

**“The Opportunities and Risks of the Sharing Economy”**

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Benefits Consumers, and Raises Policy Questions"**

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I would like to thank Chairman Burgess and Ranking member Schakowsky for inviting me to testify on issues stemming from the growth of the sharing economy. The range of innovations that have collectively come to be known as the sharing economy offer both significant benefits to consumers and the economy more generally. Ideally, the sharing economy allows for idle assets to be more fully utilized. The sharing economy should make it easier for a household to rent out an empty house or room. It should also give people the option to do work in their spare time to earn extra income. In these and other ways the sharing economy can offer substantial benefits.

However, the sharing economy also presents substantial risks. The country has built up an extensive regulatory structure over many decades to protect workers, consumers, and property owners. The sharing economy will require the modernization of this regulatory structure. In some cases, regulations have outlived their usefulness and should be eliminated. However, many of these regulations serve important public purposes. If the sharing economy is used as a way to circumvent them, then it will impose substantial costs on society.

I will use my testimony to outline the sorts of issues that sharing economy firms have raised. Many of the regulatory issues posed by sharing economy firms arise at the state or local level. However, some of the issues affect laws set at the national level. Furthermore, the federal government can assist state and local governments in successfully modernizing regulations to deal with sharing economy innovations. For these reasons, the sharing economy raises many questions on which Congress should have input.

There are four basic types of regulatory issues posed by the sharing economy. First, it raises a number of issues on labor regulation. Most sharing economy firms treat the people who work for them as independent contractors. This denies them the range of protections they would have as employees. The appropriateness of this classification as well as the construction of alternative protections for independent contractors are important questions for policy makers.

The second category is consumer protection regulation. There are a variety of protections that have been put in place at all levels of government to ensure that services and products meet minimal standards of both quality and safety.

The third category of regulations concerns property rights. This comes up most prominently with rental services like Airbnb. Many apartment leases and condominium association rules restrict the ability to rent out units to third parties. If Airbnb and other services provide a mechanism for evading these restrictions, then it undermines their effectiveness.

The last category is rules prohibiting discrimination in the provision of services. There are laws at all levels of government prohibiting discrimination based on race, gender, and other

factors and also ensuring accessibility for people with disabilities. These laws will have to be adjusted to ensure that the growth of sharing economy firms does not undermine their purpose.

There is also an important question about collection and payment of taxes by sharing economy firms. It is possible that Internet-based providers may use this platform as a way to avoid the taxes imposed on their traditional competitors.

These issues are dealt with in turn below.

## **1. Labor Regulations**

In the ideal vision of the sharing economy, the people who provide services are treating it as a spare-time activity, where they can earn some additional income. It is not a person's primary source of income. For this reason, sharing economy firms argue that its workers, who they treat as independent contractors, do not need the same sort of protections accorded employees.

This argument raises two issues. First, it is not clear to what extent the description is accurate. While we don't have reliable data at this point, there are certainly many accounts of people who treat their work for Uber, Lyft, or other sharing economy companies as a full-time job. The second issue is what sort of protections people working in the sharing economy should be guaranteed even if their work should not be viewed as comparable to a traditional job.

On the first point, whatever the current number of people who rely on sharing economy companies for full-time or near full-time employment is, that number is almost certain to grow as the sharing economy grows. For this reason, it is appropriate that people working for sharing

economy companies should enjoy protections that are comparable to those of traditional employees. Among these protections is the right to bargain collectively. This means that people working for companies like Uber or Lyft should be able to organize and negotiate for better pay and working conditions without the threat of being fired. There have been several cases brought before the National Labor Relations Board (NLRB) and in federal court arguing that people working for these companies are employees.

It is possible that these bodies will resolve the issue by saying that people working for these and other sharing economy companies are employees and therefore entitled to all the protections of employees. Nonetheless it is likely that, however these cases are resolved, there will still be substantial gray areas. For this reason, it would be helpful for Congress to more clearly define who should be counted as an employee, or perhaps more importantly who should be entitled to employee-like protections.

The range of issues involved is lengthy. In addition to the right to bargain collectively, employees are also subject to wage and hours regulations. This means that they are entitled to earn at least the minimum wage and to get an overtime premium if they work more than 40 hours a week. Workers are also eligible for unemployment benefits if they are laid off due to insufficient demand. They also are covered by workers' compensation through which they are insured against loss wages and medical expenses resulting from on-the-job injuries.

It would require some effort to redesign these protections to make them compatible with a sharing economy relationship that may be less formal than a traditional employer-employee relationship, but it is a doable task and there is a clear public purpose in adjusting regulation. It

makes little sense to require traditional employers to meet minimum wage standards and pay overtime premiums if we don't apply comparable rules to sharing economy competitors.<sup>1</sup> Not only does this put law-abiding firms at a disadvantage; it is basically giving them a back-door way around rules they choose not to follow. If we require traditional employers to meet wage and hour rules and but allow sharing economy companies to ignore them, we can expect to see rapid growth of sharing economy companies.

