home to around 27,000 restaurants and they employ over 270,000 New Yorkers. To assist restaurant owners, SBS offers many resources that help them start, operate, and grow. Our services to support restaurants include our **Government Navigation** and **Compliance Advisory** services, which help restaurant owners navigate the regulatory process and ensure that they are in compliance with the regulations necessary to maintain public health and safety. To date, Compliance Advisors have provided more than **3,000 on-site consultations** for restaurants, helping these businesses avoid common violations before their inspections and saving them more than **\$83 million** in potential fines. We also help restaurant owners access capital, hire new employees, and fund employee training through our **NYC Business Solutions Centers**. Annually, SBS helps open roughly 500 restaurants, fill nearly 3,000 open positions at restaurants, and connect about 100 restaurants to around \$4 million in financing.

SBS is committed to helping neighborhood businesses thrive in their communities. SBS provides eligible business owners with legal services on topics including lease negotiations, formalizing oral lease agreements, and landlord harassment through our **Commercial Lease Assistance Program**. Of the more than 500 businesses served through the program, more than 25% are accommodation and food service establishments. To help neighborhood businesses adapt to changing market conditions, SBS runs the **Love Your Local** grant program. To date we have provided technical assistance and over two million dollars in grant funding to forty-one small businesses, including twenty-nine restaurants. Through Love Your Local, SBS aims to identify common challenges that are impacting the profitability of small businesses so that we can develop and test new business services to support the growth and retention of longstanding businesses across the five boroughs.

SBS is committed to working directly with the restaurant industry to understand their most pressing challenges. SBS's **NYC Food & Beverage Industry Partnership** is made up of over thirty New York City restaurant industry leaders, key professional associations, and community-based organizations that focus on skills training. This partnership allows us to work directly with the industry on priority issues impacting both employers and workers to support the growth of the sector. Key priorities include helping restaurants navigate the regulatory environment, addressing the demand for skilled workers, and providing support to adapt to the rising costs of doing business in the city. Of the major challenges elevated by the industry, members of the partnership cited the recruitment of skilled employees as one of the most important. This year, SBS launched **First Course NYC**, an apprenticeship program that teaches the culinary skills

necessary for a career as a line cook, a position that is highly in-demand in New York City's restaurant industry.

Technology continues to impact many industries across New York City. Ghost kitchens capitalize on the popularity of food delivery applications and are a relatively new feature of the restaurant industry landscape. Ghost Kitchens, which have also been called virtual kitchens, delivery kitchens, or cloud kitchens, are commercial food preparation and kitchen facilities designed to produce delivery-only meals for consumers. While they share many characteristics with other food service models, such as food halls, fast casual businesses, and incubator kitchens, ghost kitchens pose potential opportunities and challenges for small, storefront restaurants. For a business that makes the bulk of its profits through delivery, ghost kitchens could provide opportunities for business owners to reach the delivery market without the overhead of operating a full-service restaurant. However, it may be challenging for neighborhood restaurants already struggling to utilize technology and reach the delivery market to compete with businesses operating out of ghost kitchens.

The landscape of the restaurant industry is continually evolving and SBS aims to help business owners be nimble in adapting to changing market conditions. SBS is committed to working with our agency partners and the industry to better understand the opportunities, challenges, and impacts of ghost kitchens to better inform our small business owners. This is a new issue and we look forward to continuing to engage with the City Council and to learn from our industry stakeholders. Thank you and I am happy to answer any questions.

**Testimony of
the New York City Hospitality Alliance
Before the Committee on Small Business**

February 6, 2020

My name is Andrew Rigie, and I am Executive Director of the New York City Hospitality Alliance. The Hospitality Alliance ("The Alliance") is a not-for-profit trade association representing restaurant and nightlife establishments throughout the five boroughs. I want to thank Chair Gjonaj and members of the committee for the opportunity to testify about **"Ghost Kitchens" "Virtual Restaurants" and the Future of the Restaurant Industry**. My following comments first appeared in a column I published in Forbes on this matter titled, *Should Restaurants Be Scared Of Ghost Kitchens?*

Restaurant food delivery is a big business that's expected to grow to \$76 billion by 2022. This represents a major source of potential revenue for businesses in a very competitive sector. But is the restaurant industry being haunted by ghost kitchens that seek a large chunk of this market share?

Yes, ghost kitchens are real, and no, there's nothing paranormal about them.

Similar to commissary space that brick-and-mortar restaurants can rent to cook their delivery food, ghost kitchens offer restaurants several benefits including the ability to open delivery-only locations in neighborhoods outside their delivery-zone and free up space at their primary locations, which usually aren't designed for delivery production. These ghost kitchens provide space that's customized to optimize a restaurant's delivery business, and helps restaurants generate new business and brand awareness.

But some ghost kitchens have no brick-and-mortar locations associated with them. These virtual kitchens can be standalone businesses, or locations to test cuisine, gain followings and generate excitement before turning concepts into brick and mortar restaurants.

As this sector grows, ghost kitchens could create opportunity for the restaurant industry. But left unchecked, this Dr. Jeckyll is likely to become Mr. Hyde. How?

A Thought Experiment

Uber founder Travis Kalanick's venture, [CloudKitchens](#), a player in the ghost kitchen sector, has already partnered with UberEats, Grubhub and other third-party delivery companies. Imagine that CloudKitchens merges with UberEats. Or that Grubhub acquires a competitor like [Kitchen United](#) and vertically integrates the businesses. These companies would control: 1) the platform from which consumers search and process food orders, 2) the kitchens where the food is cooked, 3) the people (or, the [robots](#)) who deliver it to consumers, and 4) a growing list of labor services that may eventually include cooks who can be automated (which restaurants like [Spyce](#) have shown is possible).

To streamline purchasing for their restaurant tenants, the owners of ghost kitchen facilities can acquire or start their own food purchasing groups. Using data collected through their ghost and virtual restaurant tenants they can analyze food costs and usage, reduce waste and negotiate lower rates for food purchases. When the owners of ghost kitchens have built out this infrastructure, they'll be enticed to experiment with operating their own virtual restaurants, which means they will become direct competitors to their brick and mortar and virtual tenants (think about how AmazonBasics competes with merchants on their marketplace that sell similar products). The owners could use the vast trove of data about the most popular and profitable cuisines in their ghost kitchens, and other data points not available to their tenants, to optimize sales and operate data-driven virtual restaurants. They can then charge tenants higher fees for their restaurants' menu items to be listed before their own in search results and paid advertisements. Celebrity chefs and well-known restaurants may benefit when they're tapped to create and inspire menus for the virtual restaurants owned by the kitchen centers.

The owners of ghost kitchen facilities could also attract new delivery customers and reward existing ones by pressuring restaurant tenants to participate in promotions, which The New York Times reported is similarly happening in [India where restaurants are rebelling against, and boycotting food delivery apps](#) as a result.

Preparing for the Future

Restaurateurs should prepare for operating in ghost kitchens as well as for the competition other ghost kitchen brands and virtual restaurants will pose. If the trend sticks, rental kitchen spaces will be ripe for chefs, restaurateurs, entrepreneurs and food enthusiasts to open new businesses and expand their existing delivery radius. Companies may rent multiple kitchens and open their own virtual food halls. This will flood the market with new delivery options that will compete for customers with existing brick and mortar restaurants, many of whom are already struggling in today's challenging businesses environment.

Imagine a not too distant future when restaurants throughout your city conduct their food delivery operations out of ghost kitchens. Brick and mortar restaurants will rely on the ghost kitchens as a conduit to their own customers, as a production facility, and as a large revenue stream that financially supports their physical locations. This dynamic will give incredible leverage to the owners of ghost kitchens over their restaurant tenants, enabling them to increase rents, jack up fees, and enact other business practices that come at their expense.

While I am very wary of over-regulation, lawmakers must consider smart policies like requiring that restaurants are provided access to and own all customer data and operational analytics generated by their businesses operating as ghost and virtual kitchens. The law must allow restaurants the option of clearly disclosing certain third-party fees to consumers, such as delivery charges. This will allow consumers to decide if the third-party service is worth the price. Then, market forces will help keep third-party fees reasonable, so they're not artificially inflated behind the scenes on the backs of small business owners who individually lack negotiating power to lower fees. Anti-competitive behavior must also be closely monitored because of the potential for a few companies to dominate the ghost and virtual kitchen market at the expense of brick and mortar restaurants.

Some of the possibilities I've warned of have already begun to happen, as Food & Wine recently explained ([The Biggest Names in Food Delivery Are Getting into the Restaurants Business](#)). If we look at the history of players involved in the delivery sector, like [Grubhub](#) and [UberEats](#), both have a history of exploiting restaurants, so I'm not convinced that they will try and help restaurants with ghost kitchens. It seems more likely that the entry of certain companies into this market, will

in part be intended to excite their investors into believing that ghost kitchens are the 'next big thing' and can be profitable, which will distract from the struggles their other business models face. But, anyone with knowledge of the restaurant industry knows that this is not the business to go into to make a fortune. There's only so much money for all these entities to profit from without one or all losing money.

Ghost kitchens are inevitable, and any leverage restaurants have will only decline from this point forward. That's why now is the time to act. Restaurateurs must demand fair terms and conditions in their contracts, carefully consider the pros and cons of handing over key operational duties to third-party companies and contemplate what it will mean for their own businesses and our industry long-term. And lawmakers, who have regulated brick and mortar restaurants over the course of decades must enact smart policies to ensure the playing field is level.

Thank you for your consideration of our comments.

Respectfully submitted,

Andrew Rigie
Executive Director
NYC Hospitality Alliance

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The image is a composite graphic. The top-left section features the text 'NYC | HOSPITALITY ALLIANCE' in a bold, sans-serif font against a blue-tinted background of a city street. The top-right section shows a blurred image of a person wearing a helmet, likely a delivery person, in a busy urban environment. The bottom-left section shows a blurred image of a person riding a bicycle on a city street. The bottom-right section is a solid black area containing the title 'GRUBHUB/SEAMLESS SURVEY' and the date 'FEBRUARY 2020' in white text.

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ALLIANCE

GRUBHUB/SEAMLESS SURVEY

FEBRUARY 2020

INTRODUCTION

In 2019, news broke that Grubhub/Seamless, the mega-sized delivery company was charging their restaurant clients bogus fees for phone call orders that customers did not place. Shortly thereafter, the restaurant industry's outrage at the company's tactics, which long simmered under the surface, finally boiled over. Further reporting uncovered that the delivery company was engaged in other questionable business practices that come at the expense of restaurants. This resulted in U.S. Senator Charles E. Schumer calling on Grubhub/Seamless to fix their exploitative business model. The New York City Council also held an oversight hearing into the restaurant delivery industry.

Much of the testimony at the hearing, and the conversations about Grubhub/Seamless have focused on their bogus fees, market dominance, increased fees, customer data policies, and technological strategies that drive restaurants' direct orders through Grubhub/Seamless' own channels to increase the fees they collect from restaurants. More recently, news broke that the company was listing restaurants on their website without receiving consent, which has caused problems for the businesses and consumers. It's been reported that the City Council, and other regulatory bodies, are now considering regulatory measures to reign in the giant delivery company.

