Understanding Total Cost of Ownership

As foodservice operators examine their expenses, they are using total cost of ownership to help make purchasing decisions that generate a higher return on investment.

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The concept of total cost of ownership is not a new one to the foodservice industry. Approaching an equipment purchase from a total cost of ownership perspective encourages the operator to look at factors beyond the invoice price, including operating costs, maintenance and service. By taking these factors into account, operators can better understand the return on investment that a particular piece of equipment will provide and make informed purchasing decisions. An operator might pay a bit more upfront, but the business should recapture that investment and more over the product's life cycle.

Despite the inherent benefits of this sound business practice, it appears this holistic approach to purchasing foodservice equipment has been slow to catch on. "Unfortunately, operators are often driven by budget and time constraints that can limit their possibilities," says David Zabrowski, senior engineer/senior project manager of Pacific Gas & Electric Co.'s Food Service Technology Center.

While many operators and consultants might want to skip the steps associated with determining total cost of ownership because of a lack of resources, it remains a worthwhile time investment. "When you spend $60,000 to $70,000 for a piece of equipment, saving $10,000 to $20,000 on energy or maintenance over the course of its service life is significant," says Dipak Negandhi, senior engineer, Unified Brands. Negandhi also is a member of NAFEM's Technology Liaison Committee and chair of ASTM's committee for foodservice standards. "And for consultants, it's a way to add value to their relationships."

The good news is that it appears foodservice operators are warming to this approach to purchasing equipment. "Life-cycle costs are very important to us," says Angela Hughes, senior facility leader for Pizza Hut Facility Management. "If an item costs too much over its service life, we will quit buying it. It's not about the up-front costs anymore. If the product does not hold up, it is not worth what we paid for it."

Some restaurant chains use the data from a total cost of ownership study to help create or refine existing equipment packages. "This analysis can help sell franchisees on the new equipment and the results of a comprehensive energy analysis can be taken to energy utilities to make a case for incenting a retrofit," Zabrowski says.

For example, the equipment package at Rock 'n' Joe, a coffee house and lounge, is simple: key items are a refrigerated prep table, panini grills, shelving, reach-in refrigeration, dishwasher and, of course, an espresso machine. Despite the streamlined equipment package, the total cost of ownership for each item is critical to the restaurant chain's success.

"Funding is so hard to get now that we have to produce as much bang for the buck as we can," says Kevin Brennan, the chain's founder and CEO. "Initially, we were just looking at the invoice but we look at other factors such as electricity and maintenance. We've been going through our whole equipment package and trying to tighten costs."

For example, each Rock 'n' Joe location was using 72-cubic-ft. refrigerators and freezers; careful analysis indicated to Brennan and his team that such capacity wasn't needed. As a result, the chain switched to smaller units with a total cost of ownership that was less than the larger units. This adjustment was significant as the costs of other key equipment, such as the espresso machines, was increasing.

rockin joe

With its base equipment package established, Rock 'n' Joe now makes minor adjustments based on anticipated sales volume for each new location. For example, the restaurant chain is opening a location in a train station that will feature more grab-and-go items, but only one staff member working the register.

Factors outside the foodservice industry continue to drive interest in total cost of ownership. "The recent education stimulus funding required an analysis of the equipment efficiency in the application process," Zabrowski says. "Schools have had to make a case that the energy consumption and associated operating cost would be reduced with the new equipment. Appliance energy consumption analysis also plays into LEED and sustainability-related projects. Many of the higher profile LEED restaurants were required to model appliance energy use and involved an analysis of the payback on the higher equipment costs. And then there's the issue of rising utility costs, which play right into this strategy."

Rock 'n' Joe's original location saw its monthly electricity costs rise to $1,400 from $1,000 this past summer, prompting the store to explore energy-saving alternatives. "We looked at the lighting package and ways to be more efficient in terms of electricity used and the type of fixtures," Brennan says. "We're a small concept and saving money on electricity means a lot to us. When you multiply that out over a few months, you are looking at buying another piece of equipment."

Approach to Purchasing

Supporting operations and product delivery remains the most important factor when purchasing any piece of foodservice equipment. "The equipment has to match the menu you are going to put out, and because you are going to change that menu quite a bit, that equipment has to be flexible," says Danny Koontz, director of facilities management for Ruby Tuesday.

Ruby Tuesday'

Ruby Tuesday's cookline consists of griddles, fryers, convection ovens and conveyor ovens. "If we decide to rollout a new item for the menu we have to adapt to what's there," Koontz says. "One of those four pieces has to be able to take care of it."

Ease of operation is an important consideration for most foodservice operators making purchasing decisions. "Too many bells and whistles end up causing you problems," Koontz says. "Don't make the equipment too hard for the cook or the employees in the restaurant to use. ... And the local service guy needs to be able to fix the piece of equipment on the spot, so there can't be too many parts."

