Issue: The Sharing Economy

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By: Patrick Marshall

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Is it really different from traditional business?

Executive Summary

What's called the sharing economy—peer-to-peer transactions conducted via the Internet and smartphones—has changed how people arrange car rides, find vacation lodging and more. Revenue is projected to soar in the coming years, although profitability remains untested. But as businesses such as Uber, Lyft and Airbnb flourish, regulation and collection of taxes, primarily by state and local authorities, have become more difficult to enforce. Traditional businesses such as taxis and hotels complain that these newcomers are gaining an unfair advantage by ducking oversight that's meant to protect consumers. Additionally, debate has grown over whether service providers in the sharing economy are independent contractors or employees. Some of the key issues under debate: Is the sharing economy more efficient than traditional markets? Should regulators treat the sharing economy the same way as conventional competitors? Are sharing-economy companies platforms for independent contractors, or are they employers?

Overview

A Lyft car, marked with a bright pink mustache, lines up next to a traditional taxi in San Francisco traffic. Ride-hailing services such as Lyft are among the most visible players in the sharing economy. The taxi industry charges that these new firms compete unfairly. (Justin Sullivan/Getty Images)

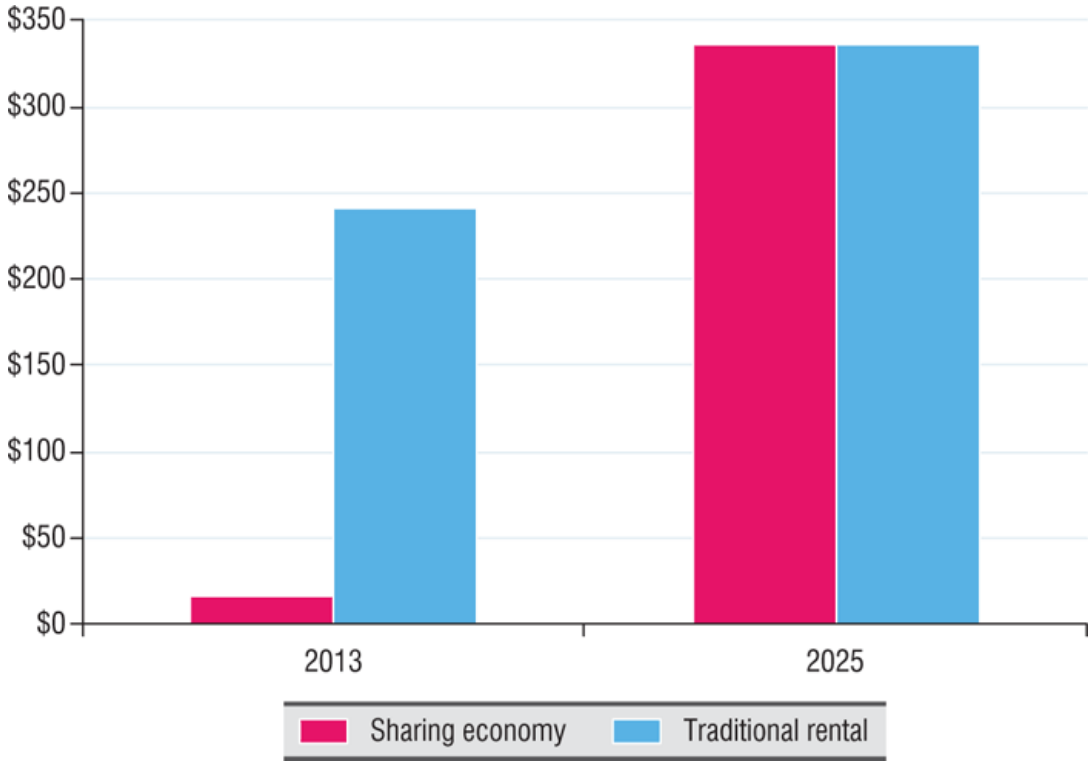
The "sharing economy"—in which consumers connect with service providers using Internet applications instead of relying on traditional providers—is booming. On a typical day, an estimated 247,000 items are sold on Etsy, 140,000 people rent accommodations through Airbnb and 1 million people ride with Uber. [1]

Because very few sharing-economy companies are publicly traded, it's unknown whether they are profitable. But many sharing-economy companies are attracting major investments and have quickly become players in the economy. Based on venture capital funds raised, The Wall Street Journal estimated Uber's value at more than $40 billion and Airbnb at $25 billion. [2]

In fact, according to the Federal Trade Commission, sharing-economy transactions totaled about $26 billion globally in 2013. [3] And PricewaterhouseCoopers (PwC), an auditing and consulting firm, estimates that in 10 years, the biggest sectors of the sharing economy could see $335 billion in global revenue. PwC projects that by 2025, sharing-economy companies will account for about half of the business in their market sectors, up from only 6.25 percent in 2013. [4]

Sharing Economy to Match Rental Revenue by 2025

Projected revenue for rental services, by sector, in $U.S. billions, 2013 and 2025



Note: 2025 estimates based on historical data and projected growth rates and economic outcomes for 10 industry sectors.

Source: "The sharing economy—sizing the revenue opportunity," PricewaterhouseCoopers, 2014, http://tinyurl.com/ophtwcf

Internet-based sharing businesses will generate an estimated $335 billion in revenue by 2025, the same amount projected for five traditional rental sectors (equipment rental, B&B and hostels, car rental, book rental and DVD rental).

What's more, sharing-economy companies are emerging in numerous niche markets. It's not, in short, just about renting apartments and hailing cars. There is a platform that cities can use to share heavy equipment (MuniRent), a platform that skiers, bicycle and surfboard owners can use to rent their recreational equipment (Spinlister) and a platform that musicians can use to share their equipment (GearLode). (See Short Article, "Niche Markets Offer Big Potential.") There is also a robust group of platforms that connect investors to individuals and small businesses seeking funding (Funding Circle, LendingClub, Prosper, TransferWise).

"It's clear that consumers are embracing it," says John Breyault, vice president of public policy at the National Consumers League, a consumer advocacy group in Washington, D.C.

Of course, the sharing economy—which has also been described as a peer-to-peer economy—is not actually new.

"Peer-to-peer businesses were around long before the Internet," Philip Auerswald, associate professor of public policy at George Mason University, told a House hearing on the sharing economy last year. "Indeed, there was a time in this country and elsewhere in the world (roughly until the end of the 19th century) when the peer-to-peer economy *was* the economy. Large corporations providing consumer services simply did not exist. Regulation governing consumer services was minimal. People provided services on a personal basis to other people who were very much like them." [5]

While peer-to-peer transactions may not be new, analysts say, how those transactions occur is. The Internet and smartphones have allowed transactions to take place around the block or around the globe, almost instantaneously. "It's these different technologies that are making things easier," says Dean Baker, an economist and the cofounder of the Center for Economic and Policy Research, a Washington, D.C., think tank. (See Expert Views, "Pro/Con: Dean Baker on Regulating the Sharing Economy.")