In an effort to better understand the restaurant industry's experience with Grubhub/Seamless, the New York City Hospitality Alliance surveyed restaurants in January 2020. The operators of 300 restaurants in New York City participated in the survey. Here are the results:

SURVEY SNAPSHOT

- 90.3% of respondents said Grubhub/Seamless' fees are unreasonable.
- 61.1% of respondents said their Grubhub/Seamless orders are barely profitable, while 20% are observing a loss of business.
- 78.2% of respondents reported Grubhub/Seamless increased fees on their restaurants one or more times.
- 64.1% of respondents have either raised menu prices or are considering raising prices to offset Grubhub/Seamless fees.
- 48.4% of respondents have added a delivery surcharge due to Grubhub/Seamless fees.
- 66.6% of respondents said that customers who used to order direct from their restaurants now order via Grubhub, so the restaurant now pays a fee.
- Less than 10% of respondents have a positive experience with Grubhub/Seamless.

WHY DO YOU USE GRUBHUB/SEAMLESS?

“

Customers ask for it, but the fees were not as high when i started working with them. ”

- Mediterranean Restaurant

“

Because most New Yorker's only use Seamless/Grubhub. 'Necessary evil'.

- Sandwich Shop ”

“

I still list it because I feel like they have taken me (and/or my customers) hostage. ”

- Mexican Restaurant

“

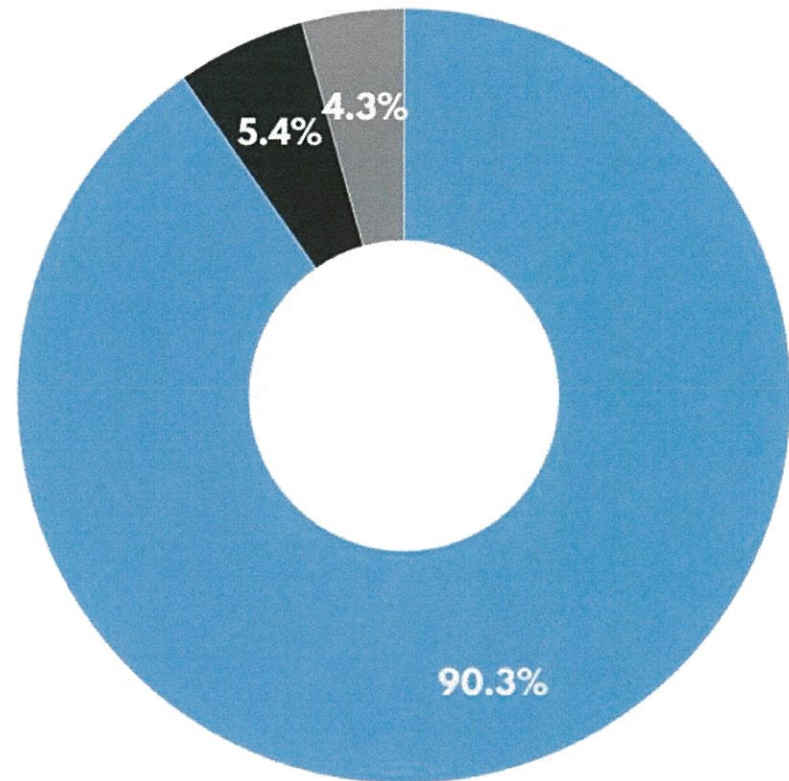
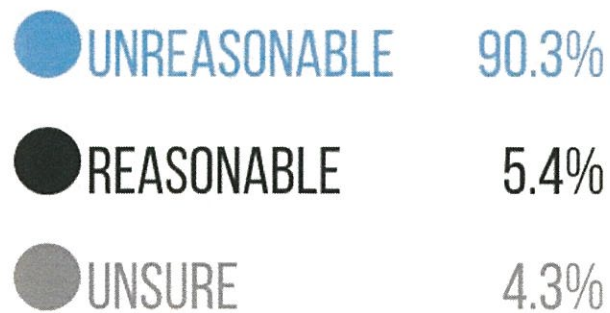
You have to work with them if you are going to deliver at scale in New York City.

They are a monopoly. ”

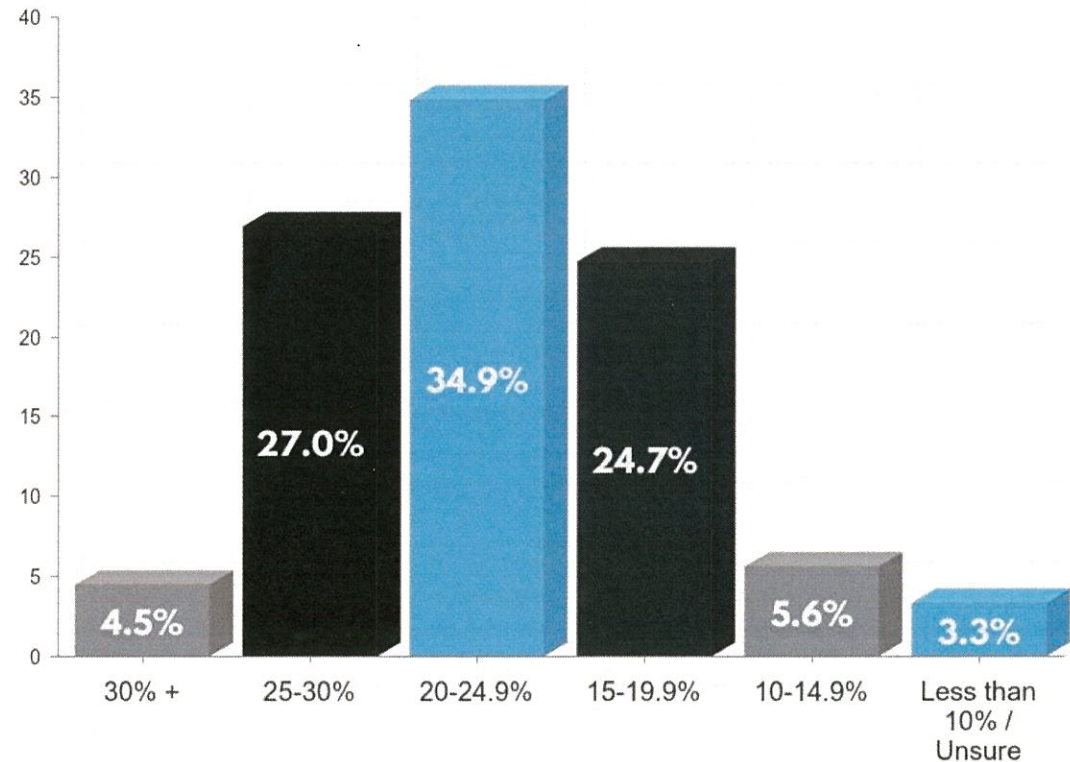
- Fast-Casual Restaurant



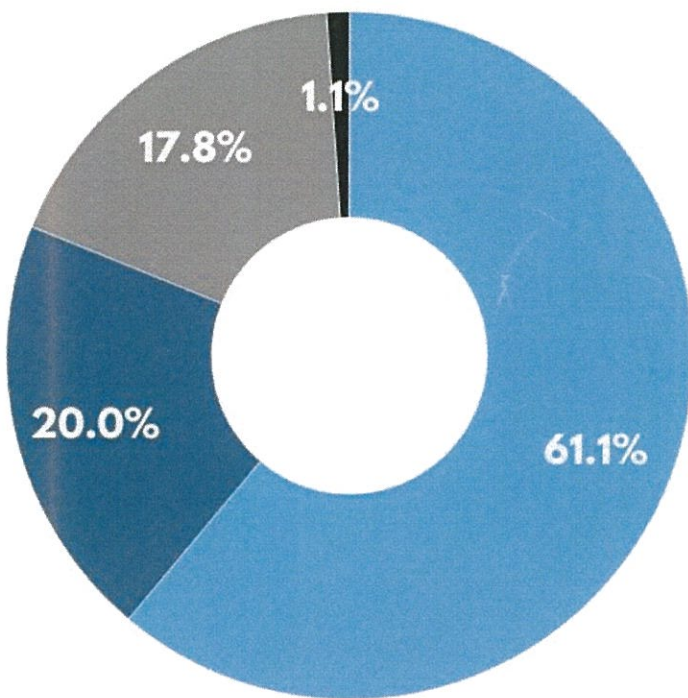
HOW DO YOU DESCRIBE THE FEES GRUBHUB/SEAMLESS CHARGE YOUR RESTAURANT?

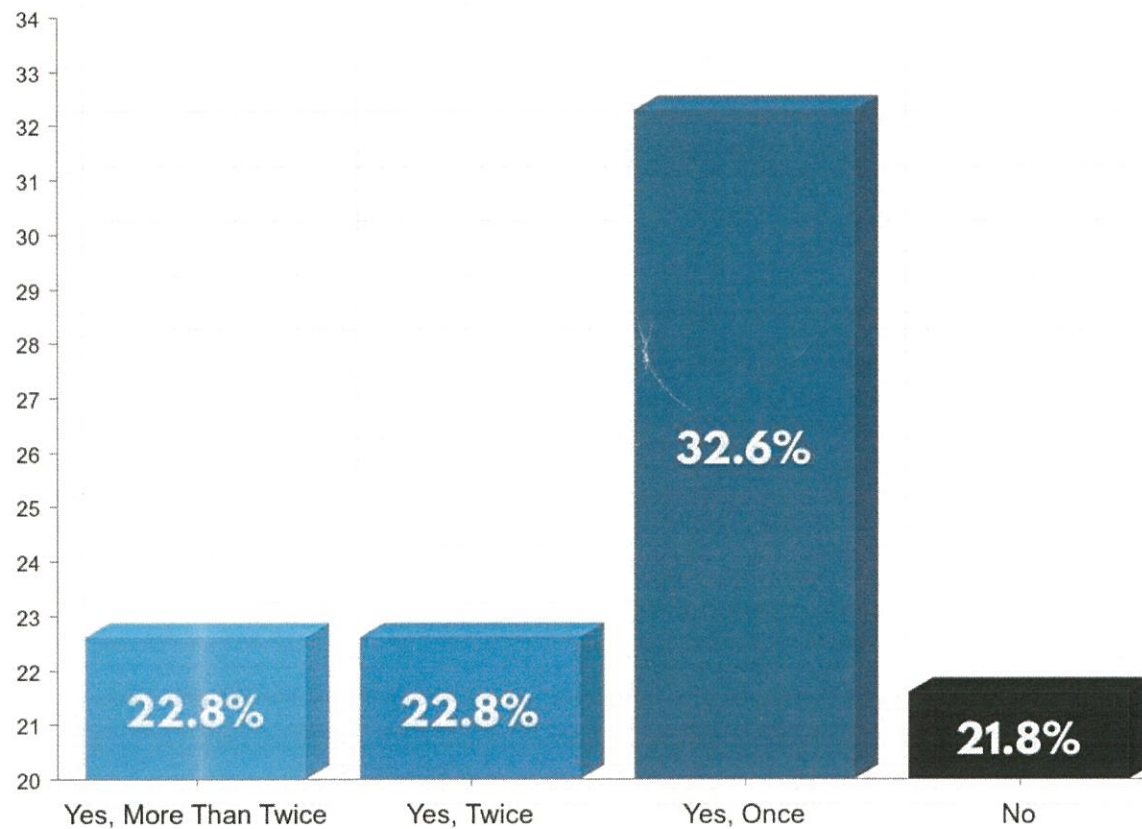


WHAT PERCENTAGE FEE DO YOU PAY GRUBHUB/SEAMLESS PER ORDER?