Furthermore, the logic of many of these rules would apply regardless of whether we think workers in the sharing economy are like traditional employees. For example, would we not expect sharing economy companies to be responsible for injuries workers have while doing work for them even if we don't classify them as employees? Also, traditional employers are expected to withhold taxes from workers' paychecks. This is done not only to increase compliance, but also to avoid situations in which workers face large tax liabilities every April. It would be possible to have comparable withholdings in a sharing economy relationship even if the worker is not classified as an employee.

## **2. Consumer Protection**

In the sectors of the economy where the sharing economy has had the greatest impact to date, ride-hailing services and short-term rentals, their growth has posed a considerable challenge to

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<sup>1</sup> In some cases it may be difficult to apply rules like the minimum wage to sharing economy activities, but in many cases it will not be difficult. For example, in the case of Uber, the company has information on the number of hours a worker drives and their gross revenue. It can impute costs per mile for their vehicle to back out a net wage that would have to be at least as high as required by the relevant minimum wage statutes.

the existing consumer regulatory structure. In both areas, it has proved difficult to apply the existing system of regulations directly to the new sharing economy companies that have entered the market.

In the case of ride-hailing services, the incumbent taxi industry was heavily regulated to ensure that both the cars and drivers were safe. Cities require that drivers get commercial driving licenses requiring a higher standard of driving proficiency than is needed for a normal license. They also require drivers to go through a background check to ensure that they don't have a criminal record indicating that they could pose a risk to passengers.

Taxis are also required to undergo regular inspections to ensure that they meet safety standards. In addition, taxis are generally required to carry substantial insurance so that passengers can be compensated if they are injured during a ride.

These requirements do not apply directly to Uber, Lyft, and other ride-hailing services. Both of these companies do claim to screen their drivers to ensure their competence and also to check their backgrounds. But this is done voluntarily and not as a response to regulations from which they claim exemptions. Both companies now also provide their passengers with insurance for their ride, although in many cities this may be less insurance than that required for the incumbent taxi industry.

There is also a risk in the taxi industry that the new ride-hailing services may effectively be cherry picking customers and possibly making taxi service for less affluent customers unprofitable. These services are set up so as to require that customers have both a smart phone and credit card to be able to use them. This effectively excludes the population that lacks one or

both. This group tends to be less affluent. While low- and moderate-income people may not be frequent users of taxis, they will often need them for doctor appointments, trips to the hospital, or grocery shopping. If the incumbent taxi companies cannot survive the competition from Uber and other sharing economy companies, this segment of the population may find it more difficult to meet its transportation needs. To date, this has not been an issue, but it is a potential problem that policymakers need to follow.

In the case of short-term rentals through Airbnb-type services, the established hotel industry is required to meet certain safety standards, most importantly a standard that its guests will be adequately protected against the risk of fires. Hotels are regularly inspected to ensure that they don't subject guests to excessive risks of fire and also that they are prepared to respond to a fire, should one occur. This means having working fire extinguishers readily accessible and also making sure that guest rooms have multiple exit paths in the event that one route is blocked due to a fire.

This sort of regulatory structure does not transfer readily to the Airbnb model. Airbnb does not have the ability to inspect every unit or room in a unit that is posted on its site. However, it could institute a requirement that anyone listing on the site have an insurance policy that covers guests against fire or other harm while they are staying with their host. The insurer will presumably set the price of the policy to incorporate the risk posed by the specific circumstances.

There is an argument that many regulations have been put in place over the years largely to protect incumbent firms. This is especially true in the taxi industry, where regulations

effectively prevented competition for well-entrenched incumbents. However, most consumer regulations were put in place to meet legitimate public concerns. It may often be the case that these concerns can be met with less onerous rules than now exist. For example, it may not be necessary to have taxi drivers take and pass a special drivers' education course to ensure that they are safe drivers. Nonetheless, it is reasonable to expect that people who are driving commercially will meet more than the minimal standards necessary to get a driver's license in many states. For example, my 84-year-old mother, who has a Washington State driver license, should not be an Uber driver.

State and local governments should be encouraged to experiment with more flexible forms of regulation. This can mean self-regulation. For example, a ride-sharing company can submit its procedures for ensuring that drivers and vehicles are safe to a public safety authority. The company can then be subject to random checks to ensure that it is complying with its stated policies. This sort of process is important not only for public safety but also to open up sectors to new competitors. A politically powerful firm like Uber may be confident that it can avoid being subject to existing taxi regulations, whereas an upstart competitor may not be so lucky. The goal should be clear rules that apply common standards to both existing firms and any new firms that enter the sector.