Indeed, the Internet has fundamentally changed the nature of peer-to-peer transactions. Where previously those dealings involved only the buyer and seller of goods or services, now they are mediated through a software platform, which is owned by a company or, in some cases, a nonprofit organization. That change has led to two developments. First, regulation and collection of taxes, primarily by state and local authorities, have become more difficult to enforce. Second, there is growing debate over whether service providers in the sharing economy are really independent contractors or employees.

The stakes involved are high. If regulators require sharing-economy companies to conform to laws governing employers' treatment of employees, the prices of their goods and services will likely rise and their competitive advantage against traditional companies will be reduced.

Chicago taxi driver Keith Williams joins a February 2015 protest against smartphone-hailed car services. Cities across the world are wrestling with how to regulate such sharing-economy companies. (Scott Olson/Getty Images)

Corporate involvement in the sharing economy, some analysts say, means that much of this economy has little or nothing to do with sharing. “Make no mistake about it, today's sharing economy is big business, involving lots and lots of money and all kinds of players motivated powerfully by financial gain,” said Nancy Koehn, a professor at Harvard Business School. [6]

Although the Internet has enabled the sharing economy to blossom, other factors also have contributed. “While some of these sharing models might have resulted from a need for frugal spending after the global economic recession of 2008,” wrote entrepreneurship professors Boyd Cohen and Jan Kietzmann, “their success was also driven by a growing environmental consciousness combined with the ubiquity of Internet and associated information and communication technologies which make sharing possible at scale.” [7]

Koehn speculated that deeper aspects of consumer psychology may explain the booming popularity of many sharing-economy companies. “There is a directness about calling a limo ride yourself on Uber or Lyft and then rating the driver and car after you get to your destination that is both empowering and seemingly more transparent than calling a car service or hailing a taxi,” she said. “Individuals from all walks of life, particularly younger consumers, simply do not have much trust in established business, governmental, and other large-scale organizations. Against this backdrop, many consumers—and sellers—find peer-to-peer buying and selling to be more appealing because it is not so closely associated with a big business that may (or may not) have a mixed track record in their minds.” [8]

The relatively new technologies that power the sharing economy have put many transactions outside the purview of regulators. While cities issue taxi medallions to a limited number of service providers, they have little control over the drivers who connect to passengers using Uber, Lyft or Sidecar. And while cities license and tax hotels, they haven't yet developed a way to manage and monitor homeowners and companies renting through sharing-economy companies such as Airbnb.

As a result, although consumers generally seem happy with the savings and convenience delivered by sharing-economy companies, many of those companies are beginning to feel pressure from several directions. Those include their contractors (or employees) unsatisfied with wages and the lack of benefits; government agencies and competing businesses that claim sharing-economy companies are dodging needed regulation; municipalities that accuse service providers of failing to pay taxes; and consumer groups that say some companies are underserving certain groups of people.

Not surprisingly, the greatest amount of attention has focused on the most successful sharing-economy companies: Uber and Airbnb.

"The growth of illegal hotels is rapidly becoming one of the biggest obstacles in the struggle to protect and expand New York City's stock of affordable housing," Democratic New York state Sen. Liz Krueger told the Federal Trade Commission in May. "Online platforms like Airbnb lure individuals into breaking the law with promises of more income from operating illegal hotels, leaving residents with an increasingly scarce supply of affordable housing." [9]

New York state Sen. Liz Krueger charges that weak regulation of Airbnb reduces New York City's supply of affordable housing and exposes consumers to dangers. (Andrew H. Walker/Getty Images for Women's Campaign Fund)

Krueger also charged that the lack of effective regulation over Airbnb exposes consumers to drawbacks of which they may not be aware. "Most illegal hotels fail to meet federal, state and city accessibility requirements for people with disabilities," she said. "Far from being a harmless service that promotes 'sharing,' companies like Airbnb threaten public safety and make it more difficult for everyday New Yorkers to find an affordable place to live."


Brian Chesky: "Hosts … are regular people."

Airbnb did not to respond to repeated requests for comment. In a blog post in 2013, however, CEO Brian Chesky argued that the company actually helps New Yorkers stay in their homes. "In New York, our 15,000 hosts are regular people from all five boroughs. Eighty-seven percent of them rent the homes in which they live," wrote Chesky. "On average, they are at the median income level and more than half of them depend on Airbnb to help them stay in their home." [10]

Ride-sharing companies have drawn even greater criticism from competitors and regulators. "The thing with Uber and Lyft, what they're doing is they are cutting corners on safety and responsibility under the guise of the sharing economy," says Dave Sutton, a spokesman for the Taxicab, Limousine & Paratransit Association, which represents 1,100 taxicab companies. "Their insurance has gaps, which has come to light, and more and more will be revealed. Their background checks are not conducted by law enforcement and don't involve fingerprinting. And those are truly undercutting public safety."

Uber declined requests for interviews and responded to questions only by providing links to materials on the company's website. The materials do not indicate that Uber's background checks include fingerprints and reviews by law enforcement agencies.

The reaction to Uber by taxi drivers in some other countries has been even more dramatic. In early July, for example, Uber was forced to suspend its UberPop service in France after taxi drivers violently protested. [11]

Because sharing-economy companies are using new technologies that transform the way business is conducted, analysts say, a period of adjustment is inevitably needed to balance the competing interests of companies, regulators and consumers. "It is no surprise that Uber, Airbnb and other new companies find themselves operating in an area where the application of existing laws is potentially unclear," said Koehn. "It is also not surprising that these companies are fighting efforts by regulators to apply government rules and standards to their growing market." [12]

As the market presence of the biggest sharing-market companies has surged, friction with regulators—particularly at the state and local levels—has grown more pronounced in recent months.

For example, in the wake of an October report by the New York State Office of the Attorney General, which found that 72 percent of units booked via Airbnb in New York City appeared to violate state and local laws, city officials have begun filing suit and imposing fines on property owners. [13] The day after the report was released, the New York Daily News learned that New York City had filed suit against two property owners. [14]

In fact, many cities have long banned rentals of fewer than 30 days for properties that have not been inspected and licensed. And several cities have successfully pressed Airbnb to collect appropriate taxes from hosts for payment to the cities.

Employees of Airbnb work in the company's Paris office in April 2015. The company, which collects a fee for each peer-to-peer lodging transaction that takes place over its system, has moved aggressively into markets around the world. (Martin Bureau/AFP/Getty Images)

For its part, Uber has been banned by several communities and airports and has been sued by drivers who say that the company should be treating them as employees rather than independent contractors. In June, in a ruling that could be portentous, the California Labor Commissioner's Office determined that an Uber driver should be classified as an employee, not an independent contractor. Uber was ordered to reimburse the driver, Barbara Ann Berwick, $4,152.20 in expenses and other costs for the eight weeks she worked as an Uber driver. While the ruling applies only to Berwick and Uber is appealing it, the case could significantly affect Uber's competitive pricing if other courts agree that drivers are employees. [15]

“The explosion of sharing or on-demand services like Uber and Airbnb is the beginning of an economic upheaval every bit as significant as the Industrial Revolution,” warned Frank Shafroth, director of the Center for State and Local Government Leadership at George Mason University. “The on-demand economy promises to radically reshape the cost of services and change the face of the workforce. These upheavals, in turn, are altering state and local government policies—imposing unforeseen fiscal risks.” [16]

Specifically, Shafroth wrote, in addition to the challenges of recovering lost tax revenue and ensuring public safety, policymakers will have to deal with an upsurge in the number of temporary or part-time workers in the economy. “These workers are providing on-demand services at rock bottom prices. They are not working in downtown or suburban office buildings or for traditional employers, nor are they eligible for traditional health-care or pension benefits,” he said. “Leaders will need to be part of a discussion about changing rules for ‘contract workers,’ and of an even larger federalism and governance discussion about how pensions and health-care benefits are delivered in the future.”