HOW DO YOU DESCRIBE YOUR RESTAURANT'S DELIVERY ORDERS GENERATED BY GRUBHUB/SEAMLESS?

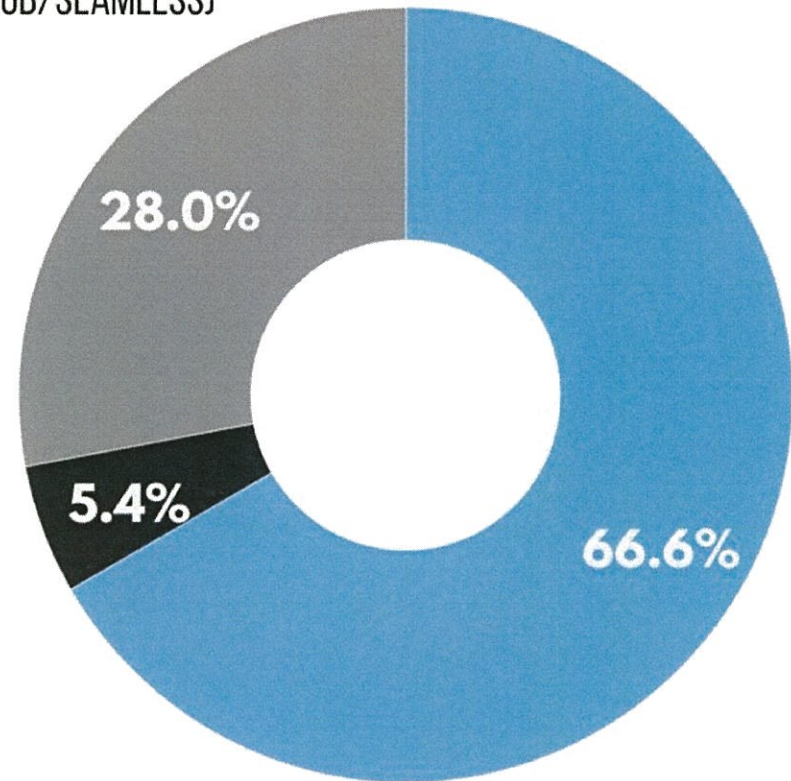
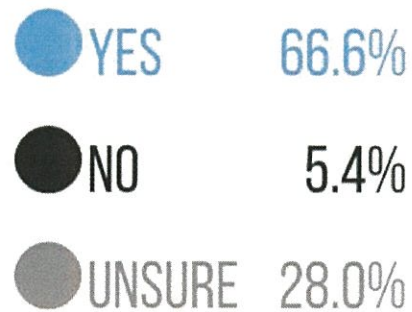




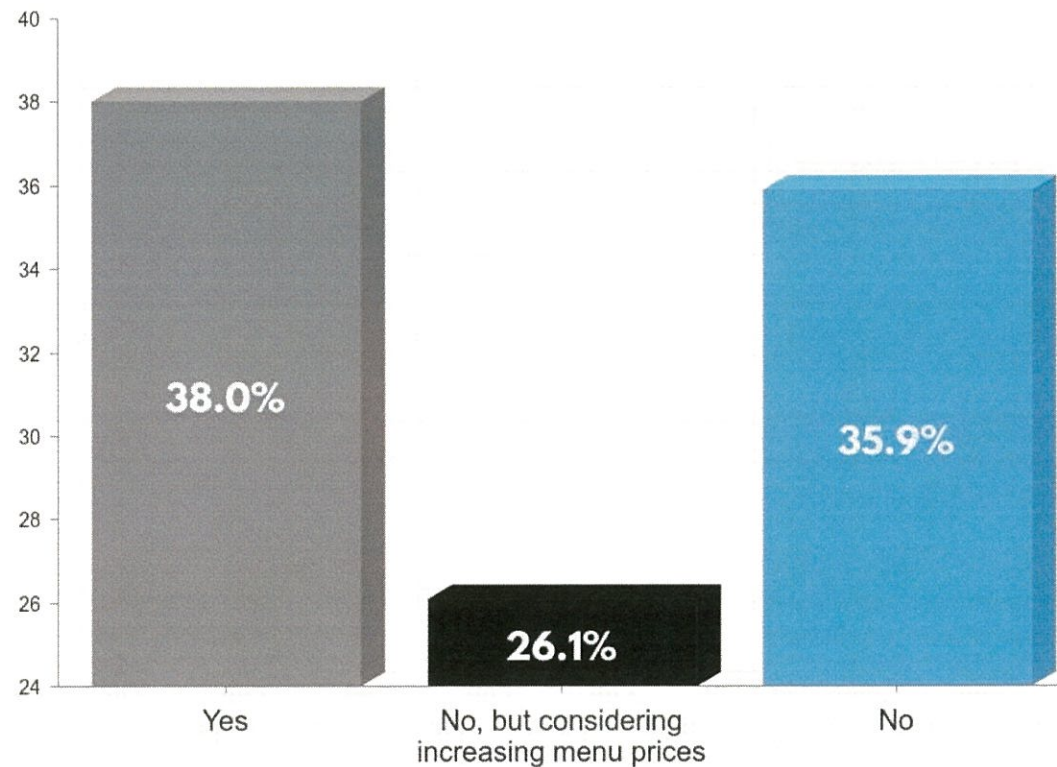
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HAS GRUBHUB /
SEAMLESS INCREASED
YOUR FEES SINCE YOU
BEGAN PROCESSING
ORDERS THROUGH
THEM?

DO YOUR DELIVERY CUSTOMERS ACQUIRED THROUGH NON-GRUBHUB/SEAMLESS CHANNELS NOW ORDER FROM YOUR RESTAURANT VIA GRUBHUB/SEAMLESS? (E.G. CUSTOMERS WHO USED TO ORDER DIRECT FROM YOUR RESTAURANT NOW PLACE THEIR ORDERS THROUGH GRUBHUB/SEAMLESS)



HAVE YOU RAISED
YOUR MENU PRICES
TO OFFSET
GRUBHUB/SEAMLESS
FEES?



“ Please lower the fees - I'm very close to breaking even on deliveries. ”

- Sports Bar

“ I'm better off not taking deliveries with Grubhub at this point. ”

- Italian Restaurant

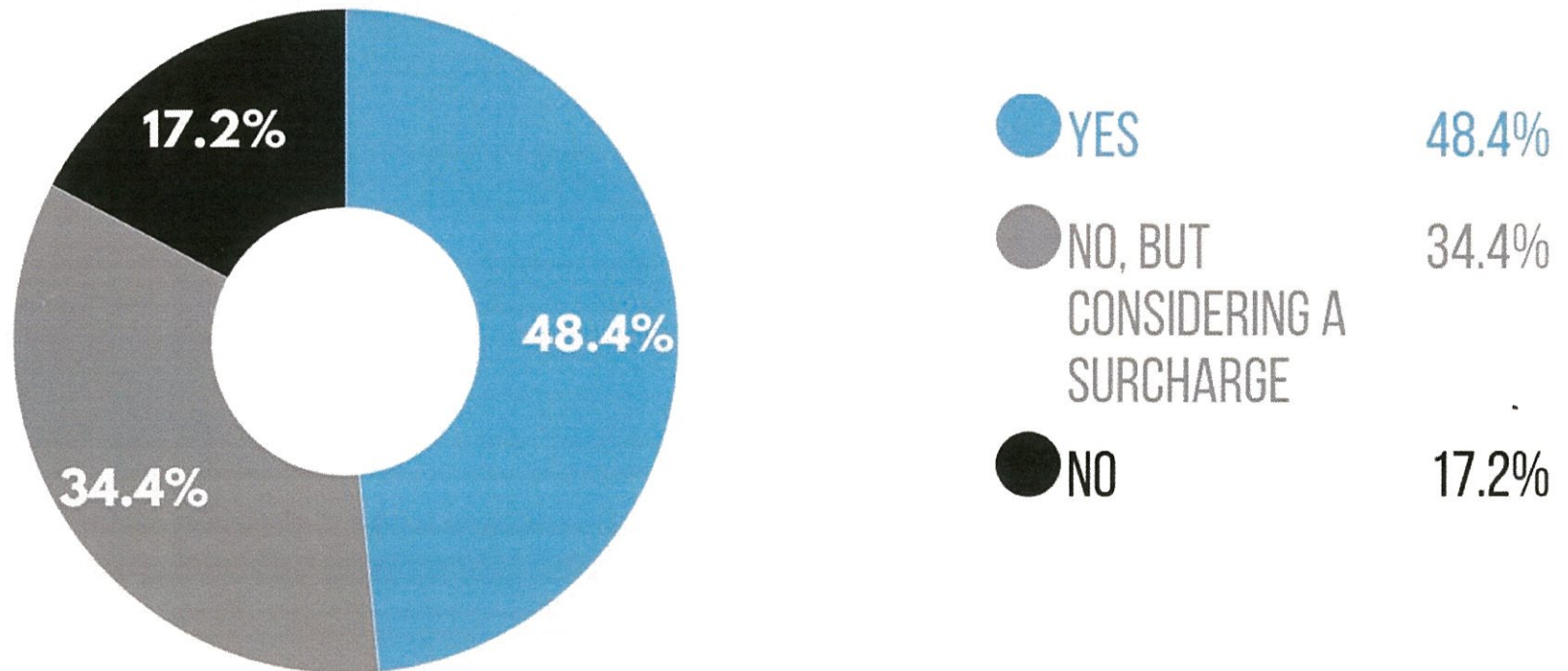
“ Dishonest. Worst customer service. Bottom feeder company putting restaurant out of business. ”