In addition to invoice and operating costs, determining the amount of revenue a piece of equipment can generate plays a role in determining a purchase. Rock 'n' Joe was looking at adding a rapid-cook oven to its package but decided against it. "I did not feel it was going to have enough of an impact on sales to warrant adding a $10,000 piece of equipment," Brennan says.

Foodservice operators' philosophy toward the purchasing and operations functions can affect their approach to total cost of ownership. "Unless the facilities and purchasing departments are joined at the hip, you can have problems when you split those functions apart," Koontz says. "When the purchasing and facilities functions are managed by the same person, it is pretty simple. That person is not going to buy something that does not have the network out there to support it."

When purchasing and operations work independently, though, their objectives can be mutually exclusive. "When your only responsibility is to purchase, then price becomes your primary concern and the warranty and benefits package that come with a piece of equipment does not come into play," Koontz says.

That's why Koontz works closely with his company's purchasing department to ensure that the equipment purchased not only meets price and quality needs but also suits long-term service and warranty. "Anybody can sell you a piece of equipment but the service and the support that goes on for the next five to seven years is not something everyone can do," he adds.

While price remains an issue for Pizza Hut, the chain tries to manage its purchasing process holistically, meaning that its purchasing, engineering and facilities management departments work more closely together. "Our purchasing department realizes you can't base everything on price because it can result in a higher total cost of ownership," Hughes says. "So we are talking to each other a lot more than was the case when I first joined the industry ten years ago."

After Purchase Costs

For most operators, after the sale costs are managed in terms of service, employee interaction, and the like. Pizza Hut continues to collect and share this data with its vendor partners. "It's a pretty powerful thing that can be good for all of us," Hughes says. "But the manufacturers need to do a better job of tracking the life cycle costs of their equipment, too."

Doing so would enable manufacturers to become more proactive in identifying issues with their equipment and sharing that information with customers. "We are trying to identify trends and it would be great to be able to work together more," Hughes says.

One issue that does not seem to have gained as much traction with operators despite receiving a lot of attention is energy efficiency. There is a need for education in this area, Zabrowski says. "Many operators may not be aware of the impact of equipment choices on their operating costs. The industry needs to wake up and be willing to pay more for equipment that offers increased performance, lower energy usage and greater reliability. As long as purchasers focus on the price as the bottom line, then the industry will continue to use the least-efficient equipment designs."

Many operators, like Koontz, plan to integrate energy efficiency but are not willing to pay a premium for it. "If everything else is even, yes, I am willing to pay 10 percent more for a piece of equipment that is more energy efficient," he says. "But we're not willing to pay 50 percent more."

In addition, saving energy tends not to be a priority for the frontline staff of a typical foodservice operation. For example, most cooks will turn all the equipment on first thing in the morning out of habit. Gradually firing up the equipment will reduce the peak energy usage charges a foodservice operation gets. "They don't pay the utility bill. The only way to get managers to understand savings and costs is to tie it back to their bonus structure. Then they will hear you," Koontz says.

The availability of parts and service can be a part of the purchasing process that foodservice operators can easily overlook. Unfortunately, during the course of the equipment's service life, the operator can pay the price in terms of lost productivity and sales when the item malfunctions. "Once, when rolling out a menu item, we bought a specific product for all the restaurants and a couple of years down the road, service became a nightmare. In retrospect we would not have bought that product," Koontz says. "You have to know the product lines and who manages the service for the product you are going to buy."

To further streamline operations, Koontz tries to consolidate equipment vendors because doing so affects service, too. "I want to have less service companies in my restaurants and this allows me to have the same service guys working on my equipment," Koontz says. "I manage service contracts just like they are insurance. I try to make it elementary for the restaurant manager. They have one person to call and if it extends past that, we take it over."

Hughes points out that she proactively replaced the equipment in the facilities she manages, but noticed that certain items were not lasting as long as they once did. As a result, she began refurbishing the equipment and replacing component parts instead. "We can't afford something that lasts less than five years because we can't afford the shorter write off," she says.

"We don't define value the way we used to," Hughes says. "On the user end, we don't look at it strictly in terms of invoice price anymore."

In making this point, Hughes cites an example of an update Pizza Hut made in its stores. The chain was using one product in all of its stores and maintaining the item was time-consuming. Hughes and her team tested other options and found a similar product that cost 20 percent more than the original item, but lasted longer and was easier to clean. "So I am spending more for each store but I don't have to touch this as much," she adds.

"When I understand the value, I will pay more," Hughes says. "And the restaurant operators are happier about it because we are not managing a quality issue."

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