Number of Part-Time Workers Peaked During Recession

Number of Americans working part time, ages 16 and older, in millions, 2005–15

Note: Part-time workers are those who indicated they would like to work full time but were working 1 to 34 hours per week for economic reasons, such as being unable to find full-time jobs.

Source: "Labor Force Statistics from the Current Population Survey," U.S. Bureau of Labor Statistics, downloaded July 20, 2015, http://tinyurl.com/m6996nd

About 6.5 million Americans work part time for economic reasons, even though they say they would prefer to work full time, a number that experts say could rise with a growing sharing economy. The number of these part-time workers jumped from 4.3 million in October 2007 to 9.1 million by March 2009 during the recession, hovering there for about two years before gradually declining.

Additionally, the expansion of the sharing economy may have a lasting impact on other industries, such as automobile manufacturing. As consumers come to rely increasingly on sharing-economy transportation services, car ownership could decline. Indeed, a 2012 report by the U.S. Public Interest Research Group and the Frontier Group found that between 2001 and 2009, the average annual number of vehicle-miles of driving by young people (16 to 34-year-olds) decreased from 10,300 miles to 7,900 miles per capita—a drop of 23 percent. The report cites the rise of services such as Zipcar as a major factor in the trend. [17]

Shafroth said, "It's not for nothing that the on-demand economy is simultaneously dubbed the disruptive economy." [18]

As the controversy around the sharing economy grows, here are some of the questions being debated:

Weighing the Issues

Is the sharing economy more efficient than traditional markets?

Sharing-economy supporters say that the companies and the platforms they offer are using technology not only to offer savings and convenience to consumers but also to make more efficient use of resources and to expand income opportunities for service providers.

The sharing economy, the staff of the House Committee on Small Business wrote in a January 2014 memo, more efficiently allocates "resources which in turn results in new consumption leading to new production." [19]

"Peer-to-peer marketplaces can have very different roles in an existing service industry," explains Chiara Farronato, an economist who is researching peer-to-peer Internet platforms. "They can actually take a thin local market and make it 'thick' and very global." She cites eBay's creation of global markets for goods that previously were difficult to sell locally. "And you can create new markets," she says. "For example, Instacart delivery options are creating a new [grocery] market that was not previously available."

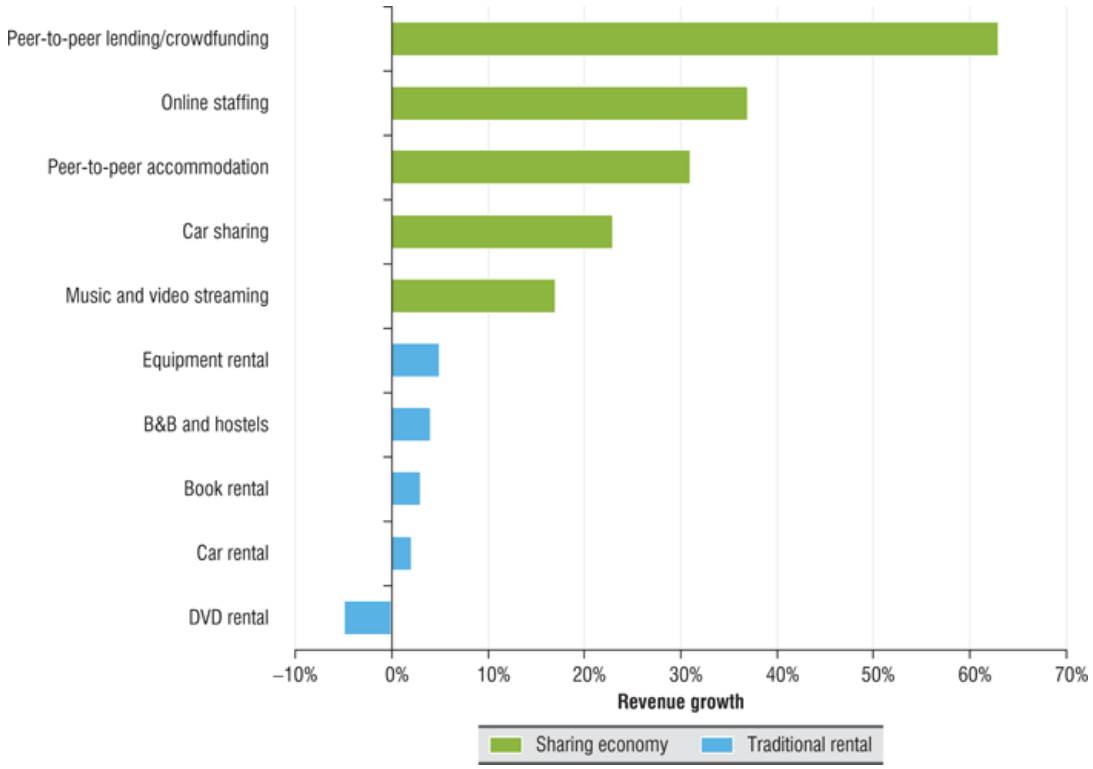
Even Airbnb, which may divert some customers from traditional hotels, has expanded the market, especially in locations where the supply of hotel rooms is constrained by either regulations or geography, Farronato says. "In San Francisco, for example, there is a limit to expansion and demand is high," she continues. "So the entry of Airbnb has actually not led to people substituting away from hotels. It's possible for more people to come to San Francisco to visit the city." Farronato says her research has shown that hotels didn't experience

Chiara Farronato: Airbnb has expanded the lodging market.

a large reduction in mean price and occupancy.

Peer-to-Peer Markets Growing More Quickly Than Traditional Sectors

Projected growth of sharing economy and traditional rental sectors, 2013 and 2025



Note: Growth estimates based on historical data and projected economic outcomes for industry sectors.

Source: "The sharing economy – sizing the revenue opportunity," PricewaterhouseCoopers, 2014, http://tinyurl.com/ophtwcf

Sharing-economy sectors are expected to grow rapidly from 2013 to 2025, with the largest revenue growth in peer-to-peer lending/crowdfunding (up 63 percent) and online staffing services (up 37 percent). Forecasters project marginal or negative revenue growth for comparable traditional rental sectors.