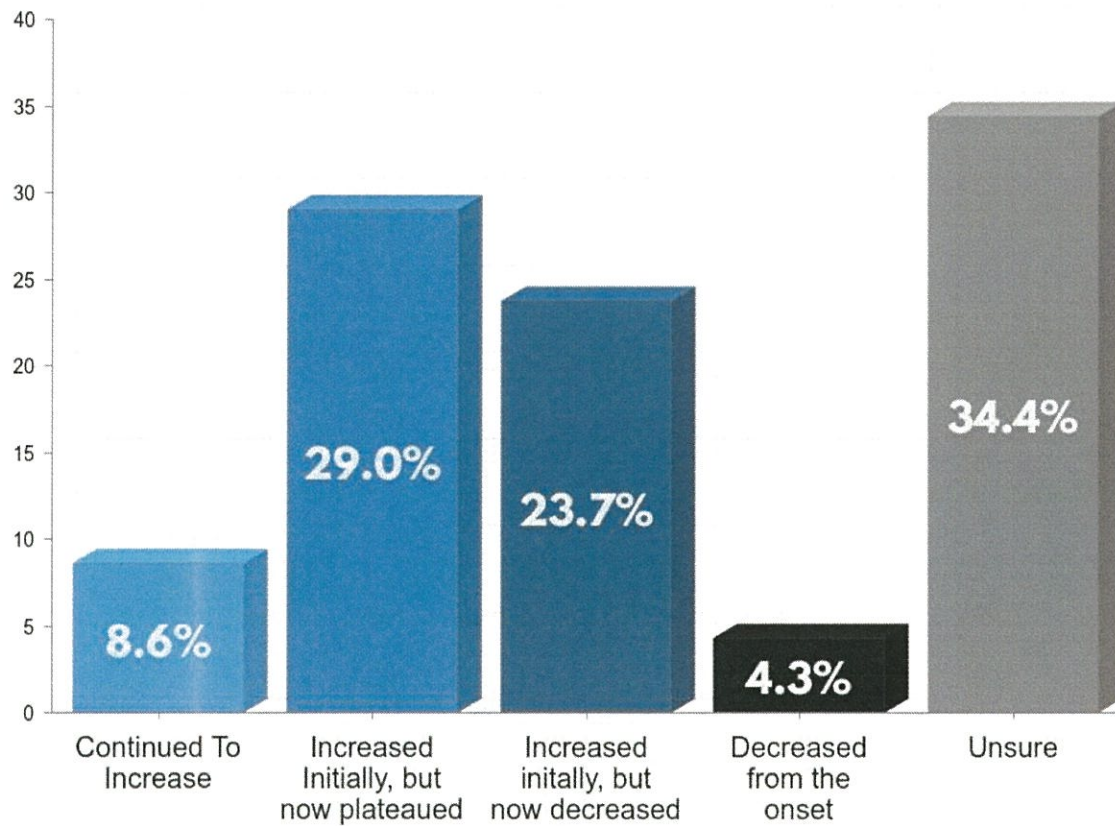
- French Restaurant

“ It was impossible for us to run our business AND fight with Grubhub to verify and discuss each call and charge. ”

- Fast Casual Restaurant

DO YOU CHARGE CUSTOMERS WHO ORDER THROUGH GRUBHUB/SEAMLESS ADDITIONAL FEES (E.G. A DELIVERY SURCHARGE) BECAUSE OF THE FEES GRUBHUB/SEAMLESS CHARGES YOUR RESTAURANT?

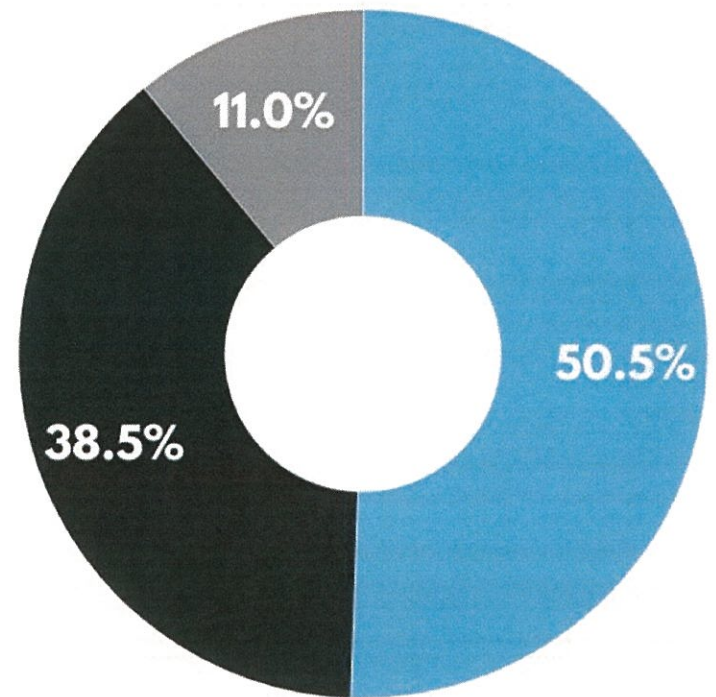
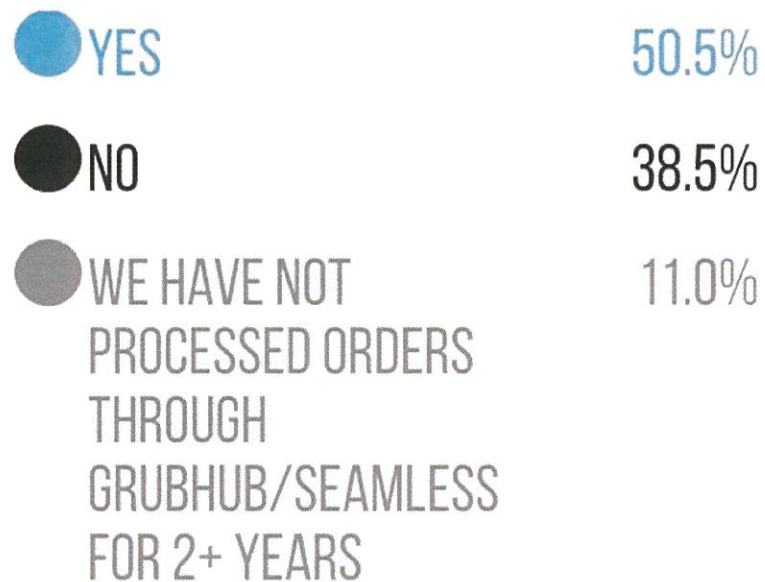




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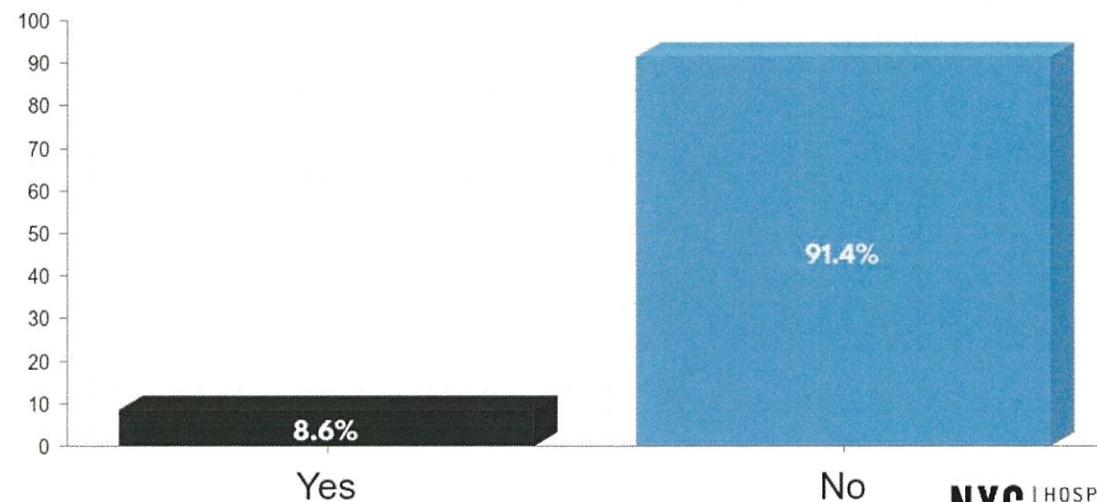
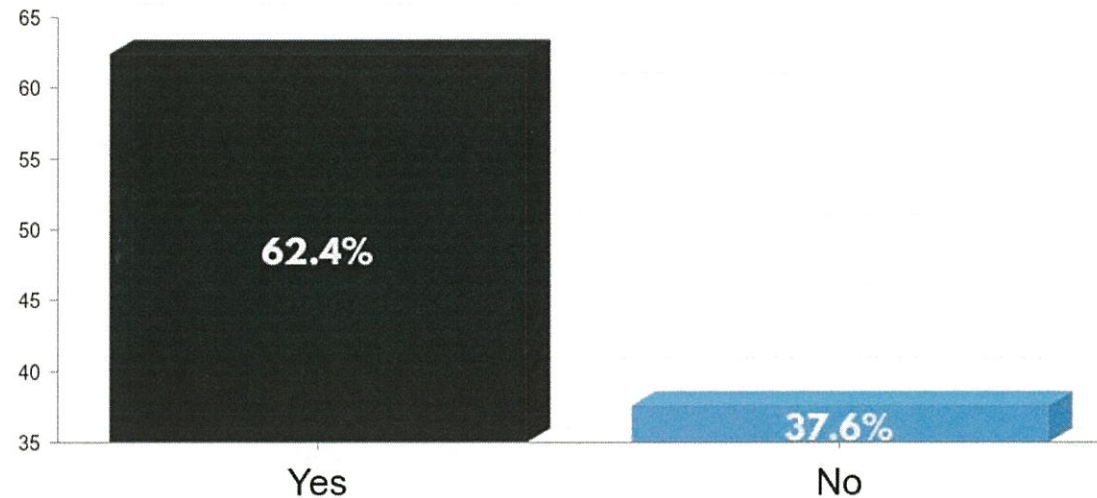
SINCE YOUR RESTAURANT
STARTED USING
GRUBHUB/SEAMLESS, THE
NUMBER OF FIRST-TIME
DELIVERY CUSTOMERS HAS?

IF YOU HAVE PROCESSED ORDERS THROUGH GRUBHUB/SEAMLESS FOR MORE THAN 2 YEARS, HAVE YOU NOTICED A DECLINE IN THE TOTAL NUMBER OF ORDERS?

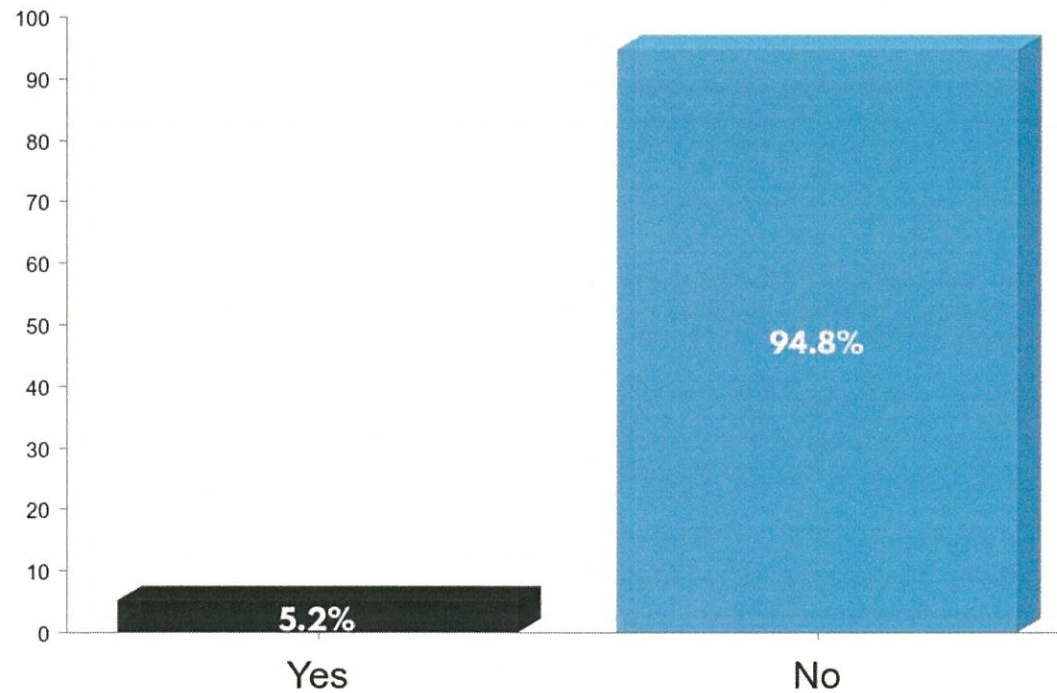


HAS YOUR RESTAURANT BEEN
CHARGED FEES BY
GRUBHUB/SEAMLESS FOR
CUSTOMER PHONE CALLS THAT
DID NOT GENERATE AN ORDER?