### **3. Property Rights**



There are many restrictions on the use of rental or owned property that are imposed by other property owners. Some of these restrictions may be undermined by Airbnb and similar rental companies.

It is common for apartment leases to prohibit subleasing or renting out rooms. Such prohibitions both limit wear and tear on the apartment unit and limit the number of people who are entering the building. The latter can be both a nuisance, as in people entering and leaving at odd hours, and also a safety concern. Similar rules are also often put in place for condominium buildings or cooperatives. Using Airbnb or a similar rental service would likely be a violation of many apartment leases or condo association by-laws.

There is a fairly straightforward remedy for this problem. Services like Airbnb can require that users submit a copy of their apartment lease or condominium association rules and be held liable for violations if they allow a person to use the service for a property where such rentals are prohibited.

As a related issue, in many cities and counties, Airbnb has been held to be in violation of zoning rules that ban either the commercial use of residential property or limit an area to single-family units or in other ways restrict population density. As is the case with regulation in the taxi industry, the existing regulation may not be optimal. The best route forward is determine the extent to which the goals of the regulation meet legitimate public needs and modernize the rules to accommodate sharing economy companies.<sup>2</sup>

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2 There is also an issue in some cities with rent controlled or stabilized units. Airbnb can be used to evade the restrictions on rent increases, since there is no regulation applied to the charges for rentals through Airbnb.

In the same vein, there is evidence that Airbnb has been used to evade rules designed to protect affordable housing in some cities. In this case also, providing a service through the Internet should not be a mechanism for undermining regulation.<sup>3</sup>

#### **4. Rules on Discrimination**

Over the last five decades, there have been laws and regulations put in place at all levels of government that prohibit discrimination based on race, sex, religion, disability, and other factors. These laws are enforced against businesses, with companies often facing substantial penalties for violations.

Insofar as traditional hotels and motels lose out to Airbnb-type rental services, it will be considerably more difficult to enforce anti-discrimination measures. As a practical matter, it will be difficult to determine if specific individuals had discriminated in deciding to whom they would rent their unit or a room within the unit. There is not an obvious remedy to prevent such discrimination, but it is important that policymakers be aware of the risk. At the least, it would be useful to conduct regular testing to determine, for example, if African Americans, Hispanics, or other distinct groups have more difficulty renting out units than whites.<sup>4</sup>

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3 See for example, Samaan, Ray, 2015. "Airbnb, Rising Rent, and the Housing Crisis in Los Angeles," Los Angeles, CA: Laane, available at <http://www.laane.org/airbnb-report>.

4 It is worth noting in this respect that one of the benefits of Uber is that African Americans can summon a car without the driver knowing their race. This prevents them from being able to discriminate in deciding whether to pick up the customer. This avoids the well-documented discrimination that African Americans face in being picked by taxis working for the incumbent industry.

One area in which discrimination can be easily detected and remedied is in the case of the people with disabilities. For example, both taxis and hotels are typically required by state or local laws to accommodate the people who use wheelchairs. In the case of taxis, this usually means having a certain percentage of the taxi fleet being wheelchair accessible. Hotels are usually required to have a portion of their rooms be wheelchair accessible. It would be possible to impose similar requirements on sharing economy firms. A company like Uber would be required to keep track of the percentage of its drivers who can accommodate customers with disabilities. A service like Airbnb could do the same with those renting units. If the percentage is below a threshold, then a fee can be assessed which would be paid to the taxi companies and hotels that are accessible. This would prevent these companies from being a situation where they could simply pass off the cost of meeting the needs of people with disabilities on their traditional competitors.

## **5. Tax Collection**

Tax collection is another area in which the sharing economy poses important policy problems. The incumbent companies competing with sharing economy companies are subject to a wide variety of taxes. For example, hotels often have to pay a special hotel tax in addition to a state and/or local sales tax. As noted earlier, traditional employers are obligated to collect income

and payroll taxes from their workers' paychecks. It does not make sense to allow a segment of the market to enjoy special tax privileges because they are ordered over the Internet.<sup>5</sup>

The tax laws should apply equally to individuals renting out rooms through Airbnb and to hotel chains. Sharing economy companies should be required to report income to the relevant taxing authorities. This should not be an excessive burden, since in most cases the companies will already have all the necessary information on file.

## **6. Conclusion**

The Internet allows for a range of services to be provided at lower cost and more quickly than earlier technologies. Consumers and the economy as a whole can benefit from the spread of Internet-based sharing economy companies. However, this new technology can also be used as a mechanism to evade taxes and necessary regulation. It will be important to modernize and redesign regulations prevent sharing economy companies from going this route. We want companies to compete to provide better and cheaper services, not to determine who can more effectively game the regulatory structure and the tax code.

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<sup>5</sup> Amazon has gained much of its market dominance because it has been exempted for most of its existence from having to collect the same sales taxes as its brick-and-mortar competitors, most of which are far smaller businesses.