Similarly, while Uber has no doubt diverted some riders—and drivers—from other transportation providers, at least one study has found that the company has expanded jobs and ridership overall. "The availability of modern technology, like the Uber app, provides many advantages and lower prices for consumers compared with the traditional taxi cab dispatch system, and this has boosted demand for ride services, which, in turn, has increased total demand for workers with the requisite skills to work as for-hire drivers, potentially raising earnings for all workers with such skills," write Princeton economist Alan B. Krueger and Jonathan V. Hall, head of policy research at Uber Technologies. [20]

The study has been questioned by some economists, who note that it is based on selected Uber data. "Krueger's study looks at gross income for Uber drivers and compares it with ostensibly net income for cab drivers in the same cities," Baker of the Center for Economic and Policy Research says. "The reason he doesn't have an estimate of the net for Uber drivers is that he doesn't know how many miles those Uber drivers drove. Uber has that data. They just chose not to give it to him."

Sarah Cannon, Google Capital manager, and Lawrence H. Summers, former U.S. Treasury secretary, defend the sharing economy. "These firms bring significant economic, environmental, and entrepreneurial benefits, including an increase in employment," they argued in a Harvard Business Review article. They added that car-sharing services should reduce carbon dioxide emissions, benefiting the environment. [21]

Some analysts have estimated that for every shared vehicle, between nine and 13 private vehicles are removed from the roads, either by members selling a personal vehicle or postponing a planned purchase. [22] According to Susan Shaheen, an expert in innovative mobility research at the University of California, Berkeley, car sharers report reducing the vehicle miles traveled by 44 percent. [23]

While acknowledging that sharing-economy companies have had positive effects on markets, some analysts—as well as competitors—say that in some cases sharing-economy companies simply move jobs from existing industries to the new companies. They charge that these companies gain their competitive advantage by evading taxes, regulations and the cost of providing employee benefits.

“There are obviously some efficiencies there, using the technologies to connect buyers and sellers,” Baker says. “And I'm sure there is some net job creation. But I suspect that for the most part it is displacement, that you have lost jobs in the traditional cab industry, and you're replacing them with Uber drivers.”

Ride-sharing services, Baker says, are also evading regulations, and consumers may not even be aware of the hidden costs. “There are hidden costs in the sense that people are maybe getting a car that's not safe, or a driver who is not safe.” Baker acknowledges that Uber has begun to take steps to ensure the safety of drivers and cars. “But they originally were trying to evade that,” he says. “It remains an ongoing issue.”

Some analysts say that while consumers may like the low prices that companies can offer by avoiding costly regulations, the overall impact on jobs is to drive wages down.

“There are a lot of articles coming out saying that these sharing-economy companies are turning people into mini-entrepreneurs, but in many cases, the way some people look at it, they are exploiting people,” says Giana Eckhardt, professor in the School of Management, Royal Holloway, University of London.

Eckhardt notes that independent contractors not only often work for lower wages but also don't receive benefits, such as health insurance and sick leave. What's more, independent contractors must make their own payments for Social Security and Medicare, costs that are normally paid by a worker's employer.

Of the growing chorus of complaints by Uber drivers, Joseph De Wolf Sandoval, an Uber driver and the president of the California App-Based Drivers Association, told a reporter, “It's not just a small group of disgruntled or unprofessional drivers, as Uber would like to cast us. It's a nationwide feeling of general unhappiness and unease with policies and programs that are being promulgated by Uber without the drivers' input whatsoever.” [24]

When Uber lowered fares in July, some drivers took exception. “Since Uber implemented the 20 percent off discount on all Uber rides, I've been losing $200 a week,” Oris Fortuna, an Uber driver, said. “To make up for it, you have to work 20 percent more. That means more mileage and more gas. An $8 trip is not worth it.” [25]

Should regulators treat the sharing economy the same way as conventional competitors?

Sharing-market companies, along with free market advocates, argue that the new platforms driving the sharing economy have features that make the old regulatory frameworks unnecessary.

“While some regulators are tempted to regulate sharing economy companies like their competitors, to do so would be a mistake that betrays a misunderstanding of how the sharing economy works,” wrote Matthew Feeney, a policy analyst at the Cato Institute, a libertarian think tank. [26]

Matthew Feeney: Customer ratings head off bad behavior.

According to Feeney, the online customer ratings that sharing-economy companies such as Uber and Airbnb have made a central part of their business models are more effective than regulations at stopping misbehavior. “Badly behaved providers and consumers in the sharing economy do not last long, and the lack of anonymity means that anyone who does commit a crime is unlikely to escape justice,” Feeney said.

As for dealing with bad actors, Arun Sundararajan, professor of information, operations and management sciences at New York University's Stern School of Business, says that the platforms can deal with them more efficiently than can regulators. “The interests of the platforms are well aligned with facilitating safe and profitable peer-to-peer trade (since their revenues are directly linked to the volume and continued growth of such trade),” Sundararajan told a House hearing in written testimony in January 2014. “The platforms are also better positioned to ‘take action’ against infringing entrepreneurs and consumers (for example, by simply disconnecting them from the platform).” [27]

Even in the absence of formal regulation, the review tools offered by sharing-economy platforms are not the only options for keeping bad actors in check.

“We have to remember there are always civil and criminal protections that will keep people safe,” says Christopher Koopman, a research fellow at the Mercatus Center at George Mason University. “Just a few mistakes by these firms could sink one of these companies before they really have a chance to take off.” (See Expert Views, “Pro/Con: Christopher Koopman, Matthew Mitchell and Adam Thierer on Regulating the Sharing Economy.”)

Other analysts point out the review system poses several problems, starting with the possibility that sharing-economy companies can

manipulate the process.

Asked what assurance consumers have about the integrity of companies' review systems, economist Farronato says simply, “It's their word.” She notes that historically 15 percent of reviews on Yelp proved to be fake. “The peer-to-peer platforms are very different in how they handle fake reviews,” she says. “Some are working much harder than others. My take is that large companies are probably doing a very good job of weeding out the fake reviews.”

Koopman says, in fact, that companies have a vested interest in earning consumers' trust. “If people are not trusting the rating systems, they're no longer trusting the companies,” he says. “If they are no longer trusting the companies, they're not going to want to do business with them anymore.”

A second problem, some analysts say, is that a negative consumer review doesn't appear until after something bad has happened.

“Unfortunately it takes a tragedy and then people become aware,” says Sutton of the Taxicab, Limousine & Paratransit Association.

Ideally, advocates of regulation argue, regulators require behaviors that prevent abuses from happening in the first place.

Uber has begun running background checks on drivers, which Baker calls “wonderful.” But unless there's a regulatory framework that requires those checks, he adds, “there's no guarantee they will always be doing it.”

Baker says the need for regulations is just as great for hostelry services like Airbnb. “With hotels we have a set of regulatory structures that ensure they're not fire traps, that they are not a nuisance to their neighbors,” he says.

And regulations often go beyond simple safety issues to require companies to meet societal goals. “There are important services that we expect people to have access to, and that means all people,” says Baker. He notes that because of the Americans with Disabilities Act, cab companies must have a certain number of handicapped-accessible cabs. “That is a totally legitimate public purpose,” he says. “But Uber is not bound by that and as long as we have the two systems side by side, Uber is essentially dumping off the cost on the traditional cab companies.”