IF YES, HAVE YOU BEEN
REIMBURSED FOR BY
GRUBHUB/SEAMLESS FOR FEES
GOING BACK 120 DAYS?



HAVE YOU BEEN
REIMBURSED FOR
FEES IN EXCESS OF
120 DAYS?



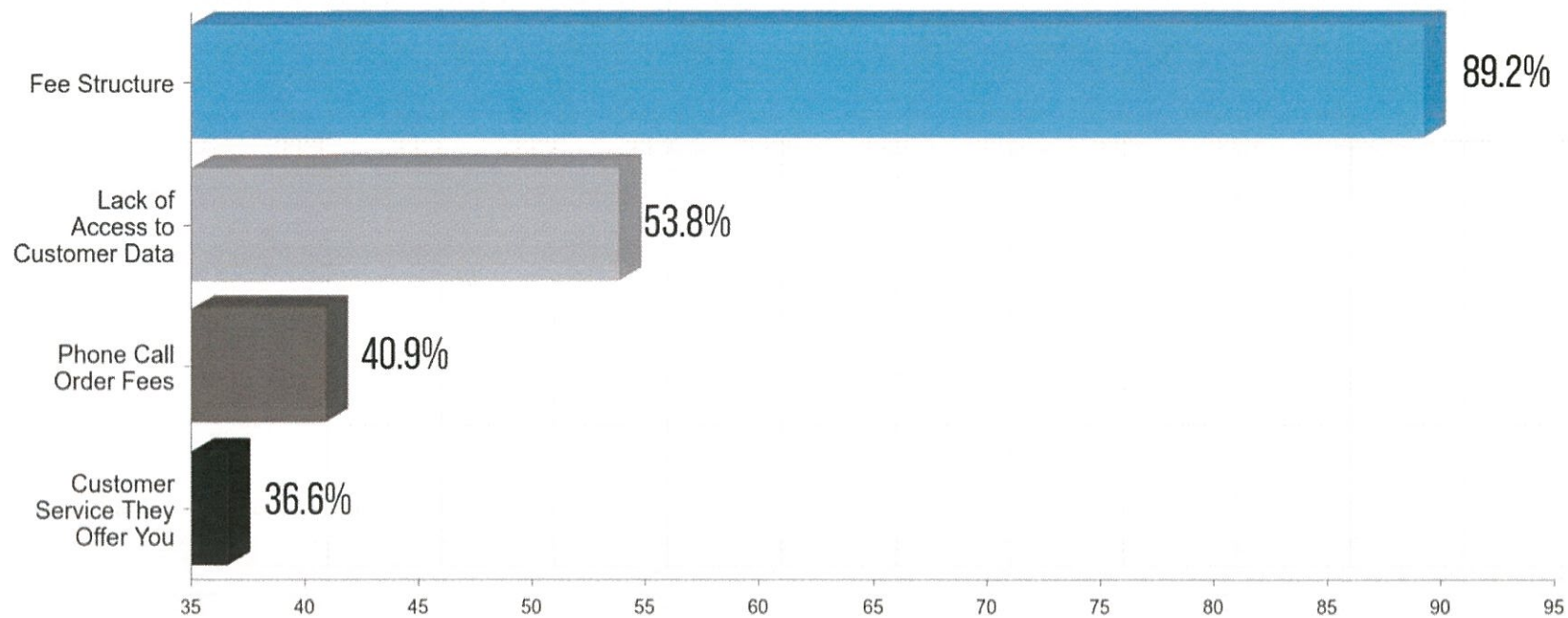
“ The worst though is the placement of our restaurant on their algorithm. They said if we increased their commission, we would get a better placement (i.e. higher up in the customers' restaurant default list), ”
but that wasn't the case.

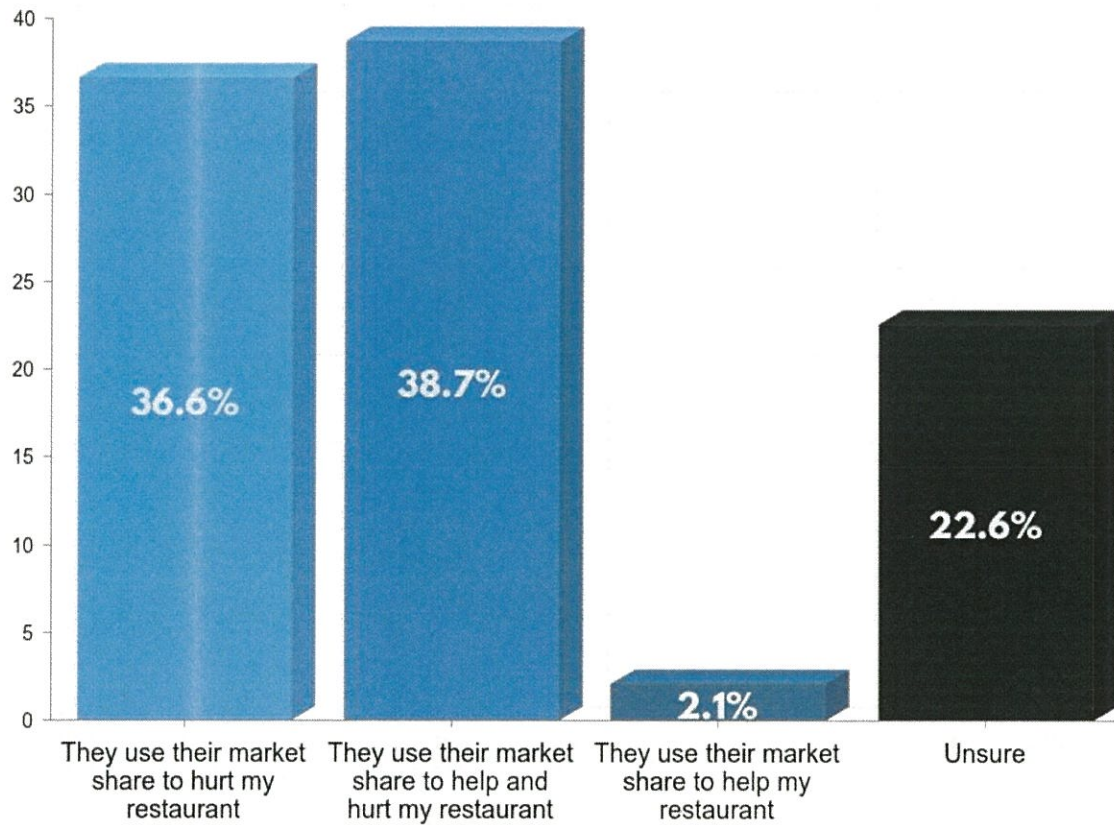
- Sandwich Shop

“ We fought for reimbursement before the issue became publicly known. We were never reimbursed and were given the run around. It was impossible for us to run our business AND fight with Grubhub to verify and discuss each call and charge. ”

- Fast Casual Restaurant

WHICH GRUBHUB/SEAMLESS PRACTICES CONCERN YOU MOST? (RESPONDENTS CHECKED ALL THAT APPLIED)

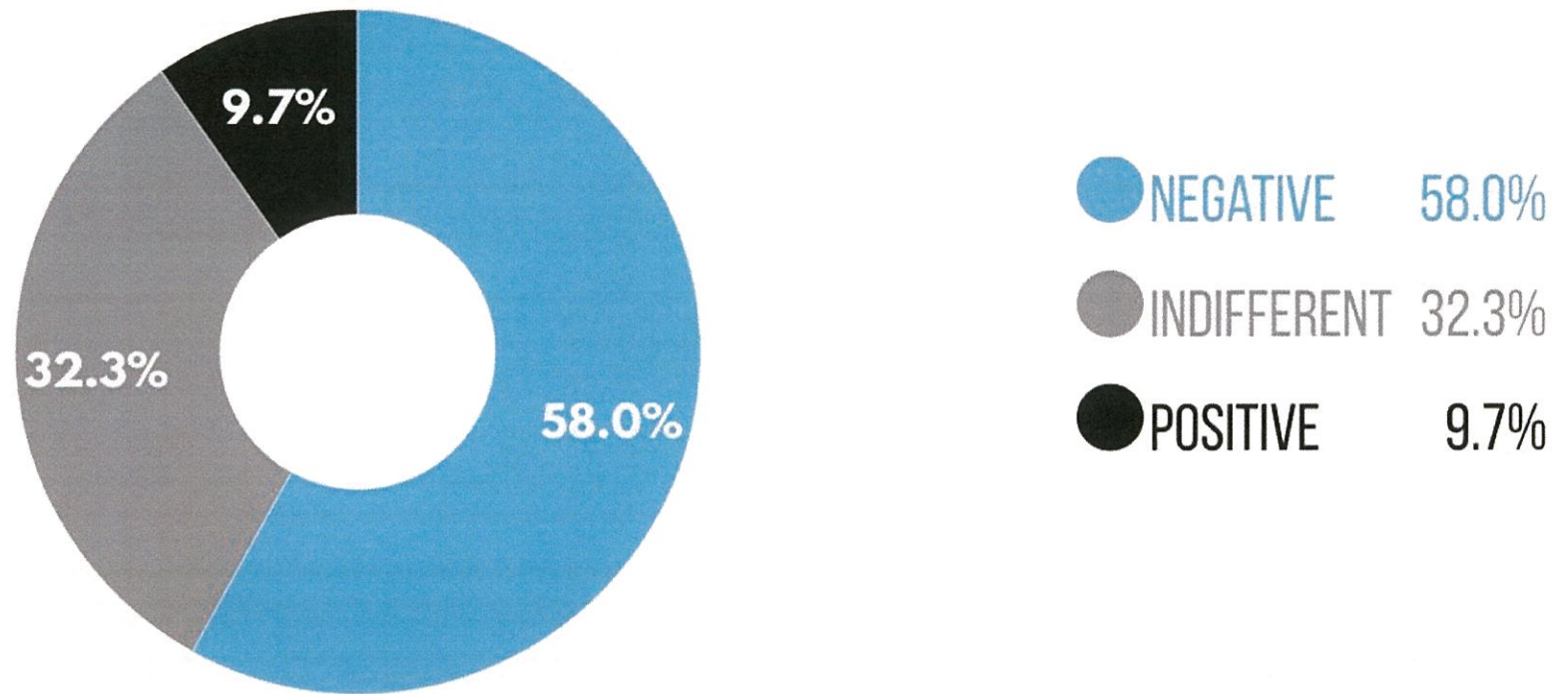




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HOW DOES
GRUBHUB/SEAMLESS LARGE
MARKET SHARE IMPACT YOUR
RESTAURANT?