Free market advocates say the problem is regulation itself—and that the solution is to remove the regulations that apply to traditional companies. “Rather than pursue legislation that seeks to regulate sharing economy companies like their traditional competitors,” Feeney wrote, “lawmakers ought to deregulate these competitors in order to make the regulatory playing field as level as possible while allowing for innovative disruptors to enter markets.” [28]

Are sharing-economy companies platforms for independent contractors, or are they employers?

Sharing-economy companies that connect service providers with customers say they are simply providing a convenient platform to help the two parties connect. An Uber spokesperson, talking on background, described Uber as a technology company that matches riders with drivers. The company classifies drivers as “partners,” not employees.

As long as service providers are considered independent contractors, companies aren't bound by minimum wage and overtime laws, nor do they incur expenses for such things as unemployment insurance, workers' compensation and health insurance.

However, service providers have sued some sharing-economy companies—including Uber and Lyft—saying they are really employees and should receive benefits. Those lawsuits are pending, and neither company responded to requests to discuss them.

The initial indications are that the companies may face a tough sell of their argument that the companies are just platforms and not transportation companies with driver employees. Judge Edward Chen of the federal District Court in San Francisco called that argument “fatally flawed,” noting, “It is clear that Uber is most certainly a transportation company, albeit a technologically sophisticated one.” [29]

As for the argument that the drivers are independent contractors and not employees, Chen said that the issue will have to be decided at trial under California law.

The California Labor Commission's determination in early June that at least one Uber driver was, in fact, an employee, will likely be taken into consideration.

“Defendants hold themselves out as nothing more than a neutral technological platform, designed simply to enable drivers and passengers to transact the business of transportation,” the Labor Commissioner's Office wrote in its decision. “The reality, however, is that defendants are involved in every aspect of the operation.” [30]

While several other states—including Georgia and Texas—have ruled Uber drivers to be contractors, Florida authorities decided in May that a former Uber driver had been an employee for purposes of claiming unemployment benefits. Uber is appealing that decision.

There is no federal law defining the difference between independent contractors and employees, nor have states been consistent in defining the terms. But, according to Kai Falkenberg, former editorial counsel for Forbes magazine and currently a visiting professor at

Cardozo School of Law, there are a number factors the courts tend to consider in making such determinations, including the amount of control the company exerts over the service provider's activities.

For its part, the Internal Revenue Service applies “the usual common law rules” in determining employee status for tax purposes. This involves determining the extent to which the company exerts behavioral control and financial control over the service provider, as well as factors such as contract obligations, if any, and provision of benefits, such as health insurance. [31]

“One of the reasons that Uber drivers might be considered as employees is the degree of control that the companies are exerting,” Falkenberg says. “And one of the manifestations of that is, interestingly, through the rating system. That seems to be a significant degree of control.”

Falkenberg explains that Uber relies on its customer review system to cultivate trust in the service. If drivers get bad reviews from customers, they are likely to be let go.

“The companies really want to provide the best caliber service, and they want the people using the service to trust them,” she says. “There's a tension between providing a high level of service but without changing your status from basically being a platform that provides a matchmaking service to a company that is actually employing people who are providing a service.”

“For all practical purposes they are employees and if we're just going to play a semantic game here then there is no point in the regulations in the first place,” Baker says of Uber drivers. “Obviously if you have the option to define someone as an independent contractor rather than an employee, and evade all of the regulations, then you've given companies enormous incentive to classify people as independent contractors.”

Some analysts say the real problem is with the way important benefits are tied to employed positions vs. independent contractors.

“The sharing economy in a lot of ways is putting a spotlight on weak spots in public policy,” says Koopman. “One of those is why we continue to insist on tying health insurance to employment.”

Arun Sundararajan: Labor laws should be updated.

Sundararajan of the Stern School of Business agreed. “The dichotomy of employees and independent contractors is out of date,” he wrote. Sundararajan called for labor laws to “be updated to provide a social safety net to people whose chosen form of work is something other than full-time employment. Health coverage, insurance against workplace injuries, paid vacations and maternity leave: these have long been universal entitlements in many economies. They should not become exclusive perks for a dwindling band of salaried employees.” [32]

Background

Out of the Shadows

Before the development of effective monetary systems, nearly all economic activity took place within sharing economies that relied upon either barter or gifting to exchange goods and services. After the Industrial Revolution and the rapid spread of capitalism in the mid-1700s, the exchange modes of the sharing economy were relegated to an unofficial shadow economy in industrialized countries.

Some sources point to Harvard law professor Yochai Benkler as the first person to articulate the modern concept of the “sharing economy.” Benkler coined the term “commons-based peer production” to describe activities in which numbers of people work together, primarily over the Internet, to create value. Benkler further developed the concept in his 2004 paper, “Sharing Nicely: On Shareable Goods and the Emergence of Sharing as a Modality of Economic Production.” [33]

Benkler was describing a trend that had been developing for several years. Increasingly, individuals and companies were taking advantage of the emerging capabilities of the Internet to connect people to information, products and each other. As early as 1995, when a person had something to sell, she could simply post it on eBay or Craigslist and instantly reach thousands of people instead of having to take out a relatively expensive ad in the local newspaper that might reach a small number of people.

Not surprisingly, different sectors of the sharing economy developed independently and at different times as new technologies enabled more complex interactions.

The earliest companies in the modern sharing economy were those focused on connecting individual buyers of products and services with individual sellers.

Person-to-Person (P2P) Markets

"It's hard to believe now, but until 1991, commercial enterprise on the Internet was strictly prohibited. Even then, the rules favored public institutions and forbade 'extensive use for private or personal business,'" wrote Wired executive editor Keven Kelly. [34] In the eyes of the National Science Foundation (NSF), which at the time was the primary authority governing Internet activity, "the Internet was funded for research, not commerce," he said.

Harvard law professor Yochai Benkler outlined the evolution of the modern sharing economy in a 2004 paper.

The NSF didn't officially lift its prohibition on commercial activity until 1995. [35] Even before then, however, e-commerce had begun. In 1992, Book Stacks Unlimited in Cleveland opened one of the first commercial sales websites that supported credit card processing. Only two years later, what would become a dominant e-commerce site—Amazon.com—was founded. [36]

Book Stacks Unlimited and Amazon were, of course, e-commerce sites rather than sharing-economy platforms. But they pioneered the technologies that would drive the emergence of online services that allowed consumers to share products through the Web.

And in 1995, two companies that would evolve into two of the largest drivers of the sharing economy appeared.

In early 1995, Craig Newmark began an email distribution list to inform his community of Internet developers in the San Francisco area about local events. The service proved popular—especially for its job listings and listings of items for sale—and as the mailing list grew others began to contribute items. By 1996, Newmark converted the mailing list to a website, craigslist.org. [37]

Craig Newmark, founder of Craigslist, poses outside the company's San Francisco office in 2006. What began in 1995 as an email list evolved into a powerful platform for person-to-person advertising. (Justin Sullivan/Getty Images)

EBay, also founded in 1995, was intended from the start by its founder Pierre Omidyar to be a commercial site for selling goods and services. Unlike Amazon, however, eBay aimed at connecting individual sellers with individual buyers through online auctions. [38]

In 2008, Shelby Clark, then a graduate student at Harvard Business School, realized that the P2P model didn't have to be limited to individuals buying and selling products. It could also be used for sharing things like personal cars. On Thanksgiving Day in Boston that year, Clark wanted to visit his cousins but he didn't have a car. “It was a frickin awful winter day in Boston,” he recalled in an interview. “It was snowing and the freezing wind was coming from every direction and I'm biking through the snow and sleet to get this damned car. Meanwhile, I'm passing all these cars that are covered in snow. They clearly hadn't been driven in weeks.” [39] That's when he got the idea to develop a platform on which car owners could offer their vehicles for rent.

Clark couldn't find any such service online, but he did discover the major hurdle he had to clear: insurance. Existing policies didn't cover car rentals between individuals. It took Clark 18 months to arrange appropriate coverage, after which he started RelayRides.

Also in 2008, Joe Gebbia and Brian Chesky were inspired to apply the model to another underused resource: living space.

“Joe Gebbia and Brian Chesky were two jobless friends living together when they received a terrifying letter from the landlord,” wrote Alex Stephany, author and CEO of a European sharing company called JustPark. [40] The letter informed them that their rent was increasing by 25 percent. Chesky didn't have the money. “He had days to find a solution when the two noticed all the unused space in their living room,” wrote Stephany. “What if someone would pay to sleep there? Gebbia had just been camping and had an airbed. They blew it up … and came up with the concept of ‘airbed and breakfast’: cheap accommodation on your beds with a no-frills breakfast of Pop-Tarts.”

Two days later, www.airbedandbreakfast—later to be known as Airbnb—was born. The company grew so quickly that, in 2015, it has 1.2 million listings in 190 countries. [41]

But the power of the Internet-powered sharing economy isn't just about big markets. It also allows smaller communities to connect across great distances.

Poshmark, a platform founded in 2011 that runs on a mobile application, connects women who want to buy and sell used clothes with each other. Sellers take photos of their items to offer for sale. When an item is sold, the Poshmark app emails the seller a shipping label addressed to the buyer. [42]

Product Sharing and Renting

While P2P markets connect individual buyers to individual sellers, Robin Chase's idea in 1999 was to provide a platform and products that individuals could easily share.

She had met a friend at a café in Cambridge, Mass., Chase recalled. The friend had just returned from a vacation in Germany and mentioned that she had come across a car being rented to people by the hour or by the day. Chase, who would become a cofounder of Zipcar, wondered if that idea might work in Cambridge.

“My husband drove our car out to his suburban office every morning, where it would sit in the parking lot all day,” Chase wrote. “And while I definitely needed a car sometimes, there was absolutely no way I wanted to buy another, park it on the street in our city neighborhood, maintain it, and shovel it out after snowstorms.” [43]

Zipcar began with an initial investment of $50,000. “Four months later, Zipcar had $68 in its bank account and three days before going live,” Chase said. “The plan was to place four cars in four reserved parking spaces, one near each of four consecutive subway stops in Cambridge and Boston.” [44]

According to Chase, the company's goal was to make renting a car “as easy and convenient as getting cash from an ATM.” [45] Chase and her team accomplished this by creating a website for making reservations, then placing devices in the cars that could read members' cards for unlocking, enabling the ignition and tracking distances.

At the same time as major sharing-economy companies were launching, so too were scores of nonprofit grassroots efforts that, collectively, have greatly affected the economy and communities' use of resources.

In May 2003, for example, Deron Beal started the Freecycle Network to connect his friends and a few nonprofits in Tucson, Ariz., so that they could exchange goods they no longer needed without charge. Freecycle Network now has 5,000-plus groups and more than 7 million members worldwide. [46] It's a grassroots and entirely nonprofit movement of people who are giving (and getting) stuff for free in their own towns and keeping good things out of landfills.

Peer-to-Peer Loans

As companies were helping people share goods and services, some companies turned to the Internet to allow people to loan each other money instead of going through banks and other financial institutions, which generally charge higher rates of interest.

The first such peer-to-peer lending service was Zopa, begun in Great Britain in 2005. Since then, Zopa has made more than $1.4 billion in loans with reserves pooled from more than 51,000 people. [47]

The next year, the first peer-to-peer lending company in the United States—Prosper Marketplace—launched in San Francisco.

According to a Federal Deposit Insurance Corp. report, however, early peer-to-peer lending platforms had few qualifications for borrowers, which led to defaults and high loss rates. The report noted that the major peer-to-peer services have tightened borrower requirements. [48]

Some platforms gave a twist to the peer-to-peer lending model by combining it with features of eBay-like auctions to create "crowdfunding." The best-known of these platforms—Kickstarter—was founded in 2009. Kickstarter provides a structured means for individuals or companies to pitch their products and services in order to enlist contributions. As of July 27, Kickstarter says it has funded 89,000 projects since 2009, with 9.1 million contributors pledging $1.8 billion. [49]

Fee-for-Service Markets

The preeminent example of fee-for-service firms are transportation network companies (TNCs), including Uber, Lyft and Sidecar. With TNCs—which offer rides to consumers, booked via websites or mobile apps—the vehicles aren't actually shared or rented. Instead, drivers with their own vehicles share the TNC platform to offer their services to consumers.

While car-renting companies such as Zipcar and car-sharing companies such as RelayRides had established themselves years earlier, TNCs, which deliver services on a moment's demand, had to await the development and ubiquity of smartphones and the apps that run on them.

That technological hurdle was cleared by 2009 when Uber was founded as "UberCab" by Travis Kalanick and Garrett Camp.

The Beginnings of Regulation

Regulators have struggled to find ways not only to regulate the various types of sharing-economy companies but also to monitor their activities and collect appropriate taxes. For the most part, such efforts have taken place at the local level.

The TNCs have drawn the greatest attention, because they compete in an industry that has long been heavily regulated for public safety reasons and because governments want to control their effects on communities and public facilities, such as airports. This process of fitting TNCs into the existing regulatory frameworks has been a challenge that has resulted in a patchwork of requirements.

In June 2014, Colorado became the first state to pass legislation creating a statewide regulatory framework for TNCs. [50] The legislation specifies necessary levels of insurance and details requirements for regular background checks. The state Public Utilities Commission is empowered to revoke or suspend a company's permit, but penalties against drivers are prohibited. Other measures include yearly safety inspections of drivers' vehicles and exterior markings signifying them as vehicles for hire. In addition, the TNC cannot discriminate against riders based on their location or destination, nor can it charge additional fees for passengers with disabilities.

Current Situation

Regulatory Pressure Grows

The sharing economy is filled with companies that have as many differences as similarities. In fact, the only thing they have in common is that customers access goods or services through the Internet.