WHAT IS YOUR OVERALL EXPERIENCE WITH GRUBHUB/SEAMLESS?



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For questions or comments, please contact info@thenycalliance.org

thenycalliance.org | [@theNYCalliance](https://www.instagram.com/theNYCalliance)



In regards to ghost kitchens and the future of dining in NYC

Good morning. My name is Kathleen Reilly and I am the NYC Government Affairs Coordinator for the New York State Restaurant Association. We are a trade group that represents food and beverage establishments in New York City and State. We are the largest hospitality trade association in the State, and we have advocated on behalf of our members for over 80 years. Our members represent a large and widely impacted and regulated constituency in New York City. They also represent one of the last strongholds for the brick and mortar landscape, as New York City contends with the transformative impact of e-commerce and changing consumer behavior. To ensure the continued viability of the restaurant industry, New York City must prioritize a fair and healthy business environment so these hardworking New Yorkers can continue earning their livelihoods.

Today, the Council has taken the opportunity to discuss ghost kitchens, which are growing in popularity around the country and notably in New York City. We applaud the Council for keeping a finger on the pulse of emerging trends, and for having the foresight to bring them to the community for comment so early on. In a ghost kitchen, a space is used as a commercial kitchen that cooks food for delivery only. Some ghost kitchens are associated with existing storefront concepts, while others operate as their own independent concept. Often, the operators of ghost kitchens partner with third party delivery platforms to get their food to customers.

From our perspective, ghost kitchens are reacting to the difficult business environment that has been created in New York City. As a business model, they allow for renting less expensive space, focusing solely on a kitchen footprint, and eliminating customer-facing staff. In a city where rent and property tax pose a major burden, labor is ever more expensive, and regulations are consistently handed down from the City and State, our legislators have incentivized a business model like this.

With that in mind, our stance on ghost kitchens themselves is simply that they should be held to the same regulatory and inspection standards as their restaurant counterparts. So long as the playing field is level, we don't take specific issue with ghost kitchens existing. Functionally, they are just one step away from a business serving food to New Yorkers from a takeout counter. More importantly, though, ghost kitchens are a symptom of a very difficult business environment in New York City. They are part of a trend, where we see more and more quick service and delivery-oriented businesses, and pressure to minimize floorspace and staffing.

The question we want to leave Council Members with today is this: what do we imagine for the future of dining in New York City? Our city has been a proud culinary capital of the world. As a voice for the restaurant industry, we fully believe in the importance of brick and mortar restaurants as a space to share food, traditions, and culture with New Yorkers and visitors from near and far. We also know for a fact that the restaurant industry employs thousands of New Yorkers. If ten

years from now, the dining landscape of the city is dominated by takeout and delivery options with only a few true full-service restaurants remaining, will that be an outcome that we are proud of? And if not, what are we prepared to do to protect and preserve the viability of restaurants in this city?

In conclusion, the New York State Restaurant Association is appreciative that the Council has gotten this conversation started. We look forward to being part of this discussion as it develops, and as any new questions about the role of ghost kitchens arise. We urge the Council Members to keep in mind the business environment that led to ghost kitchens' popularity. We also believe in the importance of restaurants in the future of New York City dining, and we encourage our legislators to consider means of supporting these businesses. Thank you for the ongoing conversation.

Respectfully Submitted,

Kathleen Reilly

NYC Government Affairs Coordinator

New York State Restaurant Association

315 W 36th St., 7th Floor

New York, New York 10018

Zuul Kitchens Testimony

Prepared for the Committee on Small Business, New York City Council

For Oversight: "Ghost Kitchens" "Virtual Restaurants" and the Future of the Restaurant Industry

February 6, 2020

Corey Manicone, Co-founder and CEO of Zuul Kitchens

Good morning.

My name is Corey Manicone and I am the founder and CEO of Zuul Kitchens. Joining me today is Sean Fitzgibbons, Zuul's co-founder and Chief Business Development Officer.

I would like to start by saying thank you to Council Member Mark Gjonaj, his staff, and the New York City Council for inviting us to speak here today. We appreciate the opportunity to share public testimony. Today I will speak on behalf of our business, some of its members, and the greater New York City restaurant community. On a personal level, I recognize the importance of this conversation and thank you all for being here to participate.

What I hope to communicate today is the potential for collaboration and spirit of innovation that I and the extended Zuul community envision for the healthiest future of New York City's restaurants. Zuul was founded with the mission to allow food entrepreneurs and operators the opportunity to build sustainable businesses. I welcome this opportunity to elaborate on Zuul's mission, address the unique features of ghost kitchens, and amplify our partners.

Some years ago my father owned and operated an IHOP in Fort Collins, Colorado. I can recall many early memories of mopping floors, washing dishes, and tackling the less glamorous tasks necessary to operating a restaurant. Early success with the family IHOP compelled my parents to open their own bar and grill, further exposing me to the realities of owning and operating a small restaurant business. The eventual failure of the bar and grill, then the IHOP, compelled me to wash my hands of any and all involvement in the restaurant industry.

Fast forward many years later and I came to work as the first full-time employee at Relay Delivery, New York City's largest last mile fulfillment operator for restaurants. During my time at Relay I personally

performed hundreds if not thousands of food deliveries and experienced [firsthand] the most common challenges of performing food deliveries in New York City.

During my time at Relay I began to see first-hand just how big the behavioral shift amongst consumers was. Positioning ourselves as a partner allowed me to have insight into our customers' data, and as such, it became very clear that anywhere from 40-60% of their revenue was going out the door with a courier. So I sat back and remembered all of the historical challenges my father faced first hand, and now, there is a whole new (and massive) challenge that is -- the restaurant infrastructure was never built with intent of supporting off-premises dining. Which is why when any of us walk into a fast-casual restaurant here in New York City, we typically have to swim through a sea of couriers to get to the front to order. It impedes the better margined business that is the retail foot traffic.

This experience led me to contemplate, what if, for the first time ever, we very strategically and thoughtfully designed a piece of real estate that optimized for delivery and off-premise dining.

Enter ghost kitchens...

Ghost kitchens are delivery-only kitchens leased to local restaurants to expand their delivery business without the expense of building a new restaurant. Ghost kitchens are the latest in a series of delivery-only restaurants that have been founded here in New York City. A number of restaurants have opened their own locations that cook only takeout and delivery orders. Rather than each restaurant opening their own delivery kitchen, ghost kitchens offer delivery-only kitchens as a service. The ghost kitchen operator designs, builds, and permits the ghost kitchen (typically a commissary kitchen). Then, each restaurant leases a dedicated space within the ghost kitchen facility.

Each kitchen comes pre-equipped with gas and electric connections, a commercial exhaust hood, a three compartment dish sink, and a hand sink. The ghost kitchen is then responsible for operating all shared spaces. This shared service to the restaurants includes storage, bulk dishwashing, and delivery dispatch. This model allows restaurants to focus on cooking, while the ghost kitchen operator handles the rest.

As stated earlier, most restaurants were not designed and built for delivery. They often lack a dedicated dispatch center, integrated technology stack, and specialized delivery equipment.

Physically, their location was selected for dine-in customers, not delivery customers at home. This means that restaurants are paying prime real estate prices for a kitchen that is serving guests that may or may not live or work nearby or have the time to dine. As dine-in foot traffic continues to decline, delivery is often the only channel that is growing for a restaurant. Quoting Yong Zhao, the founder and CEO of Junzi Kitchen:

“The traditional business model of restaurants is becoming unsustainable especially in the urban environment given the rising cost of rent and labor. It’s crucial to be innovative to improve the efficiency and reduce the cost of middle men of the restaurant industry, especially when the new generation customer prefers more delivery of food than before.”

With this context we set out to build New York City’s first ghost kitchen facility. After securing a lease for a 5,000 sq ft space in lower Manhattan, we designed and built out the space to house nine individual kitchens, two dish pits, a walk-in refrigerator, dry storage space, shared break room, three bathrooms, and a dispatch center.

Much like opening a full service restaurant, opening a ghost kitchen follows the same process. We work with the Department of Buildings to file our design and construction plans, we worked closely with ConEd to supply the kitchen with gas for our members, and we worked with the Department of Health to certify our kitchen and continue to work with the Department of Health to ensure our kitchens are up to code.

Specifically, Zuul kitchens are designed with two types of areas - space that is shared by the restaurants and space that is dedicated to a single restaurant. As the ghost kitchen operator, Zuul is responsible for the operation of all shared spaces including the courier and dispatch centers, cold and dry storage, and dishwashing. For these spaces, Zuul Kitchens is permitted as a Wholesale Food Establishment under Permit H26.

Furthermore, each restaurant’s dedicated space is then permitted individually as a General Food Service Establishment under Permit H25. This is the same permit type that all restaurants in New York City must receive, and we’re very proud to report that to-date all of our restaurant members have received a letter grade of A.

In September, Zuul officially opened our first facility in SoHo, located at 30 Vandam Street. Over the next three months, our six restaurant members moved in, set up their kitchens, and began cooking delivery orders. Our members include Sarge's Deli, Stone Bridge Pizza, Naya, Junzi, Positive Foods, and sweetgreen.

We're now working to design many future locations and hire team members to provide additional support to our members. We take a consultative approach to supporting our members as they adapt their business to the ghost kitchen format. The Zuul team is grounded in many years of experience in the hospitality industry.

Last week, Zuul announced the acquisition of Ontray, a small software business out of Philadelphia. Ontray has developed an online food-ordering service that provides independent restaurants with tools to process delivery operations from their own websites. Quoting Tyler Wiest, Founder of Ontray and now Chief Technology Officer of Zuul:

"Joining Ontray and Zuul Kitchens is a natural move. Both companies share a similar goal: returning the power and purse back to individual restaurants. We both believe that restaurants' full-time focus should be on running a restaurant -- not burdensome, expensive tasks like online ordering or delivery operations."

By building our own platform for direct delivery orders, we are enabling our members to generate more orders at a higher profit margin. Further, we will openly share data with our members and work with them to implement improvements based on analysis and feedback.

As Zuul works to build our New York City-based ghost kitchens, we always keep the restaurant's perspective front of mind. As a team, Zuul understands food delivery from multiple angles: hospitality, logistics, and technology. Restaurants have always evolved their form factor, from full service to fast casual and the drive thru. Ghost kitchens are the latest innovation in restaurants and provide independent operators a new option to consider in their operations portfolio. By building a delivery-only kitchen, we offer a specialty restaurant format designed to compliment a business's existing locations and extend their brand digitally through delivery. Because these kitchens share a common roof and work together, they are more efficient as Zuul provides shared services for all restaurants.

Thank you for your attention, and I will now pass the mic to my co-founder Sean Fitzgibbons.

Sean Fitzgibbons, Co-founder and CBDO of Zuul Kitchens

Good morning.

My name is Sean Fitzgibbons and I am the co-founder and Chief Business Development Officer of Zuul Kitchens. I would like to echo Corey in saying thank you to the Committee on Small Business for inviting us here today.

In my role at Zuul, I spend most days meeting with local restaurant owners. We discuss their current operations and work together to determine if Zuul is a good fit for their long-term business plan. Through these conversations, I've seen that each restaurant has unique needs and reasons for choosing a ghost kitchen. Some restaurants are looking to expand into new neighborhoods, others have too much delivery demand at their restaurants and need additional cooking space to keep up with delivery. Some simply see it as a de-risked investment based on our flexible lease terms and low capital requirements.

We have close working partnerships with our restaurant members, some of whom are here today. *[Motion to Enrique and other members.]* One of them is Enrique Mendez, the founder of Stone Bridge Pizza here in Manhattan. I'd like to read a quote from Enrique about his perspective on the ghost kitchens and the state of the restaurant industry.

"The casual dining segment of the restaurant industry, dominated by small independent operators, finds itself in the midst of one of its most transformational periods in recent memory. As a result, operators face tremendous challenges which threaten their very existence. Most of these challenges are not those caused by secular trends triggered by demographic transformation, but are in fact related to dislocations in the industry's value chain caused by urban gentrification and the incursion of third party technology tools at the transactional level.

Ghost Kitchens are the response to many of these challenges, stemming from the increasing importance of delivery as a way to reach consumers, while also addressing the need for more efficient use of physical space, shared infrastructure and technological synergies between operators. In addition to this, they provide a way for operators to grow without the enormous capex and risks associated with building and opening a standalone dine-in store.

Ghost Kitchens are a means to achieve such efficiencies and provide a way for operators to sustain and grow their existing businesses while fighting off the forces that are currently threatening their survival.”

Zuul is committed to supporting independent operators and works with a diverse set of restaurant members: from local restaurants with one location to a national restaurant with almost 100 locations. Before each of our members joined, we worked with them in a financial modelling session to understand their current business model and how to adapt it to the ghost kitchen format. In particular, we looked at their projected revenue, labor model, and delivery fees to estimate profit from operating their restaurant in a Zuul kitchen.

For example, prior to joining Zuul, Sarge's Deli had one location in Midtown East. They often received requests for deliveries downtown, but it was difficult to deliver below 14th street. They had been considering expansion options, but traditional expansion didn't make sense for their business. Sarge's saw a Zuul ghost kitchen as a low-risk opportunity to expand for the first time and meet their takeout and delivery demand, which is currently 40-50% of sales.

Naya saw Zuul as a flexible way to expand their business to meet customer demand for delivery. Hady Kfoury, the founder of Naya had this to say:

“Some days we are forced to turn away delivery orders because our busiest locations are overwhelmed by dine-in demand. Having a ghost kitchen allows our restaurants to remain busy while meeting additional demand for delivery orders.”

These are common stories that I hear from restaurant owners and operators. When partnering with restaurant members, we've found that our business model is a good fit for small, local restaurants

looking to extend their digital brand presence throughout the NYC market. The ghost kitchen format works particularly well for restaurants that already have an established brick and mortar dine-in restaurant. Following the hub-and-spoke model, the restaurant serves as the hub with the ghost kitchen as the spoke. This means the restaurant can outsource delivery to a kitchen that was designed to deliver while keeping their dine-in restaurant busy as a destination and brand experience for guests.

Once a business decides to join Zuul as a restaurant member, we partner with them to design their ghost kitchen to their specifications. For example, ghost kitchens have a smaller footprint and sometimes restaurants need to bring in new equipment to adapt their operations. When Stone Bridge was designing their kitchen, we knew a stone pizza oven wouldn't be able to fit into the space, so they needed a new oven. Zuul's chef worked with Stone Bridge to evaluate the performance of multiple ovens at a test kitchen downtown. After installing and launching the new oven, it worked so well that Stone Bridge wanted to install another one back at their main restaurant.

As a delivery-only kitchen operator, we also have to have a strong program for technology and logistics. Zuul maintains relationships with specific software and delivery businesses to provide specialty support to our restaurant members. This includes a logistics firm who can deliver to high-security buildings downtown and an order aggregator for streamlining fulfillment.

Once a restaurant is open in their Zuul kitchen, we continue working with them to refine their ghost kitchen menu and operations based on data and guest feedback. We provide data openly to restaurant members and analyze it with them to determine what changes are recommended. Sometimes this means removing items that don't travel or sell, other times it means adding new items to meet a repeat special customer request. Whenever we work with restaurants to expand their menu, the items are wholly owned by the restaurant and attributed to their brand.

For example, we recently spent time working with Sarge's Deli to review their first three months of operational data. Based on feedback we received from downtown employees, Zuul worked with Sarge's to develop new combo items that appeal to the weekday lunch market. These new items create a smoother ordering experience for guests and generate higher volume orders for Sarge's.

Beyond operational support, Zuul works to ensure our restaurant's financial success by generating delivery sales for our members. We use our unique position as a ghost kitchen to offer a single source

menu, which features menu items from across all our restaurant members. This creates a differentiated delivery experience for guests looking to order multiple cuisines together for the same meal. We pay particular attention to demand generation for our members and make it a priority. To ensure their long-term success, we will continue to innovate ways to bring more orders directly to our members.

As we look to the future, one such innovation is Zuul's reusable bowl program. In speaking with clients about our single source menu, we've heard repeatedly that employees are looking for more sustainable food delivery solutions to their weekday lunch. As a company focused on delivery, we know that true sustainable and zero-waste delivery can only be achieved through closed loop logistics. We are working with our logistics providers and corporate clients to build a delivery solution that allows our restaurant members to eliminate the cost of delivery packaging by plating all orders in reusable bowls. As the ghost kitchen, Zuul then takes responsibility for managing the collection, washing, and stocking of the bowls for reuse.

To make these innovative programs and our restaurant members successful, Zuul intends to stay focused on the New York City market. The NYC food delivery market is unlike any other in the country due to the City's vertical density. As we look to help our restaurant members navigate NYC delivery, Zuul intends to grow our business and expand here in New York. We are currently evaluating potential ghost kitchen locations in Brooklyn, Manhattan, and Queens.

In closing, I want to again thank the New York City Council and Committee on Small Business for your continued support for restaurants across the city. As the future of the restaurant industry continues to evolve, Zuul intends to be an active member of the community in helping to set the standard for ghost kitchens. We're committed to open data sharing with our members and supporting them at every step. NYC is our home and we look forward to growing alongside our restaurant partners for years to come.

My name is Matt Newberg, I have spent the past eight years living in New York working as a product manager and entrepreneur in the technology field after graduating from the Wharton School of Business at University of Pennsylvania. Last summer, I released a 25-minute investigative online video that featured three delivery-only, ghost kitchen providers in Los Angeles, interviewing restaurateurs from each of them to make better sense of this new trend. While this began as a side project, the response from this piece launched me on a new path to form HNGRY, a new media platform that examines how technology shapes the way people eat. I have done extensive research into online food delivery and ghost kitchen providers, visiting different sites in Los Angeles, San Francisco and New York and speaking with as many restaurateurs, real estate operators, and employees as possible. I am here today to share my knowledge of the power that these kitchens hold and the potential impact that I foresee on our communities, workers, and small businesses.

My conversations have led me to conclude that the goal of these startups is to build kitchen infrastructure, automation, and logistics that are optimized to deliver food at a lower price than dining in a restaurant or cooking at home, just like in China. Because they aggregate dozens of restaurant brands and convenience items under a single roof, large players like CloudKitchens can leverage higher average order values to subsidize the cost of delivery, making it free for the end consumer. Imagine ordering a burger, your significant other ordering sushi, and adding in a bottle of wine to one delivery order. And because they are located in facilities that are optimized for the last mile of delivery rather than foot traffic, all of this is delivered at breakneck speeds that we have yet to fully experience in this country.

At a high level, you can think of a ghost kitchen like a virtual food court that you might find at an airport, where a small number of companies are responsible for a wide variety of concepts. Today, these kitchens plug into third party delivery marketplaces like UberEats, Seamless, Postmates, and DoorDash but tomorrow it could all exist on a single platform. It's quite analogous to Amazon, but instead of books, it's freshly prepared food that we feed our bodies.

This infrastructure is largely fueled by nearly \$2bn of foreign capital from the sovereign wealth funds of Saudi Arabia and Dubai for startups like CloudKitchens and Reef Technologies respectively. On the surface, they are repurposing real estate like parking garages, warehouses, and strip malls for the on-demand economy. They have eliminated the front-of-house in exchange for designated delivery pickup areas and feature exterior signage designed to ensure drivers, not diners, can locate the right facility. Thanks to a credit line provided by Goldman Sachs, CloudKitchens alone has the ability to turn its \$700mm of equity capital into a \$2.8bn war chest, at a minimum, to purchase any property that can be conceivably subdivided into dozens of kitchens.

As famous entrepreneur and early Uber investor Gary Vaynerchuk explained to a room full of marketing execs last summer, "It is unbelievable how much disruption is coming. The only thing that's going to be left is the brand, the affinity that the customer has for the brand and that's it."

It makes total sense that as fast casual and quick serve restaurants witness the majority of their sales shift away from dine-in towards off-premise channels like drive-thru, pickup, and delivery, that restaurateurs adapt to this new world of convenience.

But despite their lower upfront costs, the significant fees charged by delivery marketplaces and regular operating costs still make it incredibly difficult for the average independent restaurateur to turn a profit. A recent study from Kitchen Fund, an investor group that backs brands like Sweetgreen, by Chloe, and Inday found that a ghost kitchen operator must generate at least \$650,000 in annual sales in order to break even. By comparison, the average Chipotle store generates just under \$400,000 from both delivery and pickup, about 18% of an average retail location's sales. Both CloudKitchens and Kitchen United have experienced significant turnover from tenants since opening. The latter only has two of its original seven tenants remaining from its first location.

Because many restaurants cannot stay afloat selling a single brand in a ghost kitchen, providers like CloudKitchens equip their tenants with custom-built software that makes it easy to launch multiple concepts from each of their 225 square foot kitchens.

To illustrate this point, inside just one CloudKitchens 11,000sqft warehouse in West Adams, Los Angeles, there are 27 individual kitchens that are responsible for 115 unique restaurant listings on every single delivery platform at the time of my investigation.

These are all virtual concepts, some of which aggregate items across multiple kitchens inside the warehouse, enabling that dinner date scenario I mentioned earlier. You won't discover them by walking down the street. If you want to see them firsthand I suggest you google "site:postmates.com 1842 w washington blvd." If successful, I fear that the diverse set of local restaurants around this neighborhood such as Sophie's Cuban Cuisine, Pisillo Italian Panini, Bombay's Indian Restaurant, and Leo's Bagels would be replaced with virtual concepts like: Fry Me A River, Italian Stallion, WTF is a Quesorito?!, Late Night Munchies, Panini Gang, Try Tasty Tacos, and Morning After.