Most of these businesses—such as Etsy, MuniRent and Zimride (a ride-sharing service for companies and universities)—pose few, if any, problems for consumers or regulators. That's because they simply connect providers to consumers and are not engaged in the types of activities that require safety regulations to protect the public. Most sharing-economy companies are also generally free of controversy because they are not directly competing with traditional companies. And most don't rely extensively, if at all, on service providers who might press claims for employee benefits.

Other companies—most notably, Uber, Lyft and Airbnb—are facing increasing pressure from regulators, employees and competitors.

In the last five months alone, legislatures, city councils, regulators and others have been active on numerous fronts:

- In early March, the Vermont Department of Financial Regulation issued a consumer alert, "Be aware before you share." The alert warned residents wanting to drive that participation in sharing-economy businesses could expose them to major liabilities if they lack appropriate insurance. The state labor commissioner announced she was investigating Uber in Vermont to determine whether its drivers are employees or independent contractors. [51]
- On April 21, the Portland, Ore., City Council voted 3–2 to end a prohibition on ride-sharing companies by allowing them to operate

under a 120-day pilot program. The two dissenting council members indicated that they still have concerns about minimum insurance coverage and Uber's business practices. [52]

- On May 4, California Democratic state Sen. Mike McGuire introduced legislation that would require companies such as Airbnb to adhere to local laws with regard to vacation rentals, including paying occupancy taxes. The legislation also calls for data reporting on room rates and the number of nights stayed by renters. [53]
- On May 5, Uber announced that it was ceasing operations in Kansas after the state Legislature overrode the governor's veto to pass legislation with stricter insurance requirements and background checks for drivers. [54]
- On May 12, the Santa Monica, Calif., City Council adopted a home-sharing ordinance that prohibits the rental of an entire unit for less than 30 days. The ordinance also requires hosts to obtain a business license and to pay a 14 percent hotel tax. Proceeds from the tax will help pay for enforcement officers and staff to search online for illegal rentals. [55]
- On May 26, San Francisco International Airport and the San Francisco Municipal Transportation Agency petitioned the California Public Utilities Commission to impose tighter regulations on ride-sharing companies. Specifically, the agencies called for mandated vehicle inspections, a limit of 375,000 miles on vehicles, the use of permanent “trade dress” markers on vehicles and training for drivers. [56]
- On May 29, Republican Nevada Gov. Brian Sandoval signed legislation providing a regulatory framework for ride-sharing services in the state. The framework includes a 3 percent tax on fares. [57]
- On June 18, Lyft agreed to pay the state of New York $300,000 to settle claims that it was in violation of state and municipal laws. The agreement also placed tighter requirements on insurance for Lyft drivers, and required the company to comply with state and local laws covering for-hire car services. [58]

Companies Responding

One of the major challenges facing sharing-economy companies is that to do business nationally, they must conform to not just one regulatory authority but potentially hundreds of state, municipal and port authorities.

“It's a problem for the companies,” says John Browning, a Southern Methodist University adjunct law professor who also works with tech start-ups. “They have lobbyists going to 50 different state legislatures.”

Browning says federal legislation could simplify things, although no bill has been introduced. “Are there companies, particularly in the tech sector, that have an interest in getting some sort of federal legislation? Absolutely,” he says. “That would give companies some measure of predictability, reliability and, to a certain extent, protection.”

Perhaps in anticipation of, or to fend off, regulation, many of the larger sharing-economy companies, in addition to stepping up lobbying efforts, have been introducing or increasing their own insurance coverage and taking other steps, such as performing background checks for relevant service providers.

“Generally, these companies want to at least have the appearance that they are in line with consumer expectations,” says Breyault of the National Consumers League. “By and large, I think they are implementing these because they want to avoid more onerous regulations that could harm their business model.”

Uber, for example, instituted background checks for drivers in 2014 that cover:

- County courthouse records going back seven years for every county of residence.
- Federal courthouse records going back seven years.
- The multistate criminal database going back seven years.
- A National Sex Offender Registry screen.
- A Social Security trace, which ensures the number is valid and confirms names and addresses.
- Checks of existing motor vehicle records, as well as regular future checks. [59]

Critics, however, charge that the background checks aren't thorough enough because they do not include fingerprinting and processing through law enforcement agencies.

In July 2014, Uber also announced it had obtained a commercial insurance policy to provide $1 million of liability coverage per incident, as well as contingent comprehensive and collision insurance. [60] The new coverage applies to Uber's most widely used service, called

UberX. (Commercial insurance already covered the company's other more specialized services such as black-car limo rides.)

In March 2015, Uber and the Property Casualty Insurers Association of America (PCI) announced model legislation for consideration by states that they jointly developed; 18 states have already passed laws that mirror the model, according to Robert Passmore, PCI's senior director for personal lines.

“Auto insurance is based on years and years of track records and loss history,” says Passmore. “We don't have a lot of loss history behind these folks.” Thus, says Passmore, it's especially important to have clear rules about what kinds of coverage are required.

Airbnb, too, has moved to provide insurance. As of January 2015, the company's Host Protection Insurance provides up to $1 million in coverage in the event a guest is injured on a host's property during a stay. The insurance applies only in the United States. [61]

Airbnb has also made agreements with some localities—including the District of Columbia, San Francisco, Phoenix, Portland, Ore., San Jose and Chicago—to collect taxes owed by hosts and pay them directly to the local government. While Airbnb did not respond to requests for comment, its website notes that these agreements make “the tax collection process easier for all parties involved.”

“In many cases, these taxes were designed for hotels and folks with teams of lawyers and accountants, and the reality is that the person who's renting out his basement in Cleveland Park [in D.C.] once a month probably doesn't have tax experts on payroll,” Nick Papas, an Airbnb spokesman, told a Washington Post reporter. “You shouldn't need a lawyer and a tax specialist if you want to rent out your house.” [62]

According to Stephen Cordi, the deputy chief financial officer in the Office of Tax and Revenue in D.C., it was Airbnb that approached the city about making the arrangement to pay taxes.

“It's undoubtedly true that people particularly at the bottom end of this probably didn't know what to do,” Cordi told The Washington Post. While individual Airbnb hosts should have been registering with the city and paying the taxes all along, he said, “this will eliminate the need for them to do that.”

Still, according to Norton Francis, senior research associate at the Tax Policy Center, which provides research on taxes for the Urban Institute and the Brookings Institution, cities and states are “losing tax revenue because of these new forms” of services in the sharing economy. “The product isn't any different; it's the delivery,” he said. “States are one step behind commerce in an effort to try to maintain their tax bases.” [63]

Looking Ahead

Rivals Need to Adapt

The technologies that define the sharing economy—the Internet-enabled applications that allow consumers to connect directly to service providers—are clearly not going to disappear.

“I think this is the beginning of the second-order issues of the sharing economy,” says Koopman of the Mercatus Center. “The first-order issues were whether the sharing economy should exist at all. That debate is settled. The sharing economy is here to stay. Now comes the second wave of issues for sharing economy firms: How are the regulators going to treat them?”

Because the technologies driving the sharing economy are new, the old regulatory frameworks are no longer appropriate, most analysts agree. Even those who maintain the need for strong regulatory structures acknowledge that in some areas changes are warranted. “You can make plenty of arguments, and there some truth to them, that a lot of the regulations that we have in place are excessive,” says Baker of the Center for Economic and Policy Research.