There are 185,000 single-unit full-service restaurants like these in the US, accounting for nearly a third of the total dining landscape by volume. According to the Bureau of Labor Statistics, independently owned restaurants employ just over 3 million workers. As restaurants shift towards an optimized off-premise, ghost kitchen model, the need for front-of-house staff is eliminated and the number of back-of-house cooks is drastically reduced.

Cashiers, hosts, and waiters account for ~60% of this workforce. These jobs are replaced by apps in a ghost kitchen environment. Dishwashers become a shared service within the entire facility, therefore that number trends towards zero. The remaining third of back of house staff shrinks in half from 5 to 2 or 3, leaving a total population of 500,000 cooks to find new work in ghost kitchens, about 17% of the current workforce.

Those 2-3 workers could halve again thanks to CloudKitchens' Silicon Valley operation that is working on building advanced conveyor systems. This could hypothetically evolve towards robotics.

While ghost kitchens could create positive efficiencies, like lowering carbon emissions through batched delivery orders or enabling restaurants to rapidly test new concepts, they simultaneously add another intermediate layer that makes it incredibly difficult to trace our food back to its source. On a recent investigation, I discovered that a Rachel Ray virtual restaurant concept on UberEats was originating from Reef Technologies' kitchen trailers in Chelsea and Long Island City parking lots, the latter of which was adjacent to a porta potty. These kitchens were recently shut down by the fire department due to their abundance of propane tanks that posed a safety hazard.

If there are any takeaways from my testimony today it's the power of leverage that these kitchens have in their ability to shrink a city block into a single warehouse. One liquor license that has the potential to blanket an entire city. One location that equals 13 operators, 27 kitchens, 115 concepts. There are four CloudKitchens locations in New York already, and more on the way: two in Tribeca, one in Midtown, another in Long Island City. By the end of this year, the 300-person-plus company will have a presence on every continent in the world.

It is my hope that today's discussion will inform future action that allows us to innovate while ensuring the future health and diversity of our modern workers, small businesses, and communities. Thank you.



February 6, 2020

Chairman Gjonaj, Members of the Small Business Committee:

Good morning. My name is Amy Healy and I am the senior director of public affairs at Grubhub, a leading online and mobile food-ordering and delivery marketplace with the largest and most comprehensive network of restaurant partners in the United States, as well as more than 22 million active diners.

Thank you for having me today and for the opportunity to discuss the impact of shared kitchens on New York's restaurants, its service sector employees, and its diners. I'm only a month into my time at Grubhub, but I'm looking forward to sitting down with each of you individually and developing a strong working relationship in the weeks and months to come – both on this topic, as well as Grubhub's role in the entire, burgeoning food marketplace in the city.

Amy Healy
**Senior Director of Public
Affairs**

1065 6th Avenue
New York, NY 10018

We have been connecting restaurants and diners in New York – the greatest food scene in the world – since 1999 and employ nearly 400 people on three floors near Bryant Park. Our employees live, work, breathe, and eat New York. We have proudly driven billions of dollars of revenue to local restaurants and over \$1 billion in tips to delivery workers.

Grubhub strives to elevate food ordering through innovative restaurant technologies, easy-to-use platforms, and an improved delivery experience. It is important to note that Grubhub products and services are designed to meet the changing demands of both consumers and restaurants. With stiff competition, high operating costs, and razor-thin margins, we understand that running an independent restaurant has never been for the faint of heart.

At the same time, the next decade holds tremendous opportunity for restaurant owners – especially here in New York City. Restaurants already account for \$863 billion – about 4% of U.S. gross domestic product. New digital capabilities like online ordering and delivery, next-generation point-of-sale (POS) systems, shared and virtual kitchens, as well as data-driven insights, are leveling the playing field, helping independent restaurateurs stand out in a crowded marketplace. Grubhub is thoroughly committed to working with restaurant partners of all sizes to help them use these new capabilities to grow and be successful.

The title of this hearing is "Ghost Kitchens," "Virtual Restaurants," and the Future of the Restaurant Industry. Given the nascent nature of these concepts, I wanted to spend a moment to distinguish between ghost kitchens, also known as commissary, cloud, or shared kitchens, and virtual restaurants.



In a shared kitchen, an owner leases space in a commercial kitchen that houses multiple concepts. A restaurant may utilize a shared kitchen to provide additional capacity to meet diner demand or to extend a restaurant's geographic reach.

Grubhub does not own kitchen space, nor do we have any plans to. We are in the business of connecting great restaurants with hungry diners, not real estate or restaurant operations. That said, we have partnered with restaurants and restaurant concepts to market them on Grubhub and to handle delivery logistics.

In a virtual restaurant, an owner uses excess kitchen space already owned by the restaurant. Virtual restaurants are delivery-only concepts. For example, virtual restaurants benefit small and medium sized restaurants because they help restaurateurs drive more volume from a new concept without the extra cost of a second kitchen. Since virtual restaurants utilize existing facilities, they demand significantly less capital from the restaurateur. Grubhub has partnered with many of our small and medium sized businesses by providing them advice, data and analytics (which I will more fully explain later), and marketing support to help them launch virtual restaurants, expanding their business and driving revenue without the level of financial risk required by opening an entirely new restaurant.

At Grubhub, we are always testing new ways to help restaurants get in front of diners who are likely to enjoy their food. This underscores the value that our virtual concept operators find with the Grubhub platform; it puts their concept in front of local diners from our national network of more than 20 million people. That is a lot of exposure and opportunity for restaurant owners.

The larger share of the virtual concepts we see on our platform are from independent restaurants that choose to open a virtual restaurant from their existing brick and mortar location to expand their customer base and capitalize on untapped demand in their market while driving more value from their fixed costs.

For example, this could be a brick and mortar sushi restaurant that also sets up a virtual restaurant specializing in poke bowls to use the same supply of tuna and salmon.

As I mentioned earlier, data and analytics are important tools for our restaurant partners. While complying with state and federal privacy laws and our own privacy policy, Grubhub shares data with restaurants about their business that is essential when thinking about virtual restaurants. We provide a data analytics dashboard to restaurants that includes daily and weekly sales, orders, and menu item performance metrics and trends. In addition to this dashboard, our Restaurant Success team works every day to evaluate the performance of the restaurants on our platform and to create customized plans to help our



partners be successful. We regularly share data via email to restaurant partners with suggestions about what dishes and cuisines are trending in their area to consider if they wish to open a virtual restaurant concept, but the choice of whether to open a new concept is always in the hands of the restaurant.

Grubhub has been committed to virtual concepts for the last five years, which is an example of how we're focused on making a difference with innovation that provides real value to our restaurant partners and diners. Virtual restaurants also let restaurant owners offer more creative menus without the overhead of renting additional kitchen space. Here is an example: We worked with an independent restaurant operator in Brooklyn to reach two delivery zones with their brick and mortar/virtual restaurant combo. The owner had operated a brick and mortar Mexican grill in Bay Ridge for years. But recently, after the owner took over a pizzeria restaurant in Park Slope, he decided to use the new location as a virtual Mexican grill restaurant as well -- adding another delivery zone without the added overhead.

We understand that with these new restaurant trends comes new policy and regulatory questions for local lawmakers and government agencies. And Grubhub applauds this committee for bringing together interested stakeholders at this oversight hearing so we can all better understand the implications these trends have on our local business communities. Grubhub provides the same benefits to a shared kitchen or virtual restaurant available to our brick and mortar restaurant partners. We require the same contract for a virtual restaurant or shared kitchen restaurant as we do for a brick and mortar restaurant. And every one of the business entities we partner with are required to comply with all local licensing rules and legal requirements as part of our agreement with them.

Grubhub is proud of our ability to drive revenue, attract diners, and provide tools to our small and medium sized restaurant partners that have traditionally only been available to large national restaurant brands. We continue to strive to develop products and services to help our restaurant partners adapt to changing diner demand and a changing restaurant marketplace.

Again, I thank you for inviting me here today and I look forward to your questions.

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Appearance Card

I intend to appear and speak on Int. No. Shay Kitchen Res. No. _____

☐ in favor ☐ in opposition

Date: 2/6/20

(PLEASE PRINT)

Name: Kathleen Reilly

Address: _____

I represent: New York State Restaurant Assn

Address: _____

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☐ in favor ☐ in opposition

Date: 2/6/2020

(PLEASE PRINT)

Name: Commissioner Gregg Bishop

Address: _____

I represent: NYC Small Business Services

Address: _____

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☐ in favor ☐ in opposition

Date: _____

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Name: Corinne Schiff, Deputy Commissioner

Address: NYC Dept. of Health and Mental Hygiene

I represent: _____

Address: _____

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Date: _____

(PLEASE PRINT)

Name: Corey Manicone

Address: _____

I represent: ZUL

Address: 30 Vandam St. NY, NY 10013

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☐ in favor ☐ in opposition

Date: 2/6/20

(PLEASE PRINT)

Name: Sean Fitzgibbons

Address: _____

I represent: ZUL

Address: _____

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Appearance Card

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☐ in favor ☐ in opposition

Date: 2/6/20

(PLEASE PRINT)

Name: Matthew Newberg

Address: 535 E 6th St NY, NY 10009

I represent: HNGRY Media Holdings LLC

Address: Same

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Date: _____

(PLEASE PRINT)

Name: Tom Collins

Address: 95 S. Madison Avenue

I represent: Urban Order

Address: 25 West Broadway

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☐ in favor ☐ in opposition

Date: _____

(PLEASE PRINT)

Name: Steven Picker

Address: 2 Liberty Plaza

I represent: NYC Dept. of Small Business Services

Address: _____

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☐ in favor ☐ in opposition

Date: _____

(PLEASE PRINT)

Name: Commissioner Gregg Bishop

Address: 2 Liberty Plaza

I represent: NYC Department of Small Business Services

Address: _____

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Date: 2/6/2020

(PLEASE PRINT)

Name: Amy Healy

Address: _____

I represent: Gubhub

Address: 1156 6th Avenue

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Date: 2/6/20

(PLEASE PRINT)

Name: Robert Guarino

Address: _____

I represent: 5 Napkin Burger

Address: _____

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☐ in favor ☐ in opposition

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(PLEASE PRINT)

Name: Andreas Foutsoudakis

Address: _____

I represent: tribeca Kitchen

Address: _____

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(PLEASE PRINT)

Name: Andrew Schnipper

Address: _____

I represent: Schnipper Restaurant Group

Address: _____

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Date: 2/6/20

(PLEASE PRINT)

Name: Andrew Pigie

Address: 65 West 55 Street

I represent: Hospitality Alliance

Address: _____

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(PLEASE PRINT)

Name: Jeff Bank

Address: _____

I represent: Alicart Restaurant Group

Address: _____

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Date: 2/6/20

(PLEASE PRINT)

Name: Robert Bookman

Address: _____

I represent: Pesetsky + Bookman

Address: 325 Broadway Suite 501

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