“Do you apply old regulations to new innovations or try to adapt and evolve the regulations to fit the market over time?” Koopman asks. “I think when you try to apply the old laws and the old rules to new innovation and new entrepreneurship, you end up hamstringing innovation. This should be an opportunity for everyone to critically reevaluate the regulations on the books.”

In the meantime, say some analysts, it's time for traditional companies to adapt to the new technology environment. “The entry of these new platforms has put pressure on existing suppliers,” economist Farronato says. “From the point of view of innovation, it is pressure for the better.” She adds that as traditional companies adopt the new technologies—such as online review—old regulatory frameworks may no longer be needed. “It might be the case of the industry will actually evolve in a way that the regulatory environment will be more lax,” she says.

While free market advocates worry about regulators stifling innovation, former Clinton administration Labor Secretary Robert Reich warns about the ramifications of an unfettered sharing economy.

“In effect, on-demand work is a reversion to the piece work of the nineteenth century—when workers had no power and no legal rights, took all the risks, and worked all hours for almost nothing,” Reich wrote in an article on his website. “Uber drivers use their own cars, take

out their own insurance, work as many hours as they want or can—and pay Uber a fat percent. Worker safety? Social Security? Uber says it's not the employer so it's not responsible." [64]

Of course, how consumers and investors will respond to higher costs caused by increased regulation of the sharing economy is unknown.

With respect to investors, they seem undeterred so far. "There have been very high investment levels within these areas where regulation hasn't been settled," says Eckhardt of the University of London.

Consumers' response, she says, may be more problematic. "When you start to see that competitive advantage eroding away, and prices rise, consumers may perceive [the companies] to be gouging," she says. "These so-called sharing-economy companies are, in a way, responsible for this because the way they tend to position themselves as, 'Oh, we're doing better for the world. We're somehow different than all of these regular companies.'"

About the Author

Patrick Marshall is a freelance writer in Seattle who writes about public policy and technology issues. He is a technology columnist for The Seattle Times and Government Computer News. He holds a B.A. in anthropology from the University of California, Santa Cruz, and a master's degree in international studies from the Fletcher School of Law and Diplomacy, a program of Harvard and Tufts universities.

Chronology

1990s	**Technologies that will power the sharing economy appear, and pioneer e-commerce companies take advantage.**
1991	The National Science Foundation (NSF), which controlled the Internet backbone, allows commercial access to the formerly government and academic network.
1992	E-commerce begins when Book Stacks Unlimited in Cleveland opens a website that supports credit card processing.
1994	Amazon is founded and would soon grow into a dominant e-commerce site.
1995	Craig Newmark launches an email distribution list that will be converted the next year into a website that allows people to buy and sell goods and to find jobs: craigslist.org. … eBay is founded as an online platform to connect individual sellers with individual buyers through online auctions. … NSF formally lifts its prohibition on commercial activity on the Web.
1999	Zipcar—an online car rental service—appears, with four cars stationed near subway stops in Cambridge and Boston, Mass.
2000–2007	**Early sharing-economy companies are founded.**
2003	The Freecycle Network goes online, allowing individuals and nonprofits to exchange goods they no longer need.
2004	Yochai Benkler, a Harvard law professor, publishes, "Sharing Nicely: On Shareable Goods and the Emergence of Sharing as a Modality of Economic Production," the first analysis of the modern sharing economy.
2005	Zopa, the world's first online peer-to-peer lending platform, debuts in London.
2007	Zimride, which became Lyft, begins offering on-demand rides; its drivers are independent contractors who own their own cars.
2008–Present	**Recession spurs growth of the sharing economy as regulators begin to take action.**
2008	Harvard Business School graduate student Shelby Clark launches RelayRides, a service that allows individuals to rent their personal cars to others. … Joe Gebbia and Brian Chesky, needing money to pay their rent, offer their living room online as a place for someone to sleep. A few days later, they launch www.airbedandbreakfast.com, which will soon become known as Airbnb.
2009	Kickstarter, a crowd-sourced platform for funding projects, opens. … UberCab, which will soon change its name to Uber, is founded in San Francisco.

2014 Colorado becomes the first state to pass legislation creating a statewide regulatory framework for "transportation network companies," such as Uber and Lyft. … In June, the California Labor Commissioner's Office rules that an Uber driver should be classified as an employee, not an independent contractor. … In October, the New York State Office of the Attorney General releases a report that finds that 72 percent of units booked over Airbnb in the state appeared to violate state and local laws. Within days, New York City files suit against two property owners.

2015 On May 5, Uber announces it is ceasing operations in Kansas after that state passes legislation with stricter insurance requirements and background checks for drivers. … On May 12, the Santa Monica, Calif., City Council adopts a home-sharing ordinance that prohibits the rental of an entire unit for less than 30 days. The ordinance also requires hosts to obtain a business license and to pay a 14 percent hotel tax. … On May 26, San Francisco International Airport and the San Francisco Municipal Transportation Agency petition the California Public Utilities Commission to impose tighter regulations on ride-sharing companies. … On May 29, Nevada Gov. Brian Sandoval announces passage of a regulatory framework for ride-sharing services in the state; the framework includes a 3 percent tax on fares. … On June 18, Lyft agrees to pay the state of New York $300,000 to settle claims that it was in violation of state and municipal laws. The agreement also places tighter requirements on insurance for Lyft drivers, and requires the company to comply with state and local laws covering for-hire car services.

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Airbnb
888 Brannan St., San Francisco, CA 94103
415-800-5959
www.airbnb.com
Company that provides a platform for peer-to-peer rentals of living spaces.

Cato Institute
1000 Massachusetts Ave., N.W., Washington, DC 20001-5403
202-842-0200
www.cato.org
Libertarian think tank that explores the impact of government policies, including regulation.

Center for Economic and Policy Research
1611 Connecticut Ave., N.W., Suite 400, Washington, DC 20009
202-293-5380
www.cepr.net
Think tank that focuses on the effects of economic policies.

Federal Trade Commission
600 Pennsylvania Ave., N.W., Washington, DC 20580
202-326-2222
www.ftc.gov
The U.S. commission that is charged with preventing business practices considered anticompetitive, deceptive or unfair to consumers.

Lyft
2300 Harrison St., San Francisco, CA 94110-2013
866-292-2713
www.lyft.com
Company that offers on-demand transportation network services.

Mercatus Center, George Mason University
3434 Washington Blvd., 4th Floor, Arlington, VA 22201-4508
703-993-4930
www.mercatus.org
Describes itself as "the world's premier university source for market-oriented ideas—bridging the gap between academic ideas and real-world problems."

Property Casualty Insurers Association of America
8700 W. Bryn Mawr, Suite 1200S, Chicago, IL 60631-3512
847-297-7800
www.pciaa.net
Trade association for property casualty insurers.

Uber
1455 Market St., 4th Floor, San Francisco, CA 94103

877-223-8023
www.uber.